

# Growing our business...

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for more information visit:  
[www.imperial-tobacco.com](http://www.imperial-tobacco.com)

## About this Report

Reflecting our belief that operating in a responsible manner is simply part of how we do business, this year's report incorporates our Corporate Responsibility Review to provide stakeholders with a comprehensive overview of our activities and achievements.

# ...to deliver sustainable shareholder returns

## What we do...

We are a leading international tobacco company with a balanced market footprint and a unique portfolio that offers consumers high quality brands and products across all tobacco categories.

We create value for our shareholders by driving sustainable sales growth, optimising costs and effectively utilising the cash we generate.

## How we do it...

### **Consumer Centric: Understanding what drives our consumers**

Satisfying consumers and aligning our portfolio to their evolving preferences is fundamental to our sales growth strategy.

### **Execution Excellence: A fast and flexible business focused on delivery**

We are a responsive business with strong and trusted customer and industry partnerships, which enhances our growth potential.

### **Future Foundations: Building a sustainable future**

Operating responsibly, combined with our proactive approach to tackling illicit trade and regulatory engagement, is critical to our long-term success.

 for more information  
see pages 16 – 21

# Financial Highlights

Volumes <sup>1</sup>	2010	Change	2009
White stick equivalents <small>KPI</small>	<b>348.5bn</b>	-2.9%	358.8bn
Cigarettes <small>KPI</small>	<b>308.7bn</b>	-4.2%	322.2bn
Fine cut tobacco	<b>39.8bn</b>	+8.7%	36.6bn

Financial Highlights – adjusted basis <sup>2</sup>	2010	Change	2009
Tobacco net revenue <small>KPI</small>	<b>£7,055m</b>	+3%	£6,818m
Logistics distribution fees	<b>£936m</b>	-3%	£964m
Adjusted operating profit	<b>£3,067m</b>	+5%	£2,933m
Adjusted profit before tax	<b>£2,467m</b>	+10%	£2,233m
Adjusted earnings per share <small>KPI</small>	<b>178.8p</b>	+11%	161.8p

Financial Highlights – reported basis	2010	Change	2009
Revenue	<b>£28,173m</b>	+6%	£26,517m
Operating profit	<b>£2,528m</b>	+8%	£2,337m
Profit before tax	<b>£2,118m</b>	+124%	£945m
Basic earnings per share	<b>148.5p</b>	+127%	65.5p
Diluted earnings per share	<b>148.0p</b>	+127%	65.3p
Dividend per share	<b>84.3p</b>	+15%	73.0p

1 White stick equivalents reflects our combined cigarette and fine cut tobacco volumes.

2 Management believes that these non-GAAP measures provide a useful comparison of business performance and reflect the way in which the business is controlled. Definitions are included in our accounting policies within the notes to the financial statements. Reconciliations between adjusted and reported measures are also included in the relevant notes.

## Performance Highlights

# +3%

Tobacco net  
revenue growth

# +8.7%

Fine cut tobacco  
volume growth

# +5%

Adjusted  
operating profit

# Operational Highlights


## Delivering Sustainable Shareholder Value

We made gains with our global strategic cigarette brands *Davidoff*, *West* and *Gauloises Blondes*.

We have aligned our portfolio to consumers seeking value, with particularly strong results from our regional brand *JPS*.

We have further developed our unique total tobacco portfolio, increasing our fine cut tobacco volumes by 8.7%.

We have made excellent progress in reducing our adjusted net debt levels, down by £1.5 billion to £9.3 billion.

 for our financial and operational performance  
see pages 28 – 40

## Operating Responsibly

We signed a co-operation agreement with the European Commission and the Member States of the European Union to strengthen our joint efforts to combat the illicit trade of tobacco products.

We have revised our Code of Conduct in 2010 and are continuing to embed high standards of conduct and behaviour across the Group.

Business in the Community's 2009 Corporate Responsibility Index awarded us a Gold rating with an improved score of 93.8%.

 for our corporate responsibility performance  
see pages 41 – 52



# +11%

Adjusted  
earnings  
per share

# +15%

Dividend  
per share

Adjusted net  
debt reduced  
by £1.5 billion  
to £9.3 billion



## **“Central to everything we do is our priority of creating sustainable value for our shareholders.”**

**Iain Napier**  
Chairman

We delivered strong growth in earnings and dividends with our focus on organic sales growth, cost optimisation and effective cash utilisation continuing to create value for our shareholders.

### **Results and Dividends**

We grew our tobacco net revenues by 3 per cent and our adjusted operating profit by 5 per cent to £3.1 billion. Reported operating profit grew by 8 per cent to £2.5 billion. Our adjusted earnings per share has risen by 11 per cent to 178.8 pence. Basic earnings per share was 148.5 pence (2009: 65.5 pence) as a result of movements on derivative financial instruments providing commercial hedges with gains of £210 million compared to losses of £660 million in 2009.

We also made considerable progress in reducing our adjusted net debt, which was down by £1.5 billion to £9.3 billion (2009: £10.8 billion).

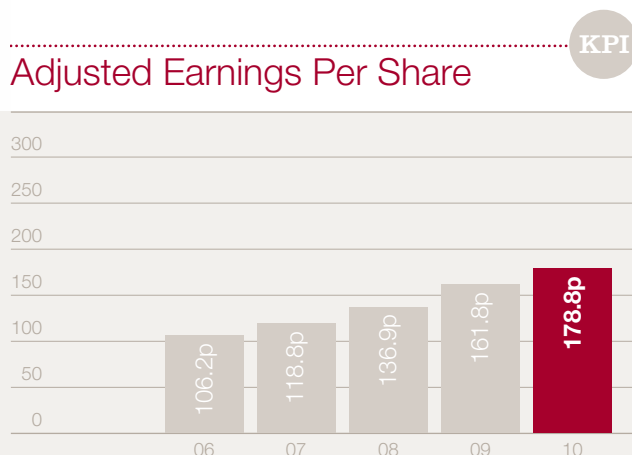
The Board recommends a final dividend of 60.0 pence per share, bringing the total dividend for the year to 84.3 pence per share (2009: 73.0 pence), representing an increase of 15 per cent. This dividend will be paid on 18 February 2011, with an ex dividend date of 19 January 2011.

### **Our Strategy for Growth**

We seek to create value for our shareholders by delivering sustainable organic sales growth, complemented by our focus on cost optimisation and effective cash utilisation. We drive sales growth through our brands, our unique total tobacco portfolio, our market footprint and our people.

### **2010 Performance Overview and Achievements**

**Sustainable Sales Growth:** During the last year we have enhanced our focus on sales growth and aligning our brand





and product portfolio to evolving consumer preferences. Price increases and a number of strong cigarette and fine cut tobacco performances more than offset the challenging environment in some markets.

Economic conditions have impacted consumer spending in Spain, the USA, Russia and Ukraine such that our overall cigarette volumes were down by 4.2 per cent. However we delivered excellent growth in fine cut tobacco with our volumes up by 8.7 per cent and, when our fine cut tobacco volumes are combined with our cigarette volumes, our overall white stick equivalent volumes were down just 2.9 per cent.

Our global strategic brands comprise around 22 per cent of our overall cigarette volumes and performed well. We delivered 3 per cent volume growth in our premium brand *Davidoff* and 2 per cent growth in *West. Gauloises Blondes* also made positive progress, with volumes up by 4 per cent in the second half of the year following temporary supply disruption in the Middle East earlier in the year. Our regional and local brands also delivered some strong performances including *JPS* which grew volumes by 13 per cent.

**Cost Optimisation:** We have delivered our Altadis acquisition synergy targets and have continued to drive efficiency improvements throughout the business. In 2010, we delivered €110 million incremental synergies bringing the total to €300 million. We remain on track to deliver our previously announced synergy target of €400 million cumulative synergies by the end of our 2012 financial year.

**Effective Cash Management:** We have generated £2.0 billion of free cash flow before dividend payments of £0.8 billion and made excellent progress in reducing our adjusted net debt, which was down £1.5 billion to £9.3 billion (2009: £10.8 billion) as at 30 September 2010. We maintained the improved working capital position we delivered last year and our cash conversion was 97 per cent, towards the top end of our target range of between 90 and 100 per cent.

#### Corporate Governance and Corporate Responsibility

The Board remains committed to the high standards of corporate governance that are rightly expected of us and that underpin the responsible way we run our business.

Integral to our strategy is our responsible approach to the manufacture and sales of our products, from the sourcing of tobacco leaf to the way in which we market to consumers.

It is vital that all our employees have a deep understanding of our behaviours and business principles – the beliefs and values that underpin all business actions and decisions. During the year we revised and enhanced our existing Code of Conduct to strengthen our governance processes and have been communicating this across the business.

#### Board Changes

Gareth Davis retired from the Board in May and was succeeded as Chief Executive by Alison Cooper. Under Gareth's leadership Imperial Tobacco has become one of the world's leading international tobacco companies and, on behalf of the Board and all our employees, I would like to thank him for his outstanding contribution to our success and wish him a long and happy retirement.

Charles Knott, Non-Executive Director, left the Board in July and Jean-Dominique Comolli, Deputy Chairman, left the Board in September. I would like to thank both Charles and Jean-Dominique for their valuable contribution and wish them well for the future.

#### In Summary

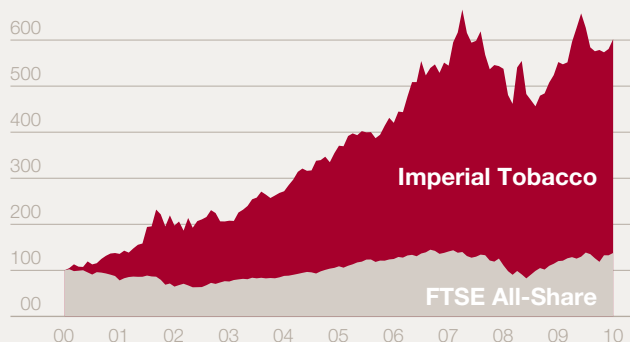
Finally, my thanks to our employees for their collective commitment to delivering high performance. They have embraced our enhanced sales focus and driven strong results, particularly given the challenging environment in some markets this year.

Looking ahead, I believe that we are in a strong position. Central to everything we do is our priority of creating sustainable value for our shareholders. The combination of our people, our brands, our market footprint and our unique total tobacco approach offers us many opportunities to build long-term sustainable growth across our business.



**Iain Napier**  
Chairman

## Total Shareholder Return



KPI

## About this Report

Reflecting our belief that operating in a responsible manner is simply part of how we do business, this year's report incorporates our Corporate Responsibility Review to provide stakeholders with a comprehensive overview of our activities and achievements.

# Strategy

## Chief Executive's Review

**“The essence of our strategy is a continual focus on growing our topline, supported by effective cost optimisation and cash utilisation.”**

**Alison Cooper**  
Chief Executive





## In this section

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10	Key Assets
16	Leveraging our Assets
22	Key Performance Indicators
25	Principal Risks and Uncertainties

I am pleased to be reporting a strong set of results in my first reporting period as Chief Executive, clearly demonstrating the success of our strategy and our sales growth credentials.

My primary objective is to build on our strong track record and to continue to create significant value for our shareholders. The essence of our strategy is a continual focus on growing our topline, supported by effective cost optimisation and cash utilisation.

We have been very successful at realising value creating business opportunities, as demonstrated by our track record of growth and we are continuing to apply this value creation mindset to our sales growth agenda. We have made excellent progress during the year in realigning our operations with our enhanced sales focus and have delivered a strong performance in spite of economic and excise driven challenges in some of our markets, notably in Spain, the USA, Russia and Ukraine.

### Our Market Environment

Around a third of the world's adult population choose to smoke and this number has remained relatively stable for a number of years. Declining consumption in mature markets is offset by growth in emerging markets as the adult population in those markets grows. In total, around 6 trillion cigarettes are consumed annually.

Our market footprint comprises a balance of mature and emerging markets, which ensures we are well positioned to maximise the sales potential of our brands and unique total tobacco portfolio. In 2010, 40 per cent of our cigarette volumes were sold in mature markets and 60 per cent were sold in emerging markets.

The impact of current economic conditions is being felt by both consumers and governments. Tobacco is a significant source of revenue for governments and excise duties have continued to increase, particularly in mature markets. In 2010 we paid over £20 billion to governments in the form of excise duties and other taxes.

Our portfolio spans all price segments and is effectively positioned for growth, aligned to consumers' requirements in both mature and emerging markets. As a result of excise driven price increases in mature markets, consumers have continued to seek value.

Rising excise duties combined with regulation have further increased the illicit trade of tobacco products which remains a significant and growing problem for consumers, governments and the tobacco industry. We have focused on anti-illicit trade activities for a number of years and we are further building our approach internationally to protect

the legitimate market in our products. We were pleased to recently sign an EU-wide co-operation agreement to strengthen our joint efforts with EU Member States.

Through our proactive regulatory engagement we seek to protect our business and to actively support consumers and retailers. We support reasonable and practical regulation, but will continue to challenge disproportionate and unnecessary regulation that undermines the principles of adult choice and the freedom of competition.

We have particular concerns about the significant adverse impact that the plain packaging of tobacco, which is currently being proposed in some markets, would have on illicit trade. Legislation that required all tobacco products to be available in the same easy-to-copy generic plain packaging would lead to a considerable increase in counterfeiting, adversely affecting governments, retailers and consumers, as well as the legitimate tobacco industry.

### Our Growth Strategy

Our strategy continues to focus on sales, cost and cash. The fundamental earnings potential of our business remains strong, with price increases and cost efficiencies complementing organic volume growth.

We use our assets – our brands, our total tobacco portfolio, our broad market footprint and our people – to build sales and have three particular areas of focus when applying our strategy: consumer centricity, execution excellence and future foundations.

You can find out more about how we apply this strategic approach on pages 16 to 21 of this report.

We have strong positions in both mature and emerging markets and have leveraged our brands and total tobacco portfolio to build sales and create value for our shareholders. We have grown shares in a number of markets including in Western, Central and Eastern Europe, in Africa and the Middle East and in Asia Pacific.

We have continued to invest appropriately to support our sustainable sales growth agenda while maintaining our ongoing focus on costs. Our operational performance has been enhanced by effective management of our cash, maintaining our improved working capital levels and further reducing our debt.

### FY10 Performance Highlights

The success of our strategy is reinforced by a number of performance highlights in the last year. Our global strategic cigarette brands *Davidoff*, *West* and *Gauloises Blondes* made gains, benefiting from brand rejuvenations to ensure they remain dynamic and appealing to consumers.

We delivered a strong fine cut tobacco performance, with excellent share gains in Central Europe. We grew our net revenues in the UK, Germany and the Rest of the EU and in Rest of the World region.

Our cash conversion was very strong at 97 per cent and we have reduced our debt by £1.5 billion with closing adjusted net debt of £9.3 billion.

### Brand Equity

*Davidoff* and *West* have been effectively positioned to capitalise on consumer trends, growing volumes by 3 per cent and 2 per cent respectively.

In Eastern Europe, we have grown volumes of *Davidoff* by 20 per cent with particular success in the growing superslims and kingsize superslims segments. We continued to grow *Davidoff's* market share in many markets including in Ukraine, Saudi Arabia and Greece.

We grew volumes of *West* in the value cigarette segment and delivered additional brand innovations with specialised filters and variants adding an extra dimension for consumers, resulting in particularly impressive growth in Turkey and Taiwan.

*Gauloises Blondes* has continued to consolidate its position celebrating its centenary in 2010 with a series of limited edition packs and new variants which were well received by consumers. We have further extended the brand's reach, with a particular focus on Eastern Europe and notable early success in the Balkans.

Complementing our strategic brands is our versatile portfolio of regional and local cigarette brands with consumer insights driving our brand and product portfolio choices at a market level. Our regional value brand *JPS* was a particular highlight and we have grown volumes by 13 per cent and delivered significant market share growth in a number of our major European markets including in the UK and Germany and in Australia. Other notable performances include *Fine* and *Excellence* in Africa and *Maxim* in Eastern Europe.

### Total Tobacco

Our total tobacco portfolio provides consumers with a comprehensive range of tobacco products.

By anticipating local consumer requirements we grew our total fine cut tobacco volumes by 8.7 per cent on a white stick equivalent basis. We made very good progress in Central Europe, with volumes growing strongly by 54 per cent across the region and *Paramount* up by 67 per cent. Another notable success during the year was the launch of *Ducados Rubio* in Spain, the first expanded make your own tobacco product in the market. Launched in June, it has since captured 5.8 per cent of the Spanish fine cut tobacco market. In addition, we had another excellent performance with snus in Scandinavia, with volumes up 24 per cent.

In cigars, despite the challenging environment we grew sales and profits with the continued recovery of our Habanos business.

### Market Footprint

Our products are sold in over 160 markets and our balanced geographic exposure provides opportunities to maximise the potential of our brands.

We drive sales growth across all markets with our global strategic brands complemented by our regional and local brand portfolio. We balance our market share targets with sustainable profit growth in mature markets, while our investment priorities target Eastern Europe, Africa, the Middle East and Asia to further build our position in emerging markets.

We also have an excellent partnership track record, with several new partnership agreements signed in the year, building our market footprint. We announced a licence agreement with KT&G for the manufacture and sale of *Davidoff* in South Korea, a manufacture and licence agreement for *West* and *Davidoff* in Mexico and a cigar collaboration framework agreement in China. In addition, we signed an import and distribution agreement for *Davidoff* in India.

### People

Since my appointment as Chief Executive in May, I have spent time in each of our regions discussing opportunities to further develop and implement our sales growth strategy. The response from our employees has been extremely positive – with our global team fully aligned behind our enhanced sales focus.

### Logistics

In logistics we delivered another positive result. Our tobacco logistics business performed robustly, with price increases and effective cost management key to maintaining our profit levels in both our tobacco logistics and our other logistics businesses.

### Our Responsible Approach

We recognise the controversial nature of tobacco and believe it is essential that tobacco products are manufactured and sold by legitimate, responsible businesses. Our commitment to managing our business responsibly has once again been recognised externally by Business in the Community, with a gold award rating. More details on our corporate responsibility performance are included on pages 41 to 52.

### Outlook: Our Priorities and Challenges

Driving sustainable sales growth is at the heart of our shareholder value agenda. We will continue to build sales across our balanced geographic footprint ensuring our versatile brand and product portfolio remains relevant and appealing to evolving consumer preferences.

Our focus on cost and efficiency continues as well as effectively utilising the cash we generate. We have the assets, the opportunities and most importantly the capabilities and value creating mindset to succeed and I believe we are well placed to continue to create sustainable value for our shareholders in the years ahead.



**Alison Cooper**  
Chief Executive

**We are focused on delivering sustainable sales growth through the smart leverage of our assets.**



## Growth Drivers

The growth drivers of our business are sales, cost optimisation and cash utilisation. At the heart of our strategy is our topline growth agenda complemented by our focus on optimising our costs and utilising our substantial cash flows to create additional value for our shareholders.

## Our Key Assets

Our growth strategy is about maximising value from our four key assets – our brands, our unique total tobacco product portfolio, our extensive market footprint and our people. Turn to pages 10 to 15 for more detail.

## How we Leverage our Assets

Smart leverage of these assets drives sales growth with three particular areas of focus: consumer centricity, execution excellence and future foundations. Turn to pages 16 to 21 for how we apply these in practice and examples of our achievements in 2010.

# Our Key Assets

## Market Footprint



[Link to Strategy](#)

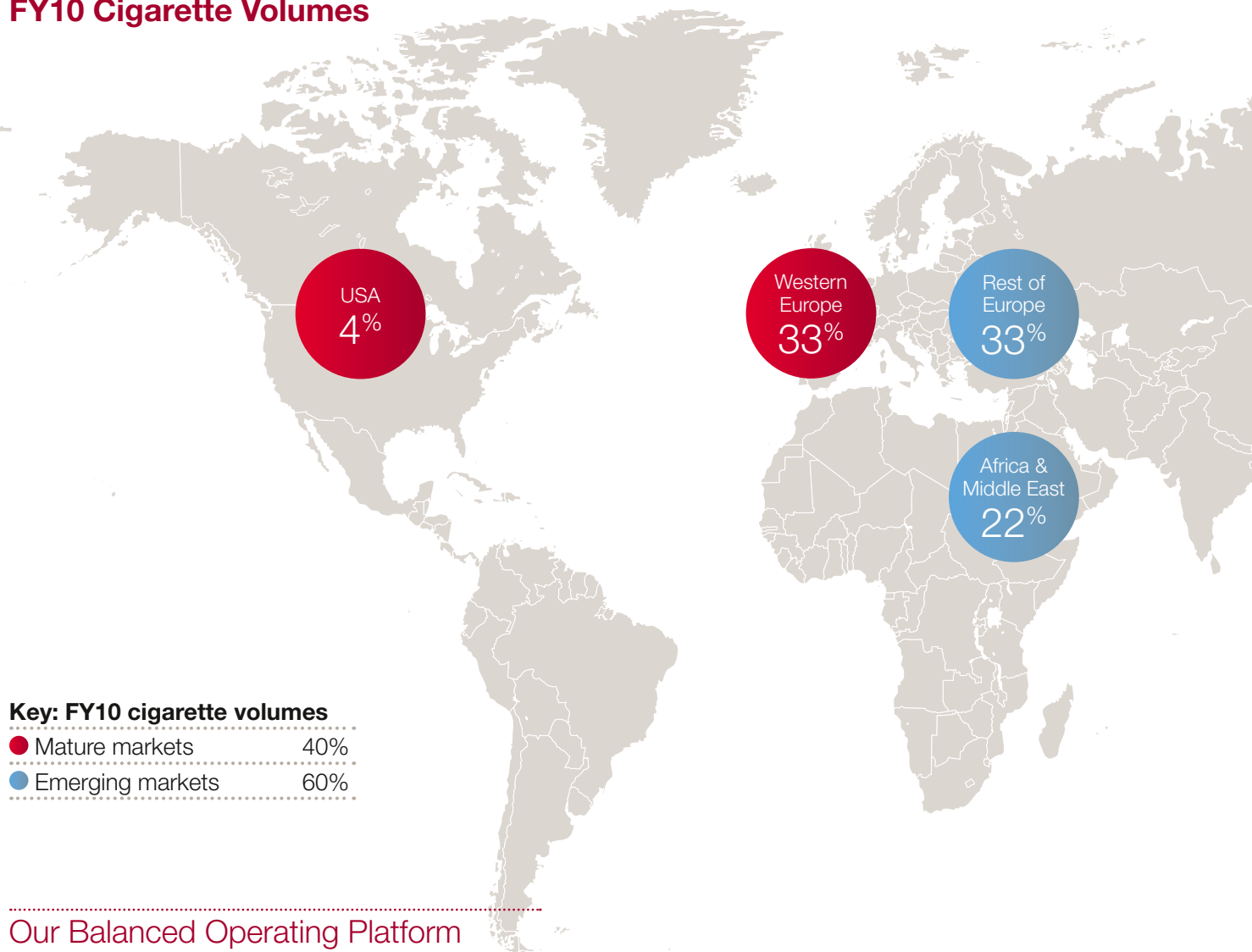
## FY10 Cigarette Volumes

Strategy

Performance

Governance

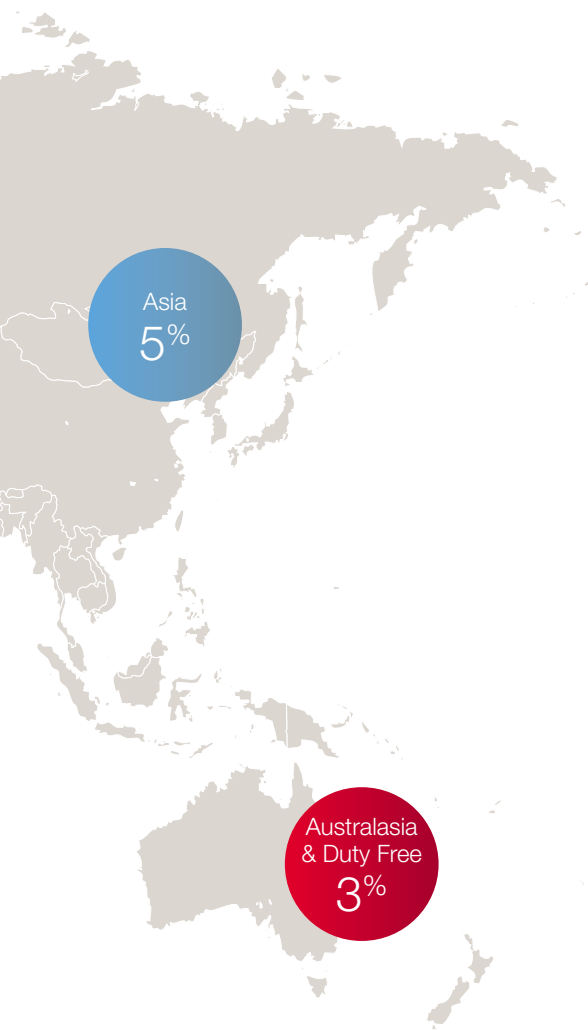
Financials



## Our Balanced Operating Platform

We have a broad market footprint with a balance of mature and emerging markets, creating a strong operating platform from which to maximise the potential of our brands. We drive sales growth across all markets with our global strategic brands complemented by our regional and local brand portfolio. We balance our market share targets with sustainable profit growth in mature markets, while our investment priorities target Eastern Europe, Africa, the Middle East and Asia to further build our position in emerging markets.

## Total Tobacco



## Our Powerful Brand and Product Portfolio

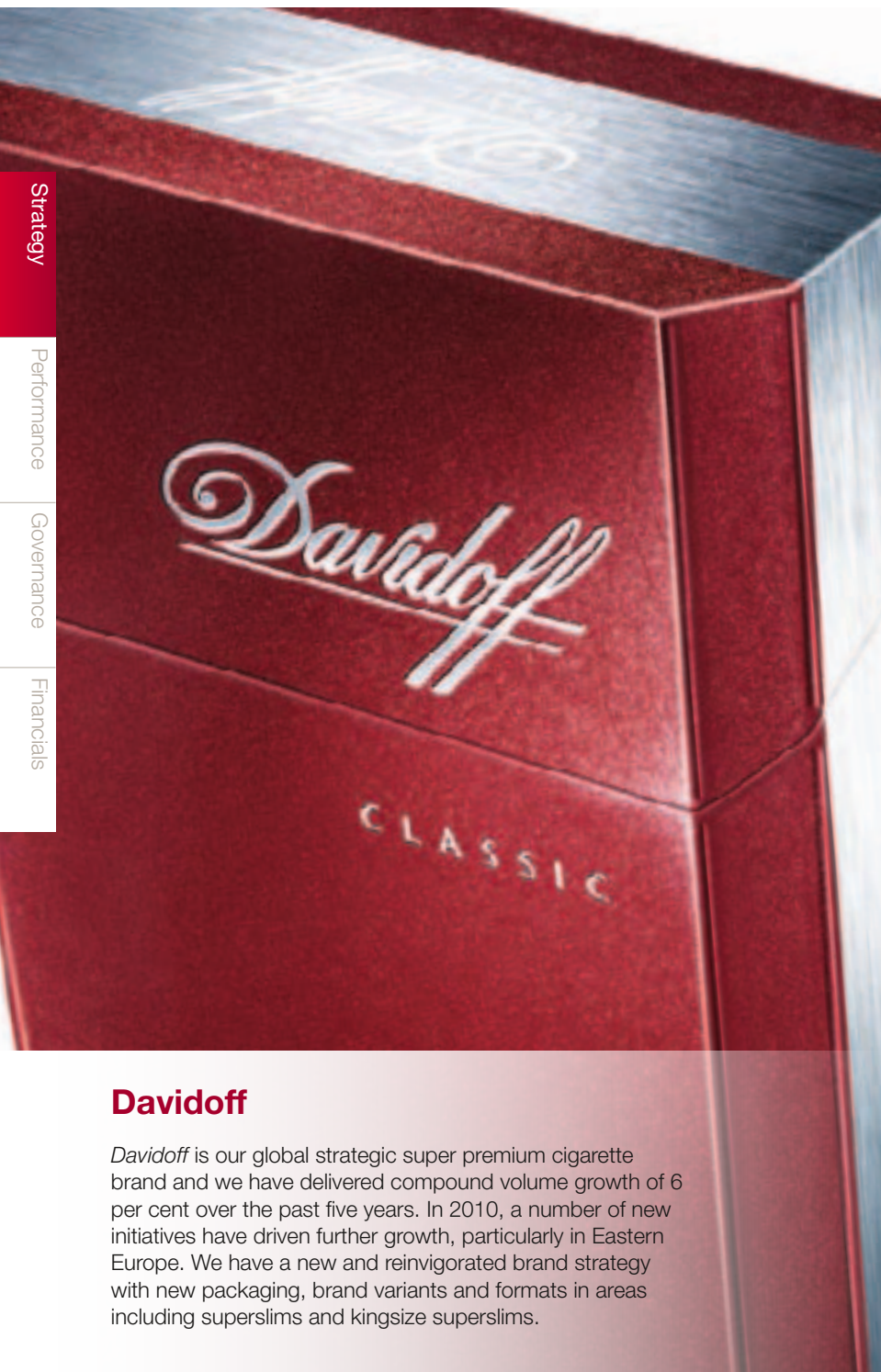
Our comprehensive brand and product portfolio considerably enhances our growth opportunities. We have strong local, regional and international brands and products across all key price segments and product types within individual markets providing us with the flexibility to best meet local consumer and customer needs. Complementing our global strategic cigarette brands *Davidoff*, *Gauloises Blondes* and *West* is our world number one position in fine cut tobacco, cigars, papers and tubes. We continue to leverage the strength of our portfolio through trade marketing excellence and our focus on innovation.



## Brand Equity



[Link to Strategy](#)



### Davidoff

*Davidoff* is our global strategic super premium cigarette brand and we have delivered compound volume growth of 6 per cent over the past five years. In 2010, a number of new initiatives have driven further growth, particularly in Eastern Europe. We have a new and reinvigorated brand strategy with new packaging, brand variants and formats in areas including superslims and kingsize superslims.



### Gauloises Blondes

*Gauloises Blondes* is our biggest selling brand by volume. In 2010 this iconic brand was 100 years old and we celebrated this centenary with a number of new formats and special editions in key markets.



Our global strategic cigarette brands *Davidoff*, *Gauloises Blondes* and *West* have benefited from brand rejuvenations to ensure they remain dynamic and aligned to consumer preferences.



### **West**

Our global strategic value for money brand is *West*. New pack designs and variants have been well received by our consumers with positive results in Taiwan and Turkey and in a number of markets in Central and Eastern Europe. We grew *West* cigarette volumes by 2 per cent during the year.

## Our People



Link to Strategy

### Our People

Our success is as much about our people as it is about our brands, products and markets. We have a culture that is conducive to success, that encourages inventiveness, shares achievements and rewards performance.

We treat our employees with fairness, dignity and respect. We seek to provide a safe working environment which attracts, retains, develops and motivates the best people so that they can meet the challenges of the business and achieve personal success as well as share in the Group's success.

Our priority is to ensure that our people continue to develop and have the right skills to support our sustainable sales growth strategy. As part of this focus we have conducted research into our current skills and capabilities and are benchmarking them against other FMCG companies. The results are helping to shape a number of initiatives. We have a loyal and highly motivated workforce and place a strong emphasis on maintaining high ethical standards in all of our business activities. Supporting our sustainable sales growth strategy is a common framework that guides our employees in their behaviour.

More details are included in our corporate responsibility performance on pages 41 to 52 of this report.



### Our Code of Conduct

Critical to delivering our sustainable sales growth strategy is our collective commitment to further embedding high standards of conduct and behaviour throughout the Group.

A key component of this is our Code of Conduct which has been revised in 2010. The Code sets out the standards of responsible behaviour that all of our employees are expected to follow at all times. The Code brings together a number of our long standing practices and policies that have helped us build and maintain the Group's reputation as a trusted business partner and employer.

The countries in which we operate have different languages, cultures, practices and ethical values. However, in a multi-national company, common standards of behaviour must be adhered to by all employees. The Code is available to employees in a number of languages. Employee workshops on the Code are underway, supported by an e-learning programme that will continue to be rolled out in 2011. Our Code of Conduct can be viewed on our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com).



Our global team is fully aligned behind  
our enhanced sales focus.



## Consumer Centric



Link to Strategy

## Understanding what drives our consumers

Satisfying consumers and aligning our portfolio to their evolving preferences is fundamental to our sales growth strategy.

We work hard to understand how our consumers are impacted by the regulatory and economic environment, and how this affects their smoking enjoyment.

Consumer behaviours and their brand and product preferences vary from market to market, which means local consumer insights are key to driving sales. We therefore make sure that our local management teams have the flexibility to align their portfolio to specific local market and consumer dynamics, within our Group strategic framework.

Our product quality management systems ensure we are fully focused on meeting the requirements of our consumers. We also invest in research and development to bring consumers innovative improvements in products and packaging.

By further embedding our consumer mindset we are better able to anticipate consumer trends at a local level across all price segments ensuring that our comprehensive brand and product portfolio remains relevant and continually meets the demands of our consumers.

We have a versatile portfolio and our products are available across the pricing spectrum, which considerably enhances our growth potential.

We are well known for our strength in value for money brands and products and this is increasingly relevant in the current economic climate. Consumers are searching for value and we have responded by developing a portfolio with significant strength in value offerings. However, our total tobacco focus has created a versatile portfolio, which also includes a broad range of premium and mainstream brands and products.



# Satisfying consumers and aligning our portfolio to their evolving preferences is fundamental to our sales growth strategy

## JPS/Australia

As in many mature markets, smokers in Australia are increasingly seeking quality products at a competitive price, and we have aligned our portfolio accordingly.

Replicating similar success in other markets, most notably in Germany, JPS has rapidly become a key component of our portfolio in Australia.

Since 2009, the JPS brand has established a 1.7 per cent share of the Australian cigarette market.

We are the only tobacco company in Australia to have grown our cigarette volumes during the last 12 months and the performance of JPS has supported our overall market share growth.

## Make Your Own (MYO)/ Central Europe

Leveraging our comprehensive brand and product portfolio continues to provide growth opportunities in our Rest of EU region.

By anticipating consumers' preferences our volumes and market share in fine cut tobacco products have significantly increased in a number of markets, particularly those in Central Europe with volumes of MYO up by 44 per cent.

A full range of Route 66 MYO products has been launched in Poland and the Czech Republic to complement our existing Paramount brand.

In September 2010 we became the first manufacturer in Finland to launch a range of MYO products by extending our cigarette brand Bonus to this sector.

## Davidoff/Eastern Europe

The Davidoff brand family has been extended in Eastern Europe in line with evolving consumer demands in the region.

Davidoff Black & White has been made available in a kingsize superslim format in Russia, Ukraine, Azerbaijan and Armenia.

The kingsize superslim category is the fastest growing segment in many markets in the region and this new variant builds on the rejuvenation of Davidoff.

## Snus Success

Our total tobacco portfolio was further broadened in 2005 through the acquisition of the Skruf snus business in Sweden.

Volumes of our snus brands Skruf and Knox continue to grow year on year, increasing by 24 per cent in 2010.

The two brands now account for more than five per cent of the combined snus market in Sweden and Norway and five years on from the acquisition we have developed significant expertise in the smokeless sector.

Our plans for a new snus factory will provide us with the additional capacity required to match increasing demand for our snus products in Scandinavia. The factory is due to be completed in 2011.



1. By anticipating consumer preferences for fine cut tobacco in Central Europe we have grown Paramount volumes by 67 per cent.

2. We have grown Davidoff by 20 per cent in Eastern Europe with particular success in the growing superslims and kingsize superslims segments.





We align our portfolio to evolving consumer preferences.

See examples overleaf of our consumer centricity in practice

Execution Excellence



Link to Strategy

A fast and flexible business focused on delivery

We are a fast and flexible business with a strong reputation for delivering results through execution excellence.

Internally, our focus is on systems and processes that continually drive operational performance, ensuring that the entire organisation is aligned with our sales growth strategy.

This is particularly important within our supply chain operations ensuring that product and information flows are integrated and that working capital is optimised.

Strong communication and processes between these teams is critical to ensure that we respond rapidly to consumer and customer requirements.

Externally, our execution excellence focus is on trade customers and industry partners.

Through our trade marketing activities we build strong and lasting relationships with retailers, working closely with them to maximise sales and supporting them in managing the impact of regulation.

Our trusted partnering credentials are highly respected in the tobacco industry. We have a strong track record of developing many successful strategic alliances and joint ventures over the years with our industry peers and with other parties around the world.

Our ability to build these relationships whilst competing effectively, gives us a unique position as the partner of choice within the tobacco industry.

Strategy

Performance

Governance

Financials





# We are a responsive business with strong and trusted customer and industry partnerships which enhances our growth potential

## South Korea

In January 2010 we entered into a licence agreement with the South Korean tobacco manufacturer KT&G.

Under the terms of the agreement, KT&G manufactures and sells our global strategic cigarette brand *Davidoff* on our behalf in South Korea.

Leveraging KT&G's experience and expertise in its home market, the partnership has led to the successful launch of *Davidoff* in convenience stores across the country, the outlet for international brands. By September, we had captured 0.4 per cent of this retail channel.

South Korea is an important global market, with a total size of around 90 billion cigarettes per annum.

## Morocco

We have a good working relationship with Phillip Morris International (PMI) and last year signed an agreement for the manufacture, distribution and merchandising of their brands in Morocco.

The agreement complements our long-standing and successful distribution agreements with PMI in the UK and Ireland.

Our subsidiary Altadis Maroc has unrivalled tobacco distribution expertise in the country and our Ain Harrouda factory is one of our leading manufacturing facilities. The PMI agreement also reflects our continuous focus on efficiency and quality improvements.

## Australia

Retailer awards received in Australia recognise our committed approach to providing first class support to our customers.

We were named as Tobacco Supplier of the Year 2009 by Spar Australia, an award judged on a range of criteria including sales value increase, levels of service and category management expertise.

The successful launch of *JPS* in Australia also earned recognition at the 7 Eleven Supplier Awards. The Best Speed to Market award reflected the excellent market share gains made by *JPS* in its first three months in the market.

Since its launch across the 7 Eleven network *JPS* has developed a share of more than 32 per cent of its growing segment and 2.8 per cent overall market share.

## Netherlands

Our business in the Netherlands has been named as a 'Golden Partner for Constructive Approach' in awards conducted by a Dutch retail trade magazine.

The award was judged on feedback received from leading retail clients for the Company's approach to category management in stores across the Netherlands. Imperial was praised for its constructive approach in providing retailers with quality advice on all products, across all tobacco categories, not just our own brands.

The award demonstrates our commitment to working closely with our customers and ultimately our consumers by sharing our knowledge of the tobacco category and providing genuine consumer choice by making the right products available at the right time and in the right place.

1. We have received a number of retailer awards in Australia including a best speed to market award for our *JPS* brand launch.

2. Left to Right – Lee Kwang-youl, Senior Managing Director, KT&G and Andrew Lochrie, Regional Director, Asia Pacific sign an agreement for the manufacture and sale of *Davidoff* in South Korea.

1



2





We build strong and lasting partnerships with retailers and industry partners.

See examples overleaf of our execution excellence in practice



Future Foundations



Link to Strategy

Building a sustainable future

Building future foundations that underpin our sales strategy and enhance our long-term sustainability is fundamental to the way we manage our business.

We drive responsible behaviour throughout the organisation. Our corporate governance and internal control procedures reinforce the high standards that our stakeholders rightly expect of us.

Our ongoing commitment to these high standards is encapsulated in our revised Code of Conduct. The code clearly sets out the standards of responsible behaviours we expect from all our employees and is currently being rolled out across the business.

Our proactive approach to regulatory engagement and tackling the illicit trade in tobacco are critical to our future success.

The counterfeiting and smuggling of tobacco products is a worldwide problem that adversely affects governments, retailers, consumers and the legitimate tobacco industry.

Enhancing our capabilities to combat illicit trade is an ongoing priority and this year we were pleased to sign a co-operation agreement with the European Commission and the Member States of the European Union to strengthen our joint anti-illicit trade initiatives.

The agreement strengthens our ability to engage with governments and regulators on a range of issues, and we will continue to support sensible, evidence based regulation.

However, we will also continue to vigorously oppose regulation that is flawed, unreasonable or disproportionate in order to protect our business and defend the rights of our customers and our consumers.

Strategy

Performance

Governance

Financials



# Operating responsibly, combined with our proactive approach to tackling illicit trade and regulatory engagement, is critical to our long-term success

## EU co-operation agreement

In September we signed an anti-illicit trade co-operation agreement with the European Commission and the Member States of the European Union. We initiated this agreement to strengthen our joint efforts to combat the illegal trade in tobacco.

Under the agreement we will work together with the European Commission and the law enforcement authorities of the Member States to tackle the smuggling and counterfeiting of tobacco products. The agreement will strengthen co-operation in a number of areas and includes payments by us of £191 million (US\$300 million) over 20 years to fund anti-illicit trade initiatives.

The agreement underlines our commitment to partner with authorities worldwide in the fight against tobacco smuggling and counterfeiting.

We encourage governments and regulators to take into account the issues surrounding illicit trade when regulating tobacco. We are particularly concerned about proposals under discussion by the authorities in some markets which would require all tobacco products to be made available in the same plain packaging. This would lead to a considerable increase in counterfeit tobacco which would significantly undermine our joint anti-illicit trade activities.

We apply stringent controls to our global network of distributors and have a dedicated team of specialists who operate internationally in conjunction with governments and customs and excise authorities on a global scale to disrupt the manufacture and supply of illicit tobacco products.

1



## Anti-illicit training in Poland

During 2010, a training course was held in Kraków by Imperial Tobacco to help customs officers tackle cigarette smuggling in Poland.

The course was conducted by experts from Imperial Tobacco Poland and was attended by around 50 customs officers.

Attendees were shown the scale and sources of tobacco products smuggled into the country and the methods of identifying legal and illicit products.

We actively support customs authorities in the fight against criminal practices in the tobacco market.

The course in Kraków was the latest in a series of initiatives we have developed with customs authorities in a number of markets.

## Supporting tobacco farmers in Malawi

Imperial Tobacco is helping to protect endangered woodland in southeast Africa.

Up to 14 per cent of Malawi's forests have been lost due to tree felling for fuel, charcoal production and subsistence as well as commercial agriculture.

We support a project to increase tree and bamboo cultivation through the Eliminating Child Labour in Tobacco (ECLT) Foundation.

We contribute to the scheme as a board member of the ECLT and have provided additional funds to its partners Total Land Care to further develop the project.

2



1. In September, we signed an anti-illicit trade co-operation agreement with the European Commission and the Member States of the European Union.

2. We continue to support tobacco farmers in Malawi.



**“We take a proactive approach to regulatory engagement and tackling the illicit trade in tobacco products.”**

**Matthew Phillips**, Group Corporate and Legal Affairs Director

See examples overleaf of future foundations in practice



# Measuring Our Performance

## Growth Drivers and Key Performance Indicators



### Our Strategy

We create value for our shareholders by delivering sustainable organic sales growth, complemented by our focus on cost optimisation and effective cash utilisation.

We measure the success of our strategy with our KPIs of total shareholder return and adjusted earnings per share.

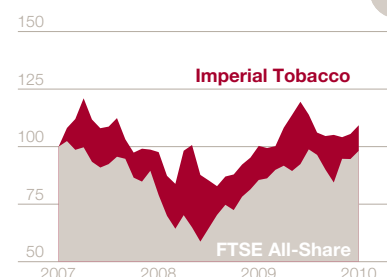
Strategy

Performance

Governance

Financials

#### Total Shareholder Return



KPI

#### Performance

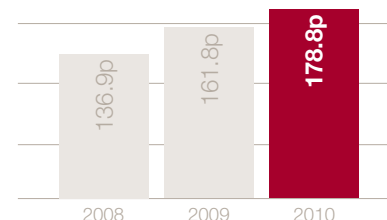
In 2010, we underperformed the FTSE All-Share Index by 3 per cent. However over three years we have outperformed by 11 per cent.

With dividends reinvested £100 invested in Imperial Tobacco 10 years ago would now be worth £603 compared to just £138 invested in the FTSE All-Share 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.

#### Adjusted Earnings per Share



KPI

#### Performance

Our organic sales growth performance complemented by our focus on cost optimisation and effective cash utilisation has enabled us to deliver 11 per cent growth in adjusted earnings per share.

#### Definition

Adjusted earnings per share is 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.

Our growth drivers of sales growth, cost optimisation and cash management are directly underpinned by a set of key performance indicators. These are the principal measures used by the Board to assess performance and continuous improvement in line with our strategy. Certain of these are linked to executive remuneration.

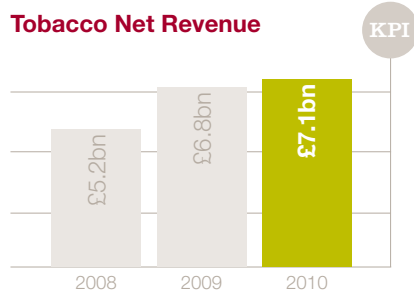
In addition to the key performance indicators, the Board reviews Corporate Responsibility performance measures to continuously improve our responsible performance. These are detailed on page 53.



We drive sales growth across our balanced operating platforms through our focus on consumer centricity, execution excellence, combined with a strong emphasis on building solid future foundations for the business.

We measure this element of our strategy through our KPIs of tobacco net revenue, cigarette volumes and white stick equivalent volumes.

#### Tobacco Net Revenue



#### Performance

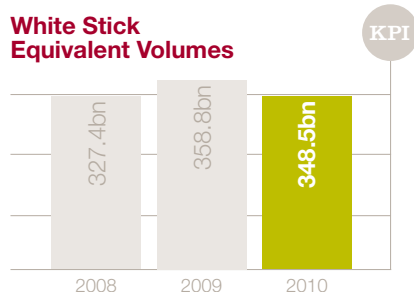
Our tobacco net revenue was up by 3 per cent to £7.1 billion (2009: £6.8 billion) with strong net revenue growth in the UK, Germany, Rest of Western Europe and Rest of the World regions.

Volume growth is one of the drivers of revenue growth although price and sales mix are equally important.

#### Definition

Tobacco net revenue comprises tobacco revenue less duty and similar items.

#### White Stick Equivalent Volumes



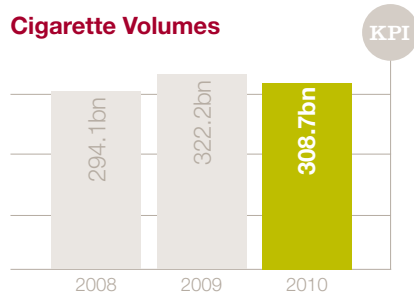
#### Performance

Overall our white stick equivalent volumes were down 2.9 per cent with strong growth across our fine cut tobacco portfolio of 8.7 per cent.

#### Definition

White stick equivalent volumes reflect our combined cigarette and fine cut tobacco volumes.

#### Cigarette Volumes



#### Performance

Our cigarette volumes were down 4.2 per cent to 308.7 billion cigarettes (2009: 322.2 billion), as a result of market declines in Spain, USA, Russia and Ukraine being partly offset by gains in Central Europe and Asia Pacific.

#### Definition

Cigarette volumes are the number of units sold in the period.

## Cost Optimisation

Cost optimisation means we seek maximum returns from our investments, focusing on efficiency improvements and increasing investment where we believe it adds value.

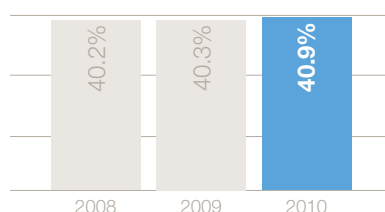
Our current priority is to continue to achieve our post-Altadis integration synergy targets whilst driving business simplification initiatives and productivity improvements across the enlarged Group.

The review of our global manufacturing portfolio is ongoing. We will maintain a particular focus on addressing surplus capacity whilst ensuring that we remain agile and responsive to changing consumer demands.

We measure this element of our strategy through our KPI of tobacco adjusted operating margin, see below.

### Tobacco Adjusted Operating Margin

KPI



### Performance

Optimising our cost base balanced with targeted investments has enabled us to achieve a tobacco adjusted operating margin of 40.9 per cent (2009: 40.3 per cent). Our operating margins were impacted by the change in business mix following the Altadis acquisition in early 2008, however since then we have continued to improve operating margins across all our reporting regions.

### Definition

Tobacco adjusted operating margin is the tobacco adjusted operating profit divided by tobacco net revenue.

## Cash Utilisation

Our business is highly cash generative, due to effective working capital controls, disciplined capital expenditure and management of tax and interest costs to ensure cash flows are optimised.

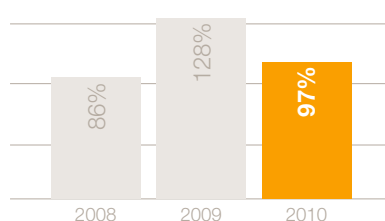
Our short term focus remains on debt reduction following the acquisition of Altadis. We also continue to make disciplined investments across the business to add value and deliver sustainable growth.

While debt reduction is our priority, we nevertheless have very strong cash flows which provide us with the headroom for further value creating deals within a reasonable timeframe. Strategic alliances will offer further growth opportunities.

We measure this element of our strategy through our KPI of our cash conversion rate, see below.

### Cash Conversion Rate

KPI



### Performance

Strong cash generation remains a key priority for the Group. Our cash conversion was strong at 97 per cent, towards the top end of our target of between 90 and 100 per cent.

### Definition

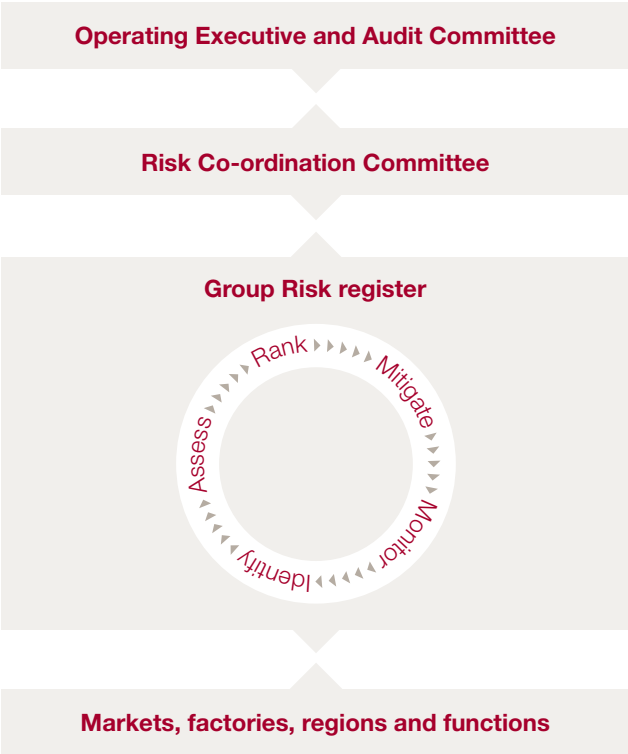
Cash conversion is calculated as cash flow from operations, interest and tax payments less net capital expenditure relating to property, plant and equipment and software as a percentage of adjusted operating profit.



# Principal Risks and Uncertainties

A detailed assessment of strategic risks within our operating environment is undertaken by management and is embedded across the Group.

## How we manage risk



### Risk Management Overview

The Risk Co-ordination Committee (RCC) assists the Operating Executive and the Audit Committee in overseeing the management of material risks. The RCC is responsible for establishing a consistent methodology for the identification, assessment and ranking of material risks to the Group, as well as identifying and assessing existing measures in place to manage and mitigate those risks. The RCC maintains a Group risk register which covers a number of strategic, operational, financial, legal, environmental, community, ethical and reputational risks. These are integrated into our decision-making and risk assessment processes.

We are subject to the same general risks and uncertainties as any other business; for example, changes in general economic conditions, including currency and interest rate fluctuations, changes in taxation legislation, the cost of our raw materials and the impact of competition, political stability in the countries in which we operate and source our raw materials and the impact of natural disasters.

We outline below the principal risks and uncertainties that are specific to and may impact on our business.

Not all these factors are within the Group's control. There may be other risks and uncertainties which are unknown to the Group, or which may not be material now, but could be material in the future.

### Risk Identification and Evaluation

Each area of the business is required to formally review its principal areas of risk and uncertainty so that major risks are reviewed at all levels across the Group. This requires individual markets, factories, regions and functions across the Group to produce annual risk assessment summaries which are compared to the Group risk register. These ongoing risk assessment summaries identify major areas of risk, including specific local risks and how they are mitigated and managed by controls embedded in business processes. This bottom up approach complements the top down approach of the RCC.

## Regulation

### Overview

The tobacco industry is subject to substantial and increasingly restrictive regulatory practices worldwide. In many of the countries in which we operate, there are regulatory restrictions affecting a wide range of matters, including where tobacco products can be smoked and their development, content, manufacture, packaging and labelling, testing, data reporting, sale, distribution, display, marketing and advertising.

Imperial Tobacco, along with all other tobacco companies, is often excluded from engaging with regulators on the development of regulatory proposals. Any future changes to regulation of the tobacco industry could have an adverse effect on the demand for our products or increase the costs related to compliance and contribute to an increase in illicit trade.

### Mitigation

We employ a number of senior and experienced Corporate Affairs specialists to manage regulatory risk and engage with regulators. We monitor proposals for new measures globally and analyse them to identify their potential impact on the Group and its products. External experts are consulted where necessary to provide advice and guidance regarding any impact. Active membership of industry bodies facilitates consistent engagement on key issues. We develop Company positions and toolkits and provide training and guidance for our markets to comply with regulation. We challenge regulation which is not based on sound legal foundation.

## Excise Duty and Illicit Trade

### Overview

Tobacco products are subject to excise duty which, in many of the markets in which we operate, represents a substantial percentage of the retail price. Substantial increases in excise duty and any unfavourable change in the tax treatment of fine cut tobacco, if widely adopted, may have an adverse effect on the demand for our products. Increasing levels of excise duty are also likely to encourage consumers in affected markets to switch from higher-priced cigarettes to lower-priced cigarettes and fine cut tobacco.

Excise duty increases also encourage both legal and illegal cross-border trade from countries with lower levels of duty. Illegal cross-border trade can take the form of genuine product smuggled illegally, cheap whites (whereby a small manufacturer produces product paying minimal tax, for the purposes of smuggling) and the production of counterfeit tobacco products. Illicit trade may lead to erosion of our brand integrity, loss of potential earnings, and potentially impact on our reputation.

There is also a risk that illegal trading in our products may result in the Group and/or our employees being subject to investigation or other proceedings by customs or other authorities which could ultimately result in penalties and fines being imposed against the Group. Although we have

implemented procedures to detect and control illegal trading of our products, such procedures can provide only reasonable and not absolute assurance of detecting non-compliance by managing rather than eliminating risk.

### Mitigation

As part of our business planning process we conduct regular reviews of our product portfolio to ensure it is aligned to consumer preferences in the context of the excise duty structure in each market.

We are committed to working with government authorities and international organisations around the world and we continue to invest considerable resources in working to counter the illicit trade in tobacco products.

In September we signed a co-operation agreement with the European Commission and the Member States of the European Union to jointly combat illicit trade in tobacco. Under the agreement we will work together with the Commission and law enforcement authorities across the EU to tackle the smuggling and counterfeiting of tobacco products.

We apply stringent controls to our customers as set out in our Group policies and standards, Code of Conduct and product supply compliance processes and procedures.

Our dedicated brand protection and security specialists operate internationally in conjunction with governments and customs and excise authorities to disrupt with a view to prevent the supply and sales of illicit product. These controls are supported by sophisticated information collection and analysis practices and complemented by developing tracking and tracing, know your customer procedures, product authentication and volume verification solutions.

## Key Market Dependency

### Overview

Any material decline in the performance of our key markets may impact on our future profit development. The continued growth of the business is underpinned by our key markets including the UK, Germany and Spain. Negative development in any of our key markets could have a material adverse impact on the Group's revenue or profits.

### Mitigation

Our international footprint and brand and product portfolio provides an increasingly balanced exposure to mature and emerging markets, while our portfolio includes international strength in cigarettes and world leadership in fine cut tobacco, cigars, rolling papers and tubes. This provides us with enhanced growth opportunities, continuing to reduce the percentage contribution of an individual market to the Group's adjusted operating profit.

## Competition Law

### Overview

We take competition law and all regulatory compliance very seriously. We have significant market positions in certain countries. As a result, we may be subject to enhanced regulatory scrutiny in these countries, which could result in investigations and adverse regulatory action by relevant competition authorities, including the potential for monetary fines and negative publicity. In April, the Office of Fair Trading imposed a fine on Imperial Tobacco, and a number of retailers for allegedly restricting competition. We strongly rejected this and have appealed the decision to the Competition Appeal Tribunal. As part of our appeal, we are asking for the fine to be quashed in its entirety.

### Mitigation

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 employ experienced internal and external lawyers specialising in competition laws to provide advice and guidance regarding interpretation and compliance with competition laws. In addition we provide training and guidance to relevant employees detailing the obligations and requirements of competition laws.

## Tobacco-Related Litigation

### Overview

Tobacco-related 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 claims to recover the alleged costs of providing medical care to individuals with diseases associated with smoking. To date, no tobacco litigation claim brought against the Group has been successful and/or resulted in the recovery of damages. However, if any claim were to be successful, it may result in a significant liability for damages, and may lead to further claims against us. Regardless of the outcome of pending litigation, the costs of defending such claims can be substantial and may not be fully recoverable. Further details of market specific litigation claims against Group companies are outlined on page 76.

### Mitigation

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.

## Financing

### Overview

The Group has significant borrowings which may impair operational and financial flexibility and performance. This could potentially cause us to dedicate a substantial portion of cash flow from operations to service this indebtedness depending on the level of borrowings, prevailing interest rates, our hedging strategy and exchange rate fluctuations. This would then reduce the funds available to the Group for operations, working capital, capital expenditure, acquisitions, dividends and for other purposes. It could also limit the Group's ability to borrow additional funds and reduce flexibility in planning for, or reacting to, competitive and industry pressures.

This could leave the Group at a competitive disadvantage and increase our vulnerability to both general market and industry pressures. This may impact our credit ratings, which may result in higher financing costs and more difficulty obtaining financing in the future especially if market conditions are weak.

### Mitigation

The Group has established a centralised treasury function, which is responsible for the management of the financial risks of the Group, together with its financing and liquidity requirements. The Group Treasury Committee oversees the operation of Group Treasury in accordance with terms of reference set out by the Board. The Board reviews all major treasury decisions and receives regular reports from the Group Treasurer.

The Group regularly forecasts its cash flows and financing requirements, and monitors developments in the capital markets, in order to ensure that it is well placed to meet the financing needs of the business.

Further details of the Group's treasury operations and the approach to managing its financing risks can be found in Note 16 to the Financial Statements on pages 123.

# Performance

## In this section

28	Financial Review
32	Operating Review
41	Corporate Responsibility

## Financial Review

### Revenue

£ million	2010	2009
Tobacco	<b>20,210</b>	18,587
Logistics	<b>8,980</b>	8,961
Eliminations	<b>(1,017)</b>	(1,031)
Group revenue	<b>28,173</b>	26,517

### Revenue

We have grown our reported revenue as our results benefited from strategic cigarette brand gains, excellent fine cut tobacco volumes and strong pricing.

### Group Earnings Performance

We grew adjusted operating profit by 5 per cent to £3,067 million (2009: £2,933 million) reflecting our focus on sales growth and cost optimisation. Leaf cost pressures remain which we continue to actively manage. Reported operating profit was up 8 per cent to £2,528 million (2009: £2,337 million). Adjusted net finance costs were 14 per cent lower than in 2009, reflecting our continued focus on working capital, debt reduction and active management of our financing. After net finance costs and tax, adjusted earnings per share grew by 11 per cent to 178.8 pence (2009: 161.8 pence). Reported earnings per share were 148.5 pence (2009: 65.5 pence), additionally reflecting fair value gains on derivative financial instruments, amortisation of acquired intangibles and other adjusting items in line with our usual practice.

### Group Earnings Performance

£ million	Adjusted		Reported	
	2010	2009	2010	2009
Operating profit				
Tobacco	<b>2,889</b>	2,750	<b>2,490</b>	2,291
Logistics	<b>176</b>	177	<b>36</b>	40
Eliminations	<b>2</b>	6	<b>2</b>	6
Group operating profit	<b>3,067</b>	2,933	<b>2,528</b>	2,337
Net finance costs	<b>(600)</b>	(700)	<b>(410)</b>	(1,392)
Profit before taxation	<b>2,467</b>	2,233	<b>2,118</b>	945
Taxation	<b>(637)</b>	(581)	<b>(596)</b>	(268)
Profit for the year	<b>1,830</b>	1,652	<b>1,522</b>	677
Earnings per ordinary share (pence)	<b>178.8</b>	161.8	<b>148.5</b>	65.5



**“Our results benefited from strategic cigarette brand gains, excellent fine cut tobacco volumes and strong pricing.”**

**Robert Dyrbus**  
Finance Director

## Reconciliation of Adjusted Performance Measures

Results have been adjusted in line with our normal practice and a reconciliation is provided below.

	Operating profit (£ million)		Net finance costs (£ million)		Earnings per share (pence)	
	2010	2009	2010	2009	2010	2009
Reported	<b>2,528</b>	2,337	<b>(410)</b>	(1,392)	<b>148.5</b>	65.5
Acquisition accounting adjustments	<b>24</b>	–	<b>–</b>	–	<b>2.0</b>	–
Amortisation of acquired intangibles	<b>451</b>	451	<b>–</b>	–	<b>37.1</b>	37.4
Fair value adjustments on derivative financial instruments providing commercial hedges	<b>–</b>	–	<b>(210)</b>	660	<b>(14.9)</b>	46.9
Restructuring costs	<b>64</b>	145	<b>–</b>	–	<b>4.8</b>	9.9
Post-employment benefits net financing cost	<b>–</b>	–	<b>20</b>	32	<b>1.3</b>	2.1
Adjusted	<b>3,067</b>	2,933	<b>(600)</b>	(700)	<b>178.8</b>	161.8

The acquisition accounting adjustments of £24 million eliminates one-off costs incurred as a consequence of investigations into alleged foreign trading violations in the period prior to our acquisition of Reemtsma.

Amortisation of acquired intangibles was unchanged at £451 million.

As explained in our accounting policies, our adjusted net finance costs exclude fair value gains and losses on derivative financial instruments providing commercial hedges. Movements in foreign exchange and interest rates have been less volatile in the current year and fair value gains on derivative financial instruments included in net finance costs were £210 million (2009: loss of £660 million).

The net financing cost of post-employment benefits amounted to £20 million compared with £32 million in 2009 and is excluded from adjusted net finance costs.

### Geographic Analysis of Tobacco

UK net revenue increased by 2 per cent to £911 million reflecting price increases in cigarette, and a strong performance in our fine cut tobacco business. Adjusted operating profit rose 2 per cent to £614 million.

In Germany due to price increases and growth in fine cut tobacco volumes we delivered a 3 per cent increase in net revenue to £853 million and 7 per cent growth in adjusted operating profit to £432 million.

## Geographic Analysis of Tobacco

	Net revenue		Adjusted operating profit		Cigarette volumes (bn)		Fine cut tobacco volumes (tonnes)	
	2010	2009	2010	2009	2010	2009	2010	2009
£ million								
UK	911	893	614	601	21.1	20.8	2,800	2,650
Germany	853	826	432	403	23.2	23.9	5,900	5,550
Spain	594	610	268	275	25.3	30.3	1,400	2,350
Rest of EU	1,577	1,490	638	566	59.6	59.3	15,000	12,650
Americas	780	861	244	288	11.9	13.8	300	650
Rest of the World	2,340	2,138	693	617	167.6	174.1	2,150	2,100
Total	7,055	6,818	2,889	2,750	308.7	322.2	27,550	25,950

Net revenue in Spain declined by 3 per cent to £594 million reflecting challenging market conditions and lower cigarette and fine cut tobacco volumes. Adjusted operating profit declined by £7 million to £268 million. Excluding the impact of foreign exchange, profits were stable benefiting from price increases and cost synergies.

In the Rest of EU, we delivered good performances in a number of markets in the region with price increases and excellent growth in our fine cut tobacco volumes increasing net revenue by 6 per cent and adjusted operating profit by 13 per cent.

In the Americas, net revenue decreased by 9 per cent to £780 million, and adjusted operating profit declined by 15 per cent to £244 million reflecting cigarette and cigar market volume declines following substantial increases in federal excise tax last year, and a highly competitive market.

In the Rest of the World, though cigarette volumes were down in Eastern Europe, we performed well in Asia-Pacific, Africa and the Middle East, benefiting from strong pricing and a favourable sales mix. We grew revenue by 9 per cent to £2,340 million and adjusted operating profit by 12 per cent to £693 million.

### Restructuring and Synergies

Tobacco profits benefited from incremental synergies from the Altadis acquisition of €110 million delivered during the year. Our cumulative synergies to date are in line with the schedule outlined at the time of the acquisition at €300 million.

Included within restructuring costs are impairments of surplus properties mainly in Spain and the USA amounting to £45 million, reflecting current property market conditions in these countries.

### Logistics

£ million (unless otherwise stated)	2010	2009
Distribution fees	936	964
Adjusted operating profit	176	177
Adjusted distribution margin	18.8%	18.4%

Against a difficult operating environment, particularly in Spain, our logistics business produced a good result with adjusted operating profit in line with last year at £176 million and an increase in adjusted distribution margin despite the impact of our initial investment in the Spanish lottery joint-venture.

### Net Finance Costs

Adjusted net finance costs were £600 million (2009: £700 million). On an adjusted basis, our interest cover was 5.1 times (2009: 4.2 times). Reported net finance costs of £410 million (2009: £1,392 million) include post-employment benefits net finance expense of £20 million (2009: £32 million) and fair value gains on derivative financial instruments providing commercial hedges of £210 million (2009: losses of £660 million).

### Taxation

The adjusted tax charge for the period was £637 million (2009: £581 million) representing an adjusted effective tax rate of 25.8 per cent (2009: 26.0 per cent). The reported tax charge was £596 million (2009: £268 million).

### Foreign Exchange

Tobacco net revenue benefited by £33 million due to currency effects, mainly as a result of the appreciation of the Australian dollar against sterling. Logistics distribution fees were reduced by £3 million as a result of currency effects. While average US dollar and euro rates were similar to last year, the foreign exchange effect of the time lag between the purchasing and consumption of tobacco was the most significant factor in an overall reduction in Group adjusted operating profit due to currency effects of £44 million.

### Dividends

The total amount of dividends payable in respect of 2010 is £885 million, an increase of 15 per cent on last year, which reflects growth in our adjusted attributable earnings to just over £1.8 billion. We have proposed a final dividend of 60.0 pence per share such that the total dividend for the year is 84.3 pence. Following approval by shareholders this dividend will be paid on 18 February 2011 with an ex dividend date of 19 January 2011.

### Cash Flow and Financing

At the end of September 2010, we had committed financing facilities in place of around £12 billion. Some 30 per cent was bank facilities with the balance raised through capital market bond issues. We remain fully compliant with all our banking covenants and are committed to retaining our investment grade credit ratings.



## Key Performance Indicators (KPIs)<sup>1</sup>

	2010	2009	2008	2007
Total Shareholder Return:				
FTSE All-Share Index	10%	+11%	-22%	+12%
Imperial Tobacco	13%	+5%	-5%	+30%
Adjusted earnings per share	178.8p	161.8p	136.9p	118.8p
Cigarette volumes	308.7bn	322.2bn	294.1bn	200.3bn
Tobacco net revenue	£7.1bn	£6.8bn	£5.2bn	£3.3bn
Tobacco adjusted operating margin	40.9%	40.3%	40.2%	45.0%
Cash conversion rate	97%	128%	86%	81%

<sup>1</sup> A full description of our key performance indicators can be found on pages 22 to 24.

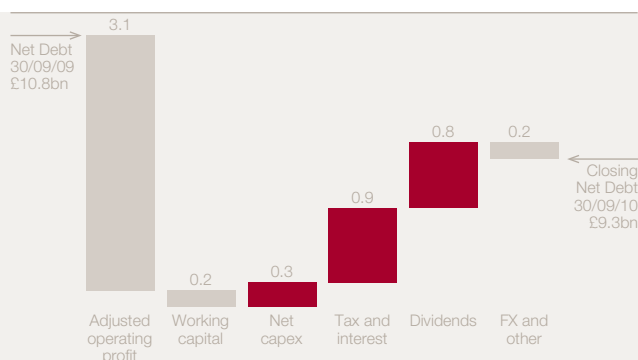
At 30 September 2010, our reported net debt had reduced to £10.0 billion from £12.0 billion at 30 September 2009 reflecting our strong cash generation. Eliminating accrued interest, the fair value of derivatives providing commercial cash flow hedges and finance lease liabilities, our adjusted net debt was £9.3 billion (30 September 2009: £10.8 billion). The denomination of our closing adjusted net debt was 50 per cent euro, 23 per cent US dollar and 27 per cent sterling. Our all-in cost of debt was stable at 5.5 per cent (2009: 5.5 per cent).

Our business remains highly cash generative and we converted 97 per cent of our profit from operating activities after net capital expenditure into cash, towards the top end of our 90 to 100 per cent target range. After a very strong working capital inflow last year we retained our focus on this important aspect of cash management. There was a working capital inflow of £0.2 billion, half of which was due to the timing of sales made in our logistics business which is expected to unwind in the new financial year. Managing our working capital remains a key priority for us as we seek to maximise returns from effective cash utilisation.

### Additions and Fixed Asset Disposals

Our cash outflows include gross capital expenditure of £283 million (2009: £253 million), reflecting our increased investment in machinery and equipment across our expanded footprint. Proceeds from disposal of fixed assets amounted to £26 million (2009: £69 million).

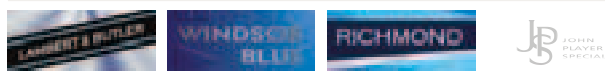
## Adjusted Net Debt Reduced by £1.5 billion



Average level of net debt £10.9bn  
(FY09: £12.8bn)

Adjusted debt figures exclude accrued interest and fair value gains and losses on derivatives providing commercial cash flow hedges and finance lease liabilities.

## United Kingdom



### Cigarette

	2010	2009
Volumes	<b>21.1bn</b>	20.8bn
Market size <sup>1</sup>	<b>44.5bn</b>	45.3bn
Market share <sup>1</sup>	<b>45.4%</b>	45.3%

<sup>1</sup> Imperial Tobacco estimates.



### Fine Cut Tobacco

	2010	2009
Volumes	<b>2,800t</b>	2,650t
Market size <sup>1</sup>	<b>5,050t</b>	4,450t
Market share <sup>1</sup>	<b>54.5%</b>	58.0%

<sup>1</sup> Imperial Tobacco estimates.

### Market Environment and Consumer Trends

We estimate that the duty paid cigarette market returned to its more usual trend of moderate decline and was down by 2 per cent to 44.5 billion cigarettes (2009: 45.3 billion).

UK consumers continue to look for value resulting in further growth in the economy cigarette segment. This segment now accounts for 22 per cent of the UK cigarette market by volume compared to 15 per cent a year ago.

In this context, fine cut tobacco market volumes have also continued to grow, up by 13 per cent, and we estimate a market of 5,050 tonnes (2009: 4,450 tonnes).

In April 2010, the Office of Fair Trading imposed a fine on Imperial Tobacco, Gallaher and a number of retailers for allegedly restricting competition. We strongly rejected this and have appealed the decision to the Competition Appeal Tribunal. As part of our appeal, we are asking for the fine to be quashed in its entirety. We are awaiting for an appeal date to be determined.

### Excise and Regulation

In his March 2010 Budget, the Chancellor raised tobacco duty by above inflation levels, resulting in an average increase of 15 pence per pack.

We oppose all unnecessary and disproportionate regulation of tobacco. Along with other tobacco manufacturers, we have applied for a judicial review of the proposed product display ban in England under the Health Act which will be considered in April 2011.

There is no credible evidence to support the idea that children start smoking or that adult smokers continue to smoke as a result of the display of tobacco products. If this legislation is implemented it is likely that it will further fuel the growth in illicit trade.

Our judicial review of the Government's proposed ban on tobacco product sales in vending machines under the Health Act, was heard in October 2010 and we are currently awaiting a judgment.

### Our Strategy

We are the market leader in the UK. In delivering sustainable sales growth, we are focused on balancing our market share targets with sustainable profit growth.

### Our Performance

Net revenue was £911 million (2009: £893 million), with adjusted operating profit of £614 million (2009: £601 million) reflecting price increases in January and September and our strong performance in fine cut tobacco.

## Performance Highlights: UK

*JPS Silver and Windsor Blue* have grown significantly and now hold 41 per cent of the growing economy segment.

*Lambert & Butler* and *Richmond* remain our two best selling UK brands, with *Lambert & Butler* kingsize the number one brand variant in the UK. Our cigarette market share was 45.4 per cent (2009: 45.3 per cent).

Our expertise in consumer value offerings has enabled us to further enhance market shares of *JPS Silver* and *Windsor Blue* which were up to 4.5 per cent and 4.4 per cent respectively (2009: 1.9 per cent and 2.6 per cent). Combined, these two brands now hold around 41 per cent of the growing economy segment.

In fine cut tobacco, our volumes grew due to our value brands *Golden Virginia Yellow* and *Gold Leaf* although not enough to offset the performance of our premium brands, such that our overall fine cut tobacco share decreased to 54.5 per cent (2009: 58.0 per cent).

### Outlook

The UK is a key market for the Group and we continue to focus on improving our leading position. We expect the more normal long-term rate of decline in the duty paid cigarette market to continue with further growth in fine cut tobacco.

We will continue to drive sales growth by ensuring that our brands and products evolve in line with changing consumer dynamics.

## Germany



### Cigarette

	2010	2009
Volumes	<b>23.2bn</b>	23.9bn
Market size <sup>1</sup>	<b>84.1bn</b>	85.8bn
Market share <sup>1</sup>	<b>26.9%</b>	27.3%

<sup>1</sup> Imperial Tobacco estimates.



### Fine Cut Tobacco

	2010	2009
Volumes	<b>5,900t</b>	5,550t
Market size <sup>1</sup>	<b>25,450t</b>	24,500t
Market share <sup>1</sup>	<b>18.2%</b>	17.6% <sup>2</sup>

<sup>1</sup> Imperial Tobacco estimates.

<sup>2</sup> Restated to reflect a changed basis of calculation.

### Market Environment and Consumer Trends

In Germany, we estimate that the duty paid cigarette market was down 2 per cent to 84.1 billion cigarettes (2009: 85.8 billion).

The growing value for money branded cigarette sector now accounts for 31 per cent of the total cigarette market (2009: 27 per cent) as consumers continued to economise and seek value products and brands.

The fine cut tobacco market was up 4 per cent to 25,450 tonnes (2009: 24,500 tonnes).

### Excise and Regulation

We continue to proactively engage with the German Government in the ongoing debate regarding potential tobacco tax increases. In Germany, with the exception of Bavaria, smoking restrictions by state are in place across the hospitality sector that allows some provision for smokers.

### Our Strategy

Our strategy in Germany is to balance market share gains while improving our profits.

We use our unique total tobacco approach to provide consumers with a wide range of fine cut and make your own tobacco products, reinforcing our leading position in this segment.

## Performance Highlights: Germany

A number of initiatives including new variants and soft packs have driven the share of *JPS* to 9.3 per cent.

## Our Performance

With a price increase in June across our value cigarette brands and strong growth in our fine cut tobacco volumes we grew our net revenue to £853 million (2009: £826 million), with adjusted operating profit up 7 per cent to £432 million (2009: £403 million).

A number of initiatives including new variants and soft packs have driven *JPS* market share up to 9.3 per cent (2009: 8.5 per cent).

*West*, positioned in the mid-priced segment in Germany has continued to be impacted by consumers' downtrading, with our overall market share declining to 26.9 per cent (2009: 27.3 per cent). In line with our global brand strategy, new pack designs and variants for *West* have recently been introduced.

From 1 April this year *Gauloises Blondes* was incorporated into our distribution network and we have subsequently extended distribution, with the "100 ans de Liberté" centenary special editions launched in the market.

Our total tobacco approach has enabled us to further consolidate the *JPS* brand franchise in the fine cut tobacco segment, with our overall market share up to 18.2 per cent (2009: 17.6 per cent). *Route 66* make your own tobacco also performed well.

## Outlook

We expect consumers to continue to economise and our strength in value brands and products means we are well placed to benefit from this dynamic. We will continue to leverage our portfolio to capitalise on growth opportunities, with a particular focus on building sales of our key brands *JPS*, *West* and *Gauloises Blondes*.

## Spain



### Cigarette

	2010	2009
Volumes	<b>25.3bn</b>	30.3bn
Market size <sup>1</sup>	<b>73.9bn</b>	83.6bn
Market share <sup>1, 2</sup>	<b>29.0%</b>	30.6%

1 Imperial Tobacco estimates.

2 Market shares reflect the domestic blonde cigarette segment.



### Fine Cut Tobacco

	2010	2009
Volumes	<b>1,400t</b>	2,350t
Market size <sup>1</sup>	<b>4,950t</b>	5,150t
Market share <sup>1</sup>	<b>32.3%</b>	42.6%

1 Imperial Tobacco estimates.

### Market Environment and Consumer Trends

The recession is continuing to have a significant impact in Spain and market conditions remain challenging.

Against this backdrop consumers have reduced their spending in almost every consumer category with the value cigarette segment now accounting for 26 per cent of the overall cigarette market (2009: 23 per cent). There has also been considerable switching into fine cut tobacco and in addition, tourism levels in Spain have declined, impacting travel retail purchases.

We estimate overall cigarette market volumes were down by 12 per cent to 73.9 billion cigarettes (2009: 83.6 billion), with fine cut tobacco volumes down by 4 per cent to 4,950 tonnes (2009: 5,150 tonnes).

## Performance Highlights: Spain

We are market leaders across all tobacco segments in Spain and have increased our share in the growing value segment with soft pack launches and repositioning of variants of *Ducados Rubio*.

Within this the travel retail market has declined by 17 per cent in cigarettes and by 36 per cent in fine cut tobacco. In the domestic market, cigarettes were down by 10 per cent and fine cut tobacco grew by 39 per cent.

The dark tobacco segment, in which we have a leading position, accounts for around 9 per cent of the overall market and has been on a declining trend for a number of years and was down 14 per cent in 2010.

#### Excise and Regulation

On 1 July 2010 the Spanish Government increased VAT to 18 per cent. Further restrictions in public smoking are expected to come into force early in 2011. Given the prevalence of increased smoking restrictions in other mature markets, we are experienced in managing such regulatory change. Although there may be a short-term impact in market volumes, our experiences show that the market returns to its normal trend in the medium term.

#### Our Strategy

Recognising the current economic situation in Spain we are focused on ensuring that our value cigarette and fine cut tobacco portfolio is aligned with consumer preferences. We have made a number of management changes in recent months to improve our sales excellence and strengthen our competitive position.

#### Our Performance

Net revenue was down to £594 million (2009: £610 million), reflecting challenging market conditions and lower cigarette and fine cut tobacco volumes, with adjusted operating profit down to £268 million (2009: £275 million).

We are market leaders across all tobacco segments in Spain and have increased our share in the growing value cigarette segment with soft pack launches and repositioning of variants of *Ducados Rubio*. In addition, we increased our distribution of *JPS*. However, despite the strong performance of our value brands, our domestic blonde market share was 29.0 per cent (2009: 30.6 per cent), as a result of downtrading pressures on *Fortuna*. We are introducing a new variant to the *Fortuna* brand family, *Fortuna Red Line*, to strengthen our portfolio.

In fine cut tobacco, our overall market share declined to 32.3 per cent (2009: 42.6 per cent), impacted by our significant travel retail position and increased competition

from cigarette branded fine cut tobacco products. In June we extended the *Ducados Rubio* brand family with the launch of the first expanded make your own product in Spain, which has since captured 5.8 per cent of the total fine cut tobacco market. The launch of *Golden Virginia Yellow* has supported the overall performance of the *Golden Virginia* brand family.

We repositioned our cigar brand *Coburn* and have increased distribution, growing its share to 11.7 per cent (2009: 0.9 per cent).

#### Outlook

We expect the ongoing economic challenges of the Spanish market to persist. We remain focused on the success of the brand and product initiatives we have undertaken to ensure our total tobacco portfolio is aligned with consumer trends.

### Rest of EU



#### Cigarette

	2010	2009
Volumes	<b>59.6bn</b>	59.3bn
Market size <sup>1</sup>	<b>361.7bn</b>	370.4bn
Market shares <sup>1</sup>		
Austria	<b>17.2%</b>	16.7%
Belgium	<b>16.1%</b>	16.0%
Czech Republic	<b>13.9%</b>	13.3%
France <sup>2</sup>	<b>23.6%</b>	23.9%
Greece	<b>11.6%</b>	11.2% <sup>3</sup>
Ireland	<b>24.5%</b>	25.3%
Italy	<b>2.3%</b>	2.4%
Netherlands	<b>12.7%</b>	12.8% <sup>3</sup>
Poland	<b>25.5%</b>	25.7%

1 Imperial Tobacco estimates.

2 Market shares reflect the domestic blonde cigarette segment.

3 Restated due to a changed basis of calculation.

Our Rest of EU region comprises the EU Member States plus Norway, Iceland, Liechtenstein and Switzerland. It excludes UK, Germany and Spain which are reported separately.

### Performance Highlights: Rest of EU

We have grown our cigarette share in a number of markets in our Rest of EU region including in Austria, the Czech Republic, Greece, Hungary and Portugal.





## Fine Cut Tobacco

	2010	2009
Volumes	<b>15,000t</b>	12,650t
Market size <sup>1</sup>	<b>40,600t</b>	38,800t
Market shares <sup>1</sup>		
Austria	<b>23.8%</b>	21.4%
Belgium	<b>11.4%</b>	11.3%
Czech Republic	<b>50.9%</b>	49.4%
France	<b>22.4%</b>	23.1%
Greece	<b>33.1%</b>	34.8% <sup>2</sup>
Hungary	<b>49.4%</b>	49.1%
Italy	<b>41.4%</b>	43.9%
Netherlands	<b>49.3%</b>	48.7% <sup>2</sup>
Poland	<b>28.6%</b>	3.2%
Portugal	<b>10.6%</b>	9.3%

1 Imperial Tobacco estimates.

2 Restated due to a changed basis of calculation.

## Regional Environment and Consumer Trends

We estimate that regional cigarette volumes were down by 2 per cent to 361.7 billion cigarettes (2009: 370.4 billion). Regional fine cut tobacco volumes were up 5 per cent to 40,600 tonnes (2009: 38,800 tonnes). The main consumer trend across the region has been to seek value brands and products.

In France, a key market for us in this region, the cigarette market was broadly stable at 55 billion cigarettes with the fine cut tobacco market up 3 per cent at 7,700 tonnes (2009: 7,500 tonnes).

## Regulation and Excise

The new tobacco taxation directive was published by the European Commission in March 2010 with the minimum excise tax structure on cigarettes changing from 2014. Fine cut tobacco minimum excise duty will also increase

progressively between 2011 and 2020. In September, the European Commission launched a public consultation on the revision of the EU Tobacco Products Directive 2001. Views are being sought on a number of issues including smokeless tobacco, pictorial health warnings, plain packaging, ingredients reporting and display and vending bans and we are preparing our submission.

## Our Strategy

This region presents us with considerable growth opportunities. Our total tobacco portfolio approach ensures our brands and products continue to evolve in line with consumer requirements.

## Our Performance

We delivered strong growth in a number of markets in our Rest of EU region and excellent growth in our fine cut tobacco portfolio, growing net revenue by 6 per cent to £1,577 million (2009: £1,490 million) and adjusted operating profit by 13 per cent to £638 million (2009: £566 million).

In France, despite growth from *News*, *JPS* and *Fortuna* our domestic blonde cigarette share was down slightly at 23.6 per cent. We are market leaders in the dark cigarette segment which continued its declining trend, impacting our overall share which was 28.2 per cent (2009: 28.8 per cent). We grew our cigarette shares in a number of markets including in Austria, the Czech Republic, Greece, Hungary and Portugal. Brand highlights include a strong performance from *JPS* in Portugal and Austria and *Route 66* in the Czech Republic and Poland.

In fine cut tobacco we grew our volumes by 19 per cent, gaining share in Austria, Czech Republic, Hungary, Ireland, the Netherlands, Poland and Portugal. Our consumer insight and innovation expertise has enabled us to capture the leading share of the roll your own and make your own tobacco segments in Central Europe. The largest market for fine cut tobacco in the region is the Netherlands and we grew *Zilver*, following its repositioning in the value segment, and *Van Nelle*.

In Scandinavia, we have grown volumes of our snus brands *Skruf* and *Knox* by 24 per cent and we will be able to capitalise on our strong performance further with our new snus factory fully operational from February 2011.

## Performance Highlights: Rest of EU

In fine cut tobacco in our Rest of EU region we grew our volumes by 19 per cent.

## Outlook

The strength of our portfolio and our agile approach leaves us well placed to benefit from consumer shifts.

We remain focused on further improving our cigarette positions across the region while building on the momentum of the considerable growth we have achieved with our fine cut tobacco and snus portfolios.

## Americas



### Cigarette

	2010	2009
Americas volumes	<b>11.9bn</b>	13.8bn
USA market size <sup>1</sup>	<b>298.5bn</b>	319.1bn <sup>2</sup>
USA market share <sup>1</sup>	<b>3.9%</b>	4.2%

<sup>1</sup> Imperial Tobacco estimates.

<sup>2</sup> USA market volumes for 2009 have been restated due to a changed basis of calculation.

### Fine Cut Tobacco

	2010	2009
Americas volumes	<b>300t</b>	650t

#### Market Environment and Consumer Trends

Our primary market in the Americas is the USA, where we estimate that the overall cigarette market declined by 7 per cent to 298.5 billion cigarettes (2009: 319.1 billion).

The USA is the second largest cigarette market by volume after China, accounting for a significant percentage of tobacco industry global profits.

The USA market remains competitive, impacted by the federal excise tax increases in April 2009, with significant promotional activity, discounting and brand repositioning by competitors.

In cigars, although the large cigar market has declined consumers have continued to seek value with the trend towards smaller sized cigars and cigarillos.

#### Excise and Regulation

The Food and Drug Administration (FDA) assumed regulatory control of the USA tobacco industry in June 2009 and has subsequently issued a number of regulatory requirements for tobacco including ingredient testing and reporting requirements.

The Tobacco Products Scientific Advisory Committee (TPSAC) of the FDA is currently debating the future of menthol in cigarettes. The committee has until March 2011 to present a report and recommendations to the FDA. The TPSAC will also be considering the testing and disclosure of tobacco product constituents.

The disparity in federal excise tax between pipe and fine cut tobacco has come under congressional scrutiny. Definitions for these categories are under development and tax harmonisation is also being considered.

#### Our Strategy

Given the size of the market and our relatively small position, the USA provides us with a unique long-term opportunity to grow our business. We are developing our sales force and our distribution capabilities, as well as investing in our brands and in a number of promotional activities to build our market share. Our cigar strategy focuses on growing our sales value in line with customer demands and maximising our profitability.

#### Our Performance

As a result of market volume declines following the substantial increases in federal excise tax last year and a highly competitive market, net revenue was down by 9 per cent to £780 million (2009: £861 million), and adjusted operating profit decreased to £244 million (2009: £288 million).

Our USA cigarette market share has been broadly stable for a number of months, although for the year it was at 3.9 per cent (2009: 4.2 per cent). We have invested in our key discount brands *USA Gold* and *Sonoma* which continue to be well positioned, with new packaging recently introduced. We have also continued to grow volumes of *Fortuna*.

## Performance Highlights: Americas

Investment in our key brands *USA Gold* and *Sonoma* and extending our distribution capabilities is strengthening our position in the USA.

Further investment in our sales force and extending our distribution capabilities has enabled us to cover significantly more customers.

Our USA cigar business remains strong and we have grown our sales in value terms. In the natural wrapper segment we have performed well. We have grown *Dutch Masters* in the cigarillo size segment and continued to expand our distribution. In the homogenised wrapper segment, we have undertaken a number of promotional and new product and packaging initiatives, particularly with *Phillies* cigarillos delivering a positive performance. In our premium handmade cigar business, we outperformed the market with our luxury brands *Montecristo* and *Romeo y Julieta*.

### Outlook

In the USA, we will continue to focus on expanding our distribution and building our position in the value segment through continued brand rejuvenation as market volumes revert to their long-term trend.

## Rest of the World



### Cigarette

	2010	2009
Volumes	<b>167.6bn</b>	174.1bn
Market shares <sup>1</sup>		
Australia	<b>17.5%</b>	16.2%
Morocco	<b>83.1%</b>	85.0%
Russia	<b>8.3%</b>	8.6%
Saudi Arabia	<b>10.2%</b>	9.8%
Taiwan	<b>11.0%</b>	9.9%
Turkey	<b>3.9%</b>	3.6% <sup>2</sup>
Ukraine	<b>20.8%</b>	20.2% <sup>3</sup>

<sup>1</sup> Imperial Tobacco estimates.

<sup>2</sup> Restated due to a changed basis of calculation.

<sup>3</sup> Restated due to a change of source.

### Regional Review

Our Rest of the World region comprises a broad range of markets which offer considerable opportunities for us to grow and develop our business. Our cigarette volumes in the year have been impacted by market declines in Russia and Ukraine, both down by 10 per cent, and by temporary supply disruption in the Middle East in the first half of the year.

### Regulation and Excise

Levels of regulation and excise vary across our diverse Rest of the World region. We focus on monitoring developments and participating in debates through our proactive engagement activities. We are particularly focused on the situation in Australia where the government has announced plans for the plain packaging of tobacco products with effect from July 2012. Plain packaging legislation has never been implemented by any government in the world and we are robustly challenging this proposal which would lead to a significant rise in counterfeit product, adversely affecting governments, retailers and consumers as well as the legitimate tobacco industry.

### Our Strategy

We drive sales by maximising the growth potential that the geographic diversity of this region offers. We particularly focus on building sales of our key global strategic brands, complemented by our local and regional brands with local consumer insights supporting our brand choices. Developing strong partnerships is also an important element of our strategy for growth in this region.

### Our Performance

We delivered a strong performance across this region, benefiting from strong pricing and a favourable sales mix. We grew net revenue by 9 per cent to £2,340 million (2009: £2,138 million), and adjusted operating profit by 12 per cent to £693 million (2009: £617 million).

### Africa and Middle East

We had a good year in Africa and increased our market share in a number of markets. *Fine* and *Excellence*, two important regional brands, continued to build on their volume growth trends. In Morocco, with the monopoly in tobacco manufacture and distribution ending this year, we continue to be well positioned and have further enhanced the position of our international brand portfolio, particularly *Gauloises*

## Performance Highlights: Rest of the World

We performed well in Africa and made further good progress with *Gauloises Blondes* in Morocco.



*Blondes*. In the Middle East, we again grew our market shares notably with *Davidoff* in Saudi Arabia, while in Turkey we posted gains with *West* driving market share higher.

### Eastern Europe

In Eastern Europe, cigarette volumes in our major markets of Russia and Ukraine have declined, impacted by rising unemployment due to the economic conditions and duty increases. However, pricing has been positive throughout the region and we delivered strong revenue growth. In Russia, although our overall market share was down to 8.3 per cent (2009: 8.6 per cent) impacted by declining volumes of our low margin value brand *Balkan Star*, we have delivered a positive performance with *Davidoff* supporting our increased share of the superslims segment and with *Maxim* in the value cigarette segment. In Ukraine, we have also had success with *Davidoff* with volumes up almost 50 per cent and our overall market share improving to 20.8 per cent. Other regional brand highlights include growth in *West* and *Style*.

### Asia Pacific

In Asia Pacific, we have delivered an excellent performance with market share, volume and profit growth. In Australia and New Zealand, we posted market share growth to 17.5 per cent and 18.5 per cent respectively (2009: 16.2 per cent and 18.3 per cent), driven by *JPS*. We have recently introduced a number of new *JPS* variants to further build on this momentum. We grew share in Cambodia and Laos. In Taiwan, we have delivered market share growth to 11.0 per cent (2009: 9.9 per cent) with *Davidoff*, *West* and *Boss*.

Following our agreement signed with KT&G earlier this year, we are pleased with the progress we have made with *Davidoff* in South Korea. In addition, in India our import and distribution agreement for *Davidoff* signed in May has made a positive start.

### Cigar

We have made encouraging progress with our luxury Habanos cigar portfolio and have grown volumes, sales and profits. Despite the economic climate we have achieved good results in a number of markets in Western Europe, Africa and the Middle East and Asia Pacific and launched a number of limited editions and exclusive series, enabling us to continue to build on the positive momentum we have achieved.

### Outlook

There are many opportunities for us to grow sales and profits in this region.

In Eastern Europe, we are investing to develop our sales force and distribution capabilities. We will continue to build on the momentum we have achieved with *Davidoff* while ensuring our product portfolio is positioned to maximise our growth in growing segments such as superslims and kingsize superslims. In Africa, we continue to develop our important regional brands such as *Excellence* and *Fine*, while in the Middle East we are focused on further enhancing *Davidoff* and *Gauloises Blondes* in the region. In Asia Pacific we are further building our position in our two major markets of Australia and Taiwan.

We will continue to effectively leverage our portfolio across the many markets in this region, while seeking to use our partnering credentials to further develop our market footprint.

## Logistics

### Overview

Our logistics business comprises operations in Spain, France, Italy, Portugal and Poland which cover several products and channels. Our logistics business is one of the largest of its kind in Europe, with more than 40 million deliveries per year and reaching around 300,000 delivery points across Europe. The point of sales served include tobacconists, convenience stores, bakeries, grocery stores, kiosks and bookshops, pharmacies, hospitals and petrol stations.

Our strategy is to further consolidate our leading positions and focus on our core profitable activities while widening the product offer to the points of sale that we reach and increasing the channels and countries that we access. Current economic conditions have presented us with challenges and we have continued to effectively manage these with our diligent approach to cost management.

We offer services across the whole logistics value chain to our customers, including order reception, storage and stock management, order preparation, transport and distribution, invoicing and collection and customer services.

## Performance Highlights: Rest of the World

We made gains with *Davidoff*, *West* and *JPS* in a number of markets in Asia Pacific, the Middle East and Eastern Europe.

Tobacco logistics delivers products for domestic and international tobacco manufacturers, including Imperial Tobacco, to tobacconists and other sales outlets in Spain, France, Italy, Portugal and Poland. The business is run on an operationally neutral basis, providing individual customer solutions based on our cutting edge technology and our specialised network. The high quality of the service we provide has allowed us to achieve a market share above 90 per cent in the distribution of tobacco in Spain, France and Italy and just under 20 per cent in Portugal.

Our integrated logistics services can assure full traceability throughout the entire logistics value chain, from pick-up and transport of the product at customers' factories to post-sale service. We can also provide specialised services for customers in a number of different sectors in Spain, Portugal, France and Italy: convenience, telecommunications, transportation, pharmaceutical, publishing, lottery and others.

We are market leaders in the distribution of convenience products to petrol stations in Spain, Portugal and France. Convenience products are also distributed to other points of sale in these countries and Italy including tobacconists, bakeries and grocery stores.

We have an e-transaction business with our own technological platform for e-recharge, installed in the main network of points of sale including in tobacconists, kiosks and convenience shops in Spain, Portugal and France. In this area, different products are offered including telephone cards and transport tickets.

We are present in the transportation segment, through courier and industrial parcel activities in Spain and Portugal. Our long distance transport network across Europe allows us to provide our customers with an integral solution for their logistics needs covering all services, from their factories to the point of sale. In addition, our logistics business is the leading logistics provider in Spain and Portugal in different sectors including pharmaceutical and publishing.

## Our Performance

Distribution fees were £936 million (2009: £964 million) with adjusted operating profit of £176 million (2009: £177 million).

Given current economic conditions, our overall logistics business has performed robustly.

In tobacco logistics, in spite of volume declines, our business has been resilient. In Spain, we have offset market declines with price increases and cost saving initiatives, performing ahead of our expectations. In France, we delivered a good performance with market volumes broadly stable and in Italy our results benefited from price increases.

In other logistics, our focus continues to be on maintaining our profitability while continuing to seek opportunities to profitably grow our operations. We have continued to gain market share in our French wholesale business and we achieved strong volume growth of 15 per cent in our pharma division. Following the signing of our joint venture last year to provide a range of services to one of the Spanish Lottery companies, we have made an upfront investment and commenced operations.

## Outlook

We will further consolidate our leading positions and focus on our core profitable activities in currently challenging market conditions. With our ongoing emphasis on enhancing our service levels to existing customers while seeking opportunities to extend our logistics footprint combined with cost saving initiatives, we believe our logistics business will continue to be effectively positioned.

## Our Corporate Responsibility strategy is integral to our overall business strategy and is embedded throughout the Imperial Tobacco Group.

Corporate responsibility is integral to our business success. We are committed to operating in a way that is financially, socially and environmentally responsible. We believe that this focus and commitment enhances our foundation for long-term sustainable sales growth.

### Information within this Report

Reflecting our belief that operating in a responsible manner is simply part of how we do business, this year's annual report incorporates our Corporate Responsibility Review to provide stakeholders with a comprehensive overview of our activities and achievements. Our performance review is structured around our strategy and highlights the progress we have made against our current objectives and the targets we are setting for the future.

Key information about CR within this report can be found as follows:

22	Key Performance Indicators
25	Principal Risks and Uncertainties
41	CR Performance Review
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### CR Information Online

More detailed and background information on our approach is available on our website.

Here you will find:

- More details on our CR Framework
- Our views on important issues in the tobacco industry
- A full progress report against our objectives set out in our CR Review published in March 2010
- Our performance aligned to the GRI index
- Case studies demonstrating our progress
- External feedback from our assurance and verification and our Stakeholder Panel

### CR Assurance and Verification Statement from Corporate Citizenship

Imperial Tobacco commissioned Corporate Citizenship to provide external assurance on its Corporate Responsibility (CR) reporting for 2010, including this corporate responsibility section of its Annual Report and Accounts and key parts of the corporate responsibility section of its website.

Imperial Tobacco has chosen to use the AA1000 Assurance Standard (AA1000AS) 2008. Our assurance is a Type 1 and the level of assurance offered is moderate as defined by the Standard. Details of our assurance scope, methodology and conclusions appear in our full statement published at [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

In our opinion Imperial Tobacco's CR reporting reflects the principles of AA1000AS (2008). In our full statement we provide information on the Company's performance against these principles and provide feedback that can help the Company and its stakeholders identify where its reporting can be strengthened in future.

### Corporate Citizenship London, November 2010

### SGS Verification

SGS United Kingdom Limited have verified the accuracy and reliability of our occupational health, safety and environment data. Their findings are available in their assurance statement published on our website.





# Our Business Context

## Our responsible approach underpins our sustainable sales growth strategy.

We have 38,000 employees, 51 manufacturing sites and consumers enjoy our products in over 160 markets.

Governments, investors and employees and a wide range of other stakeholders benefit economically through the wealth created by our business. In 2010 we paid over £20 billion to governments around the world in the form of excise and other taxes.

Our activities are multi-faceted and include tobacco leaf procurement and processing, product manufacturing, distribution and responsible sales and marketing. We source tobacco from countries including Brazil, India, China, Tanzania as well as many others in Africa, South America, Asia, North America and Europe.

Our supply chain involves tens of thousands of people. It includes tobacco growers and merchants, logistic and transport providers, machinery suppliers, utility and service providers, material suppliers, wholesalers, large commercial and individual retailers and tobacconists.

We continue to grow and develop our business in a responsible manner. In doing so we both comply with and exceed current regulatory standards as we apply our own corporate standards, sharing best practice within our wider supply chain and within our business.

We recognise the controversial nature of our product and believe it is important that it is handled by a responsible business.

Our views on important issues for the tobacco industry including smoking and health and the research and development of tobacco products are based on the work of a number of experts in their field, academics and scientists and practising physicians.

Our views are available on our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com).

Strategy

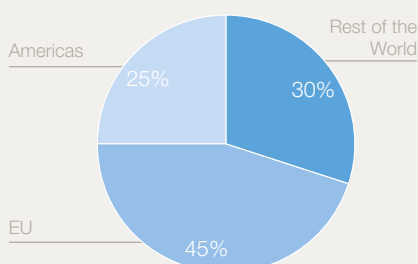
Performance

Governance

Financials

### Our Employees Worldwide

Over £20 billion was paid to governments around the world in the form of excise and other taxes.



# Corporate Responsibility and our Strategy

We understand that stakeholder issues impact the commercial success of our business therefore we have aligned our responsible approach within our strategy. In leveraging our assets of our brands, our unique total tobacco portfolio, our extensive market footprint and our people to drive sales, we have three particular areas of focus: consumer centric, execution excellence and future foundations. Our CR activities in each of these areas underpin our sustainable sales growth agenda.

## Measuring and Monitoring our CR Performance

We use our CR Framework with performance indicators to monitor our CR performance, set objectives and structure our CR reporting. The CR framework details social and environmental issues that are important to our stakeholders and to the success and sustainability of our business.

During the year we reviewed and subsequently amended our CR Framework to better reflect consumer interests, risk management, water management and societal and regulatory issues. Our revised framework incorporates our own internal reviews and feedback from our stakeholders, including our Stakeholder Panel, external benchmarking and wider economic and business developments.

Undertaking these periodic reviews enables us to consider gaps which are then addressed in our objectives and improved non-financial performance indicators.

We have progressed the implementation of new indicators in a number of areas including in employment practices, product stewardship, international marketing practices, social responsibility in tobacco production and community investment. We are aiming to report our new fully revised set of non-financial performance indicators in our 2011 report.

## CR Performance 2010 Highlights

We delivered another strong performance this year, further demonstrating our continued commitment to responsible business behaviour.

Our highlights this year include:

- Further increasing our focus on anti-illicit trade activities with a new Commercial Integrity team and completion of Market Risk Management roll-out.
- Signing a co-operation agreement with the European Commission and the Member States of the European Union to jointly combat illicit trade in tobacco.

- Further embedding high standards of conduct and behaviour with our Code of Conduct revised in 2010 and training being progressively rolled out across the Group.
- Inclusion of all tobacco suppliers in the Social Responsibility in Tobacco Production Programme, with 100 per cent compliance.
- Commencing negotiations to form a single European Works Council to represent our employee interests.
- Gold award rating in Business in the Community's 2009 Corporate Responsibility Index with a score of 93.8 per cent (2008: silver rating and a score of 84.5 per cent).
- Achieving a score of 74 per cent for 2010 (2009: 73 per cent) in SAM Research on behalf of the Dow Jones Sustainability Index.

## Our 2011 CR Focus

### Consumer Centric

- Further address and respond to consumer preferences in terms of products, quality and regulation.

### Execution Excellence

- Continue to improve OHSE management and performance.
- Further develop environmental performance management and our commitment to carbon reduction.
- Further develop our people capabilities to support our sales growth strategy.

### Future Foundations

- Continue our Code of Conduct training.
- Extending membership of our Stakeholder Panel.
- Enhance our non-financial reporting and CR performance indicators.
- Strengthen our responsible sales approach focusing on anti-illicit trade activities and youth smoking prevention.
- Further align our community investment partnerships to our business interests.
- Enhance our level of proactive regulatory engagement, supporting our business, consumers and customers.
- Target supply chain improvements by increasing dialogue with our suppliers.

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## Performance Highlights: CR

We further increased our focus on anti-illicit trade activities with a new Commercial Integrity team.

# 2010 Performance

## Consumer Centric

Satisfying consumers and aligning our portfolio to their evolving preferences is fundamental to our sales growth strategy.

In terms of CR we are focused on product quality, our product stewardship responsibilities and on reducing complexity in our portfolio.

Our product quality management systems ensure we are firmly focused on meeting consumer demands.

We conduct scientific and research programmes to improve our knowledge of tobacco products and tobacco consumption, so we can meet the future requirements of our consumers.

### Improving Product Quality

In 2010, we made further progress on how we incorporate consumers feedback into product quality improvements.

The ISO 9001 management system provides our framework for quality. A total of 32 of our 51 factories are ISO 9001 certified, with projects underway to implement the standard in eight other sites by the end of 2011.

We drive improvements using a product quality rating system (PQRS), standardised test equipment and methodology, benchmarking of final products and quality-improvement plans. PQRS is applied to all our factories and is currently being implemented in our tobacco processing sites.

### Reducing Complexity in our Portfolio

This year we have implemented a new approach to how we evaluate and reduce complexity and reduction in our portfolio to achieve the right balance between meeting consumer and regulatory demands and our product stewardship requirements.

As a result, we have reviewed and agreed complexity reduction criteria and, following an initial assessment, a number of our stock keeping units have been standardised and discontinued.

Complementing this, we have successfully reduced our blends by eight per cent.

## Ingredients Reporting and Assessment

Consumers are able to access the ingredients for a number of products via our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com).

We continued to provide regular submissions to individual government authorities on the ingredients used in our tobacco products and made 45 submissions in 2010. This includes the toxicological information which we have available on those ingredients. We monitor alleged incidents of non-compliance with technical product regulations and voluntary codes. This year there were two alleged incidents of non-compliance, however further testing of the product confirmed compliance. We comply with government regulations on tobacco product ingredients and in countries where no regulations exist we conform to international standards.

## Execution Excellence

We are a fast flexible business with a strong reputation for delivering results through execution excellence.

In terms of CR, we are focused on responsible sales and marketing, developing our people and employee engagement, occupational health and safety and our environmental performance.

Our ability to deliver results depends on the commitment and capabilities of our employees.

We work hard to ensure they have the right skills to support out sustainable sales growth strategy, are competitively rewarded and have a safe working environment as we continue to develop our occupational health and safety (OHS) processes and management.

We are committed to minimising our environmental impact. Effective environmental management presents us with business opportunities supporting our value driver of cost optimisation.

### Responsible Sales and Marketing

Selling our products in a responsible way is simply part of how we do business. All Imperial Tobacco Group companies and employees must apply our International Marketing Standards (IMS) as a minimum, regardless of geographical location. The IMS applies to all advertising, promotion and research agencies employed by us and is available on our website [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

## Performance Highlights: CR

We achieved a gold award rating in Business in the Community's 2009 Corporate Responsibility Index.

Business in the

Community



We have revised our IMS and employee communications about these revisions are ongoing. From April 2010 we introduced a monthly 'alleged breaches' report of our IMS with information collated centrally through our non-financial reporting system. Since then eight alleged breaches were reported and investigated. Three were dismissed, one was resolved and investigations into the remaining four alleged breaches are ongoing.

We believe that the decision to enjoy tobacco products is a choice for adults. We do not want children to smoke and have consistently worked with governments to prevent under-age smoking. During the year we reviewed our youth smoking prevention activities and benchmarked ourselves against our peers, with better sharing of best practice around the Group an objective for 2011.

#### **Developing our People**

We have set up a project team to further understand and research the key skills and capabilities required to deliver sustainable sales growth. We have conducted research to assess our current capabilities and benchmarked them against other FMCG companies. The results have provided valuable insight into our current skills and capabilities and are helping to shape a number of initiatives.

A broad range of development initiatives is available to our employees including our International Career Management Program and we launched a second cycle of the programme in April 2010. The programme targets employees at the early stage of their career and provides training, coaching, mentoring and international assignments over a two to three year period.

We have made a number of improvements to our performance management processes for 2010 to further strengthen our employees' performance. Our reward strategies are linked to Group, market and individual performance and we encourage employees to build a stake in the Company through share-based employee benefit schemes. Further information is included in our Remuneration report on page 78.

We have chosen not to report employment practice data for this financial year, as the data reported would have been unrepresentative of the Group as it would only reflect our operations prior to the acquisition of Altadis. We have agreed revised employment practice measures. These focus on our four main areas of general employment practice, fairness at work, health protection and wellbeing and employee relations. Case studies on our progress are available on our website. We will be reporting on our revised employment practice measures in 2011.

#### **Completing the Integration of Altadis**

A priority during the year was completing the planned organisational changes and integration of Imperial Tobacco and Altadis. We provided comprehensive outplacement support and training to affected employees in the UK, Spain, France, Belgium and Germany in addition to very competitive severance payments. Wherever possible we have relocated affected employees with a number of internal redeployment opportunities available. A case study on our approach is available on our website [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

#### **Engagement and Consultation**

Employee consultation and engagement is fundamental to our success and we actively promote two-way dialogue. A total of 72 employees representing 17 countries attended our joint European Employee Forum for Altadis and Imperial Tobacco employees to enable information and consultation at the European level.

We have won a number of awards during the year both as an employer and for our human resources practices and policies. In the UK, we were recognised for our commitment to our UK employees and awarded a "Best Companies" accreditation. In Slovakia, we were the winner of an annual survey of companies to find the country's best employer, and were commended as having effective HR policies aligned with both the employees' interests and the goals of the business. While in Greece, we won the KPMG Best People Management Initiative Award in the category of employee performance, reward management and retention.

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### **Performance Highlights: CR**

**We commenced negotiations to form a single European Works Council to represent our employees' interests.**

**Occupational Health and Safety Management (OHS)**

We have a strong commitment to improve our OHS controls. Examples of our performance are below:

- We further extended our 'Deal with It' behavioural safety training programme with training completed in our factories in Western and Eastern Europe, Africa and Asia.
- We held regional bi-annual training workshops for OHS site managers.
- We continued to progress independent certification for our OHS activities with 15 of our sites achieving OHSAS 18001 certification.

Our verified lost time accident rate for 2009 was broadly stable at 1.57 (2008: 1.56). Improvements throughout our manufacturing operations were offset by increases in sales and marketing and support functions and we are taking steps to improve this.

Provisional data for 2010 indicates that our occupational health and safety performance has significantly improved.

The number of major injuries increased, with 16 events in 2009 compared to nine in 2008. We operate in some difficult regions of the world and take our responsibilities regarding the personal security of our employees seriously. Regrettably there was one fatality when a security guard was shot in Madagascar. We have reviewed and strengthened security procedures to address the increasing level of security threats in the country.

Following the previous fatality at our Nottingham factory of a DHL driver, the Health and Safety Executive (HSE) subsequently investigated and prosecuted both Imperial Tobacco and DHL for whom the driver worked. In August 2010, we both pleaded guilty to the charges but the judge accepted that these did not cause or contribute to the driver's death. The training, assessment and supervisory issues identified were immediately rectified after the accident and best practice in regard to trailer parking was shared across the business.

**Environmental Performance<sup>1</sup>**

Our 2009 environmental performance remained on track to meet our energy and waste to landfill reduction targets and we have made good progress in reducing our water consumption in line with our overall target.

Our performance on environmental waste and absolute carbon dioxide (CO<sub>2</sub>) emissions was affected by the inclusion of Altadis data and factory restructuring activities. We are committed to reducing our carbon emissions and environmental waste and have developed a carbon saving target of 20 per cent by 2020. CO<sub>2</sub> trends were also distorted by changes in the Greenhouse Gas Protocol conversion factors and UK DEFRA guidelines which we use to inform our reporting.

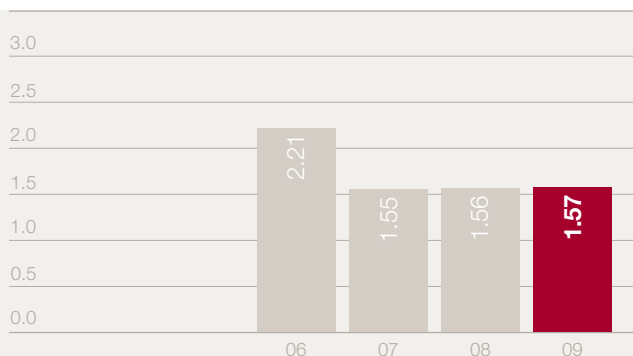
Examples of our performance are below:

- Energy consumption per million cigarette equivalents was down 14 per cent since 2001 (target down 10 per cent).
- Waste to landfill per million cigarette equivalents was down by 26 per cent since 2004 (target down 15 per cent).
- Water consumption per million cigarette equivalents was down 12 per cent since 2001 (targets are set locally).
- CO<sub>2</sub> emissions per million cigarette equivalents were down 0.37 per cent since 2001 (target down 10 per cent).
- Waste per million cigarette equivalents was up 4 per cent since 2004 (target down 10 per cent).
- We responded to 16 minor environmental complaints for noise, dust or odour and we sought to understand the issues and find remedial solutions in line with our standard practice.
- We extended ISO 14001 accreditation, with 69 per cent of our manufacturing sites now covered.
- We conducted independent energy audits at 11 manufacturing sites, with promising energy saving opportunities identified.

More detailed environmental measures are available on our website [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

<sup>1</sup> Our 2009 environmental data covers all manufacturing sites except the non-EU cigar sites which have been brought into reporting for 2010. Environmental data is reported 12 months in arrears to allow for verification.

## Lost Time Accident Frequency Rate per 200,000 hours

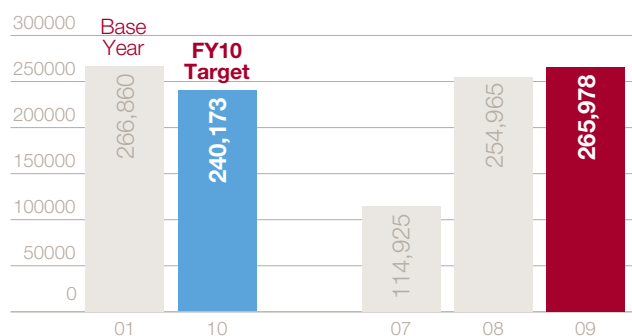


Lost time accidents (LTAs) are work-related accidents resulting in absence from one or more scheduled workdays or shifts. Our LTA frequency rate for 2009 (for all operations except Logistics) remained stable.

# Environmental Performance<sup>1</sup>

## Absolute CO<sub>2</sub> Emissions (Scope 1 and Scope 2): Manufacturing Sites and Main Offices

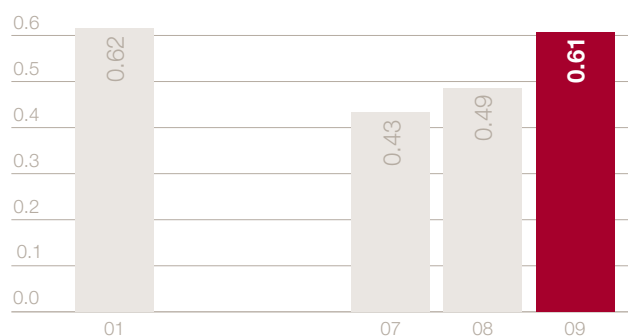
Tonnes CO<sub>2</sub>



Increases in CO<sub>2</sub> for 2009 were largely due to the inclusion of two facilities that use CO<sub>2</sub> to expand tobacco. We are currently evaluating the options to improve our current CO<sub>2</sub> recycling at these facilities. We use the Greenhouse Gas Protocol and UK DEFRA guidelines to inform our reporting. The reported increase in CO<sub>2</sub> emissions in recent years also reflects changes in these guidelines. Scope 1 carbon emissions are emissions from sources that we own or control, also known as direct emissions. Scope 2 carbon emissions are emissions from another company, for example purchased electricity, heat, cooling or steam.

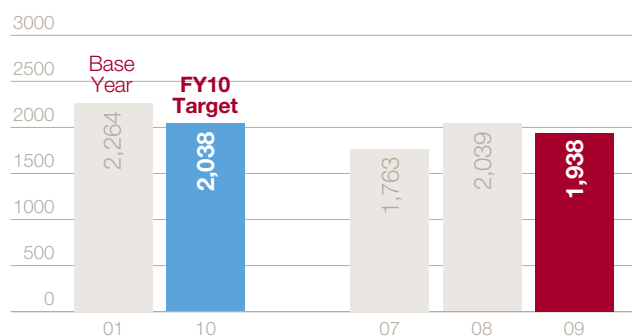
## CO<sub>2</sub> Emissions (Scope 1 and Scope 2): Tobacco Manufacturing

Tonnes CO<sub>2</sub> per million cigarette equivalents



## Energy Consumption: Tobacco Manufacturing

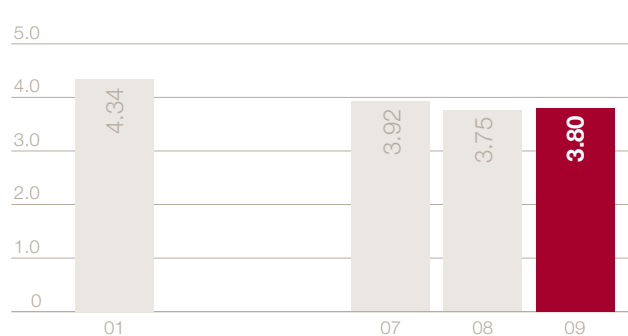
Kilowatt hours per million cigarette equivalents



We improved our energy efficiency in 2009 and remain on track for a 10 per cent reduction on our base year by the end of 2010.

## Water Consumption (mains & abstracted): Tobacco Manufacturing

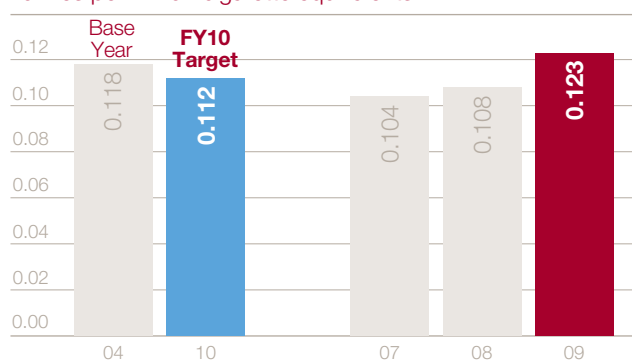
Cubic metres per million cigarette equivalents



Water conservation and protection is managed locally and we have set reduction targets in a number of countries identified as being at risk from water scarcity.

## Waste: Tobacco Manufacturing

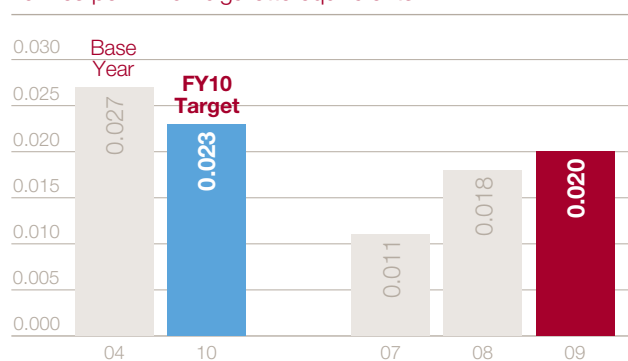
Tonnes per million cigarette equivalents



The increase in waste in 2009 was largely due to integration activities including construction projects.

## Waste to Landfill: Tobacco Manufacturing

Tonnes per million cigarette equivalents



Despite increased total waste, our waste to landfill has reduced by 26 per cent since 2004, reflecting our excellent progress with our recycling initiatives.



## Climate Change

We are committed to further reducing our carbon footprint with a commercially focused approach to carbon management. The focus of our climate change strategy is to reduce our impacts by achieving a balanced approach to carbon management through energy conservation lower carbon technologies, renewable energy and carbon offsetting. Further details on our approach is available on our website [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

Based on the results of the energy audits, potential cost savings and additional energy saving opportunities, we have developed a carbon saving target<sup>1</sup> of 20 per cent by 2020 in line with the current EU target of 20 per cent.

We continued to evaluate renewable energy opportunities within our manufacturing operation, however our main focus is on overall efficiency improvements throughout the Group. Renewable energy options are considered in all our energy studies and where factories are being upgraded or new buildings are in development.

In the UK, we made preparations to participate within the mandatory Carbon Reduction Commitment Energy Efficiency Scheme, which came into effect in April 2010.

### Carbon Disclosure Project (CDP) and Supply Chain Leadership Participation

Developing stronger relationships with our suppliers and the sharing of good environmental practices remains a priority for us. Benefits include optimising our costs and improving our security in our supply chain.

We took part in the CDP 2010 information request, and received a score of 63 per cent (2009: 62 per cent). The full CDP and our submission is available at [www.cdproject.net](http://www.cdproject.net)

We have continued our participation in the CDP Supply Chain Leadership Programme and a number of our key suppliers whom we invited to take part agreed to participate. We are working with our suppliers to further encourage participation which now covers approximately 50 per cent of our non-tobacco material purchases by value and our major global tobacco leaf suppliers.

## Future Foundations

We constantly review and manage our governance processes to ensure our long term sustainability. These are fundamental for responsible business practice.

Our key CR areas of focus are governance, business integrity and risk management, anti-illicit trade activities, regulatory engagement, and our other engagement activities across our supply chain and within the communities in which we operate.

Adult choice and anti-illicit trade activities underpin legitimate sales which are a key driver in strengthening our long term business sustainability.

We seek proactive engagement with governments and other regulatory bodies and encourage reasonable, proportionate and evidence based regulation. We support consumers in their choice to enjoy tobacco products without discrimination, and challenge disproportionate and unnecessary regulation that undermines the principles of adult choice and the freedom of competition.

We focus on continuing to engage with and influence our partners to improve social and environmental standards in the supply chain. Supporting the communities in which we operate is important to us and enables us to address issues that directly and indirectly affect our supply chain.

### Governance and Business Integrity

In our governance report on pages 54 to 72 of this report, we explain how in practice we apply the principles of good governance advocated by the Combined Code on Corporate Governance.

During the year we established a Commercial Integrity team which has responsibility for reviewing and managing our anti-illicit trade strategies and the protection of our brands. Commercial Integrity is also responsible for promoting good corporate and individual conduct across the Group and facilitating our Corporate Responsibility approach.

In 2010, we reviewed and updated our existing Code of Conduct and began a comprehensive training programme

<sup>1</sup> This target will use 2009 as a base year.

across the business. More information on how our Code of Conduct supports our employees is available on page 14 of this report and the Code is published on our website [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr).

Our Code of Conduct is supported by our public interest disclosure (whistleblowing) policy and processes. Our Code clearly reinforces our commitment to ensuring we comply with the requirements of the UK Bribery Act which comes into force next year. Following the recent publication of the draft guidance by the UK Ministry of Justice, we are conducting a full review of our current policies and practices and we will be well positioned to fulfil the requirements of the Bribery Act in line with our ongoing commitments set out in our Code of Conduct.

### **Risk Management**

During the year our Risk Co-ordination Committee has further developed our risk register which is regularly updated. On page 25 the Principal Risks and Uncertainties facing the Group are outlined with a report on the activities of the Risk Co-ordination Committee on page 68.

Our risk register covers a number of environmental, community, ethical and reputational issues and they are integrated into our decision-making and risk assessment processes. Specific local risks are managed at the local level, and integrated into the annual risk management and compliance processes. Specific training is provided as appropriate, for example in the area of health and safety awareness.

### **Anti-Illicit Trade**

The prevention and elimination of tobacco smuggling and counterfeiting is one of our major business priorities. Illicit tobacco products deprive consumers of the quality they expect, and governments and retailers of variable revenue. Illicit trade also deprives the tobacco industry of legitimate sales, undermining the responsible way in which we manage our operations and eroding the long-term sustainability of our business. We have a senior team who strategically manage and target our anti-illicit trade activities such as working with suppliers, developing technological solutions, co-ordinating within the industry and progressing support materials for markets.

## **Lao Tobacco**

**Lao Tobacco is a joint venture between the Lao Government and Imperial Tobacco. Our operations include a leaf processing facility and a cigarette factory and a partnership with Lao tobacco farmers. Lao Tobacco employs around 630 people and we work together to meet our shared social objectives. Read more about our activities at [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr)**

for more information visit:  
[www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr)



In September 2010, we signed a co-operation agreement with the European Commission and the Member States of the European Union to jointly combat illicit trade in tobacco. We have extended our memoranda of understanding (MoUs) and co-operation agreements with governments which govern jointly developed protocols to combat the smuggling and counterfeiting of tobacco products. We have 18 such agreements in place and are progressing MoUs in Morocco, Algeria, the Netherlands and Lebanon.

Our 'Know Your Customer' process seeks to ensure we only supply product to legitimate customers. The process provides us with a regular and detailed review of each of our customers. During the year we improved technology providing quicker and easier visibility. We are currently running a pilot programme before further roll-out throughout the Group. In addition, we plan to extend our 'Know Your Customer' process to handlers of finished goods, including

warehouse storage and logistics service providers. More detail on our product supply compliance is available on our website.

We have also further improved our internal processes to provide greater support, resources and intelligence to authorities when notifying them of seizures of illicit tobacco products.

We have progressed implementation of new technology into our production and logistics processes to further improve our tracking and tracing capabilities for finished tobacco products.

In addition, we continued to enhance our general training, communication and awareness of illicit trade. For example in Poland we have run a series of workshops for customs officers, where attendees were shown the scale and sources of tobacco products smuggled into Poland and the methods of identifying legal and illicit products.

### **Regulatory Engagement**

We continue to engage with regulators and government authorities in support of reasonable and practical regulation.

We recognise we are a company that manufactures and sells a controversial product. We continue to oppose regulation that undermines the rights of our consumers to enjoy smoking and our commercial freedoms such as product display bans and further encroachment on our packaging, including the plain packaging of tobacco products.

Key drivers of regulation are national governments, the European Commission, through the European Union Tobacco Products Directive (EUPTD) and the World Health Organisation, through the Framework Convention on Tobacco Control (FCTC).

We seek proactive engagement with these bodies through ongoing dialogue and by providing detailed submissions to regulatory consultations.

This engagement is both as an individual company or subsidiary, or via various industry associations such as the Confederation of European Community Cigarette Manufacturers (CECCM), the European Smoking Tobacco Association, and the European Cigar Manufacturers Association (ECMA). We have developed joint industry position papers to be used with a wide spectrum of European stakeholders, as we strive to achieve workable regulations.

It is regrettable that the FCTC continue to ignore the tobacco industry as a legitimate stakeholder in the various debates that are ongoing.

This exclusion is symptomatic of attempts to denormalise smokers and smoking, and is something we continue to resist.

Ahead of the 4th Conference of the Parties to FCTC in November 2010 we consulted with governments on the guidelines being developed and debated which include product regulation, education, cessation and alternatives to tobacco farming.

In terms of specific regulation, we remain especially focused on the situation in Australia where the government has announced plans for the plain packaging of tobacco products with effect from July 2012. Plain packaging legislation has never been implemented by any government in the world and we are robustly challenging this proposal.

As well as depriving us of our registered trademarks and diluting the value of our brands, we have particular concerns about the impact plain packaging would have on illicit trade. Making all tobacco products available in the same, easy-to-copy generic plain packaging would lead to a significant rise in counterfeit product, adversely affecting governments, retailers and consumers as well as the legitimate tobacco industry.

## Supplier Relationships

Our main supplier engagement and assessment programmes are Social Responsibility in Tobacco Production Programme (SRiTP) for tobacco suppliers and Supplier Qualification Programme for non-tobacco materials supply. We have continued to work with suppliers and business partners to tackle issues such as deforestation, environmental protection, child labour, sustainable development and poverty alleviation. One of the most important partnerships we are involved in is the Eliminating Child Labour in Tobacco (ECLT) Foundation of which we are a board member. ECLT works with communities to address the underlying causes of child labour. During the year, we have continued to provide financial support, guidance and advice in line with our long term commitment to the Foundation.

The majority of the tobacco that we use is purchased through the leading international leaf supplying companies. Only a small portion is purchased directly from growers, mainly in Morocco, Madagascar and Laos who also now participate in SRiTP. All of our tobacco suppliers (100 per cent) participated in the programme (2009: 92 per cent).

Evaluations of our supplier SRiTP self assessments for the 2009 calendar year indicated the majority of suppliers averaging a score of 60 per cent, indicating a good level of risk management. Weak performance is identified through annual review. We are increasing dialogue with weak performers to focus improvements. We aim to deliver ongoing improvements and are embedding new categories for post-harvest management and climate change. Given this change, general scores were impacted and we continue to monitor and seek to improve our performance with our suppliers.

We have also continued to roll-out our SRiTP programme with our USA cigar tobacco suppliers. All cigar suppliers have been incorporated into the rolling audit plan.

All of our non-tobacco materials suppliers are part of our supplier qualification programme which includes relevant social and environmental aspects. Our central team of non-tobacco materials buyers have received ISO accredited training and been certified as auditors. They subsequently visited suppliers at eleven sites in 2010.

In line with our enhanced Code of Conduct, we have started to progress a new supplier standard that will extend across all our suppliers Group-wide.

## Social Assessment and Human Rights

We have identified 28 manufacturing sites in countries deemed medium to high risk in terms of human rights in line with our own criteria. We use the principles of the Social Accountability SA 8000 standard and the International Labour Organization's (ILO) core conventions as a basis of evaluation of the labour practices at these sites, combined with our own employment policies, practices and standards. Our assessments of these sites have confirmed that local employment practices are aligned with our Group policy. We have conducted social assessment visits to 19 of these sites including visits to the Philippines, Puerto Rico and the Dominican Republic in 2010. Recommendations included minor improvements related to the need for formal documentation for grievance, non-discrimination and disciplinary procedures which we are progressing.

We continued to keep abreast of developments in Human Rights, including the work of the United Nation's Special Representative, Professor John Ruggie, and via our memberships of organisations such as the Confederation of British Industry and the International Chamber of Commerce. Information on our Human Rights Policy and due diligence processes including our supply chain activities is available on our website.

## Stakeholder Panel

Our Stakeholder Panel, comprising representatives from many of our main stakeholder groups including consumers, investors, suppliers, employees and community, met with us during the year to share views on our business. Their valuable input has continued to help shape our Corporate Responsibility approach and reporting.

Feedback has related to how we engage with a wider range of stakeholders across a broader geographic spread. This includes further extending the membership of the Stakeholder Panel as well as increasing our transparency on regulatory issues. We have also incorporated the Panel's improvements into our 2010 reporting.



## Community Involvement

We allocated around £3 million to community investment in 2010 as well as the management time involved to maximise the benefits from our community investment programme. During the year our employees also gave their time during normal working hours to contribute to local community programmes in a number of countries such as the UK, Greece and Poland.

As a result of our engagement activities and analysis of our benchmarks we have strengthened our community investment approach. We have joined the London Benchmarking Group which helps facilitate the sharing of good practice for community investment. We have improved the way we structure our community investment this year, with funds consistently allocated by our regional committees against the five categories below:

- **Improved livelihoods:** supporting micro-finance and sustainable agriculture projects.
- **Community wellbeing:** funding health, water, sanitation and HIV/AIDS projects and other community support projects including those working with elderly and disabled people.
- **Environment:** backing projects that tackle climate change, deforestation and protection of water sources projects.
- **Adult Education:** providing scholarships and funding courses as well as improving access to education.
- **Disaster Relief:** responding to significant global humanitarian events.

We have further reviewed the Altadis Foundation during the year to align more closely with our community investment approach. The Foundation budget has been redirected to support communities in Spain and supply chain sustainability issues in Latin America. The Foundation has successfully collaborated with a charity to provide disaster relief activities, including the provision of clean drinking water in Guatemala, assisting families to improve their domestic living conditions.

Further examples of projects and the benefits delivered to their communities are available on our website.

## Madagascar

**Our business in Madagascar involves tobacco growing, processing, manufacturing and distribution. We work closely with the communities around our operations in Madagascar and invest in practical initiatives that actively support these communities. Read more about our activities at [www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr)**

 for more information visit:  
[www.imperial-tobacco.com/cr](http://www.imperial-tobacco.com/cr)

# Non-financial performance indicators

Performance indicator <sup>1, 2</sup>	Unit	FY 2007	FY 2008	FY 2009	FY 2010
<b>Product stewardship:</b>					
Number of countries for which cigarette ingredients are published on Imperial Tobacco corporate website <sup>3</sup>	Number	35	36	36	<b>34</b>
<b>Robust processes:</b>					
Factories that have independent OHS audits (3-year rolling programme) includes OHSAS 18001 surveillance	% factories	74	77	90	<b>100</b>
Factories that have independent environmental audits (3-year rolling programme) includes ISO 14001 surveillance	% factories	87	74	81	<b>86</b>
<b>Environment:<sup>4</sup></b>					
Factories with ISO 14001 at the time of reporting <sup>5</sup>	% (ratio)	67 (21/31)	74 (23/31)	66 (37/56)	<b>69 (35/51)</b>
Environmental waste – tobacco factories only <sup>6</sup>	Tonnes/ MCE	0.104	0.108	<b>0.123</b>	
Environmental waste – manufacturing sites and main offices <sup>7</sup>	Tonnes	28,950	50,023	<b>54,966</b>	
Environmental waste to landfill – tobacco factories only	Tonnes/ MCE	0.011	0.018	<b>0.020</b>	
Environmental waste to landfill – manufacturing sites and main offices	Tonnes	3,155	8,663	<b>8,843</b>	
Energy consumption – tobacco factories only	KWh/MCE	1,763	2,039	<b>1,938</b>	
Energy consumption – manufacturing sites and main offices	GWh	459	862	<b>855</b>	
CO <sub>2</sub> equivalent emissions from energy consumed – tobacco factories only <sup>7</sup>	Tonnes/ MCE	0.434	0.486	<b>0.607</b>	
CO <sub>2</sub> equivalent emissions from energy consumed – manufacturing sites and main offices <sup>7</sup>	Tonnes	114,925	254,965	<b>265,978</b>	
<b>Supplier social responsibility:</b>					
Tobacco suppliers participating in the Social Responsibility in Tobacco Production programme	%	100	93	92	<b>100</b>
Manufacturing's non-tobacco materials suppliers covered by Supplier Qualification Programme	%	N/R	N/R	100	<b>100</b>
<b>Community investment:</b>					
Community investment donations (spend) <sup>8</sup>	£m	1.7	2.4	3.0	<b>3.1</b>
<b>Employment practices:<sup>9</sup></b>					
Sickness absence (days sickness/average number working days) incl. non-work-related and work-related absence <sup>10</sup>	%	2.98	2.96	3.93	<b>3.73</b>
<b>Occupational health and safety:<sup>11</sup></b>					
Lost time accident frequency rate <sup>12</sup>	Per 200,000 hours	1.55	1.56	<b>1.57</b>	
<b>Combating smuggling and counterfeit:</b>					
Total number of memoranda of understanding and cooperation agreements on combating smuggling and counterfeit signed with governments	Number	12	15	16	<b>18</b>

1 We have reviewed our performance indicators to ensure we have measures appropriate for the enlarged Group. We aim to report data for the new set of indicators in our 2011 report.

2 Due to the increased scale and scope of our organisation following the Altadis acquisition in January 2008, care should be taken when comparing data with previous years.

3 Cigarette ingredients information for New Zealand and Moldova has been temporarily removed from our website, pending update of product descriptors.

4 Environmental data is reported 12 months in arrears to allow for data collection and verification. Efficiency measures relative to tobacco production are expressed as per million cigarette equivalents (MCE). FY 2009 data covers all our manufacturing sites except non-EU cigar factories (reporting for FY 2010), and excludes our logistics business (aim to report for FY 2011).

5 ISO 14001 data for 2008 excludes the Altadis factories.

6 Waste data for 2007 and 2008 have been restated as a result of slight variations detected during audit and verification. Increase in waste in 2009 was largely due to integration activities, for example factory clean-ups, construction projects and differences in reporting by Altadis.

7 We use the GHG Protocol and UK DEFRA guidelines to inform our reporting. The reported increase in CO<sub>2</sub> emissions in recent years reflects changes in these guidelines.

8 Community investment donations do not include value of employee time, in-kind contribution or management costs.

9 Employment indicators are under review therefore data is unavailable for FY 2010, except sickness absence data.

10 2010 sickness absence data covers the majority of employees, excluding Logistics.

11 OHS data is reported 12 months in arrears to allow for data collection and verification. 2009 data covers the majority of employees, excluding Logistics.

12 Lost time accidents are work-related accidents resulting in absence from one or more scheduled workdays or shifts.

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## Chairman's Introduction

The challenging economic and business environment reinforces the need for effective leadership and high standards of corporate governance. We are confident that the strong leadership provided by our newly appointed Chief Executive and her fellow Directors will ensure we remain in a position to deliver our growth strategy. This strong leadership is supported by our long-established and embedded governance practices, robust internal controls, remuneration policy, and our high ethical standards.

### Our Corporate Structure Explained

We have two main businesses: tobacco and logistics. Our tobacco business comprises the manufacture, marketing and sale of tobacco and tobacco-related products. Our logistics business comprises the distribution of tobacco products for major tobacco manufacturers, including Imperial Tobacco, as well as a wide range of non-tobacco products and services.

### What Does Good Governance Mean To Us?

To us good governance means ensuring the right processes are in place to support our strategic direction. To deliver this strategy we must maintain appropriate controls to minimise unacceptable risk to our stakeholders whilst also maintaining an environment which enables our management to effectively implement that strategy. Good governance also means ensuring we treat our stakeholders in a fair and just manner.

### How We Achieve Good Governance In Practice

Our Executive Directors have a wealth of experience in the tobacco industry, complemented and supplemented by the wide range of business and financial experience of our Non-Executive Directors.

Our Directors' experience, oversight, strong leadership and constructive challenge of key decisions ensures we take our business in the right strategic direction and provides an environment in which our corporate strategy can be delivered.

We believe good governance is not just a matter for the Board but must be embraced throughout the organisation and we have reinforced this during the year by the roll-out of our updated Code of Conduct.

Both our tobacco and logistics businesses are managed within our Corporate Governance framework and are subject to our policies and control procedures. However, we run our logistics business on an operationally neutral basis in order to ensure that all its customers are treated equally.

### Managing Risk

The Group faces a number of risks, similar to those faced by many multinational companies, which may impact our financial position or prevent us from achieving our corporate strategy. Successful management of these risks is fundamental to our sustainable profitability and future growth.

Our business and the risks we face are constantly changing. We regularly review our policies and risk management procedures to ensure they are up-to-date and continue to appropriately protect our stakeholders. During the year we brought together into a single Commercial Integrity Department those activities with responsibility for reviewing and managing the enhancement by the business of our anti-illicit trade strategies, the legal protection of our brands and the driving of good corporate and individual conduct across the Group.

It is impossible to eliminate every risk. However, through our Risk Co-ordination Committee we analyse risks by reference to the likelihood of them occurring and their potential impact. This top down process complements our long established risk management controls which are embedded across the business. Further information relating to the management of risk during the year is set out on pages 25 to 27.

We also encourage employees to raise concerns they may have, including anything they believe to be wrong or dangerous. Our public interest disclosure (whistleblowing) policy allows employees to do this safe in the knowledge that they will not suffer any detriment as a consequence.

### Key Achievements in 2010

In May 2010 Mr G Davis retired as Chief Executive and, after a rigorous succession process, Mrs A J Cooper was identified as having the skills and expertise to drive the future growth of the business and was appointed his successor.

We largely completed the integration of Altadis, including embedding our processes and internal controls.

In addition we have continued to enhance our risk management and anti-illicit trade processes by further developing the approach of the Risk Co-ordination Committee and establishing our Commercial Integrity Department. On 27 September 2010 we signed a co-operation agreement with the European Commission and the Member States of the European Union. Under the co-operation agreement we will work together with the European Commission and the law enforcement authorities of the Member States of the European Union to jointly tackle the smuggling and counterfeiting of tobacco products.

In addition we have rolled-out our new Code of Conduct to over 600 managers in more than 40 workshops. The Code of Conduct has been published on our intranet and has been translated into our key business languages. The roll-out will be extended to the wider employee base during 2011.

### Key Priorities for 2011

In light of the UK Corporate Governance Code published in June 2010 we are reviewing and, if appropriate, will enhance our governance and internal control processes. In addition, to support our sustainable sales growth strategy, our priorities for

**“High standards of corporate governance and responsible management underpin our sales growth strategy.”**

**Iain Napier**  
Chairman

2011 include the further enhancement of our anti-illicit trade activities to assist in combating both the smuggling and counterfeiting of tobacco products and, following the signing of the co-operation agreement, further building on our partnership with the European Commission and the Member States of the European Union.

We also intend to complete the roll-out of training regarding our updated Code of Conduct which sets out the standards of responsible behaviour that all our employees are expected to follow and forms a key part of our preparations for ensuring compliance with the UK Bribery Act. We are also embedding an e-learning system to further support this training.

On 1 October 2010 the Chief Executive's Committee was replaced by the Operating Executive and the Development Executive to enhance support for our sustainable sales growth strategy. During 2011 this revised management structure will be embedded into the business.

Our governance processes support and underpin our sustainable sales growth strategy and we will continue to drive these during the year. We will also continue to support reasonable regulation of tobacco products but will challenge regulation that undermines the principles of adult choice and the freedom of competition.

Looking ahead I believe that achieving these key priorities will put us in a strong position to build on our track record of creating long-term sustainable value for our shareholders and provide a strong platform for growth throughout the business.



**Iain Napier**  
Chairman



## Achievements in 2010

- Appointment of new Chief Executive
- Altadis integration in final stages moving towards business as normal
- Ongoing enhancement of our risk management processes
- Enhancement of our anti-illicit trade activities including signing co-operation agreement with the EU and Member States

## Priorities for 2011

- Review compliance with the new UK Corporate Governance Code
- Further enhance anti-illicit trade activities, including building on our partnership with the EU and Member States
- Complete roll-out of updated Code of Conduct
- Ensure compliance with provisions of the UK Bribery Act
- Embed our new management structure



# Board of Directors

The Board is our principal decision making forum and is accountable to shareholders for our performance and the good conduct of our affairs.

Our Board focuses on areas that are important to our shareholders – strategy, risk management, operational performance, leadership development and regulatory matters.

for more information visit:  
[www.imperial-tobacco.com](http://www.imperial-tobacco.com)

## 1. Iain Napier, FCMA

### Chairman, 61

Appointed Chairman in January 2007.  
 Non-Executive Director from March 2000.  
 Chairman of Nominations Committee.

Iain was formerly main Board Director of Bass PLC, Chief Executive of Bass Leisure and then of Bass Brewers and Bass International Brewers. He was then Vice President UK and Ireland for Interbrew SA until August 2001. He was Chief Executive of Taylor Woodrow International Housing and Development from 2001 to 2005.

Non-Executive Chairman of McBride PLC and John Menzies plc, and a Non-Executive Director of Molson Coors Brewing Company and William Grant & Sons Holdings Limited.

## 2. Alison Cooper, BSC, ACA

### Chief Executive, 44

Appointed Chief Executive in May 2010.  
 Chief Executive's Committee to 30 September 2010;  
 Operating Executive and Development Executive from 1 October 2010.

Alison joined Imperial Tobacco in 1999 and was appointed as Chief Executive on 13 May 2010. She has held a number of senior roles in the Group including Director of Finance & Planning, Regional Director Western Europe, Corporate Development Director and Chief Operating Officer.

Previously she was with PricewaterhouseCoopers where she had worked with Imperial Tobacco for several years in a number of areas, including acquisitions.

Alison became Group Financial Controller in 2001 and was responsible for the financial management and control of the Group. In 2003 she became Director of Finance & Planning and a member of the Chief Executive's Committee, the then senior management steering group responsible for implementing Group strategy.

In 2005 Alison was appointed Sales and Marketing Regional Director for Western Europe.

She was appointed to the Board as Corporate Development Director in July 2007, with responsibility for strategic planning, business development and corporate affairs, and she was a key member of the Altadis acquisition team. Following her appointment as Chief Operating Officer in March 2009, Alison took on responsibility for all of the Group's sales and marketing, manufacturing and cigar business activities, whilst retaining her existing responsibilities.  
 Non-Executive Director, Inchcape plc since 1 July 2009.

## 3. Robert Dyrbus, BSC, FCA

### Finance Director, 58

Appointed Finance Director on demerger in 1996.  
 Chief Executive's Committee to 30 September 2010 and Operating Executive from 1 October 2010.

Robert was Finance Director of Imperial Tobacco Limited from November 1989 and one of the three-man Hanson team involved in the strategic reorganisation of the Group. Since then he has played an integral part in shaping the strategic direction of the Group.

No external Director appointments.

## 4. Graham Blashill, BSC

### Group Sales and Marketing Director, 63

Appointed to the Board in October 2005.

Chief Executive's Committee to 30 September 2010; Operating Executive and Development Executive from 1 October 2010.

Graham is responsible for global sales and marketing activities. With over 40 years' experience with the Group he has held a number of senior sales and marketing positions, including Managing Director UK and Regional Director for Western Europe.

No external Director appointments.



1

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**5. Pierre Jungels, CBE (HON), PHD, C ENG****Senior Independent Non-Executive Director, 66**

Appointed Non-Executive Director in August 2002.

Chairman of the Remuneration Committee;  
Member of the Nominations Committee and the Audit Committee.

Pierre has held numerous senior international positions within the oil industry with Shell International, Petrofina SA and British Gas PLC. He became CEO of Enterprise Oil in 1996, leading the business to substantial geographic and financial growth until retirement in November 2001. Chairman of Oxford Catalyst Group PLC, Director of Baker Hughes Inc., Chairman of Rockhopper Exploration PLC and a Non-Executive Director of Woodside Petroleum Ltd.

**6. Ken Burnett, MA, MBA, PHD, M Inst M****Non-Executive Director, 58**

Appointed Non-Executive Director in April 2006.  
Nominations Committee.

Ken is an independent management consultant and a co-founder and Director of K-Energy, an alternative energy company. He was President, Asia Pacific of Allied Domecq from 1996 until its acquisition by Pernod Ricard in 2005. Prior to joining Allied Domecq, he held senior management positions in the Asia Pacific region with Seagram, Interbrew and International Distillers & Vintners Ltd (now part of Diageo plc).

Director of K-Energy Pty Limited.

**7. Michael Herlihy, MA (Oxon), Solicitor****Non-Executive Director, 57**

Appointed Non-Executive Director in July 2007.

Nominations Committee, Audit Committee and Remuneration Committee.

Michael 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 of both private and public market transactions.

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

**8. Susan Murray****Non-Executive Director, 53**

Appointed Non-Executive Director in December 2004.

Nominations Committee, Audit Committee and Remuneration Committee.

Susan was a Board member at Littlewoods Limited from October 1998 until January 2004, latterly as Chief Executive of Littlewoods Stores Limited. Prior to this she was worldwide President and Chief Executive of The Pierre Smirnoff Company, a part of Diageo plc. Susan is also a former Non-Executive Director of SSL International plc, Aberdeen Asset Management PLC, Wm Morrison Supermarkets plc and a former council member of the Advertising Standards Authority. Non-Executive Chairman of Farrow & Ball and Non-Executive Director of Compass Group PLC and Enterprise Inns Plc. Also fellow of the Royal Society of Arts.

**9. Berge Setrakian****Non-Executive Director, 61**

Appointed Non-Executive Director in June 2008.

Nominations Committee.

Berge is a senior partner in the law firm Dewey & LeBoeuf LLP and has extensive expertise in international transactions. He was a Non-Executive Director of Altadis, S.A. having been appointed in May 2004 and was a Non-Executive Director of Investcom, a telecommunications company which was acquired in 2006 by MTN, a Johannesburg-based company. Berge is currently the Executive Chairman and CEO of AGBU, the largest philanthropic Armenian organisation in the world. He also serves as a Non-Executive Director on various not-for-profit organisations.

Non-Executive Director of Interaudi Bank of New York, Executive Chairman and CEO of AGBU, Non-Executive Director of The Morganti Group, Inc.

**10. Mark Williamson, CA (SA)****Non-Executive Director, 52**

Appointed Non-Executive Director in July 2007.

Chairman of Audit Committee;  
Member of the Nominations Committee and Remuneration Committee.

Mark has considerable international financial and general management experience. He joined International Power in 2000 as Group Financial Controller and was appointed to the Board as Chief Financial Officer in 2003. Previously, he was Group Financial Controller and Group Chief Accountant at Simon Group, the engineering and bulk chemicals storage group.

Serves on the Board of International Power plc.

**11. Matthew Phillips, LLB****General Counsel & Company Secretary to 30 September 2010; Group Corporate & Legal Affairs Director and Company Secretary from 1 October 2010, 40**

Appointed Company Secretary in October 2004.

Chairman of the Disclosure Committee, Chairman of the Risk Co-ordination Committee, Secretary to and Member of the Chief Executive's Committee to 30 September 2010; Operating Executive and Development Executive from 1 October 2010, Secretary to the Board and to the Audit, Nominations and Remuneration Committees. Matthew joined Imperial Tobacco's legal department in 2000 and was closely involved in the acquisitions of Reemtsma and Altadis. Previously he worked for law firms Linklaters and Burges Salmon.

No external Director appointments.



**Our commitment to maintaining high standards of corporate governance and business conduct remains fundamental to ensuring our long-term sustainability.**

## Introduction

We remain committed to high standards of corporate conduct and this report, together with the Directors' Remuneration Report, seeks to explain how in practice we apply the principles of good governance advocated by the Combined Code on Corporate Governance published in June 2008 (the Code). This report also includes the information required by the Disclosure and Transparency Rules (DTR) 7.2 to be contained in the Company's corporate governance statement, with the exception of the information required by DTR 7.2.6, which is located on page 144.

The Code sets out governance recommendations and best practice provisions which apply to UK listed companies and with which companies must either comply or provide an explanation for areas of non-compliance. The Code is publicly available on the Financial Reporting Council's website [www.frc.org.uk](http://www.frc.org.uk).

It is the Board's view that the Company has been fully compliant with the Code throughout the 2009/2010 financial year.

In light of the UK Corporate Governance Code (the Revised Code) published in June 2010 we are reviewing and, if appropriate, will enhance our governance and internal control processes. As advocated by the Revised Code, we are introducing annual re-election for all Directors with effect from our Annual General Meeting (AGM) in 2011 and, in addition, we are proposing a resolution to amend our Articles of Association accordingly.

## How we meet our governance responsibilities in practice

### A. Directors

- 1 The Board: How do we ensure the Company is headed by an effective, collectively responsible Board?
- 2 Chairman and Chief Executive: How do we ensure no one individual has unfettered powers of decision?

- 3 Board balance and independence: How do we ensure a sensible balance of Executive and Non-Executive Directors?
- 4 Appointments to the Board: How rigorous is our procedure for the appointment of new directors to the Board?
- 5 Information and professional development: How do we induct and regularly inform our Board?
- 6 Performance evaluation: How do we formally evaluate our Board and Committees' performance annually?
- 7 Re-election: How do we ensure planned and progressive refreshing of the Board?

### B. Remuneration

- 1 The level and make-up of remuneration: What is our approach to remuneration and how do we link it to performance?
- 2 Procedure: What is our formal procedure for developing our policy on executive remuneration?

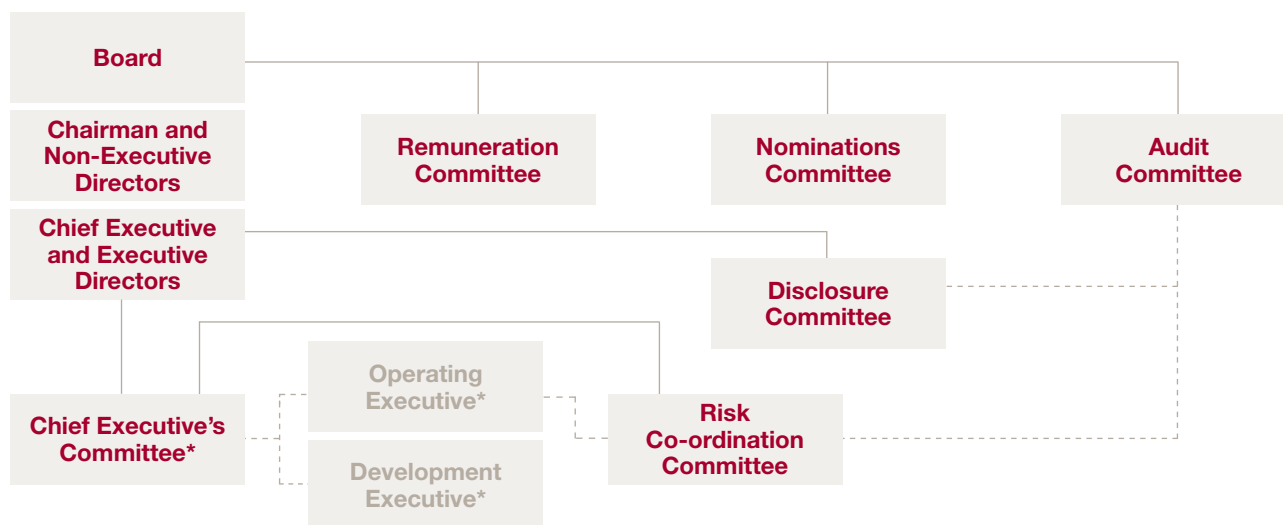
### C. Accountability and audit

- 1 Financial reporting: How do we ensure we present a clear and balanced assessment of the Company's position?
- 2 Internal control: What does our Board do to maintain a sound system of internal control?
- 3 Audit Committee and Auditors: How do we formally apply financial reporting and internal control principles?

### D. Relations with shareholders

- 1 Dialogue with institutional shareholders: How does our Board ensure that a satisfactory dialogue with shareholders takes place?
- 2 Constructive use of the AGM: How does the Board effectively use the AGM to engage with investors?

## Management and Corporate Structure



\* From 1 October 2010 the Chief Executive's Committee was replaced by the Operating Executive and Development Executive.

### A. Directors

#### 1 The Board: How do we ensure the Company is headed by an effective, collectively responsible Board?

##### Board and Board Committees

##### Board Structure

The Board met six times during the year (with two of the meetings having a duration of two days) and is scheduled to meet five times in the 2010/2011 financial year.

Our Directors for the year to 30 September 2010 are shown on page 60. Their biographies, on pages 56 and 57, demonstrate a detailed knowledge of the tobacco industry and the wider fast-moving consumer goods (FMCG) sector. This is supported with a wide range of international business and financial experience which is vital to our ongoing development and long-term sustainability. Their biographies also include details of any other major directorships.

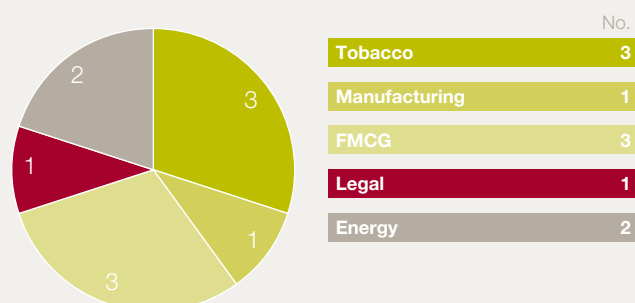
##### Board Operations

The Board is our principal decision making forum and manages overall control of the Group's affairs. Key to this control is the schedule of matters on which the Board alone may make decisions. These include approving our commercial strategy, corporate plans, major corporate activities and our financial statements, together with dividends. In addition, it is only the Board who can appoint and remove Directors and our Company Secretary.

To ensure the effective operation of our Board, the General Counsel & Company Secretary (from 1 October 2010 Group Corporate and Legal Affairs Director) provides advice on all governance and regulatory matters. He also assists the Chairman and Chief Executive in setting the agenda for each Board and Committee meeting.

All Directors are equally accountable to our shareholders for the proper stewardship of our affairs and the success of the Company. All Board and Committee meetings during the year were held in an open atmosphere with chairmen

### Director industry background/experience





## Structure of the Board and Board Committees

Board	Remuneration Committee	Nominations Committee	Audit Committee
<b>Iain Napier, Chairman</b> Alison Cooper Gareth Davis <i>(to 12 May 2010)</i> Graham Blashill Ken Burnett Jean-Dominique Comolli <i>(to 14 September 2010)</i> Robert Dyrbus	<b>Pierre Jungels, Chairman</b> Michael Herlihy Charles Knott <i>(to 17 July 2010)</i> Susan Murray Berge Setrakian Mark Williamson Matthew Phillips <i>(Secretary)</i>	<b>Iain Napier, Chairman</b> Ken Burnett Jean-Dominique Comolli <i>(to 14 September 2010)</i> Michael Herlihy Pierre Jungels Charles Knott <i>(to 17 July 2010)</i> Susan Murray	<b>Mark Williamson, Chairman</b> Michael Herlihy Pierre Jungels Charles Knott <i>(to 17 July 2010)</i> Susan Murray Matthew Phillips <i>(Secretary)</i>

encouraging robust and constructive challenge and debate. This enables our Non-Executive Directors to use their judgement, experience and independence to critically review and, where appropriate, challenge strategies proposed by management, thereby ensuring the further development of our business, effective use of our resources and maintaining our high standards of conduct. The approach ensures we act in the best long-term interests of our shareholders, while taking account of the wider community of interests represented by our employees, customers and suppliers. Where appropriate, papers presented to our Board covered environmental, community, ethical and reputational issues, thereby fully integrating them into our decision making and risk assessment processes.

During the year matters considered by the Board included the Chief Executive's succession, the evolving strategic direction of the business, a review of Group funding arrangements (specifically refinancing through Bond issues) and the continued integration of the Altadis business.

At its June 2010 meeting, senior managers from across the business presented to the Board on key strategic issues. During the year the Board also considered and approved annual and medium-term plans and operating results.

By reviewing the Group's results at each Board meeting we ensure Directors are kept informed on our progress.

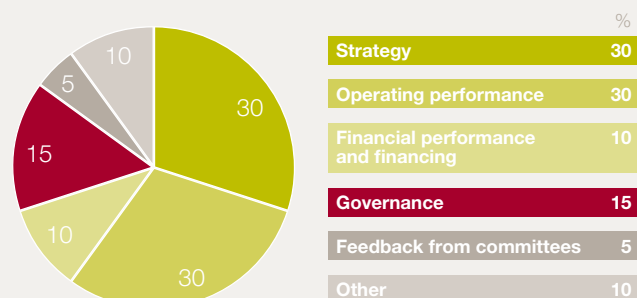
Between Board meetings, Directors are supplied with monthly performance reports, including detailed commentary and analysis. To ensure Directors were fully informed on all Committee matters, the Committee chairmen reported on the proceedings of their Committee at the subsequent Board meeting with copies of Committee minutes distributed to all Directors. Our Non-Executive Directors also had regular separate meetings at which the main item discussed was succession planning.

Our Non-Executive Directors 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 below, together with a record of each Director's attendance at Board and Committee meetings during the year.

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 chairmen of the Committees communicate regularly with the Chief Executive and other members of the Chief Executive's Committee (from 1 October 2010 the Operating Executive).

In order for Directors to fulfil their duties they can seek both independent professional advice, at our expense, and the advice and services of the General Counsel & Company Secretary and other employees.

## How the Board spends its time



As part of the Group's policy of annual review, the terms of reference for each of these Committees were reviewed and, where necessary, updated during the year and are published on our website, [www.imperial-tobacco.com](http://www.imperial-tobacco.com). They are also available from the Company Secretary.

## Meetings of the Board, Board Committees and Shareholders

	Board	Audit Committee	Remuneration Committee	Nominations Committee <sup>1</sup>	Annual General Meeting
Total number of meetings in Financial Year	6	3	4	1	1
Number of meetings attended in Financial Year					
<b>Executive Directors</b>					
Mrs A J Cooper	5/5	–	–	–	1/1
Mr G Davis <sup>2</sup>	4/4	–	–	–	1/1
Mr G L Blashill	6/6	–	–	–	1/1
Mr R Dyrbus	6/6	–	–	–	1/1
<b>Non-Executive Directors</b>					
Mr I J G Napier	6/6	–	–	1/1	1/1
Dr K M Burnett <sup>3</sup>	5/6	–	–	1/1	1/1
Mr J-D Comolli <sup>4</sup>	6/6	–	–	1/1	1/1
Mr M H C Herlihy	6/6	3/3	4/4	1/1	1/1
Dr P H Jungels	6/6	3/3	4/4	1/1	1/1
Mr C F Knott <sup>5</sup>	5/5	3/3	2/2	1/1	1/1
Ms S E Murray	6/6	3/3	4/4	1/1	1/1
Mr B Setrakian <sup>3</sup>	4/6	–	–	0/1	1/1
Mr M D Williamson	6/6	3/3	4/4	1/1	1/1

<sup>1</sup> Held in the form of a meeting of all Non Executive Directors as required by the Committee's Terms of Reference.

<sup>2</sup> Mr Davis retired from the Board on 12 May 2010.

<sup>3</sup> Dr Burnett was unable to attend one Board meeting due to travel restrictions associated with the Icelandic volcanic ash cloud. Mr Setrakian was unable to attend one Board meeting due to a family bereavement. He was also unable to attend a further Board meeting and the Nominations Committee meeting, but for both meetings gave full consideration to the matters to be discussed and provided his input to the chairmen.

<sup>4</sup> Mr Comolli resigned from the Board on 14 September 2010.

<sup>5</sup> Mr Knott resigned from the Board on 17 July 2010.

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

## Chief Executive's Committee



**Alison Cooper**  
Chief Executive

### Members

Alison Cooper

Gareth Davis (to 12 May 2010)

Graham Blashill

Robert Dyrbus

Gary Aldridge (Manufacturing Director)

Fernando Dominguez (Chief Operating Officer Cigar Business)

Matthew Phillips (General Counsel & Company Secretary, (from 1 October 2010 Group Corporate and Legal Affairs Director))

Kathryn Turner (Group Human Resources Director)

### Overview

To ensure that the business is structured to support our sustainable sales growth strategy and provide specific focus on the operational and development agendas of the business, we have established two cross-functional teams: the Operating Executive and the Development Executive, which replaced the Chief Executive's Committee on 1 October 2010.

The Chief Executive's Committee comprised all our Executive Directors together with our Manufacturing Director (who left the business on 30 September 2010), Group Human Resources Director, Chief Operating Officer Cigar

Business and the General Counsel & Company Secretary (from 1 October 2010 Group Corporate and Legal Affairs Director). It met 13 times during the year.

### Responsibilities

The responsibilities of the Committee included:

- reviewing and subsequently recommending to the Board changes to Group Strategy;
- ensuring effective implementation of Group strategy;
- reviewing accounting information prior to submission to the Board; and
- ensuring the use and level of the Group's resources are optimised.

### How the Chief Executive's Committee Met its Responsibilities During the Year

To ensure the effective implementation of Group strategy and policy our Board delegated authority of the day-to-day operation of the business to our Chief Executive and the Chief Executive's Committee. This delegation was, however, subject to the schedule of matters on which the Board alone is able to decide and those on which only our shareholders are able to decide.

In addition to implementing our strategy and ensuring that the use and level of the Group's resources are optimised and effectively managed, the Committee oversaw all the Group's activities, forecasts, policies and operations. As part of this review process the Committee developed and recommended to the Board changes in strategy to enable us to achieve our overall objective of creating sustainable shareholder value.

## Operating Executive

### Members

Alison Cooper	Matthew Phillips ( <i>Group Corporate and Legal Affairs Director</i> )
Robert Dyrbus	Walter Prinz ( <i>Group Manufacturing Research &amp; Development Director</i> )
Graham Blashill	Kathryn Turner ( <i>Group Human Resources Director</i> )
Helen Clatworthy ( <i>Group Supply Chain Director</i> )	
Fernando Dominguez ( <i>Chief Operating Officer Cigar Business</i> )	

### Overview

The Operating Executive, which will meet monthly, was established on 1 October 2010 and comprises all our Executive Directors together with our Group Supply Chain Director, Chief Operating Officer Cigar Business, Group Corporate and Legal Affairs Director, Group Manufacturing, Research & Development Director and the Group Human Resources Director.

### Responsibilities

The responsibilities of the Operating Executive include:

- preparing, and measuring performance against, the operational plan of the business and updating the plan where appropriate ensuring the Group achieves its financial and non-financial targets;
- setting and implementing the change agenda;
- ensuring the cross-functional operational performance of the business is delivering against our growth strategy;
- implementing the Group's risk management and internal control processes within the framework set by the Board;
- ensuring the Group's employees have the appropriate capabilities through development and succession plans for key roles; and
- effective internal and external communications.

## Development Executive

### Members

Alison Cooper	Claudio Righetti ( <i>Director, Strategy and Foresight</i> )
Graham Blashill	Conrad Tate ( <i>Corporate Development Director</i> )
Matthew Phillips ( <i>Group Corporate and Legal Affairs Director</i> )	
Mike Ashton ( <i>Head of Business Performance Planning</i> )	

### Overview

The Development Executive, which will meet monthly, was established on 1 October 2010 and comprises our Chief Executive; Group Sales and Marketing Director; Group Corporate and Legal Affairs Director; Head of Business Performance Planning; Director, Strategy and Foresight; and the Corporate Development Director.

### Responsibilities

The responsibilities of the Development Executive include:

- leading the process to define the Group's strategy;
- providing specific focus on the planning and development agendas of the business; and
- managing the corporate planning process.

### 2 Chairman and Chief Executive: How do we ensure no one individual has unfettered powers of decision?

Our Chairman and Chief Executive have clearly defined and separate responsibilities. However, they retain a close working relationship and meet regularly between formal 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 and profitable delivery of our strategy.

Through his effective leadership of the Board, our Chairman ensures all Directors are able to effectively contribute to discussions such that the Group fully benefits from their wide range of skills and experience. Supported by our Senior Independent Non-Executive Director, the Chairman is responsible for our effective communication with shareholders and ensuring they can raise any concerns.

Our Chief Executive, supported by the Chief Executive's Committee (from 1 October 2010, the Operating Executive and the Development Executive) which she chairs, is responsible for the successful implementation of the strategies and objectives set by the Board together with the day-to-day leadership of the Group.

### 3 Board balance and independence: How do we ensure a sensible balance of Executive and Non-Executive Directors?

We see having a Board with the right skill set as vital to our ongoing success and expansion. As evidenced by their biographies on pages 56 and 57, our Executive Directors are all experts in their specific roles and, in addition, have a wealth of experience in the wider tobacco industry. This is complemented

**“To us good governance means ensuring the processes in place are appropriate to take the business in the right strategic direction.”**

**Alison Cooper**  
Chief Executive

and supplemented by our Non-Executive Directors who bring a wide range of business and financial expertise to the Board, for example, from the wider FMCG, financial and legal sectors together with specific regional knowledge.

We believe the Board remains well balanced and appropriately constituted. The Board currently has 10 Directors: our Non-Executive Chairman, three Executive Directors and six independent Non-Executive Directors.

Mr J-D Comolli, who resigned from the Board with effect from 14 September 2010, was not classified by the Company as independent for the purposes of the Code when determining the composition of our Board and its Committees, due to his Chairmanships of certain subsidiaries within our Group and his provision of consultancy services.

Dr P H Jungels is our Senior Independent Director with whom we encourage shareholders to raise any concerns.

Following its annual evaluation (page 65) and review of potential conflicts of interest, the Board concluded at its meeting in September 2010 that all our Non-Executive Directors continue to contribute effectively and constructively to Board debate. This evaluation also concluded that our Non-Executive Directors continue to objectively challenge and robustly question management and at all times have the best interests of our stakeholders in mind. We, therefore, confirm that, with the exception of Mr Comolli (until his resignation on 14 September 2010) and our Chairman (who was only required to meet the independence criteria of the Code on appointment), our Non-Executive Directors remain independent as defined in the Code.

To address the provisions of Section 175 of the Companies Act 2006 (the Act) relating to conflicts of interest, our Articles of Association allow the Board to authorise situations in which a Director has, or may have, a conflict of interest.

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

Since adopting these procedures 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 we reviewed and reconsidered all situations entered in the Conflicts Register at our Board meeting in September 2010. We intend to perform this review and reconsideration annually.

Following the above notifications and annual review the Board is satisfied there is no compromise to the independence of those Directors who have board appointments or relationships with companies outside the Group. In order to underpin his independence we entered into an agreement with Mr B Setrakian on 25 June 2008 to minimise the risk of any conflict of interest between Dewey & LeBoeuf LLP, of which he is a partner, and the Company. This agreement remains in full force and effect and the Board confirms his compliance with its terms and, therefore, his continued independence.

## Nominations Committee



**Iain Napier**  
Chairman

### 4 Appointments to the Board: How rigorous is our procedure for the appointment of new directors to the Board?

#### Members

Mr I J G Napier, *Chairman*

Dr K M Burnett

Mr J-D Comolli  
(to 14 September 2010)

Mr M H C Herlihy

Dr P H Jungels

Mr C F Knott (to 17 July 2010)

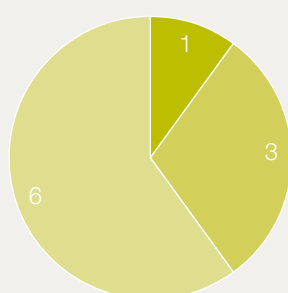
Ms S E Murray

Mr B Setrakian

Mr M D Williamson

Mr M R Phillips (*General Counsel & Company Secretary from 1 October 2010 Group Corporate and Legal Affairs Director*), acts as *Secretary to the Committee*

## Balance of Executive and Non-Executive Directors



	No.
Chairman	1
Executive	3
Non-Executive	6



**Overview**

The Nominations Committee comprises all our Non-Executive Directors and meets as required.

The Committee's terms of reference state that the succession of the Chief Executive is a matter reserved for meetings of all Non-Executive Directors rather than the Nominations Committee. Accordingly, due to the focus of nomination matters during the year being the succession of the Chief Executive, all nomination items were considered at meetings of the Non-Executive Directors.

Nomination matters considered by the Non-Executive Directors were reviewed as part of the Board performance evaluation process.

**Responsibilities**

The responsibilities of the Committee include:

- evaluation of the balance of skills, knowledge and experience of our Board;
- development of role specifications;
- formulation of succession plans; and
- making recommendations to the Board with regard to the appointment of directors.

**How the Nominations Committee Met its Responsibilities During the Year**

The appointment of the Chief Executive involved a rigorous process including the consideration of prospective candidates' performance and interviews together with internal and external benchmarking.

Following this rigorous process a formal meeting of the Non-Executive Directors recommended to the Board the appointment of Mrs A J Cooper to the position of Chief Executive. In addition to this formal meeting, the Non-Executive Directors held a number of other meetings and discussions concerning Board succession planning and other nomination matters.

**Board Changes**

We continually review the composition and balance of our Board to ensure we have the right structure, skills and expertise in place for the effective management of our multinational business.

Following approval by our Board on 9 November 2009, Mrs A J Cooper was appointed Chief Executive with effect from 13 May 2010.

On 17 July 2010 our Board accepted Mr C F Knott's resignation and on 3 August 2010 our Board accepted Mr J-D Comolli's resignation with effect from 14 September 2010.

**5 Information and professional development: How do we induct and regularly inform our Board?**

We have a detailed induction and briefing programme for Directors on appointment to the Board which is tailored to each Director's needs, taking into account their individual qualifications and experience.

Our programme includes meetings with our advisers and key employees from major functions together with site visits. These meetings also include briefings on corporate responsibility and corporate affairs issues, legal matters, product stewardship, environmental management, social impact, scientific and regulatory affairs and commercial risk management.


Ongoing training is available to all Directors to meet their individual needs. We also provide regular briefings to Directors on relevant issues such as legislation and regulation changes and corporate governance developments. For example, during the year our legal advisers gave a presentation to the Board in respect of Directors' duties and liabilities.

During our September 2010 Board meeting Directors visited our operations in France where they met senior managers and received detailed presentations on our French operations.

The Audit and Remuneration Committees also received briefings from our Auditors, PricewaterhouseCoopers LLP, and remuneration adviser, Hewitt New Bridge Street, respectively to ensure they remain up-to-date with current regulations and developments.

**“We are confident the Directors have the skills and expertise to successfully deliver our strategy.”**

**Iain Napier**  
Chairman

 The Committee's terms of reference are published on our website, [www.imperial-tobacco.com](http://www.imperial-tobacco.com)

## 6 Performance evaluation: How do we formally evaluate our Board and Committees' performance annually?

During the year, with the assistance of an external consultant, our Board formally reviewed and evaluated its performance, together with the performance of its Committees and individual Directors. Feedback from each Director was obtained through detailed questionnaires which were used as the basis for the overall evaluation of the Board and its Committees and feedback discussions between each Director and the Chairman. The results were discussed by the Board at its meetings in September 2010 and October 2010.

Our Senior Independent Director met with the Non-Executive Directors and the Board, without the Chairman present, to consider the performance of the Chairman.

After taking account of the results of the Chairman's formal performance evaluation our Senior Independent Director provided feedback to the Chairman on a one-to-one basis.

The Chairman held meetings exclusively with the Non-Executive Directors to consider, amongst other things, succession issues and the performance of the Executive Directors.

Informed by the evaluation, the Board and its Committees are satisfied they are operating and performing effectively. The evaluation did not identify any significant areas for concern nor any requirement to provide extra training for our Directors. It also confirmed that all our Directors have sufficient time, knowledge and commitment to contribute effectively to our Board and its Committees and that, following the Board changes during the year, it remains appropriately constituted in terms of the Code (and the Revised Code) and skill set.

The main area identified for review was the future size and structure of the Board, including the competencies required of potential new Non-Executive Directors who may be appointed when current Non-Executive Directors retire without seeking re-election.

Following the 2009 Board evaluation, in order to assist with Executive Director succession planning which was identified in the evaluation as the main theme requiring Board

attention, senior managers attended a number of strategy days, Board meetings and Board dinners. Further succession planning also continued to be discussed at Non-Executive Director meetings held during the year.

In order to obtain maximum value from the annual evaluations and to benefit from the varying skills and focuses of alternative facilitators, we may consider alternative facilitators, formats and approaches in future years. This will ensure our evaluations remain appropriate to the requirements of the Chairman and Board and the recommendations in the UK Corporate Governance Code published in June 2010.

## 7 Re-election: How do we ensure planned and progressive refreshing of the Board?

Following a rigorous selection process and recommendation by the Nominations Committee, Directors are appointed by the Board. They must, however, submit themselves for election by shareholders at the AGM following their appointment and, with effect from our 2011 AGM, annually thereafter in accordance with the recommendations of the Revised Code and the proposed new articles of association of the Company.

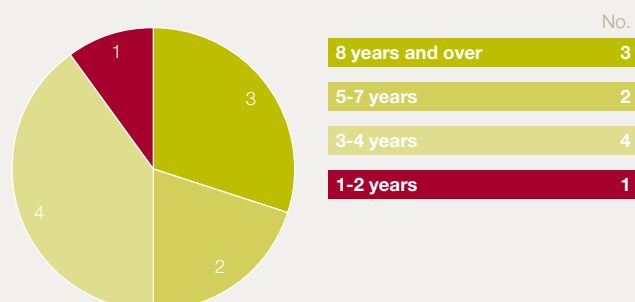
The performance of each Director is considered as part of the Board evaluation, before recommending such election or re-election. Following this evaluation the Board recommends the re-election of all Directors at our 2011 AGM.

We recognise that a number of shareholders have expressed concern that annual re-election of Directors could encourage them to take a short-term view. We are, however, confident that our remuneration policies encourage Directors to act in the best long-term interests of stakeholders, for example through long term incentive plans and shareholding requirements.

In order to facilitate smooth Board refreshment we regularly review the composition, skill set and balance of our Board, together with the length of service of each Director and thereby identify the skills required of future directors.

Our Senior Independent Director, who is also the Chairman, of the Remuneration Committee, is approaching nine years' service as a Non-Executive Director. This will be considered during the year as part of the regular review of the structure of the Board.

## Tenure of Directors



## Internal control framework



## B. Remuneration

### 1 The level and make-up of remuneration: What is our approach to remuneration and how do we link it to performance?

We ensure that our remuneration policy drives our employees to enhance our performance by focusing remuneration towards long-term performance and providing employees with the opportunity to participate in our bonus arrangements and share plans. Our overall policy is to provide remuneration at the median level of our comparator group and provide executives with the opportunity to earn upper quartile total compensation on achievement of superior business performance.

Our Remuneration Report, on pages 78 to 95, approved by our Remuneration Committee and Board, outlines our remuneration strategy and policy and its links to our key performance indicators. The Report details the Committee's activities over the financial year and contains full details of Directors' emoluments.

We evaluated the performance of the Committee as part of the Board performance evaluation process described above.

### 2 Procedure: What is our formal procedure for developing policy on executive remuneration?

Our Remuneration Committee, which solely comprises independent Non-Executive Directors, operates under clear terms of reference and is responsible for developing policy on executive remuneration and overseeing our overall remuneration policy. Full details of our procedure for developing remuneration policy and its links to strategy and risk management are given in our Remuneration Report on pages 78 to 95.

## C. Accountability and audit

### 1 Financial reporting: How do we ensure we present a clear and balanced assessment of the Company's position?

Our Board members recognise their responsibilities to ensure that the statutory requirements to deliver balanced and understandable assessments of the Company's position

are met. The Board is satisfied that these responsibilities are met by using the financial systems and applying the regulations described below, supported by our system of internal control.

This was achieved by:

- using an appropriate system of accounting records, capable of operating with reasonable accuracy and in compliance with local and international financial and legal reporting requirements. The basis used to prepare our Group financial statements is the International Financial Reporting Standards (IFRS) as adopted by the European Union. Our parent company financial statements and our Directors' Remuneration Report are prepared in accordance with applicable law and United Kingdom Generally Accepted Accounting Principles;
- using IFRS to ensure a true and fair view of the state of affairs of the Group is given, including our profit or loss for the period;
- deploying appropriate accounting policies within the framework of IFRS and ensuring these are consistently applied;
- making judgements and preparing estimates that are reasonable and prudent;
- operating within the guidelines of all the disclosure advice provided by UK and international statute;
- disclosing the business is a going concern;
- maintaining robust assurance processes and controls over our financial reporting procedures, including suitable Disclosure Committee and Board reviews; and
- extending these principles to half yearly reports and other reports in the public domain.

### 2 Internal control: What does our Board do to maintain a sound system of internal control?

#### Overview

Several ongoing activities, which satisfy the requirements of the Code, reassure our Board that a sound and robust system of internal control exists throughout our Group.

The Board recognises that we operate in an environment with some unavoidable risks (see pages 25 to 27) and ensures these risks are properly understood and suitably managed, either directly or by exercising oversight of the internal control framework detailed below. The analysis of risk and oversight of the resulting internal control measures taken to mitigate the effects of such risks are essential in enabling the Board to discharge its responsibilities to safeguard shareholders' investments, protect our assets and provide reliable financial information. Given the size and complexity of the Group such systems can, however, provide only reasonable and not absolute assurance of meeting our internal control objectives, as they manage rather than eliminate risk. They can, therefore, only provide reasonable and not absolute assurance against material misstatement or loss.

### Control Environment

The Board acknowledges that it is responsible for the Group's systems of internal control and for reviewing its effectiveness and has established a robust control environment, the key features of which are outlined in the above chart and detailed below:

- the terms of reference of the Board, including the matters on which only the Board can decide, and each of the committees it has established (see page 67);
- establishing an appropriate organisational structure with clear, appropriate and documented delegation of authority from the Board to the Chief Executive's Committee (from 1 October 2010 the Operating Executive) and executive management, including the Group's Treasury function (see page 67);
- bringing together our anti-illicit trade strategies, the protection of our brands and the management and roll-out of our Code of Conduct into a single Commercial Integrity Department (see page 67);
- the Risk Co-ordination Committee and Risk Assessment Summaries which detail the risks and risk mitigation identified by each area of the business (see page 68);
- our year end certification processes (see page 68);
- Internal Control Questionnaires detailing the existing control processes within each area of the business (see page 68);
- Group Finance which sets financial policies and standards and manages our financial reporting processes (see page 68);
- the Disclosure Committee which reviews all our major financial disclosures (see page 69);
- Group Compliance which monitors and reviews our internal controls (see page 69); and
- remuneration linked to long-term performance to discourage excessive risk taking.

Taking each in turn:

### Terms of Reference

The Board, which operates within clearly defined terms of reference, reserves certain matters for its own consideration and decision. It has established appropriate committees, which also operate within clearly defined terms of reference, to oversee our control activities. These committees include an Audit Committee, Disclosure Committee and Risk Co-ordination Committee. Our Board and Committee processes, together with those embedded in the business, are fundamental to the effectiveness of our internal control measures and the delivery of the appropriate degree of control.

### Organisational Structure

The Board regularly reviews the Group's organisational structure to seek to ensure that clearly defined lines of responsibility with appropriate delegation of authority and segregation of duties exist, with personnel of the necessary calibre in place to fulfil their roles. The aim of such delegated authority is that decisions, significant because of either their value or impact on other parts of the Group, are taken at an appropriate level as defined within the Board's terms of reference and our Corporate Documents.

The Board regularly reviews the Group's Treasury, Tax and Occupational, Health, Safety and Environmental policies. The Group's Treasury function operates within a well defined policy and framework designed to manage the Group's financing and liquidity arrangements and to manage its exposure to, amongst other treasury risks, interest rate and foreign exchange risks. In addition, the Group operates well defined procedures for appraisal, approval, control and review of capital and strategic expenditure, including acquisitions.

### Commercial Integrity

Supporting the sustainable growth of our business by enhancing our anti-illicit trade activities, together with further embedding high standards of conduct across the Group, is critical to our future success.

During the year we brought together into a single Commercial Integrity Department those activities with responsibility for reviewing and managing the enhancement by the business of our anti-illicit trade strategies, the protection of our brands and the driving of good corporate and individual conduct across the Group.

Together with the Group Company Secretariat, our Commercial Integrity Department supports our framework of policies and procedures, with which all employees are expected to comply. These policies and procedures cover key issues such as acceptable business practices, ethical compliance matters and legislation, physical and data security as well as regulatory, governance and health, safety and environmental issues.

By the end of December 2010 the updated Code of Conduct, which sets out the standards of responsible behaviour that all our employees are expected to follow, will have been rolled-out to our senior management population in a series of face-to-face workshops and cascade to the wider organisation commenced. Initially available in eight languages, the Code of Conduct is published on our website ([www.imperial-tobacco.com](http://www.imperial-tobacco.com)).



It is anticipated that the roll-out of our Code of Conduct training, to the wider employee base, will be completed during 2011. We are also embedding an e-learning system to further support this training. Our Code of Conduct forms a key part of our preparations for ensuring compliance with the UK Bribery Act.

Our public interest disclosure (whistleblowing) policy encourages employees to raise concerns about something seriously wrong or dangerous on a confidential basis, such that proportionate and independent investigation of such matters can be undertaken.

We thoroughly investigate all allegations of misconduct and irregularity and consider the implications for our control environment. We are in the process of investigating certain allegations which include fraud within one of our markets. Based on our investigations to date, we do not currently believe that these matters have a material impact on our control environment or will give rise to any material liability to the Group.

### Risk Co-ordination Committee and Risk Assessment Summaries

## Risk Co-ordination Committee



**Matthew Phillips**  
Chairman

### Members

General Counsel & Company Secretary (from 1 October 2010 Group Corporate and Legal Affairs Director) (Chairman)

Director, Commercial Integrity

Head of Group Compliance

Senior Corporate Counsel

Director of Accounting, Forecasting & Tax

General Manager, Product Development and Purchasing

Commercial Director, Sales and Marketing

Commercial Director, Supply Chain

Finance Director, Cigar Business Unit

Head of Group Security and Risk Management

Human Resources Director, Sales and Marketing

Senior Commercial Counsel (acts as Secretary to the Committee)

### Overview

To supplement our existing risk management processes, the Group has established a Risk Co-ordination Committee (RCC).

The RCC assists the Chief Executive's Committee (from 1 October 2010 the Operating Executive) and the Audit Committee in overseeing the management of material risk to the Group. The RCC comprises senior managers representing a cross section of the Group's functions.

### Responsibilities

The responsibilities of the RCC include:

- establishing a consistent methodology for identifying, assessing and ranking material risks;

- the identification and assessment of existing measures in place to manage and mitigate risks; and
- focusing and, where relevant, enhancing risk management and mitigation activities, processes and procedures across the Group.

### How the Risk Co-ordination Committee Met its Responsibilities During the Year

During the course of the year the RCC has continued to develop our risk register by identifying, assessing and monitoring the key risks we face and how such risks are mitigated and managed.

This top down approach is complemented by a bottom up approach requiring individual markets, factories, regions and functions across the Group to produce annual risk assessment summaries which are compared to the Group risk register. These rolling risk assessment summaries identify major areas of business risk including any specific local risks and demonstrate how these are mitigated and managed by controls embedded in business processes.

### Year End Certification

Our year end certification process requires each of our business entities to confirm compliance with our policies and fraud prevention processes, and that risk mitigation controls have operated effectively throughout the year. All our senior managers are also required to certify that there have been no related party transactions within their areas of control.

### Internal Control Questionnaires

Each of our business entities is required to maintain a suite of internal control questionnaires (ICQs) based on templates produced by Group Compliance. Management within each business entity is required to continually update the ICQs detailing the internal control processes in operation within that entity.

These ICQs form the basis of periodic reviews by Group Compliance who ensure that appropriate controls are operating in practice and provide adequate protection for the business.

### Group Finance

Our Group Finance Department sets financial policies and standards. It also manages our financial reporting processes to ensure the information which enables our Board to discharge its responsibilities, including the production of our Half Year and Annual Accounts, is provided on a timely basis. It 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.

Monitoring of our financial position is based on our strategic and operational plans (the Plans) which we use to identify specific targets and objectives.

Throughout the year we produce 'latest estimates' to predict the likely year end position. The latest estimates are compared with the Plans and enable us to monitor and check our performance and, where appropriate, challenge sections of the business if actual or anticipated performance varies from the Plans.

## Assurance process for financial reporting



## Disclosure Committee

**Matthew Phillips**  
Chairman

### Members

General Counsel & Company Secretary (from 1 October 2010 Group Corporate and Legal Affairs Director) (Chairman)  
Head of Group Compliance (Co-ordinator)  
Director, Commercial Integrity

Senior Corporate Counsel  
Director of Accounting, Forecasting & Tax  
Head of Corporate Communications  
Deputy Company Secretary (Acts as Secretary to the Committee)

### Overview

The Disclosure Committee comprises senior management from across our business and meets, as required, in order to consider major financial disclosures.

### Responsibilities

The responsibilities of the Committee include:

- ensuring appropriate procedures exist to confirm the accuracy, completeness and timeliness of our public financial disclosures; and
- assisting our Chief Executive and Finance Director (Senior Officers) in determining that all major financial disclosures are accurate, complete and contain all necessary disclosures and, therefore, provide a fair and accurate view of our performance.

### How the Disclosure Committee Met its Responsibilities During the Year

The Disclosure Committee reviewed all major financial disclosures including Trading Updates, Interim Management Statements, Half Year Report, Annual Report and Accounts and appropriate corporate financing documentation.

To meet its responsibilities when reviewing these major financial disclosures the Committee members made enquiries into all aspects of the business which, together with their own business knowledge, ensured disclosures were complete with no material issues omitted. The Committee reported on its reviews to our Senior Officers and, where appropriate, our Audit Committee.

The terms of reference of the Disclosure Committee were reviewed during the year to ensure they continued to be appropriate.

### Group Compliance

Our Group Compliance function monitors and measures the mitigation of risks across the Group, in addition to performing its internal audit role. During the course of each year it undertakes both targeted scheduled and ad hoc reviews throughout our businesses. The reviews are based on our ICQs. Each review results in a report to local management of the business entity identifying any potential control weaknesses which the business entity is responsible for remediating. The most significant potential weaknesses are also elevated to the Chief Executive's Committee (from 1 October 2010 the Operating Executive) to monitor the remediation proposed and subsequently undertaken by management of the business entity. At the year end Group Compliance also conducts a review of risk assessments submitted by all markets, factories, regions and functions across the Group and obtains certificates of confirmation from local management teams that appropriate internal controls and processes have been operating within their businesses throughout the year.

Group Compliance is influenced by the methodologies and characteristics of the "COSO" guidelines. Practices based on these guidelines were established under the requirements for Sarbanes-Oxley Act compliance and, subsequent to our de-registration in the USA, the most value added elements have, wherever appropriate, been retained within the business.

To support the Audit Committee and the Board in assessing the effectiveness of internal controls, Group Compliance formally reports to the Audit Committee on the outcome of its ongoing activities, including its programme of compliance reviews and any more general business reviews. This process ensures that the Audit Committee remains satisfied that the Group's exposure to major business risks is minimised and the levels of retained risk are acceptable. Group Compliance has a programme of reviews covering all our business entities on an annual, three or five yearly cycle dependent on materiality and perceived risk.

The above processes, together with reports from Group Compliance, enable the Board, either directly or through the Audit Committee, to regularly review the effectiveness of the key procedures which have been established in order to provide appropriate internal controls.

The Board confirms that an ongoing process for identifying, evaluating and managing the Group's significant risks has operated throughout the year and up to the date of the approval of this Annual Report and Accounts in accordance with the requirements of the Code and Turnbull guidance. Measures are also being undertaken to review the contents of, and the Group's compliance with, the new UK Corporate Governance Code which replaces the Combined Code during our 2011 financial year.

### 3 Audit Committee and Auditors: How do we formally apply financial reporting and internal control principles?

## Audit Committee



**Mark Williamson**  
Chairman

### Members

Mr M D Williamson, CA (SA)  
(Chairman)  
Mr M H C Herlihy  
Dr P H Jungels  
Mr C F Knott, FCMA (to 17 July 2010)

Ms S E Murray  
Mr M R Phillips (General Counsel  
& Company Secretary (from 1 October  
2010 Group Corporate and Legal  
Affairs Director), acts as Secretary to  
the Committee)

### Overview

The Audit Committee oversees our financial reporting and internal controls and provides a formal reporting link with our Auditors.

### Responsibilities

The responsibilities of the Audit Committee include:

- approval of accounting policies;
- reviewing financial statements and announcements;
- overseeing the Group's internal control processes;

- appointment of Auditors and monitoring their performance and independence; and
- overseeing our public interest disclosure policy.

### Structure

The Audit Committee comprises four Independent Non-Executive Directors. In line with the Code and our Audit Committee's terms of reference, available on our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com), it is a requirement that at least one Committee member is a financial expert. Mr M D Williamson is a qualified accountant and, therefore, meets this requirement.

The Finance Director, the Director of Accounting, Forecasting & Tax, the Head of Group Compliance, the Deputy Company Secretary and other financial managers are invited to attend each meeting of the Committee. The Head of Group Compliance meets formally with the Committee, without any Executive Director or other manager being present, at each Committee meeting.

To provide a direct line of communication between our Auditors and Non-Executive Directors, our Auditors attend each Committee meeting and have the opportunity to meet Committee members without any Executive Director or other manager present.

The performance of the Committee was evaluated as part of the Board performance evaluation process.

### How the Audit Committee Met its Responsibilities During the Year

During the year and up to the date of approval of this Annual Report and Accounts, our Audit Committee achieved its responsibilities by working with a structured agenda of matters focused to coincide with key events of our financial reporting cycle, together with standing items that the Committee is required to consider at each meeting. The Audit Committee met its responsibilities by:

- approving our accounting policies;
- monitoring and reviewing the integrity of our financial statements and any announcements or judgements they contain including our Half Year Report and Annual Report and Accounts and recommending that these be approved by our Board;

**“In order to ensure the independence and objectivity of our Auditors we maintain and regularly review our Auditor Independence Policy.”**

**Mark Williamson**  
Audit Committee Chairman

- receiving reports from, and questioning, members of Group Compliance, Group Finance and other functions. This provides the Committee with the information required to oversee our systems of internal control for financial reporting, internal control policies, corporate governance procedures, the system of risk management and to assess the review and mitigation of associated risks;
- reviewing the Auditors' presentation of their proposed audit plan, fee proposal and confirmation of their independence. This, together with management's assessment of the Auditors' effectiveness and independence, allows the Committee to establish the scope, effectiveness, independence and objectivity of our Auditors and, if appropriate, recommend their re-appointment to the Board;
- receiving and, after due consideration, approving Group Compliance's proposed work plan and compliance programme for the year. Reports from Group Compliance are then used to monitor the performance and effectiveness of controls operating throughout the business;
- overseeing our public interest disclosure (whistleblowing) policy by receiving reports of its distribution through our non-financial reporting system and receiving reports in respect of all disclosures made via the policy;
- consideration of management's report that there were no material related party matters; and
- consideration of the accounting treatment relating to ongoing enquiries detailed on pages 76 and 77.

#### Going Concern

In order to satisfy themselves that we have adequate resources for the future, the Committee and subsequently the Board reviewed the Group's committed funding and liquidity positions, its ability to generate cash from trading activities and its ability to raise external funding in the future. Our performance, as described in the Financial Review on pages 28 to 31, and our future plans and the risks we face, as described on pages 25 to 27, were also reviewed.

These reviews provided the Committee with the confidence to recommend to the Board that the Group and Company have adequate resources to meet their operational needs for the foreseeable future. For this reason the Board continues to adopt the going concern basis in preparing the financial statements.

#### Auditor Independence Policy

In order to ensure the independence and objectivity of our Auditors we maintain and regularly review our Auditor Independence Policy. This policy provides clear definitions of services that our Auditors can and cannot provide. Our Auditors may only provide non-audit services where those services do not conflict with their independence, for example tax compliance work. The policy also establishes a formal authorisation process, including the tendering for non-audit services expected to generate fees in excess of £100,000, and pre-approval by the Audit Committee for allowable non-audit work that they may perform. Our policy also establishes guidelines for the recruitment of employees or former employees of our Auditors and for the recruitment of our employees by the Auditors. Details of the audit and non-audit fees paid to the Auditors are shown on page 114.

To ensure compliance with this policy our Audit Committee carried out two reviews during the year of the remuneration received by our Auditors for audit services, audit-related services and non-audit work. These reviews ensure a balance of objectivity, value for money and compliance with this policy. The outcome of these reviews was that performance of the relevant non-audit work by our Auditors was the most cost-effective way of conducting our business and that no conflicts of interest existed between such audit and non-audit work. The fees for such non-audit work within the financial year were principally related to tax advisory work.

These reviews enabled the Audit Committee to confirm that we continue to receive an efficient, effective and independent audit service.

## Proactively Engaging with Shareholders

In September 2010 we held an investor day attended by over 60 investors, potential investors and analysts at which they had the opportunity to meet members of the Board and senior management. The central theme of the day was our strategy to deliver sustainable shareholder returns through our sales led agenda. Case studies were provided illustrating the success of our strategy in various markets. Topics discussed included the opportunities provided by our geographic footprint, brands and our total tobacco approach, together with innovation and trade marketing.

 Our Auditor Independence Policy is published on our website, [www.imperial-tobacco.com](http://www.imperial-tobacco.com)



**Statement of Auditors' Responsibilities**

Our statutory Auditors, PricewaterhouseCoopers LLP (PwC), are responsible for forming an independent opinion on the financial statements of the Group and on the financial statements of the Company as presented by the Directors, on other elements of the Annual Report and Accounts as required by legislation or regulation and for reporting their opinion to members (page 97).

PwC have been the Company's Auditors since its demerger in 1996. The Audit Committee, following a review during the year, remains satisfied with the effectiveness and independence of PwC. It has not, therefore, considered it necessary to require the audit to be put out to tender. 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). There are no contractual or similar obligations restricting the Group's choice of external auditor.

**D. Relations with Shareholders****1 Dialogue with shareholders: How does our Board ensure that a satisfactory dialogue with shareholders takes place?**

Dialogue with our shareholders is given the highest priority. During the year our Director of Investor Communications ensured the Group met its commitment to keep shareholders fully informed.

**Communication with Shareholders**

The primary means of communication with shareholders is via our Annual Report and Accounts, Half Year Report and website. In addition, we provided Interim Management Statements and Trading Updates. We have attended numerous conferences, where we presented various aspects of the business to shareholders and potential shareholders. Our Executive Directors and investor relations team met with investors after results announcements, as part of conferences and on an ad hoc basis. They also provide a point of focus for investors who wish to raise queries or concerns.

Our Chairman met with a number of key shareholders during the year and our Senior Independent Non-Executive Director was also available to meet key investors. All Directors made themselves available to meet shareholders at our AGM after

the formal business of the meeting. Together the Chairman, Chief Executive, Finance Director and Director of Investor Communications ensured the Board was fully briefed on shareholders' views such that any issues or concerns were fully understood and considered by the Board. We regularly met both with shareholder representative bodies on significant issues of interest and with corporate governance representatives of investors when requested. Through an external consultancy we undertook our annual perception study of institutional investors' views of our business.

**2 Constructive use of the AGM: How does the Board effectively use the AGM to engage with investors?**

The primary means of communication with the majority of our shareholders, who have not requested paper copies of our documentation, is through our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com). To ensure our shareholders have time to consider our Annual Report and Accounts and Notice of the AGM and lodge their proxy votes they are mailed more than 20 working days prior to the meeting.

We offer all our shareholders the choice of submitting proxy votes either electronically or in paper format. We also offer them the ability to abstain.

Our AGM provides a valuable opportunity for shareholders to meet and question our Directors. At the AGM our Chairman and Chief Executive gave presentations on our performance and current business activities.

To ensure compliance with the Code, at all general meetings separate resolutions are proposed on each discrete subject and all resolutions are put to a poll. The number of proxy votes for, against and withheld for each resolution are displayed at the meeting. The final results are published through a Regulatory Information Service and on our website following each AGM.

At our 2010 AGM we received votes representing approximately 72 per cent of our issued share capital (excluding shares held in treasury).

Full details of our AGM to be held on Wednesday 2 February 2011, together with explanations of the resolutions to be proposed, are contained in the Notice of Meeting available on our website ([www.imperial-tobacco.com](http://www.imperial-tobacco.com)) and, where applicable, posted with this Report.

**“Good governance also means ensuring we treat our stakeholders in a fair and just manner.”**

**Matthew Phillips**

Group Corporate & Legal Affairs Director

# Directors' Report: Other Information

The Directors submit their report together with the audited consolidated financial statements of the Group and the accounts of the Company for the year to 30 September 2010.

## Financial Results and Dividends

We include a review of our operational and financial performance, current position and future developments in our Directors' Report: Strategy, Performance and Governance sections on pages 6 to 95.

The profit attributable to equity holders of the Company for the financial year was £1,505 million as shown in our consolidated income statement on page 98. Note 1 to the financial statements gives an analysis of revenue and profit from operations and net assets.

The Directors have declared and proposed dividends as follows:

In £s million	2010	2009
Ordinary Shares		
Interim paid, 24.3p per share (2009: 21.0p)	246	213
Proposed final, 60.0p per share (2009: 52.0p)	609	527
Total ordinary dividends, 84.3p (2009: 73.0p)	855	740

The final dividend, if approved, will be paid on 18 February 2011 to our shareholders on the Register of Members at the close of business on 21 January 2011. The associated ex dividend date will be 19 January 2011. We paid an interim dividend on 20 August 2010 to shareholders on the register at the close of business on 23 July 2010.

## Share Capital

Details of our share capital are shown in note 20 to the Financial Statements. All shares, excluding those held in treasury, are freely transferrable and rank pari passu for voting and dividend rights. At our AGM on 2 February 2010 shareholder authority for the buyback of up to 106,794,000 ordinary shares of 10 pence each was obtained. We hold 49,569,000 of our ordinary shares in treasury, which represent 4.9 per cent of issued share capital and have an aggregate nominal value of £4,956,900. 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. Treasury shares do not carry any voting or dividend rights.

At 1 November 2010 we had been notified of the following interests in three per cent or more of our shares.

	Number of ordinary shares millions	Percentage of issued share capital
Invesco Limited	61	6.03 <sup>1</sup>
BlackRock Inc	53	5.25 <sup>2</sup>
Legal & General Investment Management Limited	45	4.41 <sup>1</sup>
Morgan Stanley Investment Management Limited	42	4.17 <sup>1</sup>
Franklin Resources Inc	41	4.04 <sup>1</sup>

1 Direct holding  
2 Indirect holding

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

The share interests of the Directors, their families and any connected persons are shown on page 83. Other than disclosed on pages 73 and 74, 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 4 to the accounts and in the Directors' Remuneration Report.

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

The following agreements, which are 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.

Some companies within the Group entered into a credit facilities agreement (the Agreement) on 18 July 2007 under which certain banks and financial institutions (the Lenders) made available to Imperial Tobacco Finance PLC and Imperial Tobacco Enterprise Finance Limited committed and uncommitted credit facilities. The Agreement provides 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, Imperial Tobacco Finance PLC and Imperial Tobacco Enterprise Finance Limited must repay each loan utilised by them under the Agreement and the total commitments under the Agreement will be immediately cancelled.

Some companies within the Group entered into a letter of credit facility agreement (the Letter of Credit) dated 12 December 2007 under which the Lenders made available to Imperial Tobacco Limited a Letter of Credit. The Letter of Credit provides that, unless the Lenders 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, Imperial Tobacco Limited must repay the Letter of Credit utilised by it under the Letter of Credit and the total commitments under the Letter of Credit will be immediately cancelled.

Imperial Tobacco Finance PLC (the Issuer) has issued bonds under the Euro Medium Term Notes 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, 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;
- 15 September 2008 €750,000,000 7.25 per cent guaranteed notes due 2014;
- 17 February 2009 £1,000,000,000 9 per cent guaranteed notes due 2022;
- 17 February 2009 €1,500,000,000 8.375 per cent guaranteed notes due 2016;
- 24 June 2009 £500,000,000 7.75 per cent guaranteed notes due 2019; and
- 24 June 2009 €1,250,000,000 5 per cent guaranteed notes due 2012.

### Charitable and Political Donations

We have continued to support the communities in which we operate by donating £3 million (2009: £3 million) to charitable causes of which £2 million (2009: £2 million) was in respect of the UK through the Charities Aid Foundation.

No political donations were made to EU political parties, organisations or candidates (2009: Nil).

### Creditor Payment Policy

Our current policy concerning the payment of the majority of our trade creditors is to follow the CBI's Prompt Payers Code (copies are available from the CBI, Centre Point, 103 New Oxford Street, London WC1A 1DU). For other suppliers, our policy is to:

- agree the terms of payment with those suppliers when agreeing the terms of each transaction;
- ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and
- pay in accordance with our contractual and other legal obligations.

This policy applies to all payments to creditors for revenue and capital supplies of goods and services without exception. Wherever possible UK subsidiaries follow the same policy and international subsidiaries are encouraged to adopt similar policies by applying local best practices.

We are an approved signatory of the Prompt Payment Code sponsored by the Department for Business Innovation and Skills.

The amount of trade creditors outstanding as at 30 September 2010 was equivalent to 43 days (2009: 44 days) of trade purchases.

### Research and Development

We support our sales growth strategy by our investment in research and development, which brings innovative improvements to the Group, both in the products supplied to the consumer and in production and marketing techniques.

### Auditors and Disclosure of Information to Auditors

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

- so far as they are aware, there is no relevant audit information (that is information needed by the Company's Auditors in connection with preparing their report) of which the Company's Auditors are 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 that the Company's Auditors are aware of that information.

A resolution to reappoint PricewaterhouseCoopers LLP as Auditors to the Company will be proposed at the AGM.

### Disclosure and Transparency Rules

The Directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Directors' Report: Strategy, Performance and Governance sections on pages 6 to 95 includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

### 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 Generally Accepted Accounting Practice (United Kingdom Accounting Standards and Applicable Law). Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the 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 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 56 and 57, 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 Directors' Report includes 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.

### Employees

Our employees are key to our ongoing success. Our employment policies aim to attract the very best people. By applying universally accepted standards for human rights we ensure they are treated with fairness, dignity and respect. This is reinforced through offering equal opportunities and fair consideration to applications for employment, career development and promotion, without having regard to an employee's gender, race, religion, age or disability. These policies also cover the continuation of employment and appropriate training for employees who become disabled during their employment.

To ensure employees can share in our success we offer competitive pay and benefit packages linked, wherever possible, to performance. Employees are encouraged to build a stake in the Company through ownership of shares, with a number of employee share plans offered during the year.

We encourage all areas of our business to keep employees informed of the financial and economic factors affecting our performance. We brief employee representatives on pan-European issues through a European Employee Forum and the Altadis European Works Council.

We regularly review the composition of the Board and the Chief Executive's Committee (from 1 October 2010 the Operating Executive) to ensure a continuous provision of the most effective leadership for the Group's development and sustainability.

Our annual talent review process is designed to identify the most capable successors for critical roles at all levels in our business. It is a bottom up process initiated at a local level and rolled up through our regions and business units. This culminates in a final talent review meeting conducted by the Chief Executive's Committee (from 1 October 2010 the Operating Executive) for presentation to the Board for review and challenge. This is a practice that is embedded across the Group and seeks to ensure a continuous talent pipeline.

To help ensure our employees are aware of the standards of responsible behaviour that they are expected to follow, it is anticipated that the roll-out of Code of Conduct training will be completed during 2011. During the year we will also embed an e-learning system to further support this roll-out. Our Code of Conduct forms a key part of our preparations for ensuring compliance with the UK Bribery Act.

### 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 chosen by employees and two 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. Further details are contained in our Remuneration Report on pages 93 and 94.

### Business Review

A review of the Group's activities and future developments is included in the Directors' Report: Strategy, Performance and Governance sections on pages 6 to 95. This review fulfils the requirements of the Business Review contained in section 417 of the Act, including the financial performance during the year on pages 28 to 31, key performance indicators on pages 22 to 24 and a description of the principal risks and uncertainties facing the Group on pages 25 to 27.

The purpose of the Annual Report and Accounts is to provide information to the shareholders of Imperial Tobacco Group PLC. The Company, its Directors, employees, agents and advisers do not accept or assume responsibility to any other person to whom this document is shown or into whose hands it may come and any such responsibility or liability is expressly disclaimed. The Annual Report and Accounts



contain certain forward-looking statements with respect to the operations, performance and financial condition of the Company and the Group as a whole. By their nature, these statements involve uncertainties since future events and circumstances can cause actual results to differ materially from those anticipated and no reliance should be placed on them. The forward-looking statements reflect knowledge and information available at the date of preparation of this Annual Report and Accounts and the Company undertakes no obligation to update these forward-looking statements. Nothing in this Annual Report and Accounts should be construed as a profit forecast.

The principal operating subsidiaries within the Group are shown on pages 157 and 158.

### Insurance

We have purchased and, throughout the year, maintained 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 Report.

### Update on Ongoing Enquiries

#### German Investigations

Certain investigations were initiated by German authorities in January 2003 into alleged foreign trading and related violations by a number of people, including Reemtsma employees, during a period prior to its acquisition by Imperial Tobacco Group in May 2002. A Board Committee established in 2003 remains in place to monitor the progress of the investigations and the Group's responses on behalf of the Board.

Between 2005 and 2007, the investigations against all but five of the individuals were terminated, either for lack of evidence or on terms agreed by the individuals with the authorities. Settlement was made at no cost to the Imperial Tobacco Group of any duty payable as a result of certain of the activities being investigated.

In September 2006, charges relating to smuggling were brought in connection with one of the investigations against 18 individuals, one of whom is a former Reemtsma employee. In October 2008, the German court agreed to open trial in relation to these charges, but no hearing has yet been held.

In November 2006, in connection with a separate investigation, charges relating to violations of the German foreign trade act were brought against four other former Reemtsma employees. In March 2010, in accordance with an agreement with the authorities, the individuals pleaded guilty and financial penalties were ordered against them and Reemtsma. These were paid at no cost to the Imperial Tobacco Group.

#### Office of Fair Trading

As previously reported, in October 2003 the UK Office of Fair Trading (OFT) commenced an investigation under the Competition Act 1998 into the operation of the UK tobacco supply chain.

On 24 April 2008, the OFT issued a Statement of Objections (SO) which set out the OFT's allegations against Imperial Tobacco Group, Gallaher, and a number of retailers. These alleged infringements relate to the period prior to 2004.

On 15 April 2010, the OFT reached a Decision. Although the OFT dropped a number of the allegations made in the SO, it found that Imperial Tobacco Group and Gallaher had separately engaged in unlawful practices with ten tobacco retailers in breach of Chapter I of the Competition Act 1998. The OFT imposed total fines of £225m on the parties involved, including a fine of £112.3m on Imperial Tobacco Group.

Under the Competition Act 1998, parties have the right to appeal OFT decisions to the Competition Appeal Tribunal (CAT), and ultimately, on a point of law to the Court of Appeal. The CAT has jurisdiction to conduct a full rehearing of the facts and has the power to uphold, vary or quash the Decision and the fine imposed.

Imperial Tobacco Group does not accept the findings in the OFT's Decision. Accordingly, Imperial Tobacco Group submitted an appeal to the CAT on 15 June 2010 against the OFT's findings of infringement and the level of the fine. Five retailers (Asda, the Co-operative Group, Morrisons (together with Safeway) and Shell) have also appealed against the Decision and the fines imposed on them by the OFT.

The CAT is in the process of establishing the timetable for these appeals, although it is unlikely that the CAT will deliver judgment on liability before the fourth quarter of 2011, while any subsequent appeal to the Court of Appeal that may be necessary is unlikely to be determined before the third quarter of 2012.

#### Update on Tobacco-Related Litigation

We are not facing any tobacco-related litigation in the UK. In the Republic of Ireland, the number of tobacco-related claims has fallen from 307 in 1997, to 11. Ten of these claims are subject to dismissal motions. The other claim is inactive. The dismissal motion in respect of one claimant was heard by the Dublin High Court in 2006. In April 2007, the court ruled that this claim should be dismissed. This decision has been appealed and the dismissal motions in respect of the nine other active claims have been stayed pending the appeal. No date has been set for the appeal hearing.

Following our acquisition of Altadis in January 2008, we are currently facing a claim in Spain brought in the Administrative Court on behalf of the Regional Government of Andalusia for reimbursement of hospitalisation expenses allegedly incurred in treating smokers. The claim was served on Altadis in July 2009 and preliminary objections were filed by Altadis and the other tobacco company defendants in September 2009. The proceedings are stayed until the Administrative Court rules on these objections.

We are not facing any claims in France. Following our acquisition of Logista in May 2008, we are currently facing two claims in Italy. One is at an initial stage and the other has been dismissed but appealed.

We understand that a purported collective claim was filed against us (and other tobacco companies) by an individual in Bulgaria in March 2008 but we have not yet been formally served with any court documents. After various rulings and appeals, which had the effect of restricting the scope of the claim, the claimant filed an amended statement of case with the Sofia City Court and a hearing is scheduled for 18 November 2010 to assess whether the claimant has fulfilled the statutory conditions for bringing a collective action.

In September 2009 an individual claim was brought against us (and others) in Turkey. We filed a statement of defence at a preliminary hearing on 3 November 2009.

Following our acquisition of Commonwealth Brands in April 2007, we are currently facing one claim brought by an individual in the United States. A motion for summary judgment was filed by Commonwealth Brands in October 2005 and remains pending.

In Australia, a claim was filed in January 2009 against Imperial Tobacco Australia Limited and other tobacco companies. The claim was discontinued in October 2009.

We understand that the Saudi Ministry of Health has issued legal proceedings against distributors for international tobacco companies to recover the alleged costs of providing medical care to individuals. No Imperial Tobacco Group company has been served with any court documents in relation to this claim.

To date, no action has been successful or settled in favour of any claimant in any tobacco-related litigation against Imperial Tobacco or any of its subsidiaries. Imperial Tobacco has been advised by its lawyers that it has meritorious defences to the legal proceedings in which damages are sought for alleged tobacco-related health effects. We will continue to vigorously contest all such litigation against us.

By order of the Board



**Matthew Phillips**

2 November 2010

Imperial Tobacco Group PLC  
Registered in England and Wales No: 3236483

# Directors' Remuneration Report

The Remuneration Committee believes our remuneration practices link closely with our sustainable sales growth strategy without encouraging management to take undue risks.

## Remuneration Committee



**Pierre Jungels**  
Chairman

### Members

Dr P H Jungels (*Chairman*)

Mr M H C Herlihy

Mr C F Knott (*to 17 July 2010*)

Ms S E Murray

Mr M D Williamson

Mr M R Phillips (*General Counsel & Company Secretary (from 1 October 2010 Group Corporate and Legal Affairs Director), acts as Secretary to the Committee*)

### Responsibilities

The responsibilities of the Remuneration Committee include:

- determination of the Remuneration Policy for Executive Directors and members of the Chief Executive's Committee (from 1 October 2010 the Operating Executive);
- recommendations to the Board in respect of the Chairman's remuneration;
- determination of targets for performance related pay elements;
- policy for Directors' pensions and contracts;
- oversight of the overall policy for senior management remuneration;
- oversight of disclosures in the Remuneration Report; and
- oversight of the Group's employee share plans.

### Overview

The Group's remuneration policy is intended to attract and retain high quality employees throughout the organisation, encourage loyalty and motivate them to achieve a high level of corporate performance in an increasingly demanding, competitive and international environment.

Performance related rewards reflect the business performance delivered by the Board and senior management in a year of significant achievement that included a revised strategic focus towards our sales growth agenda and the further integration of our Altadis acquisition.

For the financial year ending 30 September 2011 the overall structure of the Group's remuneration policy will remain unchanged. Subject to shareholder consultation, to further motivate the achievement of strategic objectives the Executive Directors' potential maximum annual bonus has been increased dependent on the achievement of stretching measurable strategic objectives. The increase will be delivered in deferred shares. In addition, the entire bonus will be subject to claw-back. These changes are discussed in the Revisions to Executive Directors' Remuneration section on page 92.

### Introduction

We have prepared this Report in accordance with the Companies Act 2006, Statutory Instrument 2008/410 The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the Regulations) and to meet the requirements of the Listing Rules of the UK Listing Authority. We describe how the principles of good governance relating to directors' remuneration set out in the Combined Code on Corporate Governance (the Code) are applied in practice. The provisions of the UK Corporate Governance Code, published by the Financial Reporting Council in June 2010, apply to the Group with effect from its financial year commencing 1 October 2010.

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 parts of the Report have been prepared in accordance with the Companies Act 2006. The Auditors' opinion is set out on page 97 and we have clearly marked the audited sections of the Report.

This Report covers the following:

- 1 the Remuneration Committee's Objectives, Membership and Main Activities in 2010;
- 2 Directors' Emoluments and Share Interests;
- 3 Review of Imperial Tobacco Group's Remuneration Policy and Practice;
- 4 Directors' Service Arrangements;
- 5 Remuneration Practices;
- 6 Executive Directors' Pensions; and
- 7 Other Information.

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### 1 The Remuneration Committee's Objectives, Membership and Main Activities in 2010

The Remuneration Committee operates under clear written terms of reference, which can be found on our website [www.imperial-tobacco.com](http://www.imperial-tobacco.com). The Remuneration Committee formally confirms that throughout the year it has complied with the governance rules and best practice provisions relating to remuneration as set out in section 1 of the Code.

The Remuneration Committee's key objectives are to:

- ensure the Group's remuneration arrangements align with our values, support our corporate strategy, including our enhanced sales focus, and drive performance as measured by our financial and non-financial key performance indicators (KPIs), see pages 22 to 24;
- maintain a competitive remuneration package appropriate to the business environment in the countries in which we operate so we can continue to attract, develop, retain and motivate a high quality pool of talented employees at all levels, whilst ensuring a clear link between reward and performance;
- ensure the remuneration policy motivates employees at all levels to enhance our performance without encouraging them to take undue risks; and
- align senior executives' remuneration with the interests of shareholders and other stakeholders, including customers and employees, by balancing financial and non-financial elements.

### Membership

The Remuneration Committee, which met four times during the year, comprises four independent Non-Executive Directors. The Committee members have no personal financial interest in the matters discussed other than as shareholders. During the year Mr I J G Napier (Company Chairman) and Mr J-D Comolli (Deputy Chairman) attended by invitation.

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

### Advice and Support

The Remuneration Committee is provided with the following internal and external advice and support:

#### Internal

During the year Mrs A J Cooper (Chief Executive from 13 May 2010), Mr G Davis (Chief Executive to 12 May 2010) and Mr R Dyrbus (Finance Director) were invited to attend to answer questions. Mr M R Phillips (General Counsel & Company Secretary) also attended as secretary to the Committee. They were all specifically excluded from any matter concerning the details of their own remuneration or conditions of service.

Mrs K A Turner (Group Human Resources Director), the Group Compensation and Benefits Manager and the Deputy Company Secretary also attended and provided internal support and advice on market and regulatory developments in remuneration practice and our employee share plans.

#### External

To assist the Remuneration Committee in setting the remuneration package for each Executive Director and member of the Chief Executive's Committee (from 1 October 2010 the Operating Executive) advice is provided by remuneration consultants Hewitt New Bridge Street (part of Aon Hewitt), and Towers Watson, both of whom are engaged by the Remuneration Committee as required. Both are signatories to the Code of Conduct for Remuneration Advisers. Neither provides any services to the Group other than those explained below.



Hewitt New Bridge Street also reviews the Group's remuneration principles and practices against corporate governance best practice and helps ensure adherence to the Group's Executive Directors' Remuneration Policy.

Executive remuneration data provided by Towers Watson was also used to assist in benchmarking to ensure the consistent application of our executive Remuneration Policy.

To ensure Remuneration Committee members are fully aware of new developments and evolving remuneration best practice, Hewitt New Bridge Street presented a review of developments in UK corporate governance, focusing primarily on executive pay governance.

Aon Hewitt is also assisting the Group in respect of the triennial valuation of its pension fund and acts as insurance brokers to the Group.

Solicitors Allen & Overy LLP are retained by the Company and provide legal advice on our employee share plans. Allen & Overy LLP and Ashurst LLP also provide services to the Remuneration Committee as and when required. Both Allen & Overy LLP and Ashurst LLP provide other legal services to the Group.

The Company has appointed Alithos Limited to undertake total shareholder return (TSR) calculations and provide advice on all TSR related matters, including advice in respect of the bespoke comparator group. Alithos Limited provides no other services for the Group.

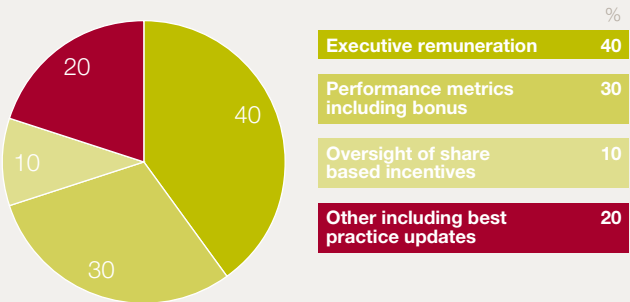
PricewaterhouseCoopers LLP, our Auditors, perform agreed upon procedures on earnings per share (EPS) calculations used in our employee share plans to assist the Remuneration Committee in determining the level of awards vesting.

**Main Activities – How the Remuneration Committee met its Objectives**

The Board is ultimately accountable for executive remuneration but delegates responsibility to the Remuneration Committee. Our Remuneration Committee addressed the following main issues during the year:

- consideration of our new Chief Executive's remuneration package upon appointment;
- consideration of our Remuneration Policy for Executive Directors;
- the annual review of the Chairman's, Executive Directors' and Chief Executive's Committee members' remuneration;
- reviewing the executive bonus targets;
- reviewing, and subsequently increasing, the executive bonus levels;
- overseeing Remuneration Policy for senior management and employees and our employee share plans;
- undertaking the annual review of the Committee's Terms of Reference; and
- the disclosures in this Report.

**How the Committee spent its time**



## 2 Directors' Emoluments for the Year Ended 30 September 2010 (Audited)

£'000	2010	2009
<b>Executive Directors</b>		
Base salary	2,414	2,612
Benefits	75	84
Pension salary supplement	276	256
Bonus	2,769	2,573
LTIP annual vesting <sup>1</sup>	3,454	2,248
SMS annual vesting <sup>2</sup>	1,183	1,453
	<b>10,171</b>	<b>9,226</b>
<b>Non-Executive Directors</b>		
Fees	1,061	1,101
Benefits	33	115
Subsidiary Board fees	–	5
Consultancy fees	442	702
	<b>1,536</b>	<b>1,923</b>
<b>Former Executive Directors</b>		
Salary of former Executive Director	75	–
Bonus of former Executive Director	77	–
Consultancy fees to former Executive Directors	106	112
Subsidiary Board fees	43	81
Benefits	2	–
	<b>303</b>	<b>193</b>
<b>Fees of former Non-Executive Directors</b>		
Subsidiary Board fees	28	28
	<b>28</b>	<b>28</b>
<b>Total remuneration</b>	<b>12,038</b>	<b>11,370</b>
<b>Chief Executive's Committee (excluding Executive Directors)</b>		
Base salary	1,583	1,342
Benefits	141	74
Pension salary supplement	110	99
Bonus	1,079	819
LTIP annual vesting <sup>1</sup>	439	285
SMS annual vesting <sup>2</sup>	360	369
	<b>3,712</b>	<b>2,988</b>

1 Value of LTIP shares vesting in the year based on the prevailing closing share price on the day of exercise.

2 Value of SMS shares vesting on maturity based on the prevailing closing share price on the day of vesting.

Note: Aggregate remuneration paid to or receivable by Executive Directors, Non-Executive Directors and members of the Chief Executive's Committee for qualifying services in accordance with IAS 24, which includes National Insurance and similar charges £17,274,754

## Key Management Compensation for the Year Ended 30 September 2010 (Audited)

£'000	2010	2009
Short-term employee benefits	9,595	9,427
Post employment benefits	636	378
Other long-term benefits	–	–
Termination benefits	–	–
Share-based payment (in accordance with IAS 24)	4,043	3,688
	<b>14,274</b>	<b>13,493</b>

**Emoluments by Individual Director (Audited)**

£'000	Base salary	Fees	Subsidiary board fees	Consultancy fees	Bonus	Pension salary supplement <sup>1</sup>	Benefits in kind <sup>2</sup>	Sub total 2010	Sub total 2009	LTIP <sup>3</sup>	SMS <sup>3</sup>	Total 2010	Total 2009	Base salary/ fees from 1/10/2010
<b>Executive Directors</b>														
Mrs A J Cooper <sup>4</sup> , Chief Executive	624	–	–	–	768	51	16	<b>1,459</b>	980	283	181	<b>1,923</b>	1,345	800
Mr R Dyrbus, Finance Director	642	–	–	–	764	225	26	<b>1,657</b>	1,530	883	304	<b>2,844</b>	2,515	642
Mr G L Blashill, Group Sales and Marketing Director	469	–	–	–	488	–	16	<b>973</b>	856	433	218	<b>1,624</b>	1,349	469
Mr G Davis <sup>5</sup> , former Chief Executive	679	–	–	–	749	–	17	<b>1,445</b>	2,159	1,855	480	<b>3,780</b>	4,017	–
	2,414	–	–	–	2,769	276	75	<b>5,534</b>	5,525	3,454	1,183	<b>10,171</b>	9,226	1,911
<b>Non-Executive Directors</b>														
Mr I J G Napier, Chairman	–	433	–	–	–	–	–	<b>433</b>	420	–	–	<b>433</b>	420	433
Mr J-D Comolli <sup>6</sup> , Deputy Chairman	–	118	–	442	–	–	33	<b>593</b>	923	–	–	<b>593</b>	923	–
Mr B F Bich <sup>7</sup>	–	–	–	–	–	–	–	<b>–</b>	65	–	–	<b>–</b>	65	–
Dr K M Burnett	–	65	–	–	–	–	–	<b>65</b>	65	–	–	<b>65</b>	65	65
Mr M H C Herlihy	–	65	–	–	–	–	–	<b>65</b>	65	–	–	<b>65</b>	65	65
Dr P H Jungels <sup>8</sup>	–	105	–	–	–	–	–	<b>105</b>	100	–	–	<b>105</b>	100	105
Mr C F Knott <sup>9</sup>	–	60	–	–	–	–	–	<b>60</b>	65	–	–	<b>60</b>	65	–
Ms S E Murray	–	65	–	–	–	–	–	<b>65</b>	65	–	–	<b>65</b>	65	65
Mr B Setrakian <sup>10</sup>	–	65	–	–	–	–	–	<b>65</b>	70	–	–	<b>65</b>	70	65
Mr M D Williamson <sup>8</sup>	–	85	–	–	–	–	–	<b>85</b>	85	–	–	<b>85</b>	85	85
	–	1,061	–	442	–	–	33	<b>1,536</b>	1,923	–	–	<b>1,536</b>	1,923	883
<b>Former Directors</b>														
Mr D Cresswell <sup>11</sup>	–	–	28	23	–	–	–	<b>51</b>	40	–	–	<b>51</b>	40	–
Mr G Davis <sup>5</sup> , former Chief Executive	75	–	–	–	77	–	2	<b>154</b>	–	–	–	<b>154</b>	–	–
Mr S Huismans <sup>12</sup>	–	–	28	–	–	–	–	<b>28</b>	28	–	–	<b>28</b>	28	–
Mr S T Painter <sup>13</sup>	–	–	15	83	–	–	–	<b>98</b>	153	–	–	<b>98</b>	153	–
	75	–	71	106	77	–	2	<b>331</b>	221	–	–	<b>331</b>	221	–

1 Further details are contained in the Executive Directors' pension section on pages 93 and 94.

2 Benefits in kind principally include the provision of a company car, health insurance and, in the case of Mr J-D Comolli, life insurance.

3 LTIP and SMS represent the value of SMS awards vesting and LTIP options exercised in the year.

4 Mrs A J Cooper's base salary on appointment as Chief Executive was £750,000.

5 Mr G Davis retired from the Board on 12 May 2010; however, he remained an employee until 4 June 2010.

6 Mr J-D Comolli was appointed on 15 July 2008 and, in addition to his Director's fees, received consultancy fees for services provided to the Group. He resigned from the Board with effect from 14 September 2010.

7 Mr B F Bich resigned from the Board on 16 September 2009.

8 Includes payment in respect of chairmanship of Board Committees at an annual rate of £15,000 in respect of the Remuneration Committee and £20,000 in respect of the Audit Committee.

9 Mr C F Knott resigned from the Board on 17 July 2010.

10 Mr B Setrakian was appointed on 25 June 2008. Until December 2008 he received remuneration in respect of Non-Executive Director appointments within Altadis' USA business.

11 Mr D Cresswell retired from the Board on 31 December 2007. However, Mr Cresswell received fees in connection with his Non-Executive Director appointments to Supervisory Boards within the Reemtsma Group and Subsidiary Boards within the Altadis Group.

12 Mr S Huismans retired from the Board on 31 January 2006. However, Mr Huismans received fees in connection with his Non-Executive Director appointments to Supervisory Boards within the Reemtsma Group and Subsidiary Boards within the Altadis Group.

13 Mr S T Painter retired from the Board on 31 May 2000 but received fees on a consultancy basis and in connection with his Non-Executive Director appointments to Supervisory Boards within the Reemtsma Group and Subsidiary Boards within the Altadis Group.

No sums were paid to any Director by way of taxable expenses allowances and no Directors waived their fees.

### Directors' Interests in Ordinary Shares (Beneficial, Family and any Connected Persons Interests) (Audited)

Directors' Interests in Ordinary Shares (Shareholdings, Options and any Connected Persons Interests, (if any))										
	Ordinary Shares			Share Save Options		Contingent Rights to Ordinary Shares (LTIP and SMS Shares)		Total Interests		
	1/10/09	30/09/10 <sup>1</sup>	1/11/10 <sup>1</sup>	1/10/09	30/09/10 <sup>1</sup>	1/10/09	30/09/10 <sup>1</sup>	1/10/09	30/9/10 <sup>1</sup>	1/11/10 <sup>1</sup>
<b>Executive Directors</b>										
Mrs A J Cooper	107,664	<b>114,336</b>	114,336	729	<b>729</b>	105,828	<b>131,057</b>	214,221	<b>246,122</b>	246,122
Mr R Dyrbus	396,866	<b>398,365</b>	398,365	689	<b>669</b>	224,539	<b>244,196</b>	622,094	<b>643,230</b>	643,230
Mr G L Blashill	153,139	<b>154,790</b>	154,790	729	<b>729</b>	116,417	<b>125,446</b>	270,285	<b>280,965</b>	280,965
Mr G Davis <sup>2</sup>	614,540	<b>616,607</b>	616,607	947	<b>947</b>	446,274	<b>433,247</b>	1,061,761	<b>1,050,801</b>	1,050,801
<b>Non-Executive Directors</b>										
Mr I J G Napier	12,538	<b>14,747</b>	14,747	–	–	–	–	12,538	<b>14,747</b>	14,747
Mr J-D Comolli <sup>3</sup>	684	<b>710</b>	710	–	–	–	–	684	<b>710</b>	710
Dr K M Burnett	1,262	<b>1,583</b>	1,583	–	–	–	–	1,262	<b>1,583</b>	1,583
Mr M H C Herlihy	2,589	<b>3,015</b>	3,015	–	–	–	–	2,589	<b>3,015</b>	3,015
Dr P H Jungels	5,276	<b>5,661</b>	5,661	–	–	–	–	5,276	<b>5,661</b>	5,661
Mr C F Knott <sup>4</sup>	1,262	<b>1,262</b>	1,262	–	–	–	–	1,262	<b>1,262</b>	1,262
Ms S E Murray	2,144	<b>2,465</b>	2,465	–	–	–	–	2,144	<b>2,465</b>	2,465
Mr B Setrakian	404	<b>725</b>	725	–	–	–	–	404	<b>725</b>	725
Mr M D Williamson	2,276	<b>2,597</b>	2,597	–	–	–	–	2,276	<b>2,597</b>	2,597

<sup>1</sup> Or date of resignation or retirement if earlier.

<sup>2</sup> Mr G Davis retired from the Board on 12 May 2010.

<sup>3</sup> Mr J-D Comolli resigned from the Board on 14 September 2010.

<sup>4</sup> Mr C F Knott resigned from the Board on 17 July 2010.

There have been no changes in these interests since 30 September 2010.

### 3 Review of Imperial Tobacco Group's Remuneration Policy and Practice

#### Remuneration Strategy

We operate in a highly competitive, international environment. Our remuneration strategy is to ensure that the level of remuneration and benefits offered motivates our talented employees at all levels across the Group. Our bonus and share plan arrangements provide a clear link between reward and performance. We set out to provide competitive remuneration to all employees, appropriate to the business environment in the countries in which we operate.

Our remuneration arrangements align with and support our corporate strategy. We continue to assign employees internationally to achieve the optimum balance of experience within the Group and facilitate employee development. Our cohesive reward structures ensure all our employees engage with our strategic goals and are motivated to achieve them.

We align the interests of shareholders and employees at all levels by, wherever possible, giving our employees the opportunity to build a shareholding in Imperial Tobacco Group through our employee share plans. This alignment is reinforced further through the Group's executive share ownership guidelines discussed on page 92. Where possible our employees were offered participation in one or more employee share plans during the year, with over 32 per cent of eligible employees participating in one or more of those plans.

#### Executive Remuneration Policy

We consider it critical to align the remuneration package for Executive Directors and members of the Chief Executive's Committee (with effect from 1 October 2010 the newly formed Operating Executive) with the Group's strategy and risk. In designing and reviewing our executive remuneration policy we aim to attract and retain high quality executives, induce loyalty and motivate them to achieve high levels of corporate performance in line with the best interests of shareholders. We, therefore, aim for our policy to be competitive whilst ensuring the overall remuneration package is not excessive.

Our executive remuneration policy supports our strategy by linking the major elements of remuneration to performance criteria aligned with our key performance indicators (KPIs). The policy includes both short-term and long-term incentives. Packages are significantly weighted towards performance related pay elements that take into account individual, functional and corporate performance. The main components are base salary, annual bonus, share matching scheme (SMS), long term incentive plan (LTIP) and pension benefits. To achieve alignment with our KPIs, the performance criteria for the SMS and LTIP are designed to motivate earnings per share and total shareholder return (TSR) growth whilst those relating to the annual bonus support key areas of performance, including a matrix incentivising growth in adjusted earnings per share, debt reduction, cigarette volume growth, growth in our global strategic brands and anti-illicit trade activities.



We continue to set base salary at around the median level of the comparator group of companies, whilst providing Executive Directors and members of the Chief Executive's Committee (with effect from 1 October 2010 the newly formed Operating Executive) with the capacity to earn upper quartile total compensation on achievement of superior business performance. Our comparator group of companies for the purposes of assessing total compensation remains the FTSE 50, excluding companies in the financial and pharmaceutical sectors, with secondary reference to the FTSE 30, excluding companies in the financial and pharmaceutical sectors.

To ensure our remuneration policy is firmly linked to our strategy and risk management, Executive Directors together with other senior managers are required to build a significant stake in the Company in accordance with our share retention guidelines and through the mandatory deferral of elements of annual bonus in the form of shares. This link is further supported through the setting of bonus and share plan targets that reflect key business imperatives, for example volume growth, debt reduction and growth in both earnings per share and TSR.

Subject to shareholder consultation, the Remuneration Committee has increased the maximum annual bonus for the financial year ending 30 September 2011 for the Chief Executive and Finance Director to 200 per cent and 150 per cent of base salary respectively (from 150 per cent and 135 per cent). This higher bonus opportunity is at or below the median level for FTSE 50 companies. The change to annual bonus opportunity is balanced by the following:

- more demanding performance conditions. To achieve the maximum bonus, executives will need to achieve outstanding performance across a series of demanding metrics including earnings per share growth, net sales growth, debt reduction and other strategic goals;
- a mandatory requirement that any portion of annual bonus that exceeds 100 per cent of base salary is delivered in the Company's shares, which must be retained for at least three years and will not be eligible for investment in the SMS;
- in addition, a new provision whereby the entire bonus will be subject to claw-back in the event of gross misconduct or misstatement of results; and,
- a more demanding performance requirement and vesting scale relating to the SMS.

The Remuneration Committee did not increase base salaries for two of the three Executive Directors, at the 1 October 2010 review. The Chief Executive's base salary was increased to £800,000 (from £750,000) in line with the Remuneration Committee's decision to align her salary with its policy and taking account of the Company's size, international profile and the critical importance of the role of the Chief Executive in driving future performance. The new base salary of £800,000, which is significantly below that of her predecessor, remains below the market median for FTSE 50 companies and the market median for Chief Executives in the FTSE 100.

#### **4 Directors' Service Arrangements**

##### **Executive Directors' Service Agreements**

The service agreement for Mr R Dyrbus was entered into at the time of the demerger of the Company from the Hanson Group. The provisions dealing with compensation on termination following a change of control in his service agreement reflect that. The service agreements for the other Executive Directors reflect the Company's established policy that Executive Directors have service agreements which are terminable on no more than one year's notice and that there is no entitlement to the payment of a predetermined amount on termination of employment in any circumstances.

There are no liquidated damages provisions for compensation on termination within Executive Directors' service agreements, except for those set out in the table below. The Executive Directors' service agreements do contain payment in lieu of notice provisions but these are at the Company's sole discretion. We are unequivocally against rewards for failure. Apart from the limited respects referred to above, the circumstances of the termination and an individual's duty and opportunity to mitigate loss are taken into account in every case. Our policy is to stop or reduce compensatory payments to former Directors to the extent that they receive remuneration from other employment during the compensation period and that any such payments would be paid monthly in arrears.

Under the Rules of the LTIP and SMS, outstanding awards vest on termination for certain reasons, including death, retirement, redundancy, the business or company in which the participant is employed ceasing to be part of the Group or on a change of control. Awards vest on a time-related pro rata basis and are subject to satisfaction of relevant performance criteria. If, however, the termination of employment is for a reason other than one of those specified in the relevant rules, an individual's full awards lapse.

### Executive Directors' Service Agreements

Executive Directors	Date of contract	Expiry date	Compensation on termination following a change of control
Mrs A J Cooper	1 July 2007	Terminable on 52 weeks' notice	No provisions
Mr R Dyrbus	21 August 1996	Terminable on 52 weeks' notice	Payment of a liquidated sum calculated by reference to benefits receivable during the notice period
Mr G L Blashill	28 October 2005	Terminable on 52 weeks' notice	No provisions

### Policy in Respect of Remuneration from External Board Appointments

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

The Executive Directors who held such appointments during the financial year were Mrs A J Cooper, who serves on the Board of Inchcape PLC and received and retained fees of £40,000, and Mr G Davis, who serves on the Board of Wolseley plc and received and retained fees of £44,063.

### Remuneration Policy for Non-Executive Directors

During the year, fees for Non-Executive Directors, and chairmanship fees in respect of the Remuneration and Audit Committees, were reviewed by the Board as a whole. The review took into account market practice with reference to the comparator group on page 84 and the various responsibilities of our Non-Executive Directors together with the need to attract and retain individuals with the relevant skills, knowledge and experience. The Chairman's remuneration was determined by the Board following recommendation from the Remuneration Committee. The Chairman and Non-Executive Directors were not permitted to take part in discussions relating to their own remuneration. With the exception of reimbursement of expenses incurred in connection with their directorship of the Company, Non-Executive Directors receive no other material pay or benefits. They are not eligible to participate in the Group's employee share plans or annual bonus schemes and are not eligible for pension scheme membership. During the year Mr J-D Comolli, however, received pension payments relating to his former executive position within the Altadis Group. The Company also provided medical insurance for Mr Comolli.

A proportion of our Chairman's and Non-Executive Directors' fees is applied to purchase shares in the Company. This is to promote alignment of their interests with those of our shareholders and is not at a level that could compromise their judgement or independence. These shares are held by a nominee during the term of their directorship.

The Company's Articles of Association enable the Board to set the remuneration of Directors within the limits set by shareholders. The current aggregate limit is £2.0 million and the aggregate amount paid in the financial year was £1.1 million. Executive Directors are remunerated in respect of their executive appointments, under the terms of their service agreements, and receive no additional fees for serving as directors.

Following his retirement from the Board in January 2006, Mr S Huismans remains a member of Supervisory Boards within the Reemtsma Group. He was also appointed as a Non-Executive Director of Altadis, S.A. upon its acquisition by the Group until 5 November 2008. Mr S Huismans received additional remuneration for fulfilling such non-executive roles.

### Non-Executive Directors' Letters of Appointment

The Chairman and Non-Executive Directors do not have service agreements with the Company but the terms of their appointment are recorded in letters of appointment which are available for viewing at our registered office during normal business hours and 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 1 February 2010. Under the terms of our current Articles of Association Non-Executive Directors stand for election at the first AGM following appointment and are subject to re-election by shareholders every three years. A resolution to amend this provision and require all Directors to stand for re-election annually is being proposed at the 2011 AGM. There are no provisions regarding notice periods in their letters of appointments 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. The letters of appointment detail the time commitment expected of each Non-Executive Director.

## 5 Remuneration Practices

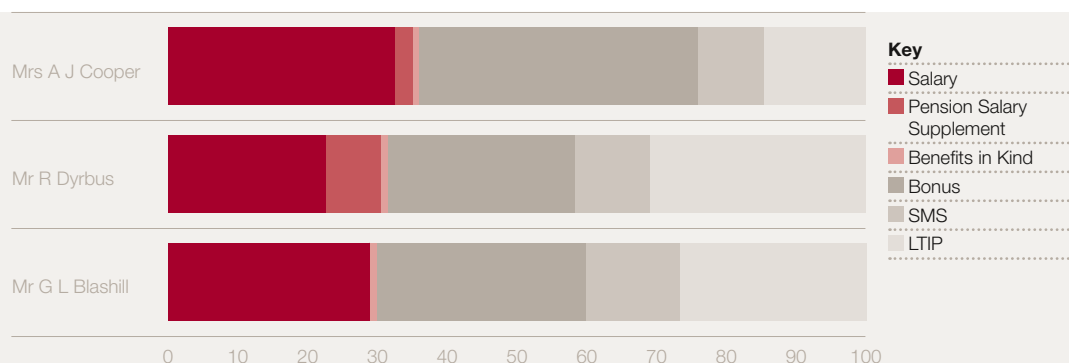
### Executive Directors' 2009/2010 Remuneration Policy

Element	Objective	Award Level	Performance Criteria	Performance Period
Base salary	Attract and retain high performing individuals reflecting market value of role and executive's skills and experience.	Median of FTSE 50 excluding companies in the financial and pharmaceutical sectors with secondary reference to the FTSE 30 excluding companies in the financial and pharmaceutical sectors.	N/A	N/A
Annual bonus	Incentivise delivery of Group objectives and enhance performance, including as measured by our key performance indicators discussed on pages 22 to 24.	Maximum percentage of base salary. Cash element: Chief Executive and Finance Director first 100%, other Executive Director first 85%.  Non-matchable deferred shares element: Chief Executive up to an additional 50% of base salary, other Executive Directors up to an additional 35% of base salary.	Financial Targets (100% of base salary Chief Executive and Finance Director, 85% of other Executive Director).  Strategic Targets (50% of base salary for Chief Executive and 35% for other Executive Directors).	1 year  3 year retention period
Share matching scheme	Incentivise growth in Group EPS (adjusted for certain items) and align with interests of shareholders.	May elect to invest some or all of gross cash element of the annual bonus in shares. These can be matched on a 1:1 basis.	Adjusted EPS growth.	3 years
Long term incentive plan	Incentivise long-term delivery of EPS and TSR (adjusted for certain items) and align with interests of shareholders.	Percentage of base salary: Chief Executive 200%, Finance Director 150%, other Executive Directors 100%.	3 elements – 50% adjusted EPS growth, 25% TSR vs FTSE 100, 25% TSR vs comparator group.	3 years

#### Base Salary

The Remuneration Committee reviews base salary annually following detailed consideration of a number of factors including individual responsibilities, performance, market value of the relevant executive and external market data. In line with our Remuneration Policy base salary is set within a range around the market median of the comparator group. Base salary is the only element of the package used to determine pensionable earnings.

### Percentage of total actual remuneration for the financial year to 30 September 2010



When setting base salary the Remuneration Committee is provided with external benchmarking data compiled by Towers Watson. The Committee is also provided with data in respect of the executive's overall package so it can be benchmarked against the comparator group. This data also enables the Committee to review the effect of any change in base pay on the executive's overall package.

In setting the remuneration policy and remuneration levels for executives, the Committee considers the remuneration arrangements and employment conditions of the wider employee population within the Group. The Group's approach for all employees, including executives, is to set remuneration that takes account of: market practice; economic conditions; the performance of the Group and of teams or individuals; collective agreements that may apply; and any legal or regulatory requirements in jurisdictions where it operates. The percentage increases for executives' base salaries effective both 1 October 2009 and 1 October 2010 were generally lower than the average for other employees of the Group located in the same region. Base salaries, effective from 1 October 2010, for some Executive Directors and other senior executives were frozen; increases were generally restricted to promotions and individuals accepting additional responsibilities. Following the Chief Executive's appointment in May 2010, her 1 October 2010 base salary increase was in line with the Remuneration Committee's decision to gradually align her salary with its policy outlined above.

### Annual Bonus

The objective of the annual bonus is to incentivise delivery of the Group's objectives and enhance performance against key financial and non-financial targets in support of our KPIs as well as other non-financial metrics such as our anti-illicit trade activities, as set out on pages 22 to 24.

For the financial year ended 30 September 2010 the potential maximum bonus was 150 per cent of base salary for the Chief Executive, 135 per cent for the Finance Director and the Chief Operating Officer and 120 per cent for the Group Sales and Marketing Director. In support of the Group's KPIs, the Remuneration Committee determined that for the financial year ending 30 September 2010 up to 100 per cent of salary (85 per cent for the Group Sales and Marketing Director) could be earned for achieving financial targets based on a matrix including growth in adjusted earnings per share and reduction of adjusted net debt. During the year we delivered adjusted EPS of 178.8 pence up 11 per cent. When combined with debt reduction of over £1 billion this resulted in 100 per cent of the financial element vesting.

The remainder of the annual bonus could be earned for performance against other stretching, quantifiable non-financial targets in important strategic areas such as volume growth and market share targets, which support our cigarette volumes and white stick equivalents KPIs, and anti-illicit trade activities, which support our focus on future foundations. The non-financial targets are not disclosed as they are considered to be commercially confidential but were met in part, with 54 per cent vesting.

This resulted in bonuses, as detailed in the table on page 82, being awarded to the Executive Directors. These payments represent 127 per cent of the Chief Executives' base salaries, 119 per cent of the Finance Director's base salary and 104 per cent of the Group Sales and Marketing Director's base salary. Cash bonuses were also earned by other senior managers for achieving relevant performance targets for the financial year.

Any bonus earned up to 100 per cent of base salary for the Chief Executive and Finance Director and 85 per cent for the Group Sales and Marketing Director is paid in cash and is eligible for investment in the SMS. Any bonus payable in excess of these levels is paid in ordinary shares which the Director is required to retain for a minimum of three years. These ordinary shares are not eligible for investment in the SMS. It is proposed that these limits will remain unchanged for the year ended 30 September 2011.

No element of the bonus is guaranteed.

### Share Matching Scheme

Under the SMS, at the discretion of the Remuneration Committee, the Executive Directors and the majority of the Group's senior management are invited to invest any proportion of their gross bonus (capped at 100 per cent of base salary for the Chief Executive and Finance Director and 85 per cent for the Group Sales and Marketing Director) in our shares. The shares are held by a nominee administered by the Employee Benefit Trusts. Provided the shares lodged are left with the nominee for three years and the participant remains an employee within the Group, they will be matched on a one-for-one basis. Employees can exercise their vote in respect of shares held in the nominee by giving written instructions to the nominee.

In respect of investments made under the SMS by Executive Directors and, from last year, investments by members of the Chief Executive's Committee, a performance criterion is applied such that matching only occurs if the Group has achieved real average annual adjusted EPS growth after adjusting for UK inflation (Real Annual EPS Growth) in excess of three per cent over the three year retention period. Measurement of the performance criterion is based on the same protocol as that applying to the LTIP and there is no opportunity to re-test if the performance criterion is not met. In setting the performance criterion for SMS awards, the Remuneration Committee has decided the Real Annual EPS Growth criterion reflects our strategy to create sustainable shareholder value.



Under the rules of the SMS, should Imperial Tobacco Group PLC 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 criterion.

### Executive Directors' Contingent Rights to shares under the Share Matching Scheme (Audited)

	Balance at 1/10/2009	Contingent rights arising	Prevailing share price at date of grant £	Vested during year	Market price at date of vesting 15/2/2010 £	Amount realised on vesting £'000	Balance at 30/9/2010 <sup>1</sup>	Actual/expected vesting date
Mrs A J Cooper	8,804	–	19.40 <sup>2</sup>	(8,804)	20.57	181	–	February 2010
	11,366	–	21.18 <sup>3</sup>	–	–	–	<b>11,366</b>	February 2011
	17,895	–	17.80 <sup>4</sup>	–	–	–	<b>17,895</b>	February 2012
	–	20,644	20.57 <sup>5</sup>	–	–	–	<b>20,644</b>	February 2013
	38,065	20,644	–	(8,804)	–	181	<b>49,905</b>	
Mr R Dyrbus	14,800	–	19.40 <sup>2</sup>	(14,800)	20.57	304	–	February 2010
	24,030	–	21.18 <sup>3</sup>	–	–	–	<b>24,030</b>	February 2011
	32,303	–	17.80 <sup>4</sup>	–	–	–	<b>32,303</b>	February 2012
	–	32,255	20.57 <sup>5</sup>	–	–	–	<b>32,255</b>	February 2013
	71,133	32,255	–	(14,800)	–	304	<b>88,588</b>	
Mr G L Blashill	10,597	–	19.40 <sup>2</sup>	(10,597)	20.57	218	–	February 2010
	13,262	–	21.18 <sup>3</sup>	–	–	–	<b>13,262</b>	February 2011
	17,684	–	17.80 <sup>4</sup>	–	–	–	<b>17,684</b>	February 2012
	–	18,735	20.57 <sup>5</sup>	–	–	–	<b>18,735</b>	February 2013
	41,543	18,735	–	(10,597)	–	218	<b>49,681</b>	
Mr G Davis <sup>6</sup>	23,323	–	19.40 <sup>2</sup>	(23,323)	20.57	480	–	February 2010
	37,859	–	21.18 <sup>3</sup>	–	–	–	<b>37,859</b>	February 2011
	52,741	–	17.80 <sup>4</sup>	–	–	–	<b>52,741</b>	February 2012
	113,923	–	–	(23,323)	–	480	<b>90,600</b>	

1 Or date of retirement if earlier.

2 Award granted 15 February 2007. Share price on date of grant adjusted from £21.96 following June 2008 rights issue.

3 Award granted 15 February 2008. Share price on date of grant adjusted from £23.97 following June 2008 rights issue.

4 Award granted 15 February 2009.

5 Award granted 15 February 2010.

6 Mr G Davis was not eligible to participate in the award granted 15 February 2010 due to his expected retirement.

There have been no changes in any Executive Directors' contingent rights since 30 September 2010.

During February 2010 annual bonuses earned in the financial year to 30 September 2006 and lodged under the SMS for a three year period matured. The performance criterion was met in full providing matched shares for participants on a one for one basis.

In respect of annual bonuses earned in the financial year to 30 September 2009 and paid in December 2009, the Executive Directors elected, in February 2010, to invest the equivalent of their entire bonus in the form of our shares under the SMS. These will be matched on a one for one basis provided they are left in the SMS for three years, the participant remains an employee within the Group and the Company has achieved in excess of three per cent Real Annual EPS Growth over the retention period.

This performance criterion and the award policy and vesting schedules were reviewed during the year by the Remuneration Committee who were satisfied they remain appropriate notwithstanding current market conditions. However, the performance criterion was amended for future awards, as discussed on page 92. These matched shares are shown within contingent rights arising above. In accordance with the Company's normal practice, Mr G Davis was not eligible to participate in this award due to his expected retirement.

It is anticipated that in February 2011 the Executive Directors will again invest the equivalent of their entire eligible annual bonus in the SMS.

### Long Term Incentive Plan

Annual conditional awards are made under the LTIP to Executive Directors and other senior management. These awards vest three years after grant and are subject to satisfying the appropriate performance criteria over the relevant three year performance period. All grants are at the discretion of the Remuneration Committee and no employee has a right to receive an award. Awards are equivalent to 200 per cent of base salary for the Chief Executive, 150 per cent for the Finance Director and 100 per cent for the other Executive Director, with awards at a lower level for other senior management.

### Current Structure

The performance criterion for all awards is split into three elements. The Remuneration Committee reviewed the performance criteria at its meeting in September 2010 and was satisfied that they remain appropriate notwithstanding current market conditions. The three elements are as follows:

### *First Element*

Fifty per cent of the award has a performance criterion based on average growth in adjusted earnings per share based on an agreed protocol, after adjusting for inflation over the period of the award. At the Remuneration Committee's request, our Auditors perform agreed upon procedures on the calculations. Twelve and a half per cent of this element (i.e. 6.25 per cent of the potential total award) vests if Real Annual EPS Growth equals three per cent and 100 per cent of this element (i.e. 50 per cent of the potential total award) vests if Real Annual EPS Growth equals or exceeds 10 per cent. Between these two points this element vests on a straight-line basis.

### *Second Element*

Twenty five per cent of the potential total award has a performance criterion based on TSR relative to the FTSE 100 Index as described below.

The performance criterion for this element is based on a sliding scale depending on TSR achieved over the relevant period. No vesting of this element occurs unless the Company's TSR ranks it in the top 50 per cent of the companies of the FTSE 100 Index.

At this performance threshold 30 per cent of this element (i.e. 7.5 per cent of the potential total award) vests. If the return ranks the Company in the top 25 per cent of the Index this element (i.e. 25 per cent of the potential total award) vests in full. Between these thresholds this element vests on a straight-line basis.

### *Third Element*

Twenty five per cent of the potential total award has a performance criterion based on TSR relative to a bespoke comparator group as described below.

The performance criterion for this element is also based on a sliding scale depending on TSR achieved over the relevant period.

No vesting of this element occurs unless the Company's TSR exceeds that of the bottom six companies constituting a comparator group comprising 12 tobacco and alcohol companies as detailed below. At this performance threshold, 30 per cent of this element (i.e. 7.5 per cent of the potential total award) vests. If the return ranks the Company in the top three of the comparator group, this element (i.e. 25 per cent of the potential total award) vests in full. Between these thresholds this element vests on a straight-line basis.

The comparator group for the November 2010 award remains:

AB InBev	Altria Group Inc.	British American Tobacco PLC	Carlsberg A/S
Diageo PLC	Heineken N.V.	Imperial Tobacco Group PLC	Japan Tobacco Inc.
Philip Morris International Inc.	Pernod Ricard S.A.	Reynolds American Inc.	SABMiller PLC

To ensure our Executive Directors and senior managers are incentivised to drive our underlying performance and to ensure that corporate actions or fluctuations in exchange rates do not unduly affect comparative underlying performance the Remuneration Committee has agreed the following protocols:

- if a company within the bespoke comparator group is delisted during the performance period it will be replaced from the start of the performance period, in an agreed order, by a substitute company from a pre-determined list of Lorillard Inc, Foster's Group Limited and Molson Coors Brewing Company;
- if any company in the comparator group undertakes a rights issue during the performance period a cash neutral approach of selling a portion of rights to take up the balance of the rights (commonly known as 'tail swallowing') will be applied; and
- to remove the undue influence of exchange rate fluctuations, TSR calculations are measured in the currency in which each company is listed.

The TSR calculations use share prices of each comparator group company averaged over a period of three months to determine the initial and closing prices rather than those applying on a single day. It is assumed that the cash flow of dividend payments is recognised on the date shares are declared ex dividend. This method is considered to give a fairer and less volatile result as improved performance has to be sustained for several weeks before it effectively impacts on the TSR calculations.

The TSR calculations are performed independently by Alithos Limited.

Each element operates independently and is capable of vesting regardless of the Company's performance in respect of the other elements.

During the year the Remuneration Committee reviewed the performance criteria, award policy, comparator group and vesting schedules for LTIP awards and decided that the three elements remain the most important measures that drive and measure sustainable improvement in shareholder value and support our longer-term KPIs, discussed on pages 22 to 24. The TSR criteria reflect comparative performance against the appropriate FTSE sector and the bespoke comparator group of companies. The EPS criterion reflects a key part of the Group's strategy to create sustainable shareholder value.

### *Vesting of Awards*

On vesting, a participant is granted an option to acquire the relevant number of shares. The option may be exercised at any time up to the seventh anniversary of its date of grant. Within this framework the vesting process in a number of jurisdictions outside the UK is amended to conform to local securities and tax legislation.

The performance periods are set prior to the granting of each annual award and there is no opportunity to re-test if any of the performance criteria are not achieved.

Under the rules of the LTIP, should Imperial Tobacco Group PLC 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.

The Remuneration Committee has absolute discretion to vary, but not increase, the extent to which any awards vest. This ensures awards only vest, and vest at an appropriate level, if there has been an improvement in the underlying financial performance of the Company, including the maintenance of long-term return on capital employed.

### Award Summary

Award as Percentage of Base Salary	Performance Criteria
200 for Chief Executive	50 per cent on EPS
150 for Finance Director	25 per cent on TSR against FTSE 100
100 for other Executive Directors	25 per cent on TSR against comparator group

### Executive Directors' Conditional Share Awards under the Long Term Incentive Plan (Audited)

	Balance at 1/10/2009	Granted during year	Date of grant	Market price at date of grant £	Vested during year (10/11/2009)	Market price at date of vesting £	Market price at date of exercise £	Lapsed during year	Amount realised on exercise £'000	Balance at 30/9/2010 <sup>1</sup>	Performance period
Mrs A J Cooper	15,803	–	01/11/06	18.57	(14,881)	18.28	19.04	(922)	–	–	2006-2009 <sup>2</sup>
	19,988	–	31/10/07	24.47	–	–	–	–	–	19,988	2007-2010 <sup>3</sup>
	31,972	–	26/11/08	14.70	–	–	–	–	–	31,972	2008-2011 <sup>4</sup>
	–	29,192	11/11/09	18.70	–	–	–	–	–	29,192	2009-2012 <sup>5</sup>
	67,763	29,192		–	(14,881)	–	–	(922)	–	81,152	
Mr R Dyrbus	49,270	–	01/11/06	18.57	(46,396)	18.28	19.04	(2,874)	–	–	2006-2009 <sup>2</sup>
	40,565	–	31/10/07	24.47	–	–	–	–	–	40,565	2007-2010 <sup>3</sup>
	63,571	–	26/11/08	14.70	–	–	–	–	–	63,571	2008-2011 <sup>4</sup>
	–	51,472	11/11/09	18.70	–	–	–	–	–	51,472	2009-2012 <sup>5</sup>
	153,406	51,472		–	(46,396)	–	–	(2,874)	–	155,608	
Mr G L Blashill	24,170	–	01/11/06	18.57	(22,760)	18.28	19.04	(1,410)	–	–	2006-2009 <sup>2</sup>
	19,752	–	31/10/07	24.47	–	–	–	–	–	19,752	2007-2010 <sup>3</sup>
	30,952	–	26/11/08	14.70	–	–	–	–	–	30,952	2008-2011 <sup>4</sup>
	–	25,061	11/11/09	18.70	–	–	–	–	–	25,061	2009-2012 <sup>5</sup>
	74,874	25,061		–	(22,760)	–	–	(1,410)	–	75,765	
Mr G Davis	103,499	–	01/11/06	18.57	(97,461)	18.28	19.04	(6,038)	–	–	2006-2009 <sup>2</sup>
	88,308	–	31/10/07	24.47	–	–	–	–	–	88,308	2007-2010 <sup>3</sup>
	140,544	–	26/11/08	14.70	–	–	–	–	–	140,544	2008-2011 <sup>4</sup>
	–	113,795	11/11/09	18.70	–	–	–	–	–	113,795	2009-2012 <sup>5</sup>
	332,351	113,795		–	(97,461)	–	–	(6,038)	–	342,647	

<sup>1</sup> Or date of retirement if earlier.

<sup>2</sup> Exercisable, upon the payment of the option exercise price of 1 penny, between 11 November 2009 and 10 November 2016.

<sup>3</sup> Exercisable, upon the payment of the option exercise price of 1 penny, between 1 November 2010 and 31 October 2017.

<sup>4</sup> Exercisable, upon the payment of the option exercise price of 1 penny, between 27 November 2011 and 26 November 2018.

<sup>5</sup> Exercisable, upon the payment of the option exercise price of 1 penny, between 12 November 2012 and 11 November 2019.

There have been no changes in any Executive Directors' awards since 30 September 2010, other than the vesting of the October 2007 – October 2010 award detailed below.

During the year, the November 2006 – November 2009 award vested partially. Based on EPS and TSR performance to the end of the financial year the first and second elements vested in full and approximately 76.7 per cent of the third element vested on 10 November 2009. The remaining shares under award lapsed.

In respect of the October 2007 – October 2010 award partial vesting occurred on 2 November 2010. Based on EPS and TSR performance to the end of the financial year the first element vested in full, approximately 74.5 per cent of the second element vested and the third element lapsed. For illustrative purposes only, the share price on 29 October 2010, being the latest practicable date prior to publication, was £19.99 valuing the awards as follows:

	Award lapsing No. of shares	Award vesting No. of shares over which option granted	Award vesting Illustrative value £'000
Mrs A J Cooper	6,269	13,719	274
Mr R Dyrbus	12,722	27,843	557
Mr G L Blashill	6,194	13,558	271

The value of any options exercised could vary significantly from that shown due to share price movements.

The Remuneration Committee regards the November 2008 – November 2011 and the November 2009 – November 2012 awards as being too distant from maturity to be included in the value projected above.

However, in respect of the November 2008 – November 2011 award, based upon interim measurement calculations prepared as at 30 September 2010, the first element would vest in full, approximately 30 per cent of the second element would vest and the third element would lapse if this performance were maintained over the relevant performance period.

In respect of the November 2009 – November 2012 award, based upon interim measurement calculations prepared as at 30 September 2010, approximately 48.6 per cent of the first element would vest and the second and third elements would lapse if this performance were maintained over the relevant performance period.

The illustrative values based on the above share price and performance criteria are as follows:

	No. of shares	November 2011 Illustrative value £'000	No. of shares	Illustrative awards vesting November 2012 Illustrative value £'000
Mrs A J Cooper	18,383	367	7,093	142
Mr R Dyrbus	36,554	731	12,507	250
Mr G L Blashill	17,797	356	6,090	122

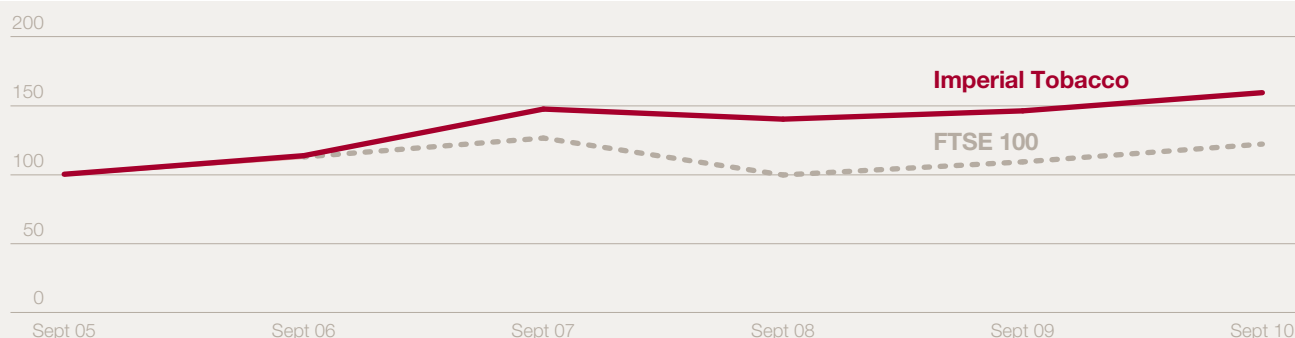
Evidence of the Group's sustained performance on a TSR basis when compared with the FTSE 100 Index is set out below.

We view the FTSE 100 Index as providing the most appropriate and widely recognised index for benchmarking our corporate performance, which is a constituent of that index, and reflects the benchmark index used as an LTIP performance criterion.

#### Share Options

The Company does not operate an executive share option scheme. Executive Directors are, however, eligible (along with all employees of the Company and participating subsidiaries of the Group, where possible) to participate in our savings related Sharesave Plan. Under this Plan options are granted to participants who have contracted to save up to £250 per month over a period of three or five years at a discount of up to 20 per cent to the closing mid-market price of an Imperial Tobacco Group PLC ordinary share on the London Stock Exchange on the day prior to invitation. In common with most plans of this type there are no performance conditions applicable to options granted under this Plan.

### Total return indices – Imperial Tobacco and FTSE 100





**Executive Directors' Share Options (Audited)**

	Balance at 1/10/2009	Granted during the year	Lapsed during the year	Exercised during the year	Market price at date of exercise 2/8/2010 <sup>1</sup> £	Balance at 30/09/2010 <sup>2</sup> £	Exercise price (rebased where appropriate) £	Range of exercisable dates of options held at 30/9/2010 <sup>3</sup>	Gains on exercise <sup>4</sup>	
									During the year £'000	2009 £'000
Mrs A J Cooper	729	–	–	–	–	729	12.54	01/08/12 – 31/01/13	–	–
	729	–	–	–	–	729		–	–	4
Mr R Dyrbus	252	–	–	(252)	18.04	–	14.96	01/08/10 – 31/01/11	1	–
	437	–	–	–	–	437	12.54	01/08/12 – 31/01/13	–	–
	–	232	–	–	–	232	15.63	01/08/13 – 31/01/14	–	–
	689	232	–	(252)	–	669		–	1	2
Mr G L Blashill	729	–	–	–	–	729	12.54	01/08/12 – 31/01/13	–	–
	729	–	–	–	–	729		–	–	8
Mr G Davis	656	–	–	–	–	656	14.96	01/08/12 – 31/01/13	–	–
	291	–	–	–	–	291	12.54	01/08/12 – 31/01/13	–	–
	947	–	–	–	–	947		–	–	

1 Mr R Dyrbus exercised on 2 August 2010.

2 Or date of retirement if earlier.

3 Any option not exercised by the end of the range of exercisable dates will expire.

4 Gains made on exercise, calculated as the difference between the exercise price and the market price on the date of exercise. Aggregate gains during the year were £776 (2009: £13,948).

There have been no changes in any Executive Directors' share options since 30 September 2010.

Our middle market share price at the close of business on 30 September 2010, being the last trading day of the financial year, was £18.97 and the range of the middle market price during the year was £17.53 to £21.54.

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.

**Share Ownership Guidelines**

We have adopted a set of 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 to align their interests with those of our shareholders.

Over a period of five years from appointment Executive Directors and other senior managers are required to build a holding in the Group's shares to a minimum value broadly equivalent to three times base salary for our Chief Executive and Finance Director and twice base salary in respect of the 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. All Executive Directors currently exceed their required shareholding.

**Revisions to Executive Directors' Remuneration**

Subject to consultation with our major shareholders and representative bodies, the Remuneration Committee has revised the policy for Executive Directors relating to the annual bonus opportunity and the SMS performance criterion as outlined below. These revisions are designed to further increase the emphasis on driving and rewarding performance, to bring the incentive pay structure more closely into line with our comparator group of FTSE 50 companies and to further support the Group's strategy by driving growth in revenues and profit, with high levels of cash conversion. The policy in respect of the LTIP and the share ownership guidelines remains unchanged.

**Maximum Annual Bonus Opportunity**

The potential maximum annual bonus will increase from 150 per cent to 200 per cent of base salary for the Chief Executive and from 135 per cent to 150 per cent for the Finance Director, but will remain unchanged at 120 per cent for the Group Sales and Marketing Director.

In support of the Group's KPIs, as set out on pages 22 to 24, the Remuneration Committee also determined that, for the financial year ending 30 September 2011, up to 75 per cent of the maximum annual bonus (representing up to 150 per cent of base salary for the Chief Executive) can be earned for achieving financial targets based on a matrix including growth in adjusted earnings per share and net revenue growth (which is subject to market share underpins). The remaining 25 per cent of the annual bonus (representing up to 50 per cent of base salary for the Chief Executive) can be earned for performance against stretching, quantifiable non-financial targets, subject to achievement of a minimum threshold in respect of the financial targets.

The non-financial targets are designed to support our growth strategy by driving performance against our key growth drivers, including volume targets incentivising sales growth in support of our cigarette volumes and white stick equivalents KPIs, debt reduction targets incentivising performance against our cash utilisation KPI and targets relating to anti-illicit trade activities supporting our focus on future foundations.

Any annual bonus earned up to 100 per cent of base salary for the Chief Executive and Finance Director and 85 per cent for the Group Sales and Marketing Director will be paid in cash and will be eligible for investment in the SMS. Any bonus payable in excess of these levels will be used to purchase the Company's shares which the Director will be required to retain for a minimum of three years. These shares are not eligible for investment in the SMS.

The Remuneration Committee further determined that from the financial year ending 30 September 2011 annual bonuses for Executive Directors and members of the Operating Executive would be subject to claw-back, during the three years following the end of the financial year in which the bonus was earned, 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 Remuneration Committee also reviewed and amended the SMS performance criterion for Executive Directors and members of the Operating Executive, from the February 2011 award onwards, such that it will continue to be based on Real Annual EPS Growth but the revised performance criterion will be on a more demanding sliding scale. Under the revised performance criterion, no matching shares will vest unless the Group's Real Annual EPS Growth is equal to three per cent, at which point one matching share will vest for every two shares invested. For maximum vesting to occur, the Group's Real Annual EPS Growth must equal, or exceed, six per cent, at which point one matching share will vest for every one share invested. Between these two points awards will vest on a straight-line basis.

#### Proposed Share Matching Scheme Vesting Scale

EPS Growth	Proposed New Scale	Previous Scale
Below RPI plus 3 per cent per annum	Zero	Zero
At RPI plus 3 per cent per annum	50%	100%
At RPI plus 6 per cent per annum	100% <sup>1</sup>	100%

<sup>1</sup> Sliding scale applies for performance between RPI plus 3 per cent and RPI plus 6 per cent.

#### 6 Executive Directors' Pensions

Since 6 April 2006 ('A' day) the Group's UK pension policy, which applies to all current Executive Directors, provides the option to maintain membership of or, in respect of new employees, join the UK Imperial Tobacco Pension Fund (the Fund) or receive a salary supplement in lieu of membership of the Fund.

The Executive Directors are all members of the Fund, the principal defined benefit scheme operated by the Group. For members who joined prior to 1 April 2002 the Fund is largely non-contributory with a normal retirement age of 60. The Fund allows members to achieve the maximum pension of two-thirds of their salary at normal retirement age, usually after 32 years' service. Pension commutation to enable participants to receive a lump sum on retirement is permitted.

For death before retirement, a capital sum equal to four times salary is payable together with a spouse's pension of two-thirds of the member's expected pension at retirement. For death in retirement, a spouse's pension of two-thirds of the member's pre-commutation pension is payable. Dependant children will also receive allowances.

Pensions increase annually by the lesser of 10 per cent and the increase in the Retail Prices Index, together with an option under the rules to surrender part of a pension in order for the annual increase to be in line with the increase in the Retail Prices Index to a maximum of 15 per cent.

New members of the Fund after 30 September 2010 will accrue pension benefits on a defined contribution basis. Members who joined the Fund prior to 1 October 2010 will continue to accrue pension benefits in the Fund on a defined benefit basis, as set out above. All Executive Directors accrue pension benefits on the defined benefit basis.

From 6 April 2006 a new tax regime was introduced by HM Revenue & Customs (HMRC) which abolished most of the detailed limits previously imposed on pension schemes and replaced them with a simplified approach. Each member now has a Lifetime Allowance (LTA), £1.80 million for retirements in the tax year 2010/2011 and a tax, called the lifetime allowance charge, is levied at retirement if the value of their pension benefit from all sources exceeds this amount. For any member whose total benefit value on 6 April 2006 exceeded the LTA, transitional arrangements allowed them to register the higher value so that they would not be subject to a large retrospective LTA charge. To qualify for this enhanced protection the member was required to opt out of Fund membership in respect of future service accrual in order to retain a final salary linked pension entitlement in respect of past service.

All Executive Directors earn benefits on the standard scale with a normal retirement age of 60. Other than Mrs A J Cooper, each of the current Executive Directors has opted out of Fund membership in respect of future service accrual as a result of registering for enhanced protection with HMRC. The detailed HMRC rules governing enhanced protection mean that it may not be permissible, in some rare circumstances, for the full final salary linked pension based on service up to 6 April 2006 to be paid from the Fund. In this event an additional pension will be paid by the Company through an unfunded unapproved retirement benefit scheme (UURBS) so that the full accrued benefit may be provided.

Mr R Dyrbus is in receipt of a salary supplement of 35 per cent of salary, which is in lieu of future pensionable service accrual and arises because his accrued pension on 6 April 2006 was well below the maximum pension of two-thirds of salary. Mrs A J Cooper is also in receipt of a salary supplement. Prior to 6 April 2006 her pension benefits were limited by the effect of HMRC's earnings cap. Although this cap was removed as from 6 April 2006, the Fund did not disapply it in respect of past pensionable service but maintained its own earnings cap going forward. For service from 6 April 2006 onwards and for pensionable salary in excess of the Fund's earnings cap, the standard Fund benefit is a pension at the lower accrual rate of 1/60ths with a 50 per cent spouse's pension and member contributions of 5 per cent of this top slice of salary are payable.

As an alternative to extra pension accrual on this top slice of salary through the UURBS, Mrs Cooper receives a salary supplement of 12 per cent of this amount.

In each case these 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.

The following table provides the information required by both the Listing Rules and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (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 (any potential UURBS entitlement is included);
- the increase in accrued pension during the year, excluding any increases for inflation in respect of the disclosure required under the Listing Rules; and
- the transfer value of the increase in accrued pension calculated in accordance with the latest Regulations.

None of the Executive Directors have made additional voluntary contributions.

### Executive Directors' Pension Disclosures (Audited)

	Disclosures required under the Regulations									Listing Rules	
	Accrued pension £'000					Transfer value of accrued pension £'000				£'000	
	Age at 30/09/2010 Years	Pensionable service at 30/09/2010 Years	At 1/10/2009	Increase during the year	At 30/09/2010	At 1/10/2009	Increase/ (decrease) during the year net of Director's contributions	Director's contribution	At 30/09/2010	Increase in accrued pension (net of inflation) during the year	Transfer value of increase (net of inflation)
Mrs A J Cooper	44	11	62	20	82	563	238	21	822	18	183
Mr R Dyrbus	57	28	315	9	324	4,921	524	–	5,445	2	31
Mr G L Blashill <sup>1</sup>	63	42	297	15	312	5,598	646	–	6,244	8	133
<b>Former Director</b>											
Mr G Davis <sup>2</sup>	60	38	689	12	701	11,913	887	–	12,800	–	–

1 Mr G L Blashill drew pension during the course of the year, as is permitted under the Fund rules. Mr Blashill was still in employment as at 30 September 2010. The transfer value figures in the table above incorporate allowance for the benefits paid out in order to provide a consistent comparison with previous figures. The accrued pension figures represent the benefits accrued, assuming that Mr Blashill first started to draw pension from the relevant date. The figures shown are consistent with those disclosed at 30 September 2009.

2 Mr G Davis retired from the Board on 12 May 2010 and drew his pension from the Fund immediately. The transfer value and accrued pension figures are calculated at 12 May 2010 allowing for market conditions at 30 September 2010.

### 7 Other information

#### Employee Benefit Trusts

The Imperial Tobacco Group 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) have been established to acquire shares in the Company by subscription or purchase. Funds to enable these acquisitions are provided by the Group to satisfy rights to shares arising on the exercise of share options and on the vesting of the SMS and LTIP awards.

As at 30 September 2010, the Company held 49,569,000 ordinary shares in treasury which can be used to satisfy options and awards under its employee share plans either directly by the Company or by the Company gifting them to the Employee Benefit Trusts.

Options and awards may also be satisfied by the issue of new ordinary shares.

Details of the shareholdings by the Employee Benefit Trusts are as follows:

	Balance at 1/10/2009	Acquired during year	Distributed during year	Balance at 30/09/2010	Ordinary shares under Award at 30/09/2010	Surplus/ (Shortfall)
Executive Trust	1,078,519	162,000	494,417	746,102	740,637	5,565
2001 Trust	2,430,573	1,750,000	1,167,106	3,013,467	4,922,476	(1,909,009)

#### Share Plan Flow Rates

Our policy has always been to satisfy all options and awards under employee share plans from market purchased ordinary shares through the Employee Benefit Trusts or through treasury shares transferred to the Employee Benefit Trusts.

The Trust Deeds of the Employee Benefit Trusts and the rules of all our employee share plans contain provisions limiting awards to five per cent in five years and ten per cent in ten years for all employee share plans with an additional restriction to five per cent in ten years for executive share plans. Currently an aggregate total of 2.8 per cent of the Company's issued share capital is subject to options and awards under the Group's executive and all employee share plans. The Employee

Benefit Trusts have also been provided with ordinary shares held by the Company in treasury in order to satisfy vesting awards and option exercises.

Since demerger in 1996, the cumulative number of shares under option and award granted pursuant to all of the Company's employee share plans totals 2.8 per cent of its issued share capital. Following initial grants on demerger, subsequent annual grants have averaged 0.3 per cent of issued share capital.

<b>Summary of Options and Awards Granted</b>		
Limit on awards	Cumulative Options and Awards granted as a percentage of issued share capital	Options and Awards granted during the year as a percentage of issued share capital
10% in 10 years	2.0	0.2
5% in 5 years	1.0	0.2
5% in 10 years (executive plans)	1.0	0.1

#### **Consultancy Agreement with Non-Executive Deputy Chairman**

In addition to his appointment as Non-Executive Deputy Chairman, Mr J-D Comolli entered into an agreement with Imperial Tobacco Limited, the Group's principal operating company.

Under this agreement he provided consultancy services to the Group and received fees up to a maximum of €850,000 per annum.

The agreement terminated on 31 January 2010 and was replaced with an eight month agreement paid at the rate of €20,000 per month. The replacement agreement terminated early upon Mr Comolli's resignation on 14 September 2010.

#### **Remuneration Arrangements for Former Executive Directors**

##### **Mr D Cresswell**

Following his retirement from the Board in December 2007, Mr D Cresswell remains a member of Supervisory Boards within the Reemtsma group and the Board of Imperial Vina Danang Company Limited.

##### **Mr M A Häussler**

Mr M A Häussler is currently in receipt of a retirement pension that has been reduced because it was taken before he reached his normal retirement age. His service agreement with the Group provided that he would receive similar overall pension benefits to those that he would have received had he remained in the Reemtsma Cigarettenfabriken GmbH pension arrangement. This was a pension for life equivalent to 42 per cent of his fixed annual salary at age 63. For death in retirement, a spouse's pension for life of 60 per cent of that amount would be payable. The pension is made up of two parts: one part payable from the unfunded pension arrangement of Reemtsma Cigarettenfabriken GmbH, the other part payable from the separately funded Imperial Tobacco Pension Fund. The pension payable under the Reemtsma arrangement and from the Imperial Tobacco Pension Fund may be increased annually in accordance with the Rules of those arrangements, or as required by law.

##### **Mr S Huismans**

Following his retirement from the Board in January 2006, Mr S Huismans remains a member of Supervisory Boards within the Reemtsma Group. He was also appointed as a non-executive director of Altadis, S.A. upon its acquisition by the Group in January 2008 until November 2008. Mr Huismans received additional remuneration for fulfilling such non-executive roles.

##### **Mr S T Painter**

Following his retirement in May 2000, Mr S T Painter entered into a consultancy agreement with Imperial Tobacco Limited, the Group's principal operating company.

The agreement, as amended in October 2001 and May 2004, ran until March 2007. Under the terms of the agreement he provided consultancy services as required and received fees at a day rate of £1,000 with a minimum fee based on 100 days' service for each 12 month period ending on 30 June 2006, and 67 days for the period 1 July 2006 to 6 March 2007.


Mr Painter continued to provide consultancy services until July 2010 as required and received fees at a day rate of £1,000. He was entitled to reimbursement for the use of his car.

Mr Painter was also a member of Supervisory Boards within the Reemtsma Group until December 2009 and, between January and October 2008, the Altadis Group for which he received additional remuneration for fulfilling such non-executive roles. He remains a Director of Altadis Maroc.

##### **Mr B Setrakian**

Following his appointment to the Board in June 2008, Mr B Setrakian retained a number of appointments within Altadis' USA business. He resigned from these appointments in December 2008. Mr Setrakian received additional remuneration for fulfilling such non-executive roles.

For the Board



#### **P H Jungels**

Chairman of the Remuneration Committee  
2 November 2010



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# Independent Auditors' Report

to the Members of Imperial Tobacco Group PLC

We have audited the Group financial statements of Imperial Tobacco Group PLC for the year ended 30 September 2010 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Balance Sheet, the Consolidated Statement of Changes in Equity, the Consolidated Cash Flow Statement, the Accounting Policies and related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

## Respective Responsibilities of Directors and Auditors

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

This report, including the opinions, has been prepared for and only for the 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.

## Scope of the Audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the 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.

## Opinion on Financial Statements

In our opinion the Group financial statements:

- give a true and fair view of the state of the Group's affairs as at 30 September 2010 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with 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.

## Opinion on Other Matters Prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the Group financial statements are prepared is consistent with the Group financial statements.

In our opinion the information given in the Corporate Governance Report set out with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

## Matters on Which We Are Required to Report by Exception

We have nothing to report in respect of the following:

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; or
- we have not received all the information and explanations we require for our audit; or
- a corporate governance statement has not been prepared by the parent company.

Under the Listing Rules we are required to review:

- the Directors' statement in the Corporate Governance Report, in relation to going concern; and
- the part of the Corporate Governance Report relating to the Company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

## Other Matter

We have reported separately on the parent company financial statements of Imperial Tobacco Group PLC for the year ended 30 September 2010 and on the information in the Directors' Remuneration Report that is described as having been audited.



## David Charles (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Bristol

2 November 2010

# Consolidated Income Statement

for the year ended 30 September 2010

£ million unless otherwise indicated	Notes	Year ended 30 September 2010	Year ended 30 September 2009
<b>Revenue</b>	1	<b>28,173</b>	26,517
Duty and similar items		(13,155)	(11,769)
Other cost of sales		(9,563)	(9,432)
Cost of sales		(22,718)	(21,201)
<b>Gross profit</b>		<b>5,455</b>	5,316
Distribution, advertising and selling costs		(2,001)	(1,979)
Administrative and other expenses		(926)	(1,000)
<b>Operating profit</b>	1	<b>2,528</b>	2,337
Investment income	5	844	1,180
Finance costs	5	(1,254)	(2,572)
Net finance costs	5	(410)	(1,392)
<b>Profit before taxation</b>	2	<b>2,118</b>	945
Taxation	6	(596)	(268)
<b>Profit for the year</b>		<b>1,522</b>	677
Attributable to:			
Owners of the parent		1,505	663
Non-controlling interests		17	14
<b>Earnings per ordinary share (pence)</b>			
– Basic	8	148.5	65.5
– Diluted	8	148.0	65.3

All activities derive from continuing operations.

# Consolidated Statement of Comprehensive Income

for the year ended 30 September 2010

£ million	Year ended 30 September 2010	Year ended 30 September 2009
<b>Profit for the year</b>	<b>1,522</b>	677
<b>Other comprehensive income</b>		
Exchange movements	(174)	709
Tax effect of exchange movements	(9)	(112)
Net actuarial losses on retirement benefits	(111)	(582)
Deferred tax relating to net actuarial losses on retirement benefits	19	173
<b>Other comprehensive (loss)/income for the year, net of tax</b>	<b>(275)</b>	188
<b>Total comprehensive income for the year</b>	<b>1,247</b>	865
Attributable to:		
Owners of the parent	<b>1,229</b>	845
Non-controlling interests	<b>18</b>	20
<b>Total comprehensive income for the year</b>	<b>1,247</b>	865

## Reconciliation from operating profit to adjusted operating profit

£ million	Notes	Year ended 30 September 2010	Year ended 30 September 2009
<b>Operating profit</b>		<b>2,528</b>	2,337
Acquisition accounting adjustments	29	<b>24</b>	–
Amortisation of acquired intangibles		<b>451</b>	451
Restructuring costs	3	<b>64</b>	145
<b>Adjusted operating profit</b>		<b>3,067</b>	2,933

## Reconciliation from net finance costs to adjusted net finance costs

£ million	Notes	Year ended 30 September 2010	Year ended 30 September 2009
<b>Net finance costs</b>		<b>(410)</b>	(1,392)
Fair value (gains)/losses on derivative financial instruments providing commercial hedges	5	<b>(210)</b>	660
Post-employment benefits net financing cost	5	<b>20</b>	32
<b>Adjusted net finance costs</b>		<b>(600)</b>	(700)



# Consolidated Balance Sheet

at 30 September 2010

£ million	Notes	30 September 2010	30 September 2009	30 September 2008
<b>Non-current assets</b>				
Intangible assets	9	20,941	22,357	19,817
Property, plant and equipment	10	1,971	2,010	1,820
Investments in associates	11	18	22	16
Retirement benefit assets	18	25	17	441
Trade and other receivables	13	97	99	98
Derivative financial instruments	16	327	134	120
Deferred tax assets	17	150	148	392
		23,529	24,787	22,704
<b>Current assets</b>				
Inventories	12	3,019	2,925	2,858
Trade and other receivables	13	3,000	3,011	2,951
Current tax assets	6	51	52	31
Cash and cash equivalents	14	773	1,036	642
Derivative financial instruments	16	243	198	99
		7,086	7,222	6,581
<b>Total assets</b>		<b>30,615</b>	<b>32,009</b>	<b>29,285</b>
<b>Current liabilities</b>				
Borrowings	16	(329)	(2,560)	(2,678)
Derivative financial instruments	16	(262)	(284)	(123)
Trade and other payables	15	(7,710)	(7,451)	(6,183)
Finance lease liabilities	26	(1)	(2)	(2)
Current tax liabilities	6	(653)	(551)	(370)
Provisions	19	(187)	(292)	(187)
		(9,142)	(11,140)	(9,543)
<b>Non-current liabilities</b>				
Borrowings	16	(10,003)	(9,507)	(9,558)
Derivative financial instruments	16	(748)	(1,033)	(163)
Trade and other payables	15	(21)	(23)	(14)
Finance lease liabilities	26	(24)	(26)	(24)
Deferred tax liabilities	17	(2,074)	(2,098)	(2,310)
Retirement benefit liabilities	18	(867)	(811)	(546)
Provisions	19	(647)	(776)	(771)
		(14,384)	(14,274)	(13,386)
<b>Total liabilities</b>		<b>(23,526)</b>	<b>(25,414)</b>	<b>(22,929)</b>
<b>Net assets</b>		<b>7,089</b>	<b>6,595</b>	<b>6,356</b>
<b>Equity</b>				
Share capital	20	107	107	107
Share premium		5,833	5,833	5,833
Retained earnings		206	(469)	(109)
Exchange translation reserve		883	1,067	476
<b>Equity attributable to owners of the parent</b>		<b>7,029</b>	<b>6,538</b>	<b>6,307</b>
Non-controlling interests		60	57	49
<b>Total equity</b>		<b>7,089</b>	<b>6,595</b>	<b>6,356</b>

In accordance with IAS 1 (Revised) Presentation of Financial Statements and as explained in the Accounting Policies note, previously reported figures for derivative financial instruments have been re-analysed between current and non-current classifications, and an additional balance sheet has been presented as at 30 September 2008.

The financial statements on pages 98 to 151 were approved by the Board of Directors on 2 November 2010 and signed on its behalf by:

**Iain Napier**  
Chairman

**Robert Dyrbus**  
Director

# Consolidated Statement of Changes in Equity

for the year ended 30 September 2010

£ million	Share capital	Share premium	Retained earnings	Exchange translation reserve	Equity attributable to owners of the parent	Non-controlling interests	Total equity
<b>At 1 October 2008</b>	107	5,833	(109)	476	6,307	49	6,356
Profit	–	–	663	–	663	14	677
Exchange movements	–	–	–	703	703	6	709
Current tax effect of exchange movements	–	–	–	(112)	(112)	–	(112)
Net actuarial losses on retirement benefits	–	–	(582)	–	(582)	–	(582)
Deferred tax relating to net actuarial losses on retirement benefits	–	–	173	–	173	–	173
<b>Total comprehensive income</b>	–	–	254	591	845	20	865
<b>Transactions with owners</b>							
Cash from employees on maturity/exercise of share schemes	–	–	6	–	6	–	6
Costs of employees' services compensated by share schemes	–	–	21	–	21	–	21
Current tax on share-based payments	–	–	2	–	2	–	2
Deferred tax on share-based payments	–	–	(3)	–	(3)	–	(3)
Dividends paid	–	–	(640)	–	(640)	(12)	(652)
<b>At 30 September 2009</b>	<b>107</b>	<b>5,833</b>	<b>(469)</b>	<b>1,067</b>	<b>6,538</b>	<b>57</b>	<b>6,595</b>
Profit	–	–	1,505	–	1,505	17	1,522
Exchange movements	–	–	–	(175)	(175)	1	(174)
Deferred tax effect of exchange movements	–	–	–	(9)	(9)	–	(9)
Net actuarial losses on retirement benefits	–	–	(111)	–	(111)	–	(111)
Deferred tax relating to net actuarial losses on retirement benefits	–	–	19	–	19	–	19
<b>Total comprehensive income</b>	–	–	<b>1,413</b>	<b>(184)</b>	<b>1,229</b>	<b>18</b>	<b>1,247</b>
<b>Transactions with owners</b>							
Cash from employees on maturity/exercise of share schemes	–	–	5	–	5	–	5
Costs of employees' services compensated by share schemes	–	–	28	–	28	–	28
Current tax on share-based payments	–	–	2	–	2	–	2
Deferred tax on share-based payments	–	–	(1)	–	(1)	–	(1)
Other deferred tax movements	–	–	2	–	2	–	2
Changes in non-controlling interests in shareholdings	–	–	(1)	–	(1)	(3)	(4)
Dividends paid	–	–	(773)	–	(773)	(12)	(785)
<b>At 30 September 2010</b>	<b>107</b>	<b>5,833</b>	<b>206</b>	<b>883</b>	<b>7,029</b>	<b>60</b>	<b>7,089</b>

Cumulative goodwill of £2,410 million relating to acquisitions prior to 1998 was written off directly to reserves in line with the requirements of the accounting standards that were in force at the time.

# Consolidated Cash Flow Statement

for the year ended 30 September 2010

£ million	Notes	Year ended 30 September 2010	Year ended 30 September 2009
<b>Cash flows from operating activities</b>	25	<b>2,859</b>	3,569
<b>Cash flows from investing activities</b>			
Interest received		29	57
Purchase of property, plant and equipment		(269)	(245)
Proceeds from sale of property, plant and equipment		26	69
Purchase of intangible assets – software		(14)	(8)
Purchase of intangible assets – trademarks and supply agreements		–	(4)
Purchase of businesses – net of cash acquired		24	(46)
Proceeds from sale of businesses – net of cash disposed		5	–
<b>Net cash used in investing activities</b>		<b>(199)</b>	(177)
<b>Cash flows from financing activities</b>			
Interest paid		(609)	(562)
Cash from employees on maturity/exercise of share schemes		5	6
Settlement of exchange rate derivative financial instruments		(299)	(5)
Increase in borrowings		1,542	4,324
Repayment of borrowings		(2,790)	(6,042)
Reduction/(increase) in collateralisation deposits		70	(125)
Repayment of obligations under finance leases		(2)	(2)
Dividends paid to non-controlling interests		(12)	(12)
Dividends paid to owners of the parent		(773)	(640)
<b>Net cash used in financing activities</b>		<b>(2,868)</b>	(3,058)
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(208)</b>	334
Cash and cash equivalents at start of year		1,036	642
Effect of foreign exchange rates on cash and cash equivalents		(55)	60
<b>Cash and cash equivalents at end of year</b>		<b>773</b>	1,036

# Accounting Policies

## Basis of Preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and IFRIC interpretations as adopted by the European Union (collectively IFRS) and 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, retirement benefit schemes, share schemes, intangible assets and property, plant and equipment.

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 the Critical Accounting Estimates and Judgements note on pages 110 and 111. 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 Group accounting policies is set out below.

## Adoption of IAS 1 (Revised) Presentation of Financial Statements

The adoption of IAS 1 (Revised) has had no impact on the net assets or results of the Group, resulting only in changes to the format and content of the primary statements including derivative financial instruments assets and liabilities (including comparatives) being classified according to their settlement as described below.

## Classification of Derivative Financial Instruments Between Assets and Liabilities

Derivative financial instruments providing commercial hedges but not designated as hedges for accounting purposes under IAS 39 were previously all classified as current assets and liabilities. Since it is our intention to hold these financial instruments to maturity we have, following the adoption of IAS 1 (Revised), now classified them according to their contractual cash settlements with the following effects.

£ million	30 September 2009			30 September 2008		
	Previously reported	Reclassification	Reclassified	Previously reported	Reclassification	Reclassified
Non-current derivative financial instrument assets	9	125	134	76	44	120
Current derivative financial instrument assets	239	(41)	198	97	2	99
Current derivative financial instrument liabilities	(564)	280	(284)	(238)	115	(123)
Non-current derivative financial instrument liabilities	(669)	(364)	(1,033)	(2)	(161)	(163)
Net derivative financial instruments	(985)	–	(985)	(67)	–	(67)

At 30 September 2010, under the previous method of classification, non-current derivative financial instrument assets would have been nil, current derivative financial instrument assets would have been £549 million, current derivative financial instrument liabilities would have been £718 million and non-current derivative financial instrument liabilities would have been £271 million.

The revised treatment has no effect on profit or loss or net assets in 2008, 2009 or 2010.

## Adoption of IFRS 8 Operating Segments

The adoption of IFRS 8 has resulted in some presentational changes, but has not significantly affected the overall level of segmental analysis provided. We have taken advantage of early adoption of 2009 annual improvements to IFRS 8 not to disclose segmental asset measures as they are not reported to the chief operating decision maker.



**Basis of Consolidation**

The consolidated financial statements comprise the results of Imperial Tobacco Group PLC (the Company) and its subsidiary undertakings.

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an enterprise taking into account any potential voting rights. 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. Transactions with non-controlling interests are treated as transactions with parties external to the Group.

Intragroup transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless costs cannot be recovered.

A list of the principal subsidiaries is included on pages 157 and 158.

**Joint Ventures**

Joint ventures are those businesses which the Group and third parties jointly control. The financial statements of joint ventures are consolidated using the proportionate method, with the Group's share of assets and liabilities recognised in the balance sheet classified according to their nature. In the same way, the Group's share of income and expenses is presented in the consolidated income statement in accordance with their function.

If necessary, adjustments are made to the financial statements of these companies to align their accounting policies with those used by the Group.

**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, which are an appropriate approximation of the rates ruling at the dates of transactions in the income and cash flow statements. 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.

Any translation differences that have arisen since 1 October 2004 are presented as a separate component of equity. As permitted by IFRS 1, any differences prior to this date are not included in this separate component of equity.

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 income statement, except when treated as qualifying net investment hedges.

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 are transferred to other comprehensive income and offset any gains or losses on translation of the net assets.

**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 collectibility of the related receivables is reasonably assured. Sales of services, which include fees for distributing third party products, are recognised in the accounting period in which the services are rendered. Licence fees are recognised on an accruals basis in accordance with the substance of the relevant agreements.

For the Logistics business, revenue comprises the invoiced value for the sale of goods and services net of sales taxes, rebates and discounts. 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.

## 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 the income statement as an expense. Where duty is a sales tax, duty is excluded from revenue. Payments due in the United States under the Master Settlement Agreement and the Fair and Equitable Tobacco Reform Act are considered to be levies having the characteristics of duty and are treated as a production tax.

## Taxes

Tax on the profit or loss for the year comprises current and deferred tax.

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. The Group 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. The Group applies this test to each individual uncertain position. The Group measures the uncertain positions based on the single most likely outcome.

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. However, the deferred tax is not accounted for 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 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 assets and liabilities are not discounted. 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.

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.

Tax is recognised in the income statement, except where it relates to items recognised in other comprehensive income or directly in equity, in which case it is recognised in other comprehensive income or equity.

## Dividends

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, while 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 arising on acquisitions made on or after 27 September 1998 is capitalised. Previously all goodwill was written off through equity in the period of acquisition. As permitted under IFRS 1, goodwill arising on acquisitions prior to 1 October 2004 is stated in accordance with UK GAAP and has not been remeasured on transition to IFRS. Goodwill is tested at least annually for impairment and carried at cost less accumulated impairment losses. Any impairment is recognised immediately in the income statement and cannot be subsequently reversed. Goodwill is allocated to groups of cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose. Gains or losses on the disposal of a Group company are determined by comparing the proceeds with the carrying value of the Group company's assets and liabilities including the carrying amount of related goodwill.

Goodwill previously written off directly to reserves under UK GAAP is not reclassified to the income statement on the disposal of the subsidiary to which it relates.

## Intangible Assets – Other

Other intangible assets are initially recognised in the 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, 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. Other trademarks, supply agreements (including customer relationships) and computer software are amortised over their estimated useful lives as follows:

Other trademarks	20 – 30 years	straight line
Supply agreements	3 – 15 years	straight line
Computer software	3 – 5 years	straight line

### Property, Plant and Equipment

Property, plant and equipment are initially recognised in the 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 depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs 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. All other repairs and maintenance costs are charged to the income statement as incurred.

Land is not depreciated. Depreciation is provided on other property, plant and equipment so as to write off the initial cost of each asset to its residual value over its estimated useful life as follows:

Buildings	up to 50 years	straight line
Plant and equipment	2 – 20 years	straight line/reducing balance
Fixtures and motor vehicles	2 – 14 years	straight line

The assets' residual values and useful lives are reviewed and, if appropriate, adjusted at each balance sheet date.

Gains and losses on disposals are determined by comparing proceeds with carrying amounts. These are included in the income statement.

### Leases

Assets acquired under finance leases are included within property, plant and equipment. They are initially valued at the lower of fair value and the present value of the minimum lease payments. The assets are depreciated over the shorter of the lease term and the useful life of the asset. The associated lease liabilities are recognised in the balance sheet and the interest element of the leasing payments is charged to the income statement.

Rental payments under operating leases are charged to the income statement on a straight line basis over the lease term.

### Impairment of Assets

Assets that are not subject to amortisation or depreciation are tested at least annually for impairment. Assets that are subject to amortisation or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised in the income statement for the amount by which the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is the higher of the fair value less costs to sell and the value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

### Financial Instruments

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 (including cash and cash equivalents). 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 income statement. For interest-bearing assets, the carrying value includes accrued interest receivable.

Cash and cash equivalents include cash in hand and deposits held on call, together with other short-term highly liquid investments.

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.

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 assets and liabilities are included in the balance sheet at fair value, which includes accrued interest receivable and payable where relevant. However, as the Group has decided (as permitted under IAS 39) not to apply cash flow or fair value hedge accounting for its derivative financial instruments, changes in fair values are recognised in the 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 on the 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) but excludes borrowing costs. 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 twelve months is classified as a current asset, consistent with recognised industry practice.

## **Provisions**

A provision is recognised in the 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**

The Group operates a number of retirement benefit schemes for its employees, including both defined benefit and defined contribution schemes.

Under a defined benefit scheme, the amount of retirement benefit that will be received by an employee is defined with respect to period of service and final salary. The amount recognised in the 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. 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 outflows.

The service cost of providing retirement benefits to employees during the year is charged to operating profit.

Past service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight line basis over the average vesting period. 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.

A credit representing the expected return on plan assets of the retirement benefit schemes during the year is included within net finance costs. This is based on the market value of the assets of the schemes at the start of the financial year. A charge is also made within net finance costs for the expected increase in the present value of the liabilities of the retirement benefit schemes during the year arising from the schemes being one year closer to payment.

For defined contribution schemes, the Group pays a defined contribution to the scheme. There are no further payment obligations once these contributions have been paid. Such contributions are recognised as an employee benefit expense when they are due. Any prepaid contributions are recognised as an asset to the extent that a cash refund or reduction in future payments is available.

## **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 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 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.



**Share Capital**

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where 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 cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to owners of the parent.

**Use of Adjusted Measures**

Management believes that reporting non-GAAP or adjusted measures provides a useful comparison of business performance and reflects the way in which the business is controlled. Accordingly, adjusted measures of operating profit, net finance costs, profit before tax, taxation, attributable earnings and earnings per share exclude, where applicable, acquisition accounting adjustments, amortisation of acquired intangibles, restructuring costs, post-employment benefits net financing cost, fair value gains and losses on derivative financial instruments in respect of commercially effective hedges and related taxation effects. Reconciliations between adjusted and reported operating profit are included within note 1 to the financial statements, adjusted and reported net finance costs in note 5, adjusted and reported taxation in note 6, and adjusted and reported earnings per share in note 8. 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 exclude all interest on items not included within 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 Accounting Adjustments**

Acquisition accounting adjustments eliminate costs charged to the income statement as a consequence of investigations into alleged foreign trading violations in the period prior to our acquisition of Reemtsma which are recoverable from the sellers. IFRS 3 requires that adjustments to the cost of an acquisition are taken to goodwill, whereas changes in measurement of assets and liabilities after the provisional fair value period are taken to the income statement. These items are excluded from our adjusted earnings measures since the costs do not relate to the current trading performance of the Group and the amounts are recoverable from the sellers.

**Amortisation 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 of acquired intangibles, other than software, and the deferred tax associated with amortisation of acquired intangibles and tax deductible goodwill. The deferred tax liability 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. Impairment of goodwill is also excluded from our adjusted measures.

**Fair Value Gains and Losses on Derivative Financial Instruments**

IAS 39 requires that all derivative financial instruments are recognised in the balance sheet at fair value, with changes in the fair value being recognised in the 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 providing commercial hedges 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 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 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 expected return on plan assets and the interest on retirement benefit liabilities, together with the unwind of discount on redundancy and social plans costs included in restructuring provisions, are reported within net finance costs. These items together with their related tax effects are excluded from our adjusted earnings measures.

### Other Non-GAAP Measures Used by Management

#### Net Revenue

Net revenue comprises the Tobacco business revenue less duty and similar items. Management considers this an important measure in assessing the profitability of Tobacco operations.

#### Distribution Fees

Distribution fees comprises the Logistics segment revenue excluding the cost of distributed products. Management considers this an important measure in assessing the profitability of Logistics operations.

#### Adjusted Net Debt

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals, the fair value of derivative financial instruments providing commercial cash flow hedges and finance lease liabilities.

### New Accounting Standards and Interpretations

The following standards and interpretations became effective for the current reporting period:

IAS 1 (Revised)	Presentation of Financial Statements
IAS 23 (Revised)	Borrowing Costs
IAS 27 (Revised)	Consolidated and Separate Financial Statements
IAS 32 and IAS 1 (amendment)	Puttable Financial Instruments
IAS 39 (amendments)	Reclassification of Financial Assets and Eligible Hedged Items
IAS 39/IFRIC 9 (amendment)	Embedded Derivatives
IFRS 1 and IAS 27 (amendment)	Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate
IFRS 2 (amendment)	Amendments to IFRS 2 Share-Based Payment – Vesting Conditions and Cancellations
IFRS 3 (Revised)	Business Combinations
IFRS 7 (amendment)	Financial Instruments: Disclosures
IFRS 8	Operating Segments
IFRIC 12	Service Concession Arrangements
IFRIC 13	Customer Loyalty Programmes
IFRIC 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction
IFRIC 16	Hedges of a Net Investment in a Foreign Operation
IFRIC 17	Distributions of Non-cash Assets to Owners

Application of these standards and interpretations has not had a material impact on the net assets or results of the Group.

The following standards and interpretations were issued but application was not mandatory for the period:

IFRS 2 (amendment)	Group Cash-Settled Share-Based Payments
IFRS 9	Financial Instruments
IFRIC 15	Agreements for the Construction of Real Estate
IFRIC 18	Transfers of Assets from Customers
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments

The Directors anticipate that the adoption of these standards and interpretations will have no material impact on the net assets or results of the Group.

# 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

In accordance with IFRS, the Group recognises liabilities where there is a present obligation from a past event, a transfer of economic benefits is probable and the amount of costs of the transfer can be reliably estimated. In such instances a provision is calculated and recorded in the financial statements. In instances where these criteria are not met, a contingent liability may be disclosed in the notes to the financial statements.

A contingent liability is a possible obligation arising from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group; or a present obligation arising from past events that is not recognised in the financial statements because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation, or because the amount of the obligation cannot be measured with sufficient reliability.

Realisation of any contingent liabilities not currently recognised or disclosed in the financial statements could have a material effect on the Group's financial condition.

As required under purchase accounting, claims and contingencies acquired by the Group through the purchase of other businesses are recorded initially at fair value. Future changes to these estimates of fair value are required to be reflected in the income statement and could have a material effect on the Group's results and financial condition.

Application of these accounting principles to legal proceedings and disputes, including cases in which claimants are seeking damages for alleged smoking and health-related effects, is inherently difficult, given the complex nature of the facts and law involved. Deciding whether or not to provide for loss in connection with such claims requires the Group's management to make determinations about various factual and legal matters beyond its control.

The Group reviews outstanding legal cases following developments in the legal proceedings at each balance sheet date, in order to assess the need for provisions in its financial statements. Among the factors considered in making decisions on provisions are 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 determinations at any time do not reflect subsequent developments or the eventual outcome of any claim, its future financial statements may be materially affected, with an adverse impact upon the Group's operating profit, financial position and liquidity.

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 revenue, profit or financial condition of the Group. Consequently, in respect of any such cases, the Group has not provided for any amounts in the consolidated financial statements.

In 2003 the Office of Fair Trading (OFT) commenced an investigation under the Competition Act 1998 into the operation of the UK tobacco supply industry in the period from 2000 to 2003. In a decision dated 15 April 2010, the OFT concluded that certain of the Group's promotional arrangements with tobacco retailers had the object of restricting competition and imposed a fine of £112.3 million on the Group. At the same time it confirmed that two other allegations included in its 2008 statement of objections had been dropped.

The Group takes compliance with competition law very seriously and continues to reject any suggestion that it acted in breach of the Competition Act or in any way contrary to the interests of consumers. On 15 June 2010 the Group submitted an appeal to the Competition Appeal Tribunal against the OFT's findings of infringement and the level of the fine. Five tobacco retailers have also submitted appeals against the OFT's decision. The Competition Appeal Tribunal may uphold, quash or vary the OFT's decision or the fine that has been imposed. As part of its appeal the Group has asked for the fine to be quashed in its entirety. Consequently, the Group has not provided for any amount in the consolidated financial statements.

### **Property, Plant and Equipment and Intangible 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. Useful lives are based on management's estimates of the period over which the assets will generate revenue, and are periodically reviewed for continued appropriateness. Due to the long lives of certain assets, changes to the estimates used can result in significant variations in the carrying value.

The Group assesses the impairment of property, plant and equipment and intangible assets subject to amortisation or depreciation whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors considered important that could trigger an impairment review 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.

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. When it is determined that there is an indicator that the carrying value may not be recoverable, impairment is measured based on estimates of the recoverable amount of the underlying assets of the cash-generating unit.

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 property, plant and equipment and intangible assets 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.

See notes 9 and 10 to these financial statements.

### **Retirement Benefits**

The costs, assets and liabilities of the defined benefit retirement schemes operating within the Group are determined using methods relying on actuarial estimates and assumptions. Details of the key assumptions are set out in note 18. The Group takes advice from independent actuaries relating to the appropriateness of the assumptions. It is important to note, however, that comparatively small changes in the assumptions used may have a significant effect on the Group's financial statements.

We estimate that a 0.5 per cent increase/(decrease) in the discount rate would increase/(decrease) the IAS 19 pension expense by approximately £1 million. We estimate that a 0.5 per cent decrease/(increase) in the expected return on plan assets would increase/(decrease) the IAS 19 pension expense by approximately £14 million.

### **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.



# Notes to the Financial Statements

## 1 Segment Information

Imperial Tobacco comprises two distinct businesses – Tobacco and Logistics. In addition to regularly reviewing results and plans for the Tobacco and Logistics businesses, the Chief Executive's Committee (which is the chief operating decision maker for the purposes of IFRS 8) regularly reviewed during the year the performance and plans of the Tobacco business analysed on a geographic basis, reflecting the importance of certain individual markets and geographic groupings. The segments presented below are therefore the Group's six Tobacco regions and the Logistics business.

The information provided to the Chief Executive's Committee is used as the basis of the segment revenue and profit disclosures provided below, with the geographic analysis of Tobacco based on the location of customers, and central Group costs allocated consistently based on management's assessment of the level of support provided. The main measure of profit used by the Chief Executive's Committee to assess performance is adjusted operating profit. Segment balance sheet information is not routinely provided to the Chief Executive's Committee.

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 Tobacco, 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.

For the purposes of the analysis below, European Union comprises the EU member states plus Norway, Iceland, Liechtenstein and Switzerland. The Cuban joint ventures are included in the Rest of the World. All of the Logistics business is located in the European Union.

### Tobacco

£ million unless otherwise indicated

	2010	2009
Revenue	<b>20,210</b>	18,587
Net revenue	<b>7,055</b>	6,818
Operating profit	<b>2,490</b>	2,291
Adjusted operating profit	<b>2,889</b>	2,750
Adjusted operating margin	<b>40.9%</b>	40.3%

### Logistics

£ million unless otherwise indicated

	2010	2009
Revenue	<b>8,980</b>	8,961
Distribution fees	<b>936</b>	964
Operating profit	<b>36</b>	40
Adjusted operating profit	<b>176</b>	177
Adjusted distribution margin	<b>18.8%</b>	18.4%

### Revenue

£ million	2010		2009	
	Total revenue	External revenue	Total revenue	External revenue
Tobacco				
UK	<b>5,105</b>	<b>5,105</b>	4,862	4,862
Germany	<b>3,755</b>	<b>3,755</b>	3,432	3,432
Spain	<b>594</b>	<b>79</b>	620	84
Rest of European Union	<b>5,275</b>	<b>4,773</b>	4,770	4,275
Americas	<b>1,373</b>	<b>1,373</b>	1,414	1,414
Rest of the World	<b>4,108</b>	<b>4,108</b>	3,489	3,489
Total Tobacco	<b>20,210</b>	<b>19,193</b>	18,587	17,556
Logistics	<b>8,980</b>	<b>8,980</b>	8,961	8,961
Eliminations	<b>(1,017)</b>	<b>–</b>	(1,031)	–
Total Group	<b>28,173</b>	<b>28,173</b>	26,517	26,517

## Tobacco net revenue

£ million	2010	2009
UK	911	893
Germany	853	826
Spain	594	610
Rest of European Union	1,577	1,490
Americas	780	861
Rest of the World	2,340	2,138
Total Tobacco	7,055	6,818

## Adjusted operating profit and reconciliation to profit before tax

£ million	2010	2009
Tobacco		
UK	614	601
Germany	432	403
Spain	268	275
Rest of European Union	638	566
Americas	244	288
Rest of the World	693	617
Total Tobacco	2,889	2,750
Logistics	176	177
Eliminations	2	6
Adjusted operating profit	3,067	2,933
Acquisition accounting adjustments – Tobacco	(24)	–
Amortisation of acquired intangibles – Tobacco	(315)	(315)
Amortisation of acquired intangibles – Logistics	(136)	(136)
Restructuring costs – Tobacco	(60)	(144)
Restructuring costs – Logistics	(4)	(1)
Operating profit	2,528	2,337
Net finance costs	(410)	(1,392)
Profit before tax	2,118	945

## Other segment information

£ million	2010			2009		
	Additions to intangible assets	Additions to property, plant and equipment	Depreciation and software amortisation	Additions to intangible assets	Additions to property, plant and equipment	Depreciation and software amortisation
Tobacco						
UK	1	18	31	1	29	31
Germany	2	119	22	1	114	22
Spain	1	12	9	1	8	11
Rest of European Union	1	51	30	2	32	30
Americas	–	7	3	1	3	4
Rest of the World	1	36	41	1	37	37
Total Tobacco	6	243	136	7	223	135
Logistics	8	26	34	5	22	34
Total Group	14	269	170	12	245	169

**1 Segment Information** *continued***Additional geographic analysis**

External revenue and non-current assets are presented for the UK and for individually significant countries.

£ million	2010		2009	
	External revenue	Non-current assets	External revenue	Non-current assets
UK	<b>5,105</b>	<b>170</b>	4,862	189
Germany	<b>3,755</b>	<b>3,317</b>	3,432	3,531
Spain	<b>2,254</b>	<b>4,471</b>	2,291	4,885
France	<b>3,907</b>	<b>3,593</b>	4,275	3,910
Rest of European Union	<b>7,671</b>	<b>2,822</b>	6,754	3,003
Americas	<b>1,373</b>	<b>3,104</b>	1,414	3,083
Rest of the World	<b>4,108</b>	<b>5,453</b>	3,489	5,788
Total Group	<b>28,173</b>	<b>22,930</b>	26,517	24,389

Non-current assets comprise intangible assets, property, plant and equipment, and investments in associates.

**2 Profit Before Taxation**

Profit before taxation is stated after charging/(crediting):

£ million	2010	2009
Raw materials and consumables used	<b>1,380</b>	1,297
Employment costs (note 4)	<b>1,235</b>	1,266
Depreciation of property, plant and equipment	<b>153</b>	152
Amortisation of intangible assets	<b>468</b>	468
Impairment of property, plant and equipment	<b>45</b>	15
Operating lease charges:		
– plant and equipment	<b>34</b>	31
– other assets	<b>23</b>	25
Net foreign exchange (gains)/losses	<b>(10)</b>	4
Write down of inventories	<b>62</b>	38
Profit on disposal of property, plant and equipment	<b>(3)</b>	(1)
Repairs and maintenance costs	<b>40</b>	45
Impairment of trade receivables	<b>3</b>	32

**Analysis of fees payable to PricewaterhouseCoopers LLP and its associates**

£ million	2010	2009
Audit fees in respect of the audit of the accounts of the Company	<b>0.9</b>	0.9
Audit fees in respect of the audit of the accounts of associates of the Company	<b>3.9</b>	4.1
Fees for other services supplied pursuant to legislation	<b>0.1</b>	0.1
	<b>4.9</b>	5.1
Advisory services relating to taxation	<b>0.6</b>	1.1
Compliance services relating to taxation	<b>0.4</b>	0.6
Other services	<b>0.1</b>	0.1
	<b>6.0</b>	6.9

It is the responsibility of the Board of Trustees of the Imperial Tobacco Pension Fund to appoint the auditors to the scheme. The Board of Trustees acts independently of Group's management. The fees paid to PricewaterhouseCoopers in respect of the audit of the Imperial Tobacco Pension Fund were £31,000 (2009: £27,000).

### 3 Restructuring Costs

£ million	2010	2009
Employment related (mainly termination)	1	116
Asset impairments	45	15
Other operating charges	18	14
	<b>64</b>	<b>145</b>

Restructuring costs in 2010 include charges for previously announced restructuring activity and further rationalisation and reorganisation of our manufacturing base, including the closure of our tubes factory in Woodstock, Canada and our cigarette factory in Tetouan, Morocco. Asset impairments in 2010 relate mainly to reductions in the carrying value of surplus property acquired through the Altadis acquisition to reflect current property market conditions.

The net charge of £64 million in 2010 includes £39 million of unused restructuring provisions reversed during the period, £38 million booked as additional restructuring provisions and £45 million booked as an impairment of property, plant and equipment. The remaining charge of £20 million was booked directly to the income statement as these costs did not meet the provisioning requirements of IAS 37.

Restructuring costs in the year ended 30 September 2009 related primarily to European Integration projects announced in June 2008 as part of the integration of Imperial Tobacco and Altadis. These projects affect sales and marketing, manufacturing and central support functions in a number of markets and are being implemented progressively over a period of three years. Costs in 2009 also included expenses related to the closure of our cigar factory in Tampa, Florida, USA announced in June 2009.

The net charge of £145 million in 2009 included £23 million of unused restructuring provisions reversed during the period, £95 million booked as additional restructuring provisions, £15 million booked as an impairment of property, plant and equipment and £19 million booked against net retirement benefit liabilities. The remaining charge of £39 million was booked directly to the income statement as these costs did not meet the provisioning requirements of IAS 37.

Restructuring costs are included within administrative and other expenses in the consolidated income statement.

### 4 Directors and Employees

#### Employment costs

£ million	2010	2009
Wages and salaries	945	971
Social security costs	199	201
Pension costs (note 18)	63	73
Share-based payments (note 21)	28	21
	<b>1,235</b>	<b>1,266</b>

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 on pages 78 to 95. These disclosures form part of the financial statements.

#### Number of people employed by the Group during the year

	2010		2009	
	At 30 September	Average	At 30 September	Average
Tobacco	31,500	30,900	31,500	32,800
Logistics	6,800	6,900	6,900	6,800
	<b>38,300</b>	<b>37,800</b>	<b>38,400</b>	<b>39,600</b>

#### Number of people employed by the Group by location during the year

	2010		2009	
	At 30 September	Average	At 30 September	Average
European Union	17,200	17,300	18,400	18,800
Americas	9,500	8,900	8,400	8,900
Rest of the World	11,600	11,600	11,600	11,900
	<b>38,300</b>	<b>37,800</b>	<b>38,400</b>	<b>39,600</b>



**5 Net Finance Costs**

£ million	2010	2009
Interest on bank deposits	(19)	(39)
Expected return on retirement benefit assets	(181)	(182)
Fair value gains on derivative financial instruments providing commercial hedges	(569)	(590)
Fair value gains on derivative financial instruments hedging underlying borrowings	–	(369)
Exchange gains on underlying borrowings	(75)	–
Investment income	(844)	(1,180)
Interest on bank and other loans	619	739
Interest on retirement benefit liabilities	186	200
Unwind of discount on redundancy and social plans	15	14
Fair value losses on derivative financial instruments providing commercial hedges	359	1,250
Fair value losses on derivative financial instruments hedging underlying borrowings	75	–
Exchange losses on underlying borrowings	–	369
Finance costs	1,254	2,572
Net finance costs	410	1,392

**Reconciliation from reported net finance costs to adjusted net finance costs**

£ million	2010	2009
Reported net finance costs	410	1,392
Fair value gains on derivative financial instruments providing commercial hedges	569	590
Fair value losses on derivative financial instruments providing commercial hedges	(359)	(1,250)
Fair value gains/(losses) on derivative financial instruments providing commercial hedges	210	(660)
Expected return on retirement benefit assets	181	182
Interest on retirement benefit liabilities	(186)	(200)
Unwind of discount on redundancy and social plans	(15)	(14)
Post-employment benefit net financing cost	(20)	(32)
Adjusted net finance costs	600	700

**6 Taxation****Analysis of charge in the year**

£ million	2010	2009
Current tax		
UK corporation tax at 28% (2009: 28%) being the rate for the year	(37)	61
Overseas taxation	534	346
Total current tax	497	407
Deferred tax		
Origination and reversal of temporary differences	99	(139)
Total tax charged to the income statement	596	268

**Reconciliation from reported taxation to adjusted taxation**

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 8.

£ million	2010	2009
Reported taxation	596	268
Tax on acquisition accounting adjustments	4	–
Deferred tax on amortisation of acquired intangibles	74	72
Tax on fair value (gains)/losses on derivative financial instruments providing commercial hedges	(59)	185
Tax on post-employment benefits net financing cost	7	11
Tax on restructuring costs	15	45
Adjusted tax charge	637	581

### 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 UK corporation tax rate for the year of 28 per cent (2009: 28 per cent) as follows:

£ million	2010	2009
Profit before tax	<b>2,118</b>	945
Tax at the UK corporation tax rate of 28% (2009: 28%)	<b>593</b>	265
Tax effects of:		
Differences in effective tax rates on overseas earnings	<b>(20)</b>	(16)
Unrecognised deferred tax assets	<b>(3)</b>	6
Items not deductible for tax purposes	<b>39</b>	14
Adjustments in respect of prior periods	<b>(13)</b>	(1)
Total tax charge	<b>596</b>	268

### Movement on current tax account

£ million	2010	2009
At 1 October	<b>(499)</b>	(339)
Charged to the income statement	<b>(497)</b>	(407)
Charged to other comprehensive income	<b>-</b>	(112)
Credited to equity	<b>2</b>	2
Cash paid	<b>365</b>	363
Exchange movements	<b>10</b>	(14)
Other movements	<b>17</b>	8
At 30 September	<b>(602)</b>	(499)

### Analysis of current tax account

£ million	2010	2009
Current tax assets	<b>51</b>	52
Current tax liabilities	<b>(653)</b>	(551)
	<b>(602)</b>	(499)

## 7 Dividends

### Dividend per share in respect of financial year

Pence	2010	2009	2008
Interim	<b>24.3</b>	21.0	20.9
Final	<b>60.0</b>	52.0	42.2
Total	<b>84.3</b>	73.0	63.1

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, while interim dividends are recognised in the period in which the dividends are paid. Consequently Imperial Tobacco Group's interim dividends are paid and recognised in the second half of the year, and final dividends in respect of a year are paid and recognised in the following financial period.

### Amounts recognised as distributions to ordinary equity holders in the year

£ million	2010	2009
Final dividend paid in the period in respect of previous financial year	<b>527</b>	427
Interim dividend	<b>246</b>	213
	<b>773</b>	640

The proposed final dividend for the year ended 30 September 2010 of 60.0p per share amounts to a proposed final dividend payment of £609 million based on the number of shares ranking for dividend at 30 September 2010, and is subject to shareholder approval. If approved, the total dividend paid in respect of 2010 will be £855 million (2009: £740 million).

**8 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	2010	2009
Earnings: basic and diluted	<b>1,505</b>	663

Millions of shares

Weighted average number of shares:		
Shares for basic earnings per share	<b>1,013.8</b>	1,012.3
Potentially dilutive share options	<b>3.1</b>	2.7
Shares for diluted earnings per share	<b>1,016.9</b>	1,015.0

Pence

Basic earnings per share	<b>148.5</b>	65.5
Diluted earnings per share	<b>148.0</b>	65.3

**Reconciliation from reported to adjusted earnings and earnings per share**

£ million unless otherwise indicated	2010		2009	
	Earnings per share (pence)	Earnings	Earnings per share (pence)	Earnings
Reported basic	<b>148.5</b>	<b>1,505</b>	65.5	663
Acquisition accounting adjustments	<b>2.0</b>	<b>20</b>	—	—
Amortisation of acquired intangibles	<b>37.1</b>	<b>377</b>	37.4	379
Fair value (gains)/losses on derivative financial instruments providing commercial hedges	<b>(14.9)</b>	<b>(151)</b>	46.9	475
Post-employment benefits net financing cost	<b>1.3</b>	<b>13</b>	2.1	21
Restructuring costs	<b>4.8</b>	<b>49</b>	9.9	100
Adjusted	<b>178.8</b>	<b>1,813</b>	161.8	1,638
Adjusted diluted	<b>178.3</b>	<b>1,813</b>	161.4	1,638

## 9 Intangible Assets

2010

£ million	Goodwill	Trademarks	Supply agreements	Software	Total
Cost					
At 1 October 2009	13,696	7,782	1,759	102	23,339
Acquisition accounting adjustment	(41)	–	–	–	(41)
Additions	–	–	–	14	14
Disposals	–	–	–	(2)	(2)
Exchange movements	(579)	(281)	(86)	(1)	(947)
At 30 September 2010	13,076	7,501	1,673	113	22,363
Amortisation and impairment					
At 1 October 2009	21	612	299	50	982
Amortisation charge for the year	–	281	170	17	468
Disposals	–	–	–	(1)	(1)
Exchange movements	–	(9)	(16)	(2)	(27)
At 30 September 2010	21	884	453	64	1,422
Net book value					
At 30 September 2010	13,055	6,617	1,220	49	20,941

2009

£ million	Goodwill	Trademarks	Supply agreements	Software	Total
Cost					
At 1 October 2008	11,896	6,744	1,519	95	20,254
Additions	–	1	3	8	12
Disposals	–	–	–	(1)	(1)
Exchange movements	1,800	1,037	237	–	3,074
At 30 September 2009	13,696	7,782	1,759	102	23,339
Amortisation and impairment					
At 1 October 2008	21	277	105	34	437
Amortisation charge for the year	–	281	170	17	468
Disposals	–	–	–	(1)	(1)
Exchange movements	–	54	24	–	78
At 30 September 2009	21	612	299	50	982
Net book value					
At 30 September 2009	13,675	7,170	1,460	52	22,357

Intangible amortisation and impairment are included within administrative and other expenses in the consolidated income statement.

Supply agreements includes Logistics customer relationships and exclusive supply arrangements in Cuba and Morocco, all acquired under the purchase of Altadis.

The £41 million reduction in goodwill in 2010 reflects an adjustment in respect of the Reemtsma acquisition and is more fully described in note 29.

Amortisation and impairment in respect of acquired intangible assets are treated as reconciling items between reported operating profit and adjusted operating profit. The adjustment comprises the amortisation and impairment charges in respect of goodwill, trademarks and supply agreements.

**9 Intangible Assets** *continued***Goodwill and intangible asset impairment review**

Goodwill and intangible assets with indefinite lives are allocated to the Group's cash-generating units (CGUs). For the Tobacco business these are based on the geographic areas in which the Group operates. A summary of the carrying value of goodwill and intangible assets with indefinite lives is set out below.

£ million	2010		2009	
	Goodwill	Intangible assets with indefinite lives	Goodwill	Intangible assets with indefinite lives
European Union	6,356	127	6,742	135
Americas	1,828	105	1,783	103
Rest of the World	2,885	341	3,071	360
Cuban cigar joint ventures	289	250	284	246
Tobacco	11,358	823	11,880	844
Logistics	1,697	–	1,795	–
	13,055	823	13,675	844

Goodwill has arisen principally on the acquisitions of Reemtsma in 2002 (mainly EU and Rest of the World), Commonwealth Brands in 2007 (Americas) and Altadis in 2008 (all CGUs).

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 recoverable amount of a CGU is determined 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. The three year plans 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, inter alia, anticipated changes in market size, prices and duty regimes, anticipated consumer uptrading and downtrading, changes in consumer preferences and other changes in product mix.

These estimates and assumptions are 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.

The compound annual growth rates implicit in these value-in-use calculations are shown below. Cash flows beyond the plan period are extrapolated using the estimated long-term growth rate of three per cent per annum. Discount rates used are based on the Group's weighted average cost of capital adjusted for the different risk profiles of the CGUs. Pre-tax discount rates ranged from 8.7 per cent to 11.3 per cent.

**Growth rates used**

	Initial growth rate <sup>1</sup>	Long-term growth rate <sup>2</sup>
European Union	2.0%	3.0%
Americas	8.5%	3.0%
Rest of the World	12.5%	3.0%
Cuban cigar joint ventures	4.7%	3.0%
Logistics	2.0%	3.0%

<sup>1</sup> Weighted average compound annual growth rate used for first three years in value-in-use calculations.

<sup>2</sup> Weighted average compound annual growth rate used to extrapolate cash flows beyond the initial three years.

The impairment test for Americas indicated headroom of £250 million and that an increase in the discount rate of 70 basis points from 11.3 per cent, a reduction of 290 basis points in the initial growth rate, or an 80 basis point reduction in the long-term growth rate would result in an impairment.

In addition to the initial growth rates shown above applied to cash flows arising in existing markets, the valuation of the Cuban cigar joint ventures includes assumptions about the timing and extent of cash flows from entry to new markets. The impairment test for the Cuban cigar joint ventures indicated headroom of £60 million and that an increase of 60 basis points in the discount rate from 10.0 per cent or a reduction of 9 per cent or more in the value of overall cash flows would result in an impairment. We do not consider any reasonable movement in other assumptions relating to the Americas and the Cuban cigar business joint ventures would result in an impairment.

For the Tobacco business in the European Union and the Rest of the World, and for Logistics, any reasonable movement in the assumptions of the impairment test would not result in an impairment.

No impairment charges have been recognised in the year in respect of goodwill and intangible assets.



## 10 Property, Plant and Equipment

2010

£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Cost				
At 1 October 2009	1,147	1,375	379	2,901
Additions	14	197	58	269
Disposals	(9)	(46)	(18)	(73)
Reclassifications	13	(17)	4	–
Exchange movements	(52)	(17)	(13)	(82)
At 30 September 2010	1,113	1,492	410	3,015
Depreciation and impairment				
At 1 October 2009	65	647	179	891
Depreciation charge for the year	14	99	40	153
Impairment	43	2	–	45
Disposals	(1)	(15)	(15)	(31)
Reclassifications	–	(7)	7	–
Exchange movements	(3)	(6)	(5)	(14)
At 30 September 2010	118	720	206	1,044
Net book value				
At 30 September 2010	995	772	204	1,971

The net book value above includes land and buildings of £37 million (2009: £59 million) held under a finance lease.

The impairment charge in 2010 relates mainly to reductions in the carrying value of surplus property acquired through the Altadis acquisition to reflect current property market conditions, which have been treated as restructuring costs.

2009

£ million	Property	Plant and equipment	Fixtures and motor vehicles	Total
Cost				
At 1 October 2008	1,042	1,198	305	2,545
Additions	13	173	59	245
Disposals	(29)	(49)	(20)	(98)
Reclassifications	(10)	–	10	–
Exchange movements	131	53	25	209
At 30 September 2009	1,147	1,375	379	2,901
Depreciation and impairment				
At 1 October 2008	24	558	143	725
Depreciation charge for the year	14	98	40	152
Impairment	23	(8)	–	15
Disposals	(3)	(14)	(13)	(30)
Exchange movements	7	13	9	29
At 30 September 2009	65	647	179	891
Net book value				
At 30 September 2009	1,082	728	200	2,010

### Land and buildings at net book value

£ million	2010	2009
Freehold	944	1,011
Leasehold	51	71
	995	1,082

No assets (2009: net book value of nil) are pledged as security for liabilities.

**11 Investments in Associates and Joint Ventures****Investments in associates**

£ million	2010	2009
At 1 October	22	16
Share of profit of associates	–	1
Disposals	(3)	–
Exchange movements	(1)	5
At 30 September	18	22

**Investments in joint ventures**

The principal joint ventures are Corporación Habanos, S.A. Cuba and Altabana S.L., Spain. Summarised financial information for the Group's share of joint ventures, which are accounted for under the proportional consolidation method, is shown below:

**2010**

£ million	Corporación Habanos	Altabana	Others	Total
Revenue	39	81	10	130
Profit after taxation	5	7	2	14
Non-current assets	201	11	7	219
Current assets	42	60	10	112
Total assets	243	71	17	331
Current liabilities	(26)	(21)	(2)	(49)
Non-current liabilities	(33)	(2)	–	(35)
Total liabilities	(59)	(23)	(2)	(84)
Net assets	184	48	15	247

**2009**

£ million	Corporación Habanos	Altabana	Others	Total
Revenue	34	72	9	115
Profit after taxation	7	6	–	13
Non-current assets	202	11	7	220
Current assets	49	52	10	111
Total assets	251	63	17	331
Current liabilities	(21)	(14)	(2)	(37)
Non-current liabilities	(30)	(4)	–	(34)
Total liabilities	(51)	(18)	(2)	(71)
Net assets	200	45	15	260

**12 Inventories**

£ million	2010	2009
Raw materials	961	912
Work in progress	57	72
Finished inventories	1,824	1,795
Other inventories	177	146
	3,019	2,925

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 £140 million (2009: £130 million) of leaf tobacco held within raw materials will not be utilised within a year of the balance sheet date.

### 13 Trade and Other Receivables

£ million	2010		2009	
	Current	Non-current	Current	Non-current
Trade receivables	2,810	–	2,730	–
Less: provision for impairment of receivables	(55)	–	(49)	–
Net trade receivables	2,755	–	2,681	–
Other receivables	145	83	226	84
Prepayments and accrued income	100	14	104	15
	3,000	97	3,011	99

Trade receivables may be analysed as follows:

£ million	2010		2009	
	Current	Non-current	Current	Non-current
Within credit terms	2,663	–	2,559	–
Past due by less than 3 months	44	–	79	–
Past due by more than 3 months	48	–	43	–
Amounts that are impaired	55	–	49	–
	2,810	–	2,730	–

### 14 Cash and Cash Equivalents

£ million	2010	2009
Cash at bank and in hand	741	649
Short-term deposits and other liquid assets	32	387
	773	1,036

£231 million (2009: £236 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.

### 15 Trade and Other Payables

£ million	2010		2009	
	Current	Non-current	Current	Non-current
Trade payables	1,248	–	1,247	–
Other taxes, duties and social security contributions	6,003	–	5,779	–
Other payables	145	–	140	–
Accruals and deferred income	314	21	285	23
	7,710	21	7,451	23

### 16 Borrowings and Derivative Financial Instruments

#### (i) Management of financial risk

The Group operates a centralised treasury function, Group Treasury, which is responsible for the management of the financial risks of the Group, together with its financing and liquidity requirements. It does not operate as a profit centre, nor does it enter into speculative transactions. The Group Treasury Committee (GTC) oversees the operation of Group Treasury in accordance with terms of reference set out by the Board. The Board reviews and approves all major treasury decisions. The GTC currently comprises the Finance Director; Director of Accounting, Forecasting and Tax; Director of Investor Communications; Cigar Business Unit Finance Director; Senior Group Management Accountant Manufacturing and Group Treasurer. The GTC agrees a framework which sets out the current expectations and boundaries to assist in the effective oversight of Group Treasury activities, covering all key areas within Group Treasury. The Group Treasurer reports on a regular basis to the Board, including the provision of a monthly treasury report, which is also provided to the GTC.

**16 Borrowings and Derivative Financial Instruments** *continued***Foreign exchange risk**

The Group is exposed to movements in foreign exchange rates due to its commercial trading transactions denominated in foreign currencies, foreign currency cash deposits, borrowings and non-sterling derivatives.

In 2010, 82 per cent of revenue (2009: 82 per cent) and 80 per cent of adjusted profit from operations (2009: 80 per cent) was in markets outside the UK. Certain sales in these markets are invoiced in currencies other than the functional currency of the selling company.

Material costs denominated in currencies other than the functional currencies of subsidiaries include 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. After taking into account other US dollar inflows the Group currently does not consider this foreign exchange cash flow risk to be material enough to hedge.

The Group has a policy of managing its balance sheet translation risk by funding acquisitions and the underlying business assets with borrowings (post cross currency swaps) in the currency of the underlying net assets. This also results in foreign currency profits from operations being partially offset by foreign currency interest costs thereby minimising the translation exposure on foreign currency profits after tax.

The Group issues debt in the market or markets that are most appropriate at the time of raising new finance and has a policy of using derivative financial instruments, such as cross currency swaps and foreign exchange swaps where necessary, to change the debt into the desired currency. At 30 September 2010, approximately 27 per cent (2009: 13 per cent) of adjusted net debt was denominated in sterling, 50 per cent in euro (2009: 56 per cent) and 23 per cent in US dollars (2009: 31 per cent).

The Group's sterling dividend to shareholders is partly sourced from foreign subsidiary earnings. In order to manage the foreign exchange cash flow risk, and to provide greater certainty as to the amount of sterling available to pay expected future dividends, the Group has entered into transactional cross currency swaps maturing between 2011 and 2015 that will convert expected euro dividends from subsidiaries into sterling.

**Cash flow and fair value interest rate risk**

The Group's interest rate risk arises from borrowings net of cash and cash equivalents. 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. Group Treasury monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals, the fair value of derivative financial instruments providing commercial cash flow hedges and finance lease liabilities. The Group's financial results are currently principally exposed to gains or losses arising from fluctuations in sterling, euro and US dollar interest rates.

In order to manage the interest rate risk on its borrowings, the Group separates its borrowing activities from its interest rate risk management decisions by issuing debt in the market or markets that are most appropriate at the time of raising new finance and uses derivative financial instruments, such as cross currency swaps and interest rate swaps where necessary, to change the debt into floating interest rates shortly after issue. The Group then transacts interest rate swaps at other times for different notional amounts and for different maturities to manage the Group's exposure to interest rate risk. At 30 September 2010, 29 per cent (2009: 32 per cent) of adjusted net debt was at a floating rate of interest, 70 per cent (2009: 67 per cent) at a fixed rate of interest and one per cent (2009: one per cent) floating within a set range.

The Group manages its interest rate exposure on a regular basis and reports the position monthly to the Board and GTC. This report shows the profit or loss impact of a defined interest rate shift for each of the major currencies of borrowings and the forecast percentage of debt fixed for at least the next ten years.

The Group has no material interest rate repricing risk since the interest rates of derivative financial instruments reset quarterly, resulting in the interest being paid or received approximating current market rates.

### Sensitivity analysis

IFRS 7 requires a sensitivity analysis that illustrates the estimated impact on the income statement and other comprehensive income due to hypothetical changes in foreign exchange rates and interest rates in relation to all of the Group's financial instruments.

The Group considers that the movements in interest rates and sterling foreign exchange rates shown in the table below represent reasonably possible changes. The impacts on income and other comprehensive income of these changes are shown in the table below. The sensitivity analysis has been prepared on the basis that the amount of net debt, the ratio of fixed to floating interest rates of the debt and derivatives portfolio, and the proportion of financial instruments in foreign currencies are all constant and on the basis of the net investment hedge designations in place at 30 September 2010. The sensitivity analysis does not reflect any change to revenue or non-finance costs that may result from changing interest or exchange rates. All financial assets and liabilities held in the functional currency of subsidiary companies are excluded from the analysis. The analysis also excludes instruments that expose the Group to interest rate and foreign exchange risk where such risk is fully hedged with another financial instrument.

£ million	30 September 2010		30 September 2009	
	Income (loss)/gain	Other comprehensive income (loss)/gain	Income (loss)/gain	Other comprehensive income (loss)/gain
100 basis point increase/50 basis point decrease in GBP interest rates	(14)/7	–	(9)/5	–
100 basis point increase/decrease in euro interest rates	(9)/9	–	(12)/12	–
100 basis point increase/25 basis point decrease in US dollar interest rates	(7)/2	–	(16)/4	–
10% appreciation/depreciation of the euro	(82)/67	(1,054)/863	(156)/128	(1,097)/898
10% appreciation/depreciation of the US dollar	(5)/4	(194)/159	(222)/181	(56)/46

The impact in the income statement due to changes in interest rates reflects the effect on net finance costs in respect of the Group's floating rate debt at 30 September 2010.

The impact in the income statement from foreign exchange rate movements primarily relates to financial instruments that commercially hedge net investments, but are not accounted for as hedges under IAS 39 (although they are commercially effective). This value is expected to be fully offset by the retranslation of the commercially hedged foreign currency net assets leaving a net impact on shareholders' funds of zero. Any gain or loss which arises is excluded from our adjusted performance measures.

The other comprehensive income impact shown for foreign exchange sensitivity relates to derivative and non-derivative financial instruments hedging net investments. This value will be more than fully offset by the retranslation of the hedged foreign currency net assets.

### Credit risk

The Group is exposed to credit risk arising from its trade receivables due from customers, as well as from cash and cash deposits and the mark-to-market of derivative financial instruments transacted with financial institutions.

The Group has some significant concentrations of customer credit risk. However, the Group has implemented policies to ensure that sales of products are made to customers with an appropriate credit history and obtains guarantees or other means of credit support to reduce the risk where this is considered to be necessary. Analysis of trade and other receivables is provided in note 13.

The Group has a policy of having no concentrations of credit risk from financial institutions that are in excess of limits agreed by the Board. The Group has placed cash deposits and entered into derivative financial instruments with a diversified group of financial institutions with suitable credit ratings in order to manage its credit risk to any one financial institution.



**16 Borrowings and Derivative Financial Instruments** *continued*

The table below summarises the Group's major financial institution counterparties by credit rating and balances at 30 September 2010:

Counterparty	30 September 2010		30 September 2009	
	S&P Credit Rating	Maximum exposure to credit risk £m	S&P Credit Rating	Maximum exposure to credit risk £m
Financial institution A	A+	137	A+	106
Financial institution B	A	136	A	81
Financial institution C	AA	131	AA	95
Financial institution D	AA-	83	AA-	21
Financial institution E	AA	80	AA	143
Financial institution F	A+	77	A+	81
Financial institution G	A+	68	A+	28

Management do not expect these counterparties to default on their current obligations.

**Liquidity risk**

The Group is exposed to liquidity risk, which represents having insufficient funds to meet the financing needs of the Group. 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 for the forecast requirements of the Group over the short to medium term. At 30 September 2010 the Group had £1,798 million (2009: £3,109 million) of undrawn committed facilities, maturing in July 2012.

As well as forecasting and monitoring the Group's core liquidity needs, the Group 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, loans from central finance companies on commercial terms, or through local borrowings by the subsidiaries in appropriate currencies. Funds over and above those required for short-term working capital purposes by subsidiary companies are remitted to Group Treasury where practical and possible and are used to pay down debt whenever possible.

The table below summarises the Group's financial liabilities by maturity based on their contractual cash flows. The contractual cash flows disclosed in the table are undiscounted and have been calculated using spot rates at the relevant balance sheet date, including interest to be paid. The balance sheet amounts disclosed in the table for derivative financial liabilities include collateral of £243 million (2009: £356 million) which has been transferred to counterparties in respect of certain derivatives with a negative fair value. The future cash inflows arising from collateral transferred have not been allocated to time periods since there is no reasonable basis upon which to do so.

**At 30 September 2010**

£ million	Balance sheet amount	Total	Contractual cash flows			
			Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years
Non-derivative financial liabilities						
Bank loans	2,061	2,087	1,549	538	–	–
Capital market issuance	8,271	11,513	530	1,942	3,304	5,737
Trade payables	1,248	1,248	1,248	–	–	–
Finance lease liabilities	25	28	3	3	22	–
Total non-derivative financial liabilities	11,605	14,876	3,330	2,483	3,326	5,737
Derivative financial liabilities						
Net settled derivatives	616	1,150	226	225	413	286
Gross settled derivatives	394					
– receipts		(6,993)	(1,975)	(1,553)	(2,765)	(700)
– payments		7,449	1,881	1,739	2,969	860
Total derivative financial liabilities	1,010	1,606	132	411	617	446

At 30 September 2009

At 30 September 2009

£ million	Balance sheet amount	Total	Contractual cash flows			
			Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years
Non-derivative financial liabilities						
Bank loans	3,517	3,580	3,001	39	540	–
Capital market issuance	8,550	12,803	546	546	5,212	6,499
Trade payables	1,247	1,247	1,247	–	–	–
Finance lease liabilities	28	33	3	3	27	–
Total non-derivative financial liabilities	13,342	17,663	4,797	588	5,779	6,499
Derivative financial liabilities						
Net settled derivatives	587	836	202	191	382	61
Gross settled derivatives	730					
– receipts		(8,524)	(2,308)	(1,037)	(3,391)	(1,788)
– payments		9,387	2,284	1,109	3,871	2,123
Total derivative financial liabilities	1,317	1,699	178	263	862	396

#### Price risk

The Group is not exposed to equity securities price risk or financial instrument price risk other than its pension assets disclosed in note 18. 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.

#### Capital risk management

The Group manages the capital structure in an efficient manner in order to minimise the cost of capital whilst ensuring that we have access to ongoing sources of finance such as the debt capital markets. The Group defines capital as adjusted net debt (see note 26) and equity attributable to equity holders of the Company (see Consolidated Statement of Changes in Equity). The only externally imposed capital requirements for the Group are interest cover and gearing covenants under the terms of the Senior Bank Facility, with which we have fully complied during both the current period and the prior period.

The Group manages the capital structure to maintain an investment grade credit rating and has and will continue to take the appropriate measures to maintain this. For example, where new equity is needed, the Group will issue the minimum required in order to maintain an investment grade credit rating. This is determined in connection with detailed discussions with credit rating agencies prior to raising new equity.

#### Fair value estimation

The fair values of financial assets and liabilities with maturities less than one year, other than derivatives, are considered to be approximate to their book values. In accordance with the IFRS 7 classification hierarchy all derivative financial instruments are classified as Level 2. This means that they are valued using techniques based significantly on observable market data such as yield curves and foreign exchange rates.

**16 Borrowings and Derivative Financial Instruments** *continued**(ii) Borrowings*

The Group's borrowings at amortised cost at the balance sheet date are as follows:

£ million	2010	2009
Current borrowings		
Bank loans and overdrafts	<b>329</b>	2,560
<b>Total current borrowings</b>	<b>329</b>	2,560
Non-current borrowings		
Bank loans	<b>1,732</b>	957
Capital market issuance:		
£350m 6.875% notes due 2012	<b>357</b>	357
€1,250m 5.0% notes due 2012	<b>1,096</b>	1,157
€500m 5.125% notes due 2013	<b>453</b>	474
€1,200m 4.375% notes due 2013	<b>1,076</b>	1,137
€750m 7.25% notes due 2014	<b>650</b>	687
€500m 4.0% notes due 2015	<b>409</b>	431
£450m 5.5% notes due 2016	<b>470</b>	470
€1,500m 8.375% notes due 2016	<b>1,363</b>	1,440
£200m 6.25% notes due 2018	<b>210</b>	210
£500m 7.75% notes due 2019	<b>509</b>	509
£1,000m 9.0% notes due 2022	<b>1,053</b>	1,053
£600m 8.125% notes due 2024	<b>625</b>	625
<b>Total non-current borrowings</b>	<b>10,003</b>	9,507
<b>Total borrowings</b>	<b>10,332</b>	12,067

Current borrowings and non-current borrowings at 30 September 2010 include interest payable of £1 million (2009: £3 million) and £291 million (2009: £299 million) respectively.

Certain borrowings drawn under revolving credit facilities have been classified as non-current borrowings, in accordance with the ultimate maturity date of those facilities, whereas contractual cash flows will be required within 12 months of the balance sheet date and may then be redrawn.

The Group has not defaulted on any loans during the year (2009: no defaults).

*(iii) Currency analysis and effective interest rates of financial assets and financial liabilities*

The currency denomination, maturities (defined as the remaining period at the balance sheet date to the contractual maturity date) and weighted average interest rates of the Group's financial assets and liabilities (excluding derivatives) at 30 September 2010 are as follows:

	Maturity								Total £m	Weighted average %
	Less than 1 year		Between 1 and 2 years		Between 2 and 5 years		More than 5 years			
	£m	%	£m	%	£m	%	£m	%		
Assets/(liabilities) (before the impact of cross currency swaps and interest rate swaps)										
Cash and cash equivalents										
Sterling	7	0.3	–	–	–	–	–	–	7	0.3
Euro	255	0.1	–	–	–	–	–	–	255	0.1
US dollars	17	0.1	–	–	–	–	–	–	17	0.1
Other	494	3.3	–	–	–	–	–	–	494	3.3
Total cash and cash equivalents	773		–		–		–		773	
Weighted average receivable interest rate		2.2		–		–		–		2.2
Trade receivables										
Sterling	514	–	–	–	–	–	–	–	514	–
Euro	1,964	–	–	–	–	–	–	–	1,964	–
US dollars	104	–	–	–	–	–	–	–	104	–
Other	228	–	–	–	–	–	–	–	228	–
Total trade receivables	2,810		–		–		–		2,810	
Trade payables										
Sterling	(40)	–	–	–	–	–	–	–	(40)	–
Euro	(990)	–	–	–	–	–	–	–	(990)	–
US dollars	(124)	–	–	–	–	–	–	–	(124)	–
Other	(94)	–	–	–	–	–	–	–	(94)	–
Total trade payables	(1,248)		–		–		–		(1,248)	
Borrowings – by currency										
Sterling	(278)	1.4	–	–	(357)	6.8	(2,868)	7.8	(3,503)	7.2
Euro	(29)	2.9	(700)	1.5	(3,274)	4.5	(1,772)	7.0	(5,775)	4.9
US dollars	(21)	1.9	(1,032)	1.0	–	–	–	–	(1,053)	1.0
Other	(1)	3.7	–	–	–	–	–	–	(1)	3.7
Total borrowings	(329)		(1,732)		(3,631)		(4,640)		(10,332)	
Borrowings – by class of instrument										
Bank borrowings	(329)	1.6	(1,732)	1.2	–	–	–	–	(2,061)	1.3
Capital market issuance	–	–	–	–	(3,631)	4.7	(4,640)	7.5	(8,271)	6.3
Total borrowings	(329)		(1,732)		(3,631)		(4,640)		(10,332)	
Weighted average payable interest rate		1.6		1.2		4.7		7.5		5.3

The effective interest rates shown in the table above have been calculated excluding the accrued interest balances.

The bank borrowings are floating rate liabilities. The majority bear interest at rates set in advance by reference to LIBOR in the case of sterling and US dollars and to EURIBOR in the case of euro borrowings. The capital market issuances in place at 30 September 2010 bear interest (pre interest rate swaps) at a fixed rate throughout their life.

**16 Borrowings and Derivative Financial Instruments** *continued*

The impact of interest rate swaps and cross currency swaps to manage the resultant interest rate risk arising is shown in section (iv) below.

The currency denomination, maturities (defined as the remaining period at the balance sheet date to the contractual maturity date) and weighted average interest rates of the Group's financial assets and liabilities (excluding derivatives) at 30 September 2009 are as follows:

	Maturity								Total £m	Weighted average %
	Less than 1 year		Between 1 and 2 years		Between 2 and 5 years		More than 5 years			
	£m	%	£m	%	£m	%	£m	%		
Assets/(liabilities) (before the impact of cross currency swaps and interest rate swaps)										
Cash and cash equivalents										
Sterling	253	0.3	–	–	–	–	–	–	253	0.3
Euro	345	3.1	–	–	–	–	–	–	345	3.1
US dollars	15	0.2	–	–	–	–	–	–	15	0.2
Other	423	3.7	–	–	–	–	–	–	423	3.7
Total cash and cash equivalents	1,036		–		–		–		1,036	
Weighted average receivable interest rate		2.6		–		–		–		2.6
Trade receivables										
Sterling	512	–	–	–	–	–	–	–	512	–
Euro	1,920	–	–	–	–	–	–	–	1,920	–
US dollars	126	–	–	–	–	–	–	–	126	–
Other	172	–	–	–	–	–	–	–	172	–
Total trade receivables	2,730		–		–		–		2,730	
Trade payables										
Sterling	(48)	–	–	–	–	–	–	–	(48)	–
Euro	(996)	–	–	–	–	–	–	–	(996)	–
US dollars	(110)	–	–	–	–	–	–	–	(110)	–
Other	(93)	–	–	–	–	–	–	–	(93)	–
Total trade payables	(1,247)		–		–		–		(1,247)	
Borrowings – by currency										
Sterling	–	–	–	–	(357)	6.8	(2,867)	7.8	(3,224)	7.7
Euro	(1,237)	1.3	–	–	(4,381)	4.4	(1,871)	7.0	(7,489)	4.5
US dollars	(1,222)	1.1	(29)	2.9	–	–	–	–	(1,251)	1.1
Other	(101)	4.8	(2)	4.8	–	–	–	–	(103)	4.8
Total borrowings	(2,560)		(31)		(4,738)		(4,738)		(12,067)	
Borrowings – by class of instrument										
Bank borrowings	(2,560)	1.3	(31)	3.0	(926)	1.3	–	–	(3,517)	1.4
Capital market issuance	–	–	–	–	(3,812)	5.4	(4,738)	7.5	(8,550)	6.5
Total borrowings	(2,560)		(31)		(4,738)		(4,738)		(12,067)	
Weighted average payable interest rate		1.3		3.0		4.6		7.5		5.0

The effective interest rates shown in the table above have been calculated excluding the accrued interest balances.

The bank borrowings are floating rate liabilities. The majority bear interest at rates set in advance by reference to LIBOR in the case of sterling and US dollars and to EURIBOR in the case of euro borrowings. The capital market issuances in place at 30 September 2009 bear interest (pre interest rate swaps) at a fixed rate throughout their life.

The impact of interest rate swaps and cross currency swaps to manage the resultant interest rate risk arising is shown in section (iv) below.



*(iv) Derivative financial instruments*

IAS 39 requires that all derivative financial instruments are recognised in the balance sheet at fair value, with changes in the fair value being recognised in the 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. See section (vi) below for details. The information contained in sections (ii) and (iii) above shows the underlying borrowing position before the effect of interest rate swaps and cross currency swaps.

The Group separates its borrowing activities from its interest rate risk management decisions by issuing debt in the market or markets that are most appropriate at the time of raising new finance and using derivative financial instruments, such as cross currency swaps and interest rate swaps, to change the debt into the desired currency and into floating interest rates shortly after issue.

The following tables set out the Group's borrowings and derivative financial instruments at 30 September 2010, and demonstrate the Group's use of derivative financial instruments to manage the Group's foreign currency exchange rate and interest rate exposures. The tables present the nominal value of such instruments used to calculate the contractual payments under such contracts, analysed by maturity date, together with the related weighted average interest rate where relevant.

Seven of the interest rate swaps have embedded options and assumptions have been made based on market information and from counterparties' expectations at 30 September 2010 to determine whether, and if so when, such options are likely to be exercised in order to determine the probable maturity date. Details of these options and the expected maturity dates are included in the footnotes to the relevant tables. The actual maturity date could be earlier or later depending upon future market conditions and a cancellation would not result in a cash flow other than in respect of interest outstanding at the cancellation date. The effect of the cancellation of any of these interest rate swaps would be to reduce the proportion of the Group's borrowings that were at a fixed rate, increasing the Group's exposure to cash flow interest rate risk. Shortly after any such cancellation Group Treasury would, if deemed necessary as part of the management of interest rate risk, transact further interest rate swaps to replace the cancelled swaps. It is currently believed that there is sufficient appetite amongst counterparties for such transactions.

Debt is issued in the market or markets that are most appropriate at the time of raising new finance.

	Matures in financial year ending in						Total
	2011	2012	2013	2014	2015	Thereafter	
	GBP equivalent at 30 September 2010 £m						
Capital market issuance							
£350m 6.875% notes due 2012	-	350	-	-	-	-	350
€1,250m 5.0% notes due 2012	-	1,082	-	-	-	-	1,082
€500m 5.125% notes due 2013	-	-	-	433	-	-	433
€1,200m 4.375% notes due 2013	-	-	-	1,038	-	-	1,038
€750m 7.25% notes due 2014	-	-	-	649	-	-	649
€500m 4.0% notes due 2015	-	-	-	-	433	-	433
£450m 5.5% notes due 2016	-	-	-	-	-	450	450
€1,500m 8.375% notes due 2016	-	-	-	-	-	1,298	1,298
£200m 6.25% notes due 2018	-	-	-	-	-	200	200
£500m 7.75% notes due 2019	-	-	-	-	-	500	500
£1,000m 9.0% notes due 2022	-	-	-	-	-	1,000	1,000
£600m 8.125% notes due 2024	-	-	-	-	-	600	600
Interest accruals, discounts and fair value adjustments	-	20	-	59	(24)	183	238
Total capital market issuance	-	1,452	-	2,179	409	4,231	8,271
Bank loans and overdrafts, borrowed at LIBOR (or equivalent) plus a margin at the time of borrowing	328	1,731	-	-	-	-	2,059
Interest accruals	1	1	-	-	-	-	2
Total bank borrowings	329	1,732	-	-	-	-	2,061
Total borrowings	329	3,184	-	2,179	409	4,231	10,332

Derivative financial instruments are then transacted to change the debt issued into the desired currency and into floating interest rates, per the following table:

**16 Borrowings and Derivative Financial Instruments** *continued*

	Matures in financial year ending in							Fair value at 30 September 2010	
	2011	2012	2013	2014	2015	Thereafter	Total	Asset	Liability
GBP equivalent at 30 September 2010 £m									
Cross currency swaps									
<i>Receive sterling, pay euro:</i>									
Notional amount	–	350 <sup>1</sup>	–	–	–	650 <sup>1</sup>	1,000	33	231
Sterling interest rate to receive (%)	–	6.7	–	–	–	5.6	6.0		
Interest margin over EURIBOR to pay (%)	–	1.3	–	–	–	0.8	1.0		
Foreign exchange swaps									
<i>Receive euro, pay US dollar:</i>									
Notional amount	1,593	–	–	–	–	–	1,593	54	–
<i>Receive euro, pay sterling:</i>									
Notional amount	272	–	–	–	–	–	272	–	9
<i>Receive US dollar, pay sterling:</i>									
Notional amount	717	–	–	–	–	–	717	1	3
Sterling interest rate derivatives									
<i>Interest rate swaps – pay variable, receive fixed:</i>									
Notional amount	–	–	–	–	–	2,100	2,100	196	–
Weighted average interest rate to receive (%)	–	–	–	–	–	8.2	8.2		
Weighted average margin over LIBOR to pay (%)	–	–	–	–	–	4.2	4.2		
Euro interest rate derivatives									
<i>Interest rate swaps – pay variable, receive fixed:</i>									
Notional amount	–	1,082	–	2,125	–	1,732	4,939	296	–
Weighted average interest rate to receive (%)	–	4.8	–	5.3	–	7.0	5.8		
Weighted average margin over EURIBOR to pay (%)	–	2.7	–	1.3	–	4.0	2.5		

Derivative financial instruments are then transacted to change a portion of the debt into fixed interest rates, thereby creating the desired interest rate risk.

	Matures in financial year ending in							Fair value at 30 September 2010	
	2011	2012	2013	2014	2015	Thereafter	Total	Asset	Liability
GBP equivalent at 30 September 2010 £m									
Sterling interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	–	351	–	428	87	663 <sup>2,4</sup>	1,529	–	157
Weighted average interest rate to pay (%)	–	4.7	–	4.9	3.9	4.9	4.8		

Euro interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	–	2,251	1,088 <sup>3</sup>	415	172	1,124 <sup>5</sup>	5,050	–	333
Weighted average interest rate to pay (%)	–	4.0	3.9	3.8	3.3	4.4	4.0		

US dollar interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	–	891	–	381	–	692 <sup>6</sup>	1,964	–	192
Weighted average interest rate to pay (%)	–	3.9	–	4.0	–	4.8	4.2		
<i>Collars purchased:</i>									
Notional amount	127 <sup>7</sup>	–	–	–	–	–	127	–	1

Additional derivatives are then transacted to manage net investment hedging risk.

Non-deliverable forward									
<i>Receive euro, pay Moroccan dirham (MAD):</i>									
Notional amount	128	–	–	–	–	–	128	–	3

Additional derivatives are then transacted to manage the foreign exchange cash flow risk associated with converting euro dividends from subsidiaries into sterling.

Cross currency swaps									
<i>Receive sterling fixed, pay euro fixed:</i>									
Notional amount	753	983	1,012	584	1,026	–	4,358	19	352
Weighted average interest rate to pay (%)	4.6	4.6	4.6	4.7	4.6	–	4.7		
Weighted average interest rate to receive (%)	5.7	5.7	5.6	5.6	5.5	–	5.6		

Additional derivatives are then transacted to manage the short-term cash flow risk associated with converting other anticipated cash flows from subsidiaries into sterling.

**16 Borrowings and Derivative Financial Instruments** *continued*

	Matures in financial year ending in						Fair value at 30 September 2010	
	2011	2012	2013	2014	2015	Thereafter	Asset	Liability
GBP equivalent at 30 September 2010 £m								
Foreign exchange forwards								
Receive euro, pay sterling:								
Notional amount	103	-	-	-	-	-	-	1
Total fair value of derivative financial instruments at 30 September 2010							599	1,282
Collateral transferred under the terms and conditions of credit support annex documents under ISDA agreements							(29)	(272)
Total carrying value of derivative financial instruments at 30 September 2010							570	1,010
The above amounts are included in the balance sheet as follows:								
Current							243	262
Non-current							327	748
							570	1,010
Net liability								440

Since it is the intention of the Group to hold all derivative financial instruments until maturity they have been classified in the balance sheet as current or non-current according to their contractual cash settlements. Where a portion of a derivative financial instrument is to be cash settled within 12 months of the balance sheet date this portion has been classified as current with the remainder being classified as non-current. Any collateral transferred to counterparties in respect of derivative financial instruments with negative fair values has been classified as current or non-current in line with the classification of the underlying derivative financial instrument since the substance of the collateral transactions is to extinguish the liabilities to counterparties. Any excess collateral transferred to counterparties has been classified as current since it is reasonably expected to be returned within 12 months of the balance sheet date.

The overall effect of the interest rate swaps live at 30 September 2010 is to convert £6,726 million of borrowings into a fixed rate with £127 million of borrowings floating within a set range, in order to manage the Group's exposure to cash flow interest rate risk.

- Principal amounts under these cross currency swaps are exchanged at the start and maturity of these trades.
- The following trades are included within this balance:  
£15 million interest rate swap maturing in 2031 where the counterparty has the option to cancel every six months throughout the life of the trade. This trade is expected to be cancelled in July 2018.  
£50 million interest rate swap maturing in 2041 where the counterparty has the option to cancel every five years throughout the life of the trade. This trade is expected to be cancelled in April 2016.
- The following trade is included within this balance:  
€1,200 million interest rate swaps maturing in 2013 where the counterparty has the option to cancel every three months throughout the life of the trade. This trade is not expected to be cancelled before its maturity date.
- The following trades are included within this balance:  
£336 million forward start ten year interest rate swaps starting in May 2012.  
£90 million forward start ten year interest rate swaps starting in May 2014.
- The following trades are included within this balance:  
€500 million forward start five year interest rate swaps starting in April 2012.  
€600 million forward start five year interest rate swaps starting in May 2012.
- The following trades are included within this balance:  
\$500 million forward start five year interest rate swaps starting in April 2012.  
\$186 million forward start ten year interest rate swaps starting in April 2012.
- The following trade is included within this balance:  
\$200 million interest rate collar maturing in 2011 where the interest rate is fixed within the range 3.78% to 6.00%.

The following tables are provided in respect of borrowings and derivative financial instruments held by the Group at 30 September 2009.

Debt is issued in the market or markets that are most appropriate at the time of execution.

	Matures in financial year ending in						
	2010	2011	2012	2013	2014	Thereafter	Total
	GBP equivalent at 30 September 2009 £m						
Capital market issuance							
£350m 6.875% notes due 2012	–	–	350	–	–	–	350
€1,250m 5.0% notes due 2012	–	–	1,144	–	–	–	1,144
€500m 5.125% notes due 2013	–	–	–	–	457	–	457
€1,200m 4.375% notes due 2013	–	–	–	–	1,098	–	1,098
€750m 7.25% notes due 2014	–	–	–	–	686	–	686
€500m 4.0% notes due 2015	–	–	–	–	–	457	457
£450m 5.5% notes due 2016	–	–	–	–	–	450	450
€1,500m 8.375% notes due 2016	–	–	–	–	–	1,372	1,372
£200m 6.25% notes due 2018	–	–	–	–	–	200	200
£500m 7.75% notes due 2019	–	–	–	–	–	500	500
£1,000m 9.0% notes due 2022	–	–	–	–	–	1,000	1,000
£600m 8.125% notes due 2024	–	–	–	–	–	600	600
Interest accruals, discounts and fair value adjustments	–	–	21	–	56	159	236
Total capital market issuance	–	–	1,515	–	2,297	4,738	8,550
Bank loans and overdrafts, borrowed at LIBOR (or equivalent) plus a margin at the time of borrowing	2,559	31	948	–	–	–	3,538
Interest accruals	1	–	(22)	–	–	–	(21)
Total bank borrowings	2,560	31	926	–	–	–	3,517
Total borrowings	2,560	31	2,441	–	2,297	4,738	12,067

Derivative financial instruments are then transacted to change the debt issued into the desired currency and into floating interest rates per the following table:

	Matures in financial year ending in							Fair value at 30 September 2009	
	2010	2011	2012	2013	2014	Thereafter	Total	Asset	Liability
GBP equivalent at 30 September 2009 £m									
Cross currency swaps									
<i>Receive sterling, pay euro:</i>									
Notional amount	–	–	350 <sup>1</sup>	–	–	650 <sup>1</sup>	1,000	33	353
Sterling interest rate to receive (%)	–	–	6.7	–	–	5.6	6.0		
Interest margin over EURIBOR to pay (%)	–	–	1.3	–	–	0.8	1.0		
Foreign exchange swaps									
<i>Receive euro, pay US dollar:</i>									
Notional amount	2,003	–	–	–	–	–	2,003	–	22
Sterling interest rate derivatives									
<i>Interest rate swaps – pay variable, receive fixed:</i>									
Notional amount	–	–	–	–	–	2,100	2,100	94	72
Weighted average interest rate to receive (%)	–	–	–	–	–	8.2	8.2		
Weighted average margin over LIBOR to pay (%)	–	–	–	–	–	4.2	4.2		



**16 Borrowings and Derivative Financial Instruments** *continued*

	Matures in financial year ending in							Fair value at 30 September 2009	
	2010	2011	2012	2013	2014	Thereafter	Total	Asset	Liability
GBP equivalent at 30 September 2009 £m									
Euro interest rate derivatives									
<i>Interest rate swaps – pay variable, receive fixed:</i>									
Notional amount	–	–	1,144	–	2,241	1,830	5,215	215	31
Weighted average interest rate to receive (%)	–	–	4.8	–	5.3	7.0	5.8		
Weighted average margin over EURIBOR to pay (%)	–	–	2.7	–	1.3	4.0	2.5		

Derivative financial instruments are then transacted to change a portion of the debt into fixed interest rates, thereby creating the desired interest rate risk.

Sterling interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	–	–	110	–	300	219 <sup>2,5</sup>	629	–	48
Weighted average interest rate to pay (%)	–	–	6.1	–	5.0	4.6	5.1		

Euro interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	485	220 <sup>3</sup>	2,501	929 <sup>4</sup>	439	1,784 <sup>6</sup>	6,358	–	317
Weighted average interest rate to pay (%)	3.7	3.9	4.0	3.9	3.8	4.2	3.9		
<i>Basis swaps – receive variable monthly, pay variable quarterly</i>									
Notional amount	1,262	–	–	–	–	–	1,262	1	–

US dollar interest rate derivatives									
<i>Interest rate swaps – pay fixed, receive variable:</i>									
Notional amount	–	–	1,001	–	501	805 <sup>7</sup>	2,307	–	148
Weighted average interest rate to pay (%)	–	–	3.9	–	4.0	4.7	4.2		
<i>Collars purchased:</i>									
Notional amount	–	125 <sup>8</sup>	–	–	–	–	125	–	5
<i>Caps purchased:</i>									
Notional amount	63 <sup>9</sup>	–	–	–	–	–	63	–	–
<i>Basis swaps – receive variable monthly, pay variable quarterly:</i>									
Notional amount	626	–	–	–	–	–	626	1	–

Additional derivatives are then transacted to manage net investment hedging risk.

	Matures in financial year ending in							Fair value at 30 September 2009	
	2010	2011	2012	2013	2014	Thereafter	Total	Asset	Liability
	GBP equivalent at 30 September 2009 £m								
Non-deliverable forward									
Receive euro, pay Moroccan dirham (MAD):									
Notional amount	134	—	—	—	—	—	134	9	—

Additional derivatives are then transacted to manage the foreign exchange cash flow risk associated with converting euro dividends from subsidiaries into sterling.

Cross currency swaps									
<i>Receive sterling fixed, pay euro fixed:</i>									
Notional amount	–	753	983	1,012	584	1,026	4,358	11	674
Weighted average interest rate to pay (%)	–	4.6	4.6	4.6	4.7	4.6	4.7		
Weighted average interest rate to receive (%)	–	5.7	5.7	5.6	5.6	5.5	5.6		

Additional derivatives are then transacted to manage the short-term cash flow risk associated with converting other anticipated cash flows from subsidiaries into sterling.

Foreign exchange forwards									
<i>Receive US dollar, pay sterling:</i>									
Notional amount	111	–	–	–	–	–	111	–	3

Total fair value of derivative financial instruments at 30 September 2009	364	1,673
Collateral transferred under the terms and conditions of credit support annex documents under ISDA agreements	(32)	(356)
Total carrying value of derivative financial instruments at 30 September 2009	332	1,317

The above amounts are included in the balance sheet as follows:

Current	198	284
Non-current	134	1,033
	332	1,317
Net liability		985

The overall effect of the interest rate swaps live at 30 September 2009 was to convert £7,429 million of borrowings into a fixed rate with £125 million of borrowings floating within a set range, in order to manage the Group's exposure to cash flow interest rate risk.

- Principal amounts under these cross currency swaps are exchanged at the start and maturity of these trades.
- The following trades are included within this balance:  
£15 million interest rate swap maturing in 2031 where the counterparty has the option to cancel every six months throughout the life of the trade. This trade is expected to be cancelled in November 2018.  
£50 million interest rate swap maturing in 2041 where the counterparty has the option to cancel every five years throughout the life of the trade. This trade is expected to be cancelled in April 2016.
- The following trade is included within this balance:  
€240 million interest rate swaps maturing in 2013 where the counterparty has the option to cancel every three months throughout the life of the trade. These trades are expected to be cancelled in February 2011.
- The following trades are included within this balance:  
€960 million interest rate swaps maturing in 2013 where the counterparty has the option to cancel every three months throughout the life of the trade. These trades are expected to be cancelled in August 2013.
- The following trades are included within this balance:  
£64 million forward start ten year interest rate swaps starting in May 2012.  
£90 million forward start ten year interest rate swaps starting in May 2014.
- The following trades are included within this balance:  
€500 million forward start five year interest rate swaps starting in April 2012.  
€900 million forward start five year interest rate swaps starting in May 2012.
- The following trades are included within this balance:  
US\$500 million forward start five year interest rate swaps starting in April 2012.  
US\$186 million forward start ten year interest rate swaps starting in April 2012.
- US\$200 million interest rate collar maturing in 2011 where the interest rate is fixed within the range 3.78% to 6.00%.
- US\$100 million interest rate cap maturing in 2010 where the interest rate is capped at 6.00%.

**16 Borrowings and Derivative Financial Instruments** *continued**(v) Reconciliation of movement in carrying value of derivative financial instruments*

The movements in the carrying value of derivative financial instruments in the year were as follows:

£ million	Fair value attributable to currency movements recognised in:		Fair value attributable to interest rate differences recognised in income statement	Total
	Statement of comprehensive income	Income statement		
Fair value gains on derivative financial instruments providing commercial hedges (note 5)	–	75	494	569
Fair value losses on derivative financial instruments providing commercial hedges (note 5)	–	(75)	(284)	(359)
Net fair value gains on derivative financial instruments providing commercial hedges	–	–	210	210
Fair value losses on derivative financial instruments offsetting underlying borrowings (note 5)	–	(75)	–	(75)
Fair value gains on derivative financial instruments designated as net investment hedges	192	–	–	192
Fair value movement during year	192	(75)	210	327
Total carrying value of derivative financial instruments at 30 September 2009 (note 16 (iv))				(985)
Collateral transferred in respect of certain derivative financial instruments with negative values				(70)
Interest on collateral transferred in respect of certain derivative financial instruments with negative values				(11)
Cash payment on settlement of matured derivative financial instruments				299
Fair value at 30 September 2010				(440)

The movements in the carrying value of derivative financial instruments in 2009 were as follows:

£ million	Fair value attributable to currency movements recognised in:		Fair value attributable to interest rate differences recognised in income statement	Total
	Statement of comprehensive income	Income statement		
Fair value gains on derivative financial instruments providing commercial hedges (note 5)	–	226	364	590
Fair value losses on derivative financial instruments providing commercial hedges (note 5)	–	(626)	(624)	(1,250)
Net fair value losses on derivative financial instruments providing commercial hedges	–	(400)	(260)	(660)
Fair value gains on derivative financial instruments offsetting underlying borrowings (note 5)	–	369	–	369
Fair value losses on derivative financial instruments designated as net investment hedges	(768)	–	–	(768)
Fair value movement during year	(768)	(31)	(260)	(1,059)
Total carrying value of derivative financial instruments at 30 September 2008 (note 16 (iv))				(67)
Collateral transferred in respect of certain derivative financial instruments with negative values				125
Interest on collateral transferred in respect of certain derivative financial instruments with negative values				11
Cash payment on settlement of matured derivative financial instruments				5
Fair value at 30 September 2009				(985)

*(vi) Hedge of net investments in foreign operations*

At 30 September 2010 external loans with a fair value of €5,465 million and US\$1,000 million (2009: €5,294 million and US\$800 million), cross currency swaps of €5,502 million (2009: €5,502 million), foreign exchange swaps of \$1,750 million (2009: \$nil) and non-deliverable forwards of MAD1,675 million (2009: MAD1,675 million) have been designated as hedges of the net investment in the Group's foreign operations. Gains or losses on the retranslation of these borrowings and derivatives are recognised as other comprehensive income to offset any gains or losses on translation of the net investments in the Group's foreign operations. Permanent intragroup loans with a fair value of €6,365 million (2009: €4,284 million) have been treated as a reduction in investments in the Group's foreign operations.

*(vii) Fair values of financial assets and financial liabilities*

Set out below is a comparison by category of carrying amounts and fair values of all financial liabilities that are carried in the financial statements at amounts other than fair values.

All financial assets and liabilities are carried at amortised cost, other than derivative financial instruments that are carried at fair value. The carrying amounts of cash and cash equivalents, trade receivables and trade payables are approximate to their fair value and so are excluded from the analysis below. Derivative financial instruments are excluded as they are carried at fair value. No assets are held as available for sale.

£ million	2010		2009	
	Carrying amount	Fair value	Carrying amount	Fair value
Current borrowings				
Sterling	278	278	–	–
Euro	29	29	1,237	1,237
US dollars	21	21	1,222	1,222
Other	1	1	101	101
Total current borrowings	329	329	2,560	2,560
Non-current borrowings				
Sterling	3,225	3,963	3,224	3,655
Euro	5,746	6,378	6,252	6,662
US dollars	1,032	1,032	29	29
Other	–	–	2	2
Total non-current borrowings	10,003	11,373	9,507	10,348

Within the table above it is only the capital market issues that have a fair value different to the carrying value and this has been calculated by comparing the current trading levels to par.

**17 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.

£ million	2010	2009
Deferred tax assets	150	148
Deferred tax liabilities	(2,074)	(2,098)
	(1,924)	(1,950)

*Deferred tax expected to be recovered within 12 months*

£ million	2010	2009
Deferred tax assets	48	207
Deferred tax liabilities	(136)	(1)
	(88)	206

*Deferred tax assets*

2010

£ million	Fixed and intangible assets	Retirement benefits	Fair value losses	Other temporary differences	Total
At 1 October 2009	(57)	79	–	126	148
Credited/(charged) to income statement	(1)	5	–	(35)	(31)
Credited/(charged) to other comprehensive income	–	10	–	(9)	1
Credited to equity	–	–	–	4	4
Transfers	(13)	–	–	46	33
Exchange movements	4	–	–	(9)	(5)
At 30 September 2010	(67)	94	–	123	150

**17 Deferred Tax Assets and Liabilities** *continued*

2009

£ million	Fixed and intangible assets	Retirement benefits	Fair value losses	Other temporary differences	Total
At 1 October 2008	(67)	69	–	390	392
Credited/(charged) to income statement	33	6	–	(39)	–
Credited to other comprehensive income	–	30	–	–	30
Transfers	(18)	(26)	–	(216)	(260)
Exchange movements	(5)	–	–	2	(3)
Other movements	–	–	–	(11)	(11)
At 30 September 2009	(57)	79	–	126	148

## Deferred tax liabilities

2010

£ million	Fixed and intangible assets	Retirement benefits	Fair value gains	Other temporary differences	Total
At 1 October 2009	<b>(2,656)</b>	<b>46</b>	<b>6</b>	<b>506</b>	<b>(2,098)</b>
Credited/(charged) to income statement	<b>77</b>	<b>(7)</b>	<b>(1)</b>	<b>(137)</b>	<b>(68)</b>
Credited to other comprehensive income	–	<b>9</b>	–	–	<b>9</b>
Credited/(charged) to equity	<b>2</b>	–	–	<b>(5)</b>	<b>(3)</b>
Transfers	<b>(1)</b>	–	–	<b>(32)</b>	<b>(33)</b>
Exchange movements	<b>136</b>	–	–	<b>(17)</b>	<b>119</b>
At 30 September 2010	<b>(2,442)</b>	<b>48</b>	<b>5</b>	<b>315</b>	<b>(2,074)</b>

2009

£ million	Fixed and intangible assets	Retirement benefits	Fair value gains	Other temporary differences	Total
At 1 October 2008	(2,279)	(123)	6	86	(2,310)
Credited to income statement	69	–	–	70	139
Credited to other comprehensive income	–	143	–	–	143
Charged to equity	–	–	–	(3)	(3)
Transfers	(115)	26	–	349	260
Exchange movements	(331)	–	–	8	(323)
Other movements	–	–	–	(4)	(4)
At 30 September 2009	(2,656)	46	6	506	(2,098)

Within other temporary differences, deferred tax assets of £81 million (2009: £180 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. Deferred tax assets of £14 million (2009: £20 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, £11 million (2009: £11 million) will expire within five years.

Also within other temporary differences, deferred tax assets of £90 million (2009: £77 million) are recognised for tax credits carried forward to the extent that the realisation of the related tax benefit through future taxable profits is probable.

The aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have not been recognised is £7 billion (2009: £8 billion). A provision of £8 million (2009: £9 million) has been made for taxation expected to arise on a planned future dividend payment of £110 million from one subsidiary. No other liability has been recognised in respect of these differences because the Group is in a position to control the timing of the reversal of the temporary differences, and it is probable that the differences will not reverse in the foreseeable future.

The June 2010 United Kingdom Budget Statement included proposals to reduce the rate of UK corporation tax by 1 per cent per annum from 28 per cent to 24 per cent by 1 April 2014. The change from 28 per cent to 27 per cent was enacted at the balance sheet date and has, therefore, been included in these financial statements. The effect of the reduction to 27 per cent has been to reduce the deferred tax liability provided at 30 September 2010 by approximately £1 million. This £1 million decrease in the deferred tax liability has increased profit for the year by £2 million and decreased other comprehensive income by £1 million.

The proposed further reductions to 24 per cent by 1 April 2014 are expected to be enacted separately each year. The overall effect of a further reduction to 24 per cent, if applied to the deferred tax balance at 30 September, would be to reduce the deferred tax liability by approximately £4 million.



## 18 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 two principal schemes are final salary defined benefit schemes and are operated by Imperial Tobacco Limited in the UK and Reemtsma Cigarettenfabriken GmbH in Germany. The UK scheme's assets are held in trustee administered funds while the German scheme is unfunded.

The results of the most recent actuarial valuations for the principal Group schemes (outside Germany) have been updated to 30 September 2010 by Towers Watson Limited, actuaries and consultants, in order to determine the amounts to be included in the balance sheet and income statement. Actuarial valuations of the pension liabilities of Reemtsma Cigarettenfabriken GmbH pension schemes were undertaken by Russ, Dr Zimmerman und Partner at 30 September 2010.

### Amounts recognised in the income statement

£ million	2010	2009
Current service cost	43	33
Past service credit	(5)	–
Losses from special termination benefits	8	28
Curtailement gains	(1)	(7)
Defined benefit costs in operating profit	45	54
Interest on retirement benefit liabilities	186	200
Expected return on retirement benefit assets	(181)	(182)
Retirement benefits net financing costs in finance costs (note 5)	5	18
Total defined benefit scheme cost	50	72
Defined contribution costs in operating profit	18	19
Total retirement benefit scheme costs in the income statement	68	91

### Retirement benefit scheme costs charged to operating profit

£ million	2010	2009
Defined benefit costs in operating profit	45	54
Defined contribution costs in operating profit	18	19
Total retirement benefit scheme costs in operating profit	63	73

Which is split as follows in the income statement:

£ million	2010	2009
Cost of sales	29	25
Distribution, advertising and selling costs	17	15
Administrative and other expenses	17	33
Total retirement benefit scheme costs in operating profit	63	73

### Defined benefit schemes – amounts recognised in the balance sheet

£ million	2010	2009
Present value of funded obligations	(3,022)	(2,845)
Fair value of scheme assets	2,960	2,798
	(62)	(47)
Present value of unfunded obligations	(780)	(747)
	(842)	(794)

Recognised in the balance sheet as:

£ million	2010	2009
Retirement benefit assets	25	17
Retirement benefit liabilities	(867)	(811)
	(842)	(794)

**18 Retirement Benefit Schemes** *continued*

## Defined benefit scheme obligations – changes in present value

£ million	2010	2009
At 1 October	<b>3,592</b>	2,874
Current service cost	<b>43</b>	33
Past service credit	<b>(5)</b>	–
Special termination benefits	<b>8</b>	28
Curtailment gains	<b>(1)</b>	(7)
Interest cost	<b>186</b>	200
Actuarial losses	<b>257</b>	524
Contributions by employees	<b>2</b>	2
Benefits paid	<b>(227)</b>	(203)
Exchange movements	<b>(53)</b>	141
At 30 September	<b>3,802</b>	3,592

## Defined benefit scheme assets – changes in fair value

£ million	2010	2009
At 1 October	<b>2,798</b>	2,769
Expected return	<b>181</b>	182
Actuarial gains/(losses)	<b>146</b>	(58)
Contributions by employees	<b>2</b>	2
Contributions by employer	<b>70</b>	53
Benefits paid	<b>(227)</b>	(203)
Exchange movements	<b>(10)</b>	53
At 30 September	<b>2,960</b>	2,798

The actual return on defined benefit scheme assets was a gain of £327 million (2009: gain £124 million).

## Amounts recognised in other comprehensive income

£ million	2010	2009
Net actuarial losses	<b>111</b>	582
Cumulative net actuarial losses since 1 October 2004	<b>446</b>	335

Defined benefit scheme – principal actuarial assumptions used in scheme valuations  
2010

	UK	Germany	Other <sup>1</sup>
Discount rate	<b>5.10%</b>	<b>4.40%</b>	<b>4.45%</b>
Expected return on scheme assets	<b>6.45%</b>	<b>n/a</b>	<b>5.26%</b>
Future salary increases	<b>4.60%</b>	<b>3.10%</b>	<b>3.64%</b>
Future pension increases	<b>3.10%</b>	<b>2.00%</b>	<b>2.23%</b>
Inflation	<b>3.10%</b>	<b>2.00%</b>	<b>2.26%</b>

## 2009

	UK	Germany	Other <sup>1</sup>
Discount rate	5.50%	5.30%	5.26%
Expected return on scheme assets	6.88%	n/a	6.00%
Future salary increases	4.50%	3.10%	3.73%
Future pension increases	3.00%	2.00%	2.37%
Inflation	3.00%	2.00%	2.28%

<sup>1</sup> Values shown are the weighted averages of the rates used for schemes outside the UK and Germany.

Assumptions regarding future mortality experience are set based on advice that uses published statistics and experience in each territory, and are provided in the table below for the defined benefit schemes in the UK and Germany, which in aggregate represent 83 per cent (2009: 83 per cent) of the Group's total defined benefit scheme obligations at the year end. The average life expectancy, in years, of a pensioner retiring at age 65 is as follows:

#### 2010

	UK		Germany	
	Male	Female	Male	Female
Life expectancy at age 65 years:				
Member currently aged 65	20.8	22.7	18.3	22.4
Member currently aged 50	21.9	23.9	20.3	24.3

#### 2009

	UK		Germany	
	Male	Female	Male	Female
Life expectancy at age 65 years:				
Member currently aged 65	19.7	21.5	18.1	22.3
Member currently aged 50	20.7	22.3	20.2	24.2

#### Categories of scheme assets and their expected rates of return

#### 2010

£ million unless otherwise indicated	UK			Other		
	Expected return per annum	Fair value	Percentage of UK assets	Expected return per annum	Fair value	Percentage of other assets
Equities	7.8%	1,426	55.0%	7.1%	133	36.1%
Bonds	4.1%	907	35.0%	4.1%	191	51.8%
Property	7.1%	259	10.0%	6.1%	15	4.2%
Other	–	–	–	4.3%	29	7.9%
		2,592	100.0%		368	100.0%

#### 2009

£ million unless otherwise indicated	UK			Other		
	Expected return per annum	Fair value	Percentage of UK assets	Expected return per annum	Fair value	Percentage of other assets
Equities	8.2%	1,424	58.0%	7.6%	137	40.5%
Bonds	4.5%	810	33.0%	5.0%	166	49.1%
Property	7.3%	221	9.0%	6.0%	16	4.8%
Other	–	–	–	3.9%	24	5.6%
		2,455	100.0%		343	100.0%

The derivation of the overall expected return on assets reflects the actual asset allocation at the measurement date combined with an expected return for each asset class. The bond return is based on current market yields. The corporate bond yield has been reduced to allow for an element of default risk. The return on equities and property is based on a number of factors including the income yield at the measurement date, the long-term growth prospects for the economy in general, the long-term relationship between each asset class and bond returns, and the movement in market indices since the previous measurement date.

Excluding any self-investment through pooled fund holdings, the Imperial Tobacco Pension Fund has no investments (2009: nil) in Imperial Tobacco Group PLC's own financial instruments.

**18 Retirement Benefit Schemes** *continued*

## History of the plans for current and prior years

£ million	2010	2009	2008	2007	2006
At 30 September					
Present value of defined benefit obligations	<b>3,802</b>	3,592	2,874	3,033	3,072
Fair value of total plan assets	<b>2,960</b>	2,798	2,769	3,238	3,035
Net total surplus/(deficit) on plans	<b>(842)</b>	(794)	(105)	205	(37)
Experience gain/(loss) on total plan liabilities	<b>63</b>	8	(18)	(19)	–
Experience gain/(loss) on total plan assets	<b>146</b>	(58)	(633)	121	144

The main UK Group scheme is the Imperial Tobacco Pension Fund (the ITPF). An actuarial valuation of the ITPF (the triennial valuation for funding purposes) was made at 31 March 2007 by Watson Wyatt Limited. The assumptions which had the most significant effect when valuing the ITPF's liabilities were those relating to the rate of investment return on the ITPF's existing assets, the rates of increase in pay and pensions and estimated mortality rates. On the basis that the ITPF is continuing, it was assumed that the future investment returns relative to market values at the valuation date would be 5.2 per cent per annum and that pay and pension increases would average 4.5 per cent and 3.0 per cent respectively. The assets were brought into account at their market value.

At 31 March 2007 the market value of the invested assets of the ITPF was £2,951 million. The total assets were sufficient to cover 114 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 102 per cent of the total benefits that had accrued to members for past service and future service benefits for current members. As there was no actuarial deficiency, it was agreed with the trustees that, with effect from 31 March 2007, no employer contributions are required. The financial position of the ITPF and the level of contributions to be paid will be reviewed at the next triennial valuation, which is expected to be completed by the end of 2010 and will consider the scheme as at 31 March 2010.

During the current year, the Group announced that with effect from 1 October 2010 new employees will no longer be eligible to join the UK defined benefit pension scheme but will be offered a defined contribution arrangement instead.

**19 Provisions**

£ million	Restructuring	Other	Total
At 1 October 2009	<b>614</b>	<b>454</b>	<b>1,068</b>
Additional provisions charged to the income statement	<b>38</b>	<b>81</b>	<b>119</b>
Unwind of discount on redundancy and social plan liabilities	<b>15</b>	–	<b>15</b>
Amounts used	<b>(147)</b>	<b>(91)</b>	<b>(238)</b>
Unused amounts reversed	<b>(39)</b>	<b>(40)</b>	<b>(79)</b>
Exchange movements	<b>(31)</b>	<b>(20)</b>	<b>(51)</b>
At 30 September 2010	<b>450</b>	<b>384</b>	<b>834</b>

Analysed as:

£ million	2010	2009
Current	<b>187</b>	292
Non-current	<b>647</b>	776
	<b>834</b>	1,068

Restructuring provisions relate primarily to European Integration projects announced in June 2008 as part of the integration of Imperial Tobacco and Altadis. They affect sales and marketing, manufacturing and central support functions in a number of markets and will be implemented progressively over a period of three years. These liabilities are expected to crystallise over a number of years. Redundancy and social plan costs have been discounted at 5.0 per cent.

Other provisions principally relate to commercial legal claims and disputes. The majority of other provisions represent the fair value at acquisition of current and potential Altadis commercial disputes, litigation and duty claims arising in the normal course of business. These liabilities are expected to crystallise within the next five years.

**20 Share Capital**

£ million	2010	2009
Authorised		
56,040,000,000 ordinary shares of 10p each (2009: 56,040,000,000)	<b>5,604</b>	5,604
Issued and fully paid		
1,067,942,881 ordinary shares of 10p each (2009: 1,067,942,881)	<b>107</b>	107

## 21 Share Schemes

The Group recognised total expenses of £28 million (2009: £21 million) related to share-based payment transactions during the year (note 4).

The Group operates a number of share-based employee benefit plans.

### International Sharesave Plan

Under the International Sharesave Plan the Board may offer options to purchase ordinary shares in the Company to employees who enter into a savings contract. The price at which options may be offered varies depending on local laws, but will not be less than 80 per cent of the mid-market price of an Imperial Tobacco Group PLC ordinary share on the London Stock Exchange on the day prior to invitation. The options may normally be exercised during the six months after expiry of the savings contract, three years after entering the Plan. The majority of awards under the International Sharesave Plan are equity-settled.

Under the UK Sharesave Plan, which is part of the International Sharesave Plan, the Board may offer options to purchase ordinary shares in the Company to UK employees who enter into an HM Revenue and Customs approved Save as You Earn (SAYE) savings contract. The options may normally be exercised during the six months after the expiry of the SAYE contract, either three or five years after entering the UK Sharesave Plan. The UK Sharesave Plan is equity-settled.

### Long Term Incentive Plan (LTIP)

Each year since demerger in 1996, annual conditional awards specified as a percentage of base salary have been made under the LTIP to Executive Directors and senior executives. The conditional awards, which vest three years after grant, are subject to the satisfaction of specified performance criteria, measured over a three year performance period. All conditional awards are at the discretion of the Remuneration Committee, with no employee having the right to receive such a conditional award. Further information relating to the performance criteria and the terms of the LTIP are set out in the Directors' Remuneration Report.

In respect of the November 2006 – November 2009 award, 94.2 per cent of the award vested on 1 November 2009, comprising 100 per cent of the EPS related element, 100 per cent of the TSR related element linked to the FTSE 100 ranking, and 76.7 per cent of the TSR element linked to the tobacco and alcohol companies comparator group.

In respect of the October 2007 – October 2010 award, 68.6 per cent of the award vested on 31 October 2010, comprising 100 per cent of the EPS related element, 74.5 per cent of the TSR related element linked to the FTSE 100 ranking, and nil per cent of the TSR element linked to the tobacco and alcohol companies comparator group.

The majority of the awards under the LTIP are equity-settled.

### Share Matching Scheme

The Share Matching Scheme is designed to encourage eligible employees to acquire and retain Imperial Tobacco Group PLC ordinary shares. The majority of the awards under the Share Matching Scheme are equity-settled.

Executive Directors and most of the Group's management may elect to invest any proportion of their gross bonus in Imperial Tobacco Group PLC ordinary shares to be held by the Employee Benefit Trusts. For the financial year ending 30 September 2010 eligibility was capped at 100 per cent of base salary for the Chief Executive and Finance Director and 85 per cent for the Group Sales and Marketing Director (2009: eligibility was capped at 100 per cent of base salary for the Chief Executive and Finance Director and 75 per cent for the other Executive Directors).

Provided the shares are left in the Trusts for three years, and the individual remains in employment within the Group, the participant will retain the original shares and receive additional shares on a 1:1 ratio. The matching of the Executive Directors' shares is subject to a performance criterion as set out in the Directors' Remuneration Report.

### 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 of Sharesave and LTIP options and on the vesting of the Share Matching Scheme. At 30 September 2010, the Trusts held 3.8 million (2009: 3.5 million) ordinary shares with a nominal value of £375,957. These are accounted for on a first in first out basis, and comprise 2.2 million treasury shares gifted to the Trusts by the Group, of which 1.9 million were gifted in financial year 2010 (2009: 0.2 million), and 1.6 million shares (2009: 3.3 million) acquired in the open market at a cost of £33.1 million (2009: £64.3 million). The acquisition of shares by the Trusts has been financed by a gift of £19.2 million and an interest free loan of £164.9 million. None of the Trusts' shares has been allocated to employees or Executive Directors as at 30 September 2010. All finance costs and administration expenses connected with the Trusts are charged to the 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.

### Cash-settled plan liabilities

As noted above certain awards are cash-settled. The total liability recognised in the balance sheet as at 30 September 2010 in respect of cash-settled awards was £0.9 million (2009: £0.6 million).



**21 Share Schemes** *continued*

Date of grant	Granted	Outstanding at 1 October 2008	Year from 1 October 2009 to 30 September 2010					
			Outstanding at start	Exercisable at start	Exercised	Lapsed/ cancelled	Outstanding at end	Exercisable at end
Sharesave options								
UK								
4 June 2003	735,332	30,133	-	-	-	-	-	-
26 May 2004	487,824	119,072	11,107	11,107	(9,988)	(1,119)	-	-
23 May 2005	454,966	151,480	122,771	-	(108,508)	(3,385)	10,878	10,878
22 May 2006	370,989	310,138	118,203	20,503	(28,088)	(1,773)	88,342	-
29 May 2007	337,134	313,652	249,847	-	(141,363)	(11,871)	96,613	11,398
13 June 2008	229,294	227,901	84,374	-	(3,665)	(7,910)	72,799	-
9 June 2009	507,915	-	505,021	-	(5,665)	(34,324)	465,032	-
25 May 2010	200,371	-	-	-	-	(1,829)	198,542	-
International								
23 May – 1 June 2005	197,115	33,205	-	-	-	-	-	-
22 May – 1 June 2006	347,332	302,135	57,031	57,031	(52,598)	(4,433)	-	-
29 May – 8 June 2007	309,381	292,614	247,361	-	(166,847)	(11,664)	68,850	68,850
13 June – 24 June 2008	381,983	378,214	237,981	-	(1,287)	(18,157)	218,537	-
16 June 2009	643,613	-	638,007	-	(1,003)	(29,238)	607,766	-
1 June 2010	370,135	-	-	-	-	(1,689)	368,446	-
US <sup>3</sup>								
1 June 2005	6,573	3,058	-	-	-	-	-	-
1 June 2006	4,872	4,846	-	-	-	-	-	-
8 June 2007	46,943	46,676	43,652	-	-	(43,652)	-	-
24 June 2008	66,310	64,440	28,890	-	-	(7,448)	21,442	-
	5,698,082	2,277,564	2,344,245	88,641	(519,012)	(178,492)	2,217,247	91,126
Conditional awards								
Share Matching Scheme								
15 February 2006	901,896	765,325	-	-	-	-	-	-
15 February 2007	737,454	674,193	643,065	-	(639,640)	(3,425)	-	-
15 February 2008	952,865	947,223	901,072	-	(99,717)	(47,947)	753,408	-
15 February 2009	1,095,203	-	1,080,726	-	(49,140)	(91,073)	940,513	-
15 February 2010	1,094,753	-	-	-	(901)	(17,894)	1,075,958	-
	4,782,171	2,386,741	2,624,863	-	(789,398)	(160,339)	2,769,879	-
Long Term Incentive Plan								
2 November 2005	449,403	373,318	1,276	-	(1,276)	-	-	-
1 November 2006	407,809	351,871	342,518	-	(322,436)	(20,082)	-	-
31 October 2007	316,649	316,649	308,582	-	(84,822)	(16,651)	207,109	-
26 November 2008	639,054	-	616,029	-	(66,329)	(101,903)	447,797	-
11 November 2009	494,282	-	-	-	(16,332)	(98,716)	379,234	-
	2,307,197	1,041,838	1,268,405	-	(491,195)	(237,352)	1,034,140	-
Total options/awards	12,787,450	5,706,143	6,237,513	88,641	(1,799,605)	(576,183)	6,021,266	91,126

Date of grant	Year from 1 October 2008 to 30 September 2009 <sup>1</sup>			Year from 1 October 2009 to 30 September 2010 <sup>1</sup>		
	Share price <sup>2</sup> at grant date	Share price <sup>2</sup> at exercise for exercises during the year	Contractual life of options/ awards outstanding at end of year	Share price <sup>2</sup> at exercise for exercises during the year	Contractual life of options/ awards outstanding at end of year	Exercise price <sup>2</sup> of options/ awards outstanding at end of year
<b>Sharesave options</b>						
<b>UK</b>						
4 June 2003	9.38	17.18	n/a	n/a	n/a	n/a
26 May 2004	10.68	16.80	4	18.33	n/a	8.76
23 May 2005	12.85	17.33	16	18.63	4	10.19
22 May 2006	14.23	16.58	24	18.71	16	12.12
29 May 2007	18.65	16.78	26	18.63	25	14.96
13 June 2008	20.05	16.11	35	19.60	23	17.50
9 June 2009	16.05	n/a	49	19.37	37	12.54
25 May 2010	17.60	n/a	n/a	n/a	46	15.63
<b>International</b>						
23 May – 1 June 2005	12.85 – 13.04	17.15	n/a	n/a	n/a	n/a
22 May – 1 June 2006	14.23 – 14.32	17.28	4	19.07	n/a	12.12
29 May – 8 June 2007	18.65 – 18.73	15.75	16	18.39	4	14.96
13 June – 24 June 2008	19.11 – 20.05	n/a	28	19.86	16	17.50
16 June 2009	15.93	n/a	40	17.93	28	12.55
25 May – 1 June 2010	17.60 – 18.40	n/a	n/a	n/a	40	15.63
<b>US<sup>3</sup></b>						
1 June 2005	\$24.10	\$18.75	n/a	n/a	n/a	n/a
1 June 2006	\$27.23	\$17.23	4	n/a	n/a	\$22.06
8 June 2007	\$37.53	n/a	16	n/a	4	\$30.39
24 June 2008	\$43.87	n/a	28	n/a	16	\$35.10
<b>Conditional awards</b>						
<b>Share Matching Scheme</b>						
15 February 2006		16.92	n/a	n/a	n/a	n/a
15 February 2007		16.19	5	20.30	n/a	n/a
15 February 2008		16.14	17	19.10	5	n/a
15 February 2009		15.86	29	19.23	17	n/a
15 February 2010		n/a	n/a	19.01	29	n/a
<b>Long Term Incentive Plan</b>						
2 November 2005		16.83	n/a	18.85	n/a	n/a
1 November 2006		16.75	1	18.89	n/a	n/a
31 October 2007		16.72	13	19.08	1	n/a
26 November 2008		17.13	26	19.06	14	n/a
11 November 2009		n/a	n/a	19.10	25	n/a

1 All measures in these columns are weighted averages. Contractual lives are stated in months.

2 Prices are in pounds unless stated otherwise. The exercise price of options/awards is fixed over the life of each option/award, except that following the rights issue in 2008 adjustments were made to the share plans outstanding at that time. In respect of the Share Matching Scheme, the Trustees sold sufficient rights 'nil paid' to enable the balance of the rights to be taken up. In the case of the Sharesave and LTIP plans the number of shares under option or subject to awards was adjusted by the relevant bonus factor. In the case of the Sharesave Scheme the option price was also adjusted by the relevant bonus factor.

3 US sharesave schemes up to and including 2008 options were granted as American Depositary Shares, each representing two ordinary shares and denominated in US dollars. Subsequent US sharesave scheme options were granted as ordinary shares and included in the international sharesave figures.

**21 Share Schemes** *continued*

The weighted average exercise prices were:

£	2010	2009
Outstanding at the start of the year	<b>13.69</b>	14.14
Granted during the year	<b>15.63</b>	12.55
Exercised during the year	<b>13.31</b>	11.13
Lapsed/cancelled during the year	<b>14.50</b>	16.63
Outstanding at the end of the year	<b>14.19</b>	13.69
Exercisable at the end of the year	<b>14.39</b>	11.70

The weighted average fair value of options granted during the year was £4.18 (2009: £4.88).

**Pricing**

For the purposes of valuing awards to calculate the share-based payment charge, the Black-Scholes option pricing model has been used for all the share option and share matching schemes and for the LTIPs except for those granted since November 2005, where the Monte Carlo model has been used.

A summary of the assumptions used in the Black-Scholes model for 2010 compared to 2009 is as follows:

	2010		2009	
	Sharesave	Share match	Sharesave	Share match
Risk-free interest rate	<b>1.4% – 2.3%</b>	<b>2.0%</b>	2.2% – 3.0%	1.7%
Volatility	<b>31.0% – 36.0%</b>	<b>36.0%</b>	31.0% – 36.0%	35.0%
Expected lives of options granted	<b>3–5yrs + 6mths</b>	<b>3yrs</b>	3–5yrs + 6mths	3yrs
Dividend yield	<b>4.4%</b>	<b>4.4%</b>	3.1%	3.1%
Fair value	<b>£3.87 – £4.42</b>	<b>£18.03</b>	£4.67 – £4.93	£16.21
Share price used to determine option price	<b>£19.53</b>	<b>£20.57</b>	£15.67 – £16.13	£17.80
Exercise price	<b>£15.63</b>	<b>n/a</b>	£12.54 – £12.91	n/a

Volatility is determined based on the three or five year share price history (the time period being determined by the length of the scheme).

Market condition features were incorporated into the Monte Carlo model for the total shareholder return elements of the LTIP, in determining fair value at grant date. Assumptions used in this model were as follows:

	2010	2009
Future Imperial Tobacco Group share price volatility	<b>30.0%</b>	28.0%
Future Imperial Tobacco Group dividend yield	<b>4.4%</b>	3.1%
Share price volatility of the tobacco and alcohol comparator group	<b>20.0% – 49.0%</b>	18.0% – 43.0%
Share price volatility of the FTSE 100 comparator group	<b>20.0% – 114.0%</b>	18.0% – 69.0%
Correlation between Imperial Tobacco and the alcohol and tobacco comparator group	<b>35.0%</b>	35.0%
Correlation between Imperial Tobacco and the FTSE 100 comparator group	<b>40.0%</b>	40.0%

**22 Shares****Treasury shares**

A total of 51,717,000 Imperial Tobacco ordinary shares was purchased through a share buy back programme at a total cost (including expenses) of £862 million before the programme's suspension on 8 February 2007. The shares purchased were not cancelled but were held in a separate treasury reserve and represent a deduction from equity shareholders' funds. The total number of shares held in treasury at 30 September 2010 is 49,569,000 (2009: 51,481,000), representing 4.6 per cent (2009: 4.8 per cent) of the issued share capital, following the gifting to the Employee Share Ownership Trusts of 1,912,000 shares in 2010 (2009: 236,000).

**Shares held by Employee Share Ownership Trusts**

Millions of shares	2010	2009
At 1 October	<b>3.5</b>	4.9
Distribution of shares held by Employee Share Ownership Trusts	<b>(1.6)</b>	(1.6)
Gift of treasury shares	<b>1.9</b>	0.2
At 30 September	<b>3.8</b>	3.5

## 23 Commitments

### Capital commitments

£ million	2010	2009
Contracted but not provided for:		
Property, plant and equipment	114	69

### Operating lease commitments

Total future minimum lease payments under non-cancellable operating leases consist of leases where payments fall due:

£ million	2010	2009
Property		
Within one year	21	18
Between one and five years	66	69
Beyond five years	7	4
	94	91
Plant and equipment (including fixtures and motor vehicles)		
Within one year	7	5
Between one and five years	11	11
	18	16

## 24 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 consolidated financial statements.

In 2003 the Office of Fair Trading (OFT) commenced an investigation under the Competition Act 1998 into the operation of the UK tobacco supply industry in the period from 2000 and 2003. In a decision dated 15 April 2010, the OFT concluded that certain of the Group's promotional arrangements with tobacco retailers had the object of restricting competition and imposed a fine of £112.3 million on the Group. At the same time it confirmed that two other allegations included in its 2008 statement of objections had been dropped.

The Group takes compliance with competition law very seriously and continues to reject any suggestion that it acted in breach of the Competition Act or in any way contrary to the interests of consumers. On 15 June 2010 the Group submitted an appeal to the Competition Appeal Tribunal against the OFT's findings of infringement and the level of the fine. Five tobacco retailers have also submitted appeals against the OFT's decision. The Competition Appeal Tribunal may uphold, quash or vary the OFT's decision or the fine that has been imposed. As part of its appeal the Group has asked for the fine to be quashed in its entirety. Consequently, the Group has not provided for any amount in the consolidated financial statements.

**25 Cash Flows from Operating Activities**

£ million	2010	2009
Profit for the year	<b>1,522</b>	677
Adjustments for:		
Taxation	<b>596</b>	268
Investment income	<b>(844)</b>	(1,180)
Finance costs	<b>1,254</b>	2,572
Share of post-tax profits of associates	<b>–</b>	(1)
Depreciation, amortisation and impairment	<b>666</b>	635
Profit on disposal of property, plant and equipment	<b>(3)</b>	(1)
Post-employment benefits	<b>(25)</b>	1
Costs of employees' services compensated by share schemes	<b>28</b>	21
Acquisition accounting adjustments	<b>14</b>	–
Movement in provisions	<b>(198)</b>	(45)
Operating cash flows before movement in working capital	<b>3,010</b>	2,947
(Increase)/decrease in inventories	<b>(213)</b>	288
(Increase)/decrease in trade and other receivables	<b>(118)</b>	202
Increase in trade and other payables	<b>545</b>	495
Movement in working capital	<b>214</b>	985
Taxation paid	<b>(365)</b>	(363)
Net cash flows from operating activities	<b>2,859</b>	3,569

**26 Analysis of Net Debt**

The movements in cash and cash equivalents, borrowings, derivative financial instruments and finance lease liabilities in the year were as follows:

£ million	Cash and cash equivalents	Current borrowings	Non-current borrowings	Derivative financial instruments	Finance lease liabilities	Total
At 1 October 2009	<b>1,036</b>	<b>(2,560)</b>	<b>(9,507)</b>	<b>(985)</b>	<b>(28)</b>	<b>(12,044)</b>
Cash flow	<b>(208)</b>	<b>2,276</b>	<b>(1,028)</b>	<b>229</b>	<b>2</b>	<b>1,271</b>
Accretion of interest	<b>–</b>	<b>1</b>	<b>9</b>	<b>(11)</b>	<b>–</b>	<b>(1)</b>
Change in fair values	<b>–</b>	<b>–</b>	<b>–</b>	<b>327</b>	<b>–</b>	<b>327</b>
Exchange movements	<b>(55)</b>	<b>(46)</b>	<b>523</b>	<b>–</b>	<b>1</b>	<b>423</b>
At 30 September 2010	<b>773</b>	<b>(329)</b>	<b>(10,003)</b>	<b>(440)</b>	<b>(25)</b>	<b>(10,024)</b>

**Adjusted net debt**

Management monitors the Group's borrowing levels using adjusted net debt which excludes interest accruals, the fair value of derivative financial instruments providing commercial cash flow hedges and finance lease liabilities.

£ million	2010	2009
Reported net debt	<b>(10,024)</b>	(12,044)
Accrued interest	<b>292</b>	291
Fair value of derivatives providing commercial hedges	<b>410</b>	890
Finance lease liabilities	<b>25</b>	28
Adjusted net debt	<b>(9,297)</b>	(10,835)



## 27 Reconciliation of Cash Flow to Movement in Net Debt

£ million	2010	2009
(Decrease)/increase in cash and cash equivalents	(208)	334
Settlement of exchange rate derivative financial instruments	299	5
(Decrease)/increase in collateralisation deposits	(70)	125
Increase in borrowings	(1,542)	(4,324)
Repayment of borrowings	2,790	6,042
Repayment of finance leases	2	2
Change in net debt resulting from cash flows	1,271	2,184
Other non-cash movements including revaluation of derivative financial instruments	326	(1,192)
Exchange movements	423	(1,349)
Movement in net debt during the year	2,020	(357)
Opening net debt	(12,044)	(11,687)
Closing net debt	(10,024)	(12,044)

## 28 Balances and Transactions with Associates and Joint Ventures

2010

£ million	Assets		Liabilities	Goods and services	
	Accounts receivable	Current loans	Accounts payable	Purchases	Sales
Associates	1	–	(1)	15	5
Joint ventures	9	12	(9)	80	48
	10	12	(10)	95	53

2009

£ million	Assets		Liabilities	Goods and services	
	Accounts receivable	Current loans	Accounts payable	Purchases	Sales
Associates	6	–	(4)	19	13
Joint ventures	9	16	(3)	44	44
	15	16	(7)	63	57

## 29 Acquisitions

2010

During 2010, agreement was reached with the sellers of Reemtsma regarding the reimbursement and settlement of costs incurred by the Group as a consequence of investigations into alleged foreign trading violations prior to our acquisition of Reemtsma in 2002. Reimbursement of £27 million received in cash and £14 million of costs settled directly by the sellers on behalf of the Group have been treated as an adjustment to the cost of the Reemtsma acquisition and so are reflected as a reduction in goodwill of £41 million in note 9. To the extent that costs were settled directly by the sellers they have been shown as a non-cash movement of £14 million to arrive at operating cash flow before movement in working capital in note 25. Costs of £24 million incurred in 2010 have been recognised in the 2010 consolidated income statement in administrative and other expenses, and have been excluded from our adjusted performance measures since the costs do not relate to the current trading performance of the Group. We have not restated our adjusted measures for prior years as the costs incurred were not significant in any individual year.

2009

On 7 October 2008 the Group paid deferred consideration of US\$81 million (£46 million) to acquire the outstanding 49 per cent minority shareholdings in 800 JR Cigar and MCM Management. The holding was already 100 per cent consolidated as control was obtained in prior periods.

# Independent Auditors' Report

to the Members of Imperial Tobacco Group PLC

We have audited the parent company financial statements of Imperial Tobacco Group PLC for the year ended 30 September 2010 which comprise the Balance Sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

## Respective Responsibilities of Directors and Auditors

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

This report, including the opinions, has been prepared for and only for the 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.

## Scope of the Audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the 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.

## Opinion on Financial Statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the Company's affairs as at 30 September 2010;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## Opinion on Other Matters Prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the parent company financial statements are prepared is consistent with the parent company financial statements.

In our opinion the information given in the Corporate Governance Report set out with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

## Matters on Which We Are Required to Report by Exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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

## Other Matter

We have reported separately on the Group financial statements of Imperial Tobacco Group PLC for the year ended 30 September 2010.



## David Charles (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Bristol

2 November 2010

# Imperial Tobacco Group PLC Balance Sheet

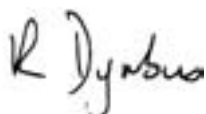
at 30 September 2010

£ million	Notes	30 September 2010	30 September 2009
<b>Fixed assets</b>			
Investments in subsidiaries	(ii)	3,035	1,035
<b>Current assets</b>			
Debtors	(iii)	3,976	6,015
Cash		48	–
		4,024	6,015
Creditors: amounts falling due within one year	(iv)	–	(208)
<b>Net current assets</b>		<b>4,024</b>	<b>5,807</b>
<b>Total assets less current liabilities</b>		<b>7,059</b>	<b>6,842</b>
<b>Net assets</b>		<b>7,059</b>	<b>6,842</b>
<b>Capital and reserves</b>			
Called up share capital	(v)	107	107
Share premium	(vi)	5,833	5,833
Profit and loss account	(vi)	1,119	902
<b>Equity shareholders' funds</b>		<b>7,059</b>	<b>6,842</b>

The financial statements on pages 153 to 156 were approved by the Board of Directors on 2 November 2010 and signed on its behalf by:



**Iain Napier**  
Chairman



**Robert Dyrbus**  
Director

# Notes to the Imperial Tobacco Group PLC

## Balance Sheet

### Basis of Preparation

The financial statements have been prepared on the going concern basis in accordance with the historical cost convention, the Companies Act 2006 and UK Generally Accepted Accounting Principles.

As permitted by section 408 of the Companies Act 2006, no separate profit and loss account has been presented for the Company. As permitted under FRS 1 (revised 1996) Cash Flow Statements the Company has not presented a cash flow statement. As permitted by FRS 29, the Company has elected not to present FRS 29 Financial Instruments: Disclosures in the notes to its individual financial statements as full equivalent disclosures are presented in the consolidated financial statements. As permitted by FRS 8 Related Party Disclosures the Company has not disclosed transactions with wholly owned subsidiaries.

The principal accounting policies are set out below.

### Investments Held as Fixed Assets

Investments held as fixed assets comprise the Company's investment in subsidiaries and are shown at cost less any provision for impairment.

### Dividends

Final dividends are recognised in the Company's financial statements in the period in which the dividends are approved by shareholders, while interim dividends are recognised in the period in which the dividends are paid.

### Financial Instruments

Non-derivative financial assets are classified as cash and debtors. Debtors 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 profit and loss account. For interest-bearing assets, the carrying value includes accrued interest receivable.

### (i) Dividends

Amounts recognised as distributions to ordinary equity holders in the year:

#### Dividend per share in respect of financial year

Pence	2010	2009	2008
Interim	24.3	21.0	20.9
Final	60.0	52.0	42.2
Total	84.3	73.0	63.1

Final dividends are recognised as a liability in the period in which the dividends are approved by shareholders, while interim dividends are recognised in the period in which the dividends are paid. Consequently Imperial Tobacco Group's interim dividends are paid and recognised in the second half of the year, and final dividends in respect of a year are paid and recognised in the following financial period.

#### Amounts recognised as distributions to ordinary equity holders in the year

£ million	2010	2009
Final dividend paid in the period in respect of previous financial year	527	427
Interim dividend	246	213
	773	640

The proposed final dividend for the year ended 30 September 2010 of 60.0p per share amounts to a proposed final dividend payment of £609 million based on the number of shares ranking for dividend at 30 September 2010, and is subject to shareholder approval. If approved, the total dividend paid in respect of 2010 will be £855 million (2009: £740 million).

### (ii) Investments Held as Fixed Assets

#### Cost of shares in Imperial Tobacco Holdings (2007) Limited

£ million	2010	2009
At 1 October	1,035	1,035
Additions	2,000	–
At 30 September	3,035	1,035

A list of the principal subsidiaries of the Company is shown on pages 157 and 158.

**(iii) Debtors: Amounts Falling Due Within One Year**

£ million	2010	2009
Amounts owed by Group undertakings	<b>3,976</b>	6,015

Amounts owed by Group undertakings are unsecured, have no fixed date for repayment and are repayable on demand.

**(iv) Creditors: Amounts Falling Due Within One Year**

£ million	2010	2009
Bank overdrafts	<b>–</b>	208

**(v) Called Up Share Capital**

£ million	2010	2009
Authorised		
56,040,000,000 ordinary shares of 10p each (2009: 56,040,000,000)	<b>5,604</b>	5,604
Issued and fully paid		
1,067,942,881 ordinary shares of 10p each (2009: 1,067,942,881)	<b>107</b>	107

**(vi) Reserves**

£ million	Share premium account	Profit and loss account
At 1 October 2009	<b>5,833</b>	<b>902</b>
Profit for the year	<b>–</b>	<b>990</b>
Dividends	<b>–</b>	<b>(773)</b>
At 30 September 2010	<b>5,833</b>	<b>1,119</b>

**Profit for the year**

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 £990 million (2009: £826 million).

**Treasury shares**

A total of 51,717,000 Imperial Tobacco ordinary shares was purchased through a share buy back programme at a total cost (including expenses) of £862 million before the programme's suspension on 8 February 2007. The shares purchased were not cancelled but were held in a separate treasury reserve and represent a deduction from equity shareholders' funds. The total number of shares held in treasury at 30 September 2010 is 49,569,000 (2009: 51,481,000), representing 4.6 per cent (2009: 4.8 per cent) of the issued share capital, following the gifting to the Employee Share Ownership Trusts of 1,912,000 shares in 2010 (2009: 236,000).

**(vii) Reconciliation of Movements in Shareholders' Funds**

£ million	2010	2009
Profit for the year	<b>990</b>	826
Dividends	<b>(773)</b>	(640)
Movements in equity shareholders' funds	<b>217</b>	186
Opening equity shareholders' funds	<b>6,842</b>	6,656
Closing equity shareholders' funds	<b>7,059</b>	6,842



**(viii) Guarantees**

Imperial Tobacco Group PLC has guaranteed various borrowings and liabilities of certain UK and overseas subsidiary undertakings, including various Dutch and Irish subsidiaries. At 30 September 2010, the contingent liability totalled £9,790 million (2009: £11,464 million).

The guarantees include the Dutch subsidiaries 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 Tobacco Group 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 2010. 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****Number of employees**

The average number of employees during 2010 was nil (2009: nil).

**Key management personnel**

The key management personnel of the Group and the Company are the same. The relevant disclosures are given in the Directors' Remuneration Report on pages 78 to 95.

**Share-based compensation**

As discussed in note 21 to the consolidated financial statements the Group provides share-based compensation to employees through a number of schemes. These are in relation to shares in the Company and the cost of providing those benefits is recharged to the employing companies in the Group.

**Directors' emoluments**

Details of Directors' emoluments and interests are provided within the Directors' Remuneration Report on pages 81 to 83. These disclosures form part of the financial statements.

# Principal Subsidiaries

The principal subsidiaries and joint ventures of the Group, which are unlisted unless otherwise indicated, are shown below.

## Registered in England and Wales, wholly owned

Name	Principal activity
Imperial Tobacco Holdings (2007) Limited	Holding investments in subsidiary companies
Imperial Tobacco Limited	Manufacture, marketing and sale of tobacco products in the UK
Imperial Tobacco International Limited	Export and marketing of tobacco products
Imperial Tobacco Finance PLC	Finance company

## Incorporated overseas, wholly owned

Name and country of incorporation	Principal activity
Altadis S.A., Spain	Manufacture, marketing, sale and distribution of tobacco products in Spain
Altadis Distribution France S.A.S., France	Distribution of tobacco products in France
Altadis Emisiones Financieras SAU, Spain	Finance company
Altadis Finance B.V., Netherlands	Finance company
Altadis Maroc S.A., Morocco	Manufacture, marketing, sale and distribution of tobacco products in Morocco
Altadis Middle East Fzco., United Arab Emirates	Marketing and sale of tobacco products in the Middle East
Altadis USA Inc., United States of America	Manufacture, marketing and sale of cigars in the United States of America
Commonwealth Brands Inc., United States of America	Manufacture, marketing and sale of tobacco products in the United States of America
Compañía de Distribución Integral Logista S.A., Spain	Distribution of tobacco products and related services in Spain
Ets. L. Lacroix Fils N.V., Belgium	Manufacture, marketing and sale of tobacco products in Belgium
Imperial Tobacco Australia Limited, Australia	Marketing and sale of tobacco products in Australia
Imperial Tobacco CR s.r.o., Czech Republic	Marketing and sale of tobacco products in the Czech Republic
Imperial Tobacco Finland Oy, Finland	Marketing and sale of tobacco products in Finland
Imperial Tobacco Hellas S.A., Greece	Marketing and sale of tobacco products in Greece
Imperial Tobacco Italia Srl, Italy <sup>1</sup>	Marketing and sale of tobacco products in Italy
Imperial Tobacco Magyarország Dohányforgalmazó Kft, Hungary	Marketing and sale of tobacco products in Hungary
Imperial Tobacco Mullingar, Republic of Ireland	Manufacture of fine cut tobacco in the Republic of Ireland
Imperial Tobacco New Zealand Limited, New Zealand	Manufacture, marketing and sale of tobacco products in New Zealand
Imperial Tobacco Norway A.S., Norway	Marketing and sale of tobacco products in Norway
Imperial Tobacco Polska S.A., Poland	Manufacture, marketing and sale of tobacco products in Poland
Imperial Tobacco Sales & Marketing LLC, Russia	Marketing and sale of tobacco products in Russia
Imperial Tobacco Sigara ve Tutunculuk Sanayi ve Ticaret A.S., Turkey	Marketing and sale of tobacco products in Turkey
Imperial Tobacco Slovakia A.S., Slovak Republic	Marketing and sale of tobacco products in the Slovak Republic
Imperial Tobacco Taiwan Co. Limited, Taiwan	Marketing and sale 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	Manufacture of tobacco products in Turkey
Imperial Tobacco Ukraine, Ukraine	Marketing and sale of tobacco products in Ukraine
OOO Imperial Tobacco Volga LLC, Russia	Manufacture of tobacco products in Russia
John Player S.A., Spain	Marketing and sale of tobacco products in the Canary Islands
John Player & Sons Limited, Republic of Ireland	Marketing and sale of tobacco products in the Republic of Ireland
Logista Italia S.p.A., Italy	Distribution of tobacco products in Italy
Reemtsma Cigarettenfabriken GmbH, Germany	Manufacture, marketing and sale of tobacco products in Germany
Reemtsma International Asia Services Limited, China	Marketing of tobacco products in China
Skruf Snus AB, Sweden	Manufacture, marketing and sale of tobacco products in Sweden

**Incorporated overseas, wholly owned** *continued*

Name and country of incorporation	Principal activity
Société Nationale d'Exploitation Industrielle des Tabacs et Allumettes S.A., France	Manufacture, marketing and sale of tobacco products in France and export of tobacco products
Supergroup S.A.S., France	Wholesale distribution in France
Tobaccor S.A.S., France	Holding investments in subsidiary companies involved in the manufacture, marketing and sale of tobacco products in Africa
Tobačna Ljubljana d.o.o., Slovenia	Marketing and sale of tobacco products in Slovenia
Van Nelle Tabak Nederland B.V., Netherlands	Manufacture, marketing and sale of tobacco products in the Netherlands
800 JR Cigar Inc., United States of America	Holding investments in subsidiary companies involved in the sale of cigars in the United States of America

**Incorporated overseas, partly owned**

Name and country of incorporation	Principal activity	Percentage owned <sup>1</sup>
Altadis Polska S.A., Poland	Manufacture of tobacco products in Poland	99.97
ZAO Balkanskaya Zvezda, Russia	Manufacture of tobacco products in Russia	99.9
Imperial Tobacco Production Ukraine, Ukraine	Manufacture of cigarettes in Ukraine	99.8
Imperial Tobacco TKS a.d., Macedonia	Manufacture, marketing and sale of tobacco products in Macedonia	99.1
Reemtsma Kyrgyzstan OJSC, Kyrgyzstan	Manufacture, marketing and sale of tobacco products in Kyrgyzstan	98.6
Société Ivoirienne des Tabacs S.A. <sup>2</sup> , Ivory Coast	Manufacture, marketing and sale of tobacco products in the Ivory Coast	74.1

**Incorporated overseas, joint ventures**

Name and country of incorporation	Principal activity	Percentage owned <sup>1</sup>
Altabana S.L., Spain	Holding investments in subsidiary companies involved in the marketing and sale of Cuban cigars	50.0
Corporación Habanos S.A., Cuba	Export of cigars manufactured in Cuba	50.0

**Partnerships**

The Group wholly owns the following partnership:

Name and country	Principal activity
Imperial Tobacco (EFKA) GmbH & Co. KG, Germany	Manufacture of tubes in Germany
Principal place of business: Industriestrasse 6, Postfach 1257, D-78636 Trossingen, Germany	

The subsidiaries listed above were held throughout the year.

The consolidated Group financial statements include all the subsidiary undertakings and entities shown above. 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 by the Company. A full list of subsidiaries is attached to the Annual Return of the Company.

<sup>1</sup> The percentage of issued share capital held by immediate parent and the effective voting rights of the Group is 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.

<sup>2</sup> Listed on the Stock Exchange of the Ivory Coast.

# Shareholder Information

## **Registered Office**

PO Box 244  
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+44 (0)121 415 7009  
0871 384 2255\* text phone for shareholders with hearing difficulties

\* calls to this number will be charged at 8p per minute from a BT landline. Mobile and other providers' charges may vary.  
Lines open 8:30am to 5:30pm, Monday to Friday.

## **ADR Depositary**

Shareholder Services for ADR Holders  
Citibank Shareholder Services  
PO Box 43077  
Providence, RI 02940-3077  
USA  
Toll-free number in the USA: 1-877-CITI-ADR (877-248-4237)  
email: citibank@shareholders-online.com

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## **Auditors**

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Bristol BS1 5QD

## **Lawyers**

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One Bishops Square  
London E1 6AD

Ashurst LLP  
Broadwalk House  
5 Appold Street  
London EC2A 2HA

**Financial Calendar and Dividends**

Half year results are expected to be announced in May 2011 and the full year's results in November 2011.

The Annual General Meeting of the Company is to be held on Wednesday 2 February 2011 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 in August and February. Payment of the 2010 final dividend, if approved, will be on 18 February 2011 to shareholders on the register at the close of business on 21 January 2011. The associated ex dividend date is 19 January 2011.

Shareholders who do not currently mandate their dividends and who wish to do so should complete a mandate instruction form obtainable from Equiniti, at the address shown.

**Share Dealing Service**

A low cost, execution-only share-dealing service for the purchase and sale of Imperial Tobacco Group PLC shares is available from NatWest Stockbrokers. NatWest Stockbrokers is authorised and regulated by the Financial Services Authority and is a member of the London Stock Exchange and PLUS. For details, please contact NatWest Stockbrokers, Premier Place, 2½ Devonshire Square, London EC2M 4BA, telephone: 0870 600 3070.

**Individual Savings Account (ISA)**

Investors in Imperial Tobacco Group PLC ordinary shares may take advantage of a low cost Individual Savings Account (ISA) and Investment Account where they can hold their Imperial Tobacco Group shares electronically. The ISA and Investment Account are operated by Equiniti Financial Services Limited. Commission starts from £5.00 and £1.75 respectively for the sale and purchase of shares.

For a brochure or to apply for an Investment Account or ISA go online to [www.shareview.co.uk/dealing](http://www.shareview.co.uk/dealing) or call Equiniti on 0845 300 0430.

**Dividend Reinvestment Plan (DRIP)**

Imperial Tobacco Group PLC has set up a dividend reinvestment plan (DRIP) to enable shareholders to use their cash dividend to buy further shares in the market. Further information can be obtained from Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA, telephone: 0871 384 2268\* (+44 (0)121 415 7173) or online at [www.shareview.co.uk](http://www.shareview.co.uk).

\* calls to this number will be charged at 8p per minute from a BT landline. Mobile and other providers' charges may vary.

**American Depositary Receipt Facility**

Imperial Tobacco Group PLC ordinary shares are traded on the OTCQX International Premier platform in the form of American Depositary Shares (ADSs) using the symbol "ITYBY". Each ADS represents two Imperial Tobacco Group PLC ordinary shares. The ADS facility is administered by Citibank, N.A. and enquiries should be directed to them at the address shown.

**Website**

Information on Imperial Tobacco Group PLC is available on our website: [www.imperial-tobacco.com](http://www.imperial-tobacco.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](http://www.shareview.co.uk).



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