



**BRITISH AMERICAN
TOBACCO**

news release

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**PRELIMINARY ANNOUNCEMENT - YEAR ENDED 31 DECEMBER 2010
SUMMARY**

	2010	2009	Change
Revenue	£14,883m	£14,208m	+5%
Profit from operations	£4,318m	£4,101m	+5%
Adjusted profit from operations	£4,984m	£4,461m	+12%
Basic earnings per share	145.2p	137.0p	+6%
Adjusted diluted earnings per share	175.7p	153.0p	+15%
Dividends per share	114.2p	99.5p	+15%

- Group revenue grew by 5 per cent to £14,883 million as a result of the continued good pricing momentum, the acquisition of PT Bentoel Investama Tbk made in June 2009 and the favourable impact of exchange rate movements. Organic Group revenue (see page 1) was up 3 per cent at constant rates of exchange.
- The reported Group profit from operations was 5 per cent higher at £4,318 million. Adjusted profit from operations (see page 1) was 12 per cent higher and would have been up 6 per cent at constant rates of exchange.
- Group volumes were 708 billion, down 2 per cent mainly due to industry declines. However, overall market share in the Group's Top 40 markets increased.
- The four Global Drive Brands achieved good overall volume growth of 7 per cent. Dunhill was up 18 per cent, Lucky Strike 2 per cent and Pall Mall grew by 8 per cent, while Kent volumes fell 1 per cent due to industry declines in its main markets.
- Adjusted diluted earnings per share rose by 15 per cent, principally as a result of the growth in profit from operations and favourable exchange movements. Basic earnings per share were up 6 per cent at 145.2p (2009: 137.0p).
- The Board is recommending a final dividend of 81.0p, payable on 5 May 2011. The total dividend in respect of 2010 is 114.2p, an increase of 15 per cent.
- Free cash flow increased by 23 per cent to £3,240 million, 92 per cent of adjusted earnings.
- Share buy-back of £750 million announced.
- The Chairman, Richard Burrows, commented "British American Tobacco remains in very good shape at the end of 2010. We have increased our competitiveness by growing our share in key markets and improving our cost base. There will be further global economic challenges ahead but we can see strong opportunities for growth too. That's why I am confident we can continue to deliver superior shareholder returns in 2011 and beyond."

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BRITISH AMERICAN TOBACCO p.l.c.

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NON-GAAP MEASURES

Adjusted profit from operations is derived after excluding the adjusting items of subsidiaries (see page 28) and associates (see page 30) from the profit from operations.

Organic growth is the growth after adjusting for mergers and acquisitions and discontinued activities. Adjustments are made to current and prior year numbers, based on the 2010 Group position.

CHAIRMAN'S STATEMENT

This has been a good year for your company in spite of difficult trading conditions. The global economic climate has affected consumer spending in many parts of the world but the inherent strength of your company's business, with its worldwide reach to emerging and developed markets, its balanced portfolio of brands and its consistent focus on innovation, continues to deliver impressive results and sustained shareholder value.

Strong business performance

Reported revenue rose by 5 per cent to £14,883 million at current rates, while organic revenue rose by 3 per cent at constant rates of exchange. Adjusted profit from operations increased by 6 per cent at constant rates of exchange and by 12 per cent to £4,984 million at current rates. The benefit from the translation of our results into sterling was £239 million.

This resulted in adjusted diluted earnings per share growing by 15 per cent to 175.7p.

Our regions all contributed to our very good results. However, the growth in illicit trade in a number of markets remains a cause for concern. For example, in Romania – one of our two main markets in our Eastern Europe region – our market share was up but industry volumes declined significantly due to large excise-driven price increases that led to a sharp rise in illicit trade.

Our overall Global Drive Brand volumes grew by 7 per cent in the year and we increased our overall market share in our Top 40 markets. Despite global recessionary pressures, we also improved our share of the premium segment in these markets.

Dividends

The Board has recommended a final dividend of 81.0p per share, which will be paid on 5 May 2011 to shareholders on the register at 11 March 2011. This takes the total dividend for the year to 114.2p, an increase of 15 per cent, and maintains our target of paying out 65 per cent of sustainable earnings in dividends.

Share buy-back programme

In 2009, the Board decided to suspend the share buy-back programme that started in 2003, in order to preserve the Group's financial flexibility during a period of economic uncertainty. As a result, no shares were bought back during 2009 and 2010. The Board has approved the resumption of the programme in 2011 with a value of up to £750 million.

Board changes

During 2010, Kieran Poynter joined our Board as a Non-Executive Director. And, at our forthcoming AGM, Ana-Maria Llopis will retire from the Board after eight years of excellent service.

At the end of February 2011, Paul Adams, our Chief Executive, retires after seven years in that role. Paul has made an immense contribution and has led your Company to a recognised position of pre-eminence in the industry.

Nicandro Durante takes over as Chief Executive on 1 March. He is very experienced in this industry and, as you will see in this report, he is committed to continuing our successful strategy and driving growth.

John Daly has joined the Board as Chief Operating Officer and he also has a lot of experience in the industry and a very good track record.

Ben Stevens, Finance Director, has been appointed as Chief Information Officer in addition to his Finance role. This means he will have direct responsibility for the transformation of the Group as we continue to develop a more integrated approach to the management of the business.

To all our directors on the p.l.c. Board and the Management Board, and to all our employees around the world, I express my thanks and appreciation for your efforts that have made this company so successful in 2010. To Paul Adams, I say thanks and I wish you a long and happy retirement.

Excellence in sustainability

We can be justly proud of our record of excellence in sustainability, which helps us create wealth for our shareholders as well as creating value for our stakeholders.

We have long had the brands and people to deliver very good results in our key markets. During the last ten years, we have become better at demonstrating that we are running our business responsibly and we have made a number of important improvements that should ensure your company's long-term success.

Our first Social Report was published in 2002 and this year sees our tenth publication, as our 2010 Sustainability Report is published alongside our Annual Report at the end of March for the first time.

Opportunities for growth

British American Tobacco remains in very good shape at the end of 2010. We have increased our competitiveness by growing our share in key markets and improving our cost base. There will be further global economic challenges ahead but we can see strong opportunities for growth too. That's why I am confident we can continue to deliver superior shareholder returns in 2011 and beyond.

Richard Burrows
23 February 2011

CHIEF EXECUTIVE'S REVIEW

A strong business in a tough marketplace

The strength of our companies worldwide and the success of our tried and tested Group strategy have enabled us to achieve very good growth through a volatile year, marked by economic uncertainty. Some emerging markets are now showing strong economic growth and even developed markets are returning to growth, yet unemployment remains stubbornly high in many parts of the world and disposable incomes are still under pressure.

So it's still a tough marketplace but our results show the true quality of our business. Our geographic diversity and strong positions in markets that have been least affected by the global recession continue to play a part in our success. However, the real story is the strength of our brands, the innovative products we bring to market and the quality of our people.

In 2010 we grew market share, we grew our leading international brands in our most important markets and we achieved significant productivity savings that were well ahead of our established targets. Our organic revenue in constant currency also rose 3 per cent despite a decline in organic volume of 3 per cent.

Our brands are strong and growing in market share

Our brands are performing well and I believe that this shows the true vitality of the Company. Collectively, our Global Drive Brands (GDBs) – Dunhill, Kent, Lucky Strike and Pall Mall – grew by 7 per cent, reflecting the successful launch of product innovations in key markets and brand migrations.

What's pleasing is that we are growing market share where it matters most. Our overall share in our Top 40 markets grew by 30 basis points to 25.3 per cent – a really encouraging result.

Productivity enabling growth

Our structural cost base has seen big changes over the past couple of years and this will continue. This is not just belt tightening, we are reconfiguring our structural costs as a result of refining our manufacturing footprint and developing new global systems that reduce local duplication of effort and resources.

Productivity savings in the supply chain, general overheads and indirect costs amounted to £327 million in 2010 and helped us achieve an overall operating margin increase from 31.4 to 33.5 per cent. This means we have achieved our £800 million per year productivity savings target for 2012 two years ahead of schedule. I can see our ability to reduce costs continuing, especially as we exploit new global systems and processes. So we've made good progress on costs and there's more to come.

Delivering sustainable growth

Our sustainability performance is also very important to us. It's all about creating shared value – how we can create economic value in a way that also creates value for our stakeholders. The work we have done in this area, not just in 2010 but over the last decade, has been recognised through external benchmarking such as the UK's Business in the Community Corporate Responsibility Index and the Dow Jones Sustainability Indexes.

We have also received very good feedback on our Sustainability Reports and, in some cases, we have surprised independent assessors, including some who are critical of our business, with the openness and transparency of our reporting and the way we integrate sustainability with our business priorities and our strategy.

We continue to make progress on our sustainability agenda – not just our impact on the environment and our people, but also the way we conduct our operations in the marketplace and throughout our supply chain. Our focus on the consumer means that we have continued to invest in our brands and the development of product innovations to drive growth, while we also invest in the longer term to ensure the business is fit to meet future challenges. This includes having the research and development capability to support our investigation of innovative products and our efforts to develop potentially reduced-harm prototypes.

Chief Executive's review cont...

Handing over

This report marks the end of an extremely enjoyable, often challenging and always interesting seven-year period for me as Chief Executive. My successor, Nicandro Durante, has much to look forward to. I know he will quickly make the role his own and his drive for success will help to ensure the continued growth of this excellent business.

I retire from the Company satisfied with the progress we have made and confident about its future. I'm clearly going to miss it. I'm tremendously proud of what we've achieved and I can only thank my colleagues in the company – all 60,000 of them – for what we've achieved together. I wish them, Nicandro and the whole business well for the future.

Paul Adams
Chief Executive

NEW CHIEF EXECUTIVE'S REVIEW

A strategy for growth

I am delighted to take on my role at a time when the opportunities for growth continue to be strong. There's no doubt that we have our work cut out to match or exceed the success of the past few years, but I know that we have the right business model, the right products and the right people, with the strongest innovations anyone in our industry has at their disposal.

Our strategy certainly won't change, although we may talk about it in a slightly different way. Our business model and balanced strategy add value to all aspects of our business and we believe this sets us apart from our competitors. We still think that delivering growth is the key to achieving our vision to lead the global tobacco industry. This means placing an even greater focus on growth and ensuring that it drives everything we do. Our growth is funded by productivity and delivered by a winning organisation that acts responsibly at all times.

Strengthening our business

In 2010, we've strengthened our brands, we've strengthened our innovations and we've increased market share. We also made good progress on our sustainability agenda and very good progress on reducing costs.

We grew overall share in our Top 40 markets and I believe that as markets start to come out of the recession, we are now armed with a stronger portfolio than we had before and are ready to take advantage of further growth opportunities. The key indicators are moving in the right direction, demonstrating the strength of our business.

Our GDBs have grown 7 per cent overall in a declining total market and our share of the adult smokers under 30 (ASU30) segment increased in our Top 40 markets.

This success has been driven by innovations we have introduced across the world – such as Lucky Strike Click & Roll in the Americas and Western Europe, and Dunhill Reloc and Kent Convertibles in Asia-Pacific.

During 2010, we saw our business improve in markets that are fundamental to our growth strategy – such as Russia, South Korea, Canada, Mexico, Japan, Nigeria, the GCC, France and Italy. We also announced our intention to move from five to four regions to reduce complexity in our management structures, achieve a better balance in the scale of our regions and to make us more agile in our decision making.

Global outlook

Paul has explained why we are confident we have a sustainable business, but where will the industry be in 10, 20 or even 40 years' time? Well, one thing we have always said is that it's not a good time to predict the long-term future when you're in a recession. Even so, few would disagree that the industry looks very robust for the foreseeable future. Forecasts suggest that the world market is likely to remain fairly stable at between 5 and 6 trillion cigarettes, more than 40 per cent of which are sold in China.

Even where we see volumes decline, we expect overall market values to grow, due to changes in the product mix. Our consumer-led innovations will continue to help us build our premium products and the strength of our brands.

Looking at market size in isolation, we've done extrapolations that cover the next 20 years and that's where demographics become important. Trends indicate that individual smokers will consume fewer cigarettes each and smaller percentages of populations will smoke.

However, with the world's population predicted to increase to seven billion by the end of 2012 and nine billion by the end of 2050, we expect there will be a very sustainable and profitable tobacco industry delivering value for a long time to come.

The World Health Organisation has forecast that there are likely to be more smokers in the year 2050 than there are today, despite the impact of regulation. That is certainly a plausible scenario given the demographics.

Managing risks

We have identified a core list of areas that we believe could represent a significant risk to our business. As can be seen from our review of the Key Group risk factors in appendix 2 to this report, we regularly monitor their potential impact and controls are in place to ensure that, where possible, they are carefully managed.

New Chief Executive's review cont...

Competitive landscape

We are looking to grow our business and we believe we can meet our financial objectives through organic growth alone. However, we continue to monitor acquisition opportunities around the world and will participate where it makes financial and strategic sense to do so.

Illicit trade

The illicit trade in tobacco products is a growing threat to legitimate companies. We support the development of the World Health Organisation's Framework Convention on Tobacco Control (FCTC) protocol aimed at creating an international regulatory framework for addressing illicit trade. However, other measures from the FCTC may drive significant excise increases, retail display bans and plain packaging, all of which could play into the hands of organised crime by creating ideal conditions for further increases in illicit trade.

A vision for success

Looking to 2011 and the years ahead, our ambitious vision of achieving leadership of our industry remains as relevant as ever. We still have much to do to deliver our vision but our strategy for growth and our increasing competitiveness mean we are well placed to succeed.

We will continue to refresh and enhance our brand portfolio, introducing consumer-focused innovations where appropriate. Our operational fitness will also continue to improve, as we implement and roll-out new global systems. I look forward to the challenges ahead and I know our people around the world do too.

Nicandro Durante
Chief Executive (from 1 March 2011)

REGIONAL REVIEW

Group revenue grew by 5 per cent in 2010. This was the result of favourable exchange rate movements, continued good pricing momentum and the acquisition of PT Bentoel Internasional Investama Tbk (Bentoel) in the middle of 2009. Organic Group revenue was up 3 per cent at constant rates of exchange.

The reported profit from operations was 5 per cent higher at £4,318 million, with a 12 per cent increase if adjusting items (as explained on pages 28 and 29), are excluded. The major difference between the growth rates of adjusted profit from operations compared to reported profit, is the goodwill and trademark impairment write-downs in respect of Turkey, as further described on page 29. All of the regions contributed to this good profit result, except for Eastern Europe where there were significantly lower industry volumes in Romania, driven by illicit trade, and an adverse exchange rate in Uzbekistan. Adjusted profit from operations was 6 per cent higher at constant rates of exchange, with all regions growing.

Group volumes from subsidiaries were 708 billion in 2010, down 2 per cent on last year, despite the acquisition of Bentoel. This was a result of lower industry volumes in some markets, mainly Turkey, Pakistan, Romania and South Africa and an increase in illicit trade.

Overall Group market share in its Top 40 markets increased with a particularly strong performance in the second half of 2010. However, volumes were down 3 per cent on last year once benefits of the acquisition are excluded.

The Global Drive Brands achieved good overall volume growth of 7 per cent following the launch of successful innovations, and this resulted in a continued improvement in market share. Excluding brand migrations, growth was 3 per cent.

Dunhill increased volumes by 18 per cent in 2010, mainly as a result of brand migrations in Brazil and South Africa and strong growth in the GCC, Russia, France, Nigeria and Indonesia. Kent was 1 per cent lower after industry volume declines in two of its main markets, Japan and Romania, despite growing market share in both. Volumes were up in Russia, Ukraine and Uzbekistan.

Lucky Strike volumes were 2 per cent higher with growth in many markets, including France, Chile and Argentina. However, this was partially offset by declines in its main markets of Germany, Spain and Japan. Pall Mall volumes increased by 8 per cent, with growth in Germany, Uzbekistan, Italy, Spain, Pakistan, Nigeria and Chile, partially offset by lower volumes in Russia, Romania, Hungary and Turkey.

Other International Brands excluding GDBs grew by 2 per cent, with good performances by Vogue, Benson & Hedges, Craven 'A', John Player Gold Leaf and Rothmans.

Adjusted profit from operations* at constant and current rates of exchange is as follows:

	2010		2009
	Adjusted profit from operations*		Adjusted
	Constant	Current	profit from
	rates	rates	operations*
	£m	£m	£m
Asia-Pacific	1,195	1,332	1,148
Americas	1,248	1,382	1,186
Western Europe	1,081	1,054	994
Eastern Europe	428	358	409
Africa and Middle East	793	858	724
	<u>4,745</u>	<u>4,984</u>	<u>4,461</u>

*Adjusted profit from operations (page 15) is derived after excluding adjusting items from profit from operations. Adjusting items include restructuring and integration costs, amortisation of trademarks, goodwill and trademark impairments and gains on disposal of businesses and trademarks as explained on pages 28 and 29.

In **Asia-Pacific**, profit was up £184 million to £1,332 million as a result of strong performances in Japan, Australia, New Zealand and Bangladesh. Favourable exchange rates and the acquisition of Bentoel were also contributing factors. At constant rates of exchange, profit would have increased by £47 million, or 4 per cent. Volumes were 2 per cent higher at 188 billion, due to increases in Bangladesh and Vietnam and the additional volumes from Bentoel, although these were partially offset by lower volumes in Australia, Japan, Taiwan and Pakistan.

Australia achieved strong profit growth through higher pricing and continued cost saving initiatives. Good performances from both Pall Mall and Winfield led to an increase in market share, although an ad-hoc excise increase in May 2010 resulted in a drop in industry volumes.

In New Zealand, profit increased due to beneficial exchange rate movements and strong growth in share by Pall Mall. However, volumes were lower, impacted by an ad-hoc excise increase and a tax equalisation for roll-your-own products.

Market share in Malaysia was up, as the share gained by Peter Stuyvesant and the resilient performances by Kent and Dunhill were partially offset by the impact of down-trading. Volumes were slightly lower due to both legal industry volume decreases as a result of hefty excise rises and increased illicit trade. Profit was up as a result of exchange rate movements and price increases, partially offset by lower volumes and higher marketing investment.

Profit grew strongly in Japan, benefiting from increased margins, exchange rate movements and lower overheads. Although industry volumes were down, following the excise rise on 1 October 2010, market share grew. Kent returned to share growth, driven by the successful launch of Nanotek, and Kool continued to grow share.

Vietnam had a solid performance, with market share gains and good volume growth, mainly due to Craven 'A'.

South Korea closed the year with market share at a record high, supported by the successful launch of Kent and the growth of Dunhill in the second half of the year. However, volumes were lower due to the contraction of the industry. Profit decreased as a result of lower volumes and investment into the launches of Kent and Dunhill innovations.

Excise and inflation-led price increases in Pakistan, combined with supply chain disruption, caused by floods, led to lower volumes and accelerated down-trading to the low-price segment and the illicit sector. Profit was adversely affected by the mix deterioration, increased costs and lower volumes.

Bangladesh achieved significantly higher market share. Operating profit was higher, reflecting improved volumes and the impact of excise-led price increases, as well as a tight control on costs.

Volumes, market share and profit in Indonesia grew through the acquisition of Bentoel and the subsequent integration with the existing business. Profit grew strongly on a comparable basis as a result of higher volumes, price increases and synergy savings resulting from the integration.

In **Americas**, profit rose by £196 million to £1,382 million. This was mainly due to strong performances from Canada, Brazil and Chile, an improved product mix and exchange rate benefits. At constant rates of exchange, profit would have risen by £62 million, or 5 per cent. Volumes were down 1 per cent at 149 billion, with the small decreases experienced in Brazil and Venezuela as a result of industry declines almost offset by higher volumes in Canada and Chile.

Profit growth in Brazil was driven by higher pricing, an improved product mix and a stronger local currency. Market share in the premium segment grew due to solid performances from Lucky Strike as well as Dunhill after the migration from Carlton. Overall market share was higher, although price increases led to lower industry volumes.

Profit in Canada was higher, with the effect of reduced illicit trade, price increases and exchange rate benefits more than offsetting continued down-trading. Substantial progress was also made on the cost base. Volume grew following a significant reduction in illicit trade due to the enforcement activities of authorities. The Group gained leadership in all cigarette segments in Canada, which contributed to a significant market share improvement, driven by John Player Standard.

Regional review cont...

In Mexico, profit was higher as a result of an improved operating margin and volume stability after many years of market decline, driven by trade-stocking in December 2010 in anticipation of a price increase. Market share stabilised with good performances from Pall Mall and Montana and the launch of Dunhill in the third quarter. In Argentina, Dunhill was launched in the last quarter of the year, and Lucky Strike showed strong volume and share growth as it capitalised on consumers' up-trading. However, profit was impacted by lower volumes and higher marketing investment.

Volumes increased in Chile, driven mainly by strong performances from Lucky Strike and Pall Mall. Profit grew significantly as a result, enhanced by price rises ahead of an excise increase, an improved product mix and lower overheads.

Market share in Venezuela was up in a contracted market. However, price increases did not cover the impact of currency devaluation on costs, higher expenses and lower volumes, which resulted in a lower profit. Market share and volumes in Colombia were maintained, although profit was slightly down.

Profit in **Western Europe** increased by £60 million to £1,054 million, mainly as a result of strong performances in Germany, Belgium, Spain, Poland, Sweden and the Netherlands, although this was partially offset by declines in Denmark, Italy and Greece. At constant rates of exchange, profit would have increased by £87 million, or 9 per cent. Regional volumes were 8 per cent lower at 119 billion as a result of declines in Poland, Germany, Switzerland and the Netherlands.

In Italy, an improved mix, coupled with a price increase and lower costs, offset some of the volume decline, although profit was depressed by an adverse exchange rate. Market share was slightly down on last year, despite share growth of Global Drive Brands and overall share increasing over the last quarter.

Profit in Germany increased as a result of higher margins from price increases in 2009 and lower costs, despite the termination of the Gauloises license agreement at the end of March. Market share was the same as last year. On a like-for-like basis, volumes were slightly down in a contracting market, despite an excellent performance by Pall Mall.

Volumes in France were stable, which kept profit in line with last year. Improved pricing and lower product costs were offset by an unfavourable product mix and marketing investment.

Profit and market share were both up strongly in Spain, driven by a favourable pricing environment and good performances by Pall Mall and Lucky Strike. Volumes were slightly down in a declining total market.

Profit was maintained in Switzerland, benefiting from price increases and lower costs. Volumes were lower, impacted by industry contraction. Market share was down although Parisienne maintained its overall share at an historic high.

The restructuring of the commercial units of Belgium and the Netherlands into one organisation was completed on 1 June 2010. There was a good growth in profit as a result of higher pricing and lower costs.

Profit increased strongly in Poland as two price increases more than offset the impact of lower industry volumes. Market share decreased despite the strong growth of Viceroy.

In Greece, industry volume declined due to excise and VAT increases during the first half of the year and lower consumer disposable income. Although market share was up, volumes were slightly lower. Profit dropped significantly due to competitor pricing and as a result of lower volumes.

Volumes and profit in Denmark were lower due to the rationalisation of various tail brands and down-trading following two significant excise increases.

Market share grew and volume increased in the United Kingdom, mainly as a result of the good performance of Pall Mall, which resulted in a significant increase in profit.

Profit in the **Eastern Europe** region decreased by £51 million to £358 million. This was principally due to lower volumes and the adverse impact of exchange rates, mainly in Uzbekistan, although this was partly offset by price increases. At constant rates of exchange, profit would have increased by £19 million, or 5 per cent. Volumes at 128 billion were 2 per cent lower, mainly due to industry declines in Romania. Market share grew in the majority of markets and regional share was also higher.

Price increases and the improved product mix in Russia increased profit. Market share grew, despite volumes being in line with last year. The Group achieved leadership in the premium segment and market share leadership in Moscow, as a result of continued excellent performances by Kent and Dunhill.

Market share in Romania was up strongly, with an impressive performance by the market leader, Kent. Increased illicit trade due to numerous large excise-driven price increases meant industry volumes declined significantly. The volume decline was only partially offset by price increases, leading to a lower profit.

In Ukraine, market share increased strongly, and excellent profit growth was achieved as a result of an improved product mix, led by growth in Global Drive Brands and stronger pricing. Group volumes increased.

Results improved in Kazakhstan due to higher margins. Market share was up as a result of a strong performance by Kent and Pall Mall. The decrease of the premium segment resulted in slightly lower volumes.

In Uzbekistan, market share grew strongly, driven by the growth of Kent and Pall Mall. However, industry volumes were lower as a result of an excise increase and profit was significantly impacted by adverse exchange rates.

Profit from the **Africa and Middle East** region grew by £134 million to £858 million in 2010. At constant rates of exchange, profit would have improved by £69 million, or 10 per cent, mainly driven by Nigeria and the Gulf Cooperation Council (GCC). Volumes were 2 per cent lower at 124 billion, following declines in Turkey, Iran and South Africa. However, these were partially offset by increases in the GCC, Egypt and Nigeria.

In South Africa, market share grew following strong performances by Peter Stuyvesant and Kent, aided by the successful migration of Courtleigh to Dunhill. Volumes were down after an almost doubling of illicit trade. However, the profit impact of this was mitigated by increased pricing and cost reduction initiatives, helped by a stronger exchange rate.

Nigeria achieved strong volume growth. Coupled with higher prices and cost reductions, this led to an impressive profit performance. A reduction in illicit trade, rural market expansion and effective distribution across all channels contributed to volume growth. Market share also grew strongly, with excellent performances from Dunhill and Pall Mall.

In the GCC markets, volume, market share and share in the Premium segment grew strongly, with Dunhill and John Player Gold Leaf the main contributors. Profit was significantly higher, benefiting from volume growth and stronger pricing.

In the rest of the Middle East volumes were lower although this was partially offset by a strong performance in the Levant. Profit was lower, as a result of a decline in volumes and higher brand investment in Levant.

An aggressive excise-driven price increase in Turkey in January 2010 led to an almost doubling of illicit trade. Nevertheless, profit rose as price increases, favourable exchange movements and reduced production overheads offset the impact of lower volumes. The brand portfolio acquired in the Tekel transaction was particularly affected by the growth in illicit trade and competitor pricing.

In Egypt, volumes and market share continued their impressive growth trend, despite the excise-led price increases in July. However, profit was adversely impacted as the excise increase was only partially recovered through higher prices. Rothmans had a good performance, expanding its leadership position among international brands.

Regional review cont...

Results of associates

Associates principally comprise Reynolds American and ITC.

The Group's share of the post-tax results of associates excluding the adjusting items explained on page 30, increased by 15 per cent to £622 million, with a rise of 11 per cent at constant rates of exchange.

The segmental analyses of the Group's share of the adjusted post-tax results of associates and joint ventures are as follows:

	2010		2009
	Adjusted share of post-tax results		Adjusted share of post-tax results
	Constant rates	Current rates	
	£m	£m	£m
Asia-Pacific	194	208	148
Americas	407	412	391
Western Europe	-	-	-
Eastern Europe	-	-	-
Africa and Middle East	2	2	2
	603	622	541

The contribution from Reynolds American increased by 5 per cent to £346 million. Excluding the impairment and amortisation of trademarks and restructuring costs, as well as the past service credit for a health plan in 2009 and the Canadian settlement in 2010, the contribution was 5 per cent higher at £409 million. At constant rates of exchange the increase was 4 per cent.

The Group's associate in India, ITC, continued its strong profit growth and its contribution to the Group rose by 35 per cent to £195 million. Excluding the impact of the dilution in the Group's shareholding, the contribution was 42 per cent higher at £204 million. At constant rates of exchange, the contribution would have been 33 per cent higher than last year.

Changes to our regional structure

As part of plans to reduce complexity, drive efficiency in management structures and achieve a better balance in the scale of the regions, the number of regions is being reduced from five to four from 1 January 2011.

Markets which currently comprise the Eastern Europe region will be merged into the Africa and Middle East region and the Western Europe region. Russia, Ukraine, Moldova, Belarus, Caucasus and Central Asia will form part of the new Eastern Europe, Middle East and Africa region (EEMEA) while Romania, Bulgaria, Serbia, Montenegro, Albania and Kosovo will become part of the Western Europe Region. (See page 27).

Cigarette volumes

The segmental analysis of the volumes of subsidiaries is as follows:

6 months to			12 months to	
30.06.10	30.06.09		31.12.10	31.12.09
bns	bns		bns	bns
95	88	Asia-Pacific	188	185
73	74	Americas	149	151
59	63	Western Europe	119	130
58	60	Eastern Europe	128	131
63	64	Africa and Middle East	124	127
348	349		708	724

DIVIDENDS

The Board recommends a final dividend of 81.0 pence per ordinary share of 25p for the year ended 31 December 2010. If approved by shareholders at the Annual General Meeting to be held on 28 April 2011, the dividend will be payable on 5 May 2011 to shareholders registered on either the UK main register or the South African branch register on 11 March 2011 (the record date).

In compliance with the requirements of Strate, the electronic settlement and custody system used by the JSE Limited (JSE), the following dates for the payment of the dividend are applicable:

Last day to trade cum dividend (JSE):	Friday 4 March 2011
Shares commence trading ex dividend (JSE):	Monday 7 March 2011
Shares commence trading ex dividend (LSE):	Wednesday 9 March 2011
Record date (JSE and LSE):	Friday 11 March 2011
Payment date:	Thursday 5 May 2011

As the Group reports in sterling, dividends are declared and payable in sterling except for shareholders on the branch register in South Africa whose dividends are payable in rand. A rate of exchange of £:R = 11.54580 as at 22 February 2011 (the closing rate on that date as quoted by Bloomberg), results in an equivalent final dividend of 935.20980 SA cents per ordinary share. From the close of business on 4 March 2011 until the close of business on 11 March 2011, no transfers between the UK main register and the South African branch register will be permitted and no shares may be dematerialised or rematerialised between 7 March 2011 and 11 March 2011, both days inclusive.

The following is a summary of the dividends declared for the years ended 31 December 2010 and 2009:

	2010		2009	
	Pence per share	£m	Pence per share	£m
Ordinary shares				
Interim				
- 2010 paid 29 September 2010	33.2	662		
- 2009 paid 29 September 2009			27.9	557
Final				
- 2010 payable 5 May 2011	81.0	1,607		
- 2009 paid 6 May 2010			71.6	1,431
	<u>114.2</u>	<u>2,269</u>	<u>99.5</u>	<u>1,988</u>

In accordance with IFRS, the proposed final dividend amounting to £1,607 million (2009: £1,431 million), payable on 5 May 2011, will be recognised in the Group accounts for the year ending 31 December 2011. For the year ended 31 December 2010, the accounts include the final dividend paid in respect of the year ended 31 December 2009, amounting to £1,431 million and the interim dividend amounting to £662 million, paid on 29 September 2010. For the year ended 31 December 2009, the accounts include the final dividend paid in respect of the year ended 31 December 2008, amounting to £1,241 million and the 2009 interim dividend, amounting to £557 million.

RISKS AND UNCERTAINTIES

The principal risks and uncertainties affecting the business activities of the Group were reviewed and updated and are summarised in a table that is attached as appendix 2 to this announcement. The table provides a brief description of the key risks to which the Group's operations are exposed and it identifies, in each case, their potential impact on the Group and the principal processes in place to manage the risk.

The key Group risks are summarised under the headings of:

- Illicit trade
- Excise and tax
- Financial
- Marketplace
- Regulation
- Legal and compliance
- Data risks

The key Group risks should be read in the context of the cautionary statement regarding forward looking statements on page 56.

GOING CONCERN

A full description of the Group's business activities, its financial position, cash flows, liquidity position, facilities and borrowings position, together with the factors likely to affect its future development, performance and position, is set out in this announcement. It will also be discussed and disclosed in the Business Review and Financial Review and in the notes to the financial statements, all of which will be included in the 2010 Annual Report that will be available on the Group's website, www.bat.com on 28 March 2011.

The Group has, at the date of this report, sufficient existing financing available for its estimated requirements for at least the next twelve months. This, together with the proven ability to generate cash from trading activities, the performance of the Group's Global Drive Brands, its leading market positions in a number of countries and its broad geographical spread, as well as numerous contracts with established customers and suppliers across different geographical areas and industries, provides the Directors with the confidence that the Group is well placed to manage its business risks successfully, despite the current financial conditions and the uncertain outlook in the general global economy.

After reviewing the Group's annual budget, plans and financing arrangements, as well as the current trading activities of the Group, the Directors consider that the Group has adequate resources to continue operating for the foreseeable future. The Annual Report has therefore been prepared on a going concern basis.

DIRECTORS' RESPONSIBILITY STATEMENT

The responsibility statement below has been prepared in connection with the company's full Annual Report for the year ended 31 December 2010. Certain parts thereof are not included within this announcement.

We confirm to the best of our knowledge:

- the financial statements, prepared in accordance with IFRS as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Group; and
- the Directors' report (which incorporates the business review), includes a fair review of the development and performance of the business and the position of the Group and the Company, together with a description of the principal risks and uncertainties that they face.

This responsibility statement was approved by the Board of Directors on 23 February 2011 and is signed on its behalf by:

Richard Burrows
Chairman

Ben Stevens
Finance Director and CIO

GROUP INCOME STATEMENT

For the year ended 31 December

	2010 £m	2009 £m
Gross turnover (including duty, excise and other taxes of £28,972 million (2009: £26,505 million))	43,855	40,713
Revenue	14,883	14,208
Raw materials and consumables used	(3,695)	(3,983)
Changes in inventories of finished goods and work in progress	(12)	35
Employee benefit costs	(2,550)	(2,317)
Depreciation, amortisation and impairment costs	(897)	(611)
Other operating income	207	196
Other operating expenses	(3,618)	(3,427)
Profit from operations	4,318	4,101
Analysed as:		
– adjusted profit from operations	4,984	4,461
– restructuring and integration costs	(311)	(304)
– amortisation of trademarks	(62)	(58)
– impairment of trademarks	(44)	-
– goodwill impairment	(249)	-
– gains on disposal of businesses and trademarks	-	2
	4,318	4,101
Finance income	27	77
Finance costs	(507)	(581)
Net finance costs	(480)	(504)
Share of post-tax results of associates and joint ventures	550	483
Analysed as:		
– adjusted share of post-tax results of associates and joint ventures	622	541
– trademark amortisation and impairments	(1)	(65)
– health plan credit	-	16
– Canadian settlements	(59)	-
– dilution in shareholding	(9)	-
– restructuring costs	(3)	(9)
	550	483
Profit before taxation	4,388	4,080
Taxation on ordinary activities	(1,248)	(1,124)
Profit for the year	3,140	2,956
Attributable to:		
Owners of the parent	2,879	2,713
Non-controlling interests	261	243
	3,140	2,956
Earnings per share		
Basic	145.2p	137.0p
Diluted	144.4p	136.3p

The accompanying notes on pages 21 to 53 form an integral part of this condensed consolidated financial information.

GROUP STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December

	2010 £m	2009 £m
Profit for the year (page 15)	3,140	2,956
Other comprehensive income		
Differences on exchange		
– subsidiaries	502	166
– associates	105	(258)
Differences on exchange reclassified and reported in profit for the year	(3)	-
Cash flow hedges		
– net fair value losses	(106)	(72)
– reclassified and reported in profit for the year	55	67
– reclassified and reported in net assets	3	(1)
Available-for-sale investments		
– net fair value gains	4	3
– reclassified and reported in profit for the year	-	(3)
Net investment hedges		
– net fair value (losses)/gains	(31)	238
– differences on exchange on borrowings	74	12
Retirement benefit schemes		
– net actuarial gains/(losses) in respect of subsidiaries	193	(295)
– surplus recognition and minimum funding obligations in respect of subsidiaries	58	(76)
– actuarial (losses)/gains in respect of associates net of tax	(54)	61
Tax on items recognised directly in other comprehensive income	1	(71)
Total other comprehensive income for the year, net of tax	801	(229)
Total comprehensive income for the year, net of tax	3,941	2,727
Attributable to:		
Owners of the parent	3,664	2,476
Non-controlling interests	277	251
	3,941	2,727

The accompanying notes on pages 21 to 53 form an integral part of this condensed consolidated financial information.

GROUP STATEMENT OF CHANGES IN EQUITY

At 31 December

2010

	Attributable to owners of the parent						
	Share capital £m	Share premium, capital redemption and merger reserves £m	Other reserves £m	Retained earnings £m	Total attributable to owners of parent £m	Non- controlling interests £m	Total equity £m
Balance at 1 January 2010	506	3,907	1,032	2,168	7,613	299	7,912
Total comprehensive income for the year (page 16)			568	3,096	3,664	277	3,941
Employee share options							
– value of employee services				67	67		67
– proceeds from shares issued		3		4	7		7
Dividends and other appropriations							
– ordinary shares				(2,093)	(2,093)		(2,093)
– to non-controlling interests						(234)	(234)
Purchase of own shares							
– held in employee share ownership trusts				(66)	(66)		(66)
Non-controlling interests - acquisitions				(12)	(12)		(12)
Other movements				26	26		26
Balance at 31 December 2010	506	3,910	1,600	3,190	9,206	342	9,548

2009

	Attributable to owners of the parent						
	Share capital £m	Share premium, capital redemption and merger reserves £m	Other reserves £m	Retained earnings £m	Total attributable to owners of parent £m	Non- controlling interests £m	Total equity £m
Balance at 1 January 2009	506	3,905	955	1,578	6,944	271	7,215
Total comprehensive income for the year (page 16)			77	2,399	2,476	251	2,727
Employee share options							
– value of employee services				61	61		61
– proceeds from shares issued		2		5	7		7
Dividends and other appropriations							
– ordinary shares				(1,798)	(1,798)		(1,798)
– to non-controlling interests						(240)	(240)
Purchase of own shares							
– held in employee share ownership trusts				(94)	(94)		(94)
Non-controlling interests - acquisitions						1	1
Non-controlling interests - capital injection						16	16
Other movements				17	17		17
Balance at 31 December 2009	506	3,907	1,032	2,168	7,613	299	7,912

The accompanying notes on pages 21 to 53 form an integral part of the condensed consolidated financial information.

GROUP BALANCE SHEET

At 31 December

	2010 £m	2009 £m
Assets		
Non-current assets		
Intangible assets	12,458	12,232
Property, plant and equipment	3,117	3,010
Investments in associates and joint ventures	2,666	2,521
Retirement benefit assets	122	105
Deferred tax assets	411	350
Trade and other receivables	272	171
Available-for-sale investments	29	26
Derivative financial instruments	128	93
Total non-current assets	19,203	18,508
Current assets		
Inventories	3,608	3,261
Income tax receivable	73	97
Trade and other receivables	2,409	2,344
Available-for-sale investments	58	57
Derivative financial instruments	145	156
Cash and cash equivalents	2,329	2,161
	8,622	8,076
Assets classified as held-for-sale	35	30
Total current assets	8,657	8,106
Total assets	27,860	26,614

The accompanying notes on pages 21 to 53 form an integral part of this condensed consolidated financial information.

GROUP BALANCE SHEET

At 31 December

	2010 £m	2009 £m
Equity		
Capital and reserves		
Share capital	506	506
Share premium, capital redemption and merger reserves	3,910	3,907
Other reserves	1,600	1,032
Retained earnings	3,190	2,168
Owners of the parent	9,206	7,613
after deducting		
– cost of treasury shares	(750)	(772)
Non-controlling interests	342	299
Total equity	9,548	7,912
Liabilities		
Non-current liabilities		
Borrowings	8,916	9,712
Retirement benefit liabilities	770	1,129
Deferred tax liabilities	509	527
Other provisions for liabilities and charges	187	144
Trade and other payables	193	180
Derivative financial instruments	92	94
Total non-current liabilities	10,667	11,786
Current liabilities		
Borrowings	1,334	1,370
Income tax payable	467	364
Other provisions for liabilities and charges	282	312
Trade and other payables	5,335	4,727
Derivative financial instruments	227	127
	7,645	6,900
Liabilities directly associated with assets classified as held-for-sale	-	16
Total current liabilities	7,645	6,916
Total equity and liabilities	27,860	26,614

The financial statements on pages 21 to 53 form an integral part of this condensed consolidated financial information

GROUP CASH FLOW STATEMENT

For the year ended 31 December

	2010 £m	2009 £m
Cash flows from operating activities		
Cash generated from operations (page 35)	5,207	4,645
Dividends received from associates	461	328
Tax paid	(1,178)	(1,095)
Net cash from operating activities	4,490	3,878
Cash flows from investing activities		
Interest received	59	83
Dividends received from investments	2	2
Purchases of property, plant and equipment	(497)	(450)
Proceeds on disposal of property, plant and equipment	61	39
Purchases of intangibles	(87)	(104)
Purchases and proceeds on disposals of investments	(1)	37
Purchase of Bentoel	-	(370)
Purchase of Tekel cigarette assets	-	(12)
Proceeds from ST trademark disposals	-	187
Purchases of other subsidiaries and associates	-	(1)
Proceeds on disposal of subsidiaries	12	-
Net cash from investing activities	(451)	(589)
Cash flows from financing activities		
Interest paid	(578)	(576)
Interest element of finance lease rental payments	(2)	(2)
Capital element of finance lease rental payments	(17)	(35)
Proceeds from issue of shares to owners of the parent	3	2
Proceeds from the exercise of options over own shares held in employee share ownership trusts	4	5
Proceeds from increases in and new borrowings	892	1,447
Movements relating to derivative financial instruments	(179)	(267)
Purchases of own shares held in employee share ownership trusts	(66)	(94)
Purchase of non-controlling interests	(12)	-
Reductions in and repayments of borrowings	(1,582)	(1,853)
Dividends paid to owners of the parent	(2,093)	(1,798)
Dividends paid to non-controlling interests	(234)	(234)
Net cash from financing activities	(3,864)	(3,405)
Net cash flows from operating, investing and financing activities	175	(116)
Differences on exchange	29	(125)
Increase/(decrease) in net cash and cash equivalents in the year	204	(241)
Net cash and cash equivalents at 1 January	1,979	2,220
Net cash and cash equivalents at 31 December	2,183	1,979

The accompanying notes on pages 21 to 53 form an integral part of this condensed consolidated financial information.

ACCOUNTING POLICIES AND BASIS OF PREPARATION

The financial information has been extracted from the Annual Report, including the audited financial statements for the year ended 31 December 2010. This financial information does not constitute statutory accounts within the meaning of Section 434 of the Companies Act 2006.

The Group has prepared its annual consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and implemented in the UK.

These financial statements have been prepared under the historical cost convention, except in respect of certain financial instruments, and on a basis consistent with the IFRS accounting policies as set out in the Annual Report for the year ended 31 December 2009, with the following amendments due to certain changes in IFRS affecting the Group. These changes are effective from 1 January 2010:

- The revised IFRS 3 (Business Combinations) and IAS 27 (Consolidated and Separate Financial Statements) change the accounting for business combinations and transactions with non-controlling interests. These revised standards are only to be applied prospectively and so there is no restatement of transactions prior to the effective date. IFRS 3 Revised has had no impact on the current period. IAS 27 Revised was applied to the acquisition of certain non-controlling interests in the year with the difference between the fair value of the consideration paid and the carrying value of the non-controlling interest recognised directly in equity. Goodwill is no longer recognised on acquisition of non-controlling interests where there is no change in control.
- Also in accordance with IAS 27 Revised, losses in the current year applicable to non-controlling interests, where their share of accumulated losses exceed their interest in the equity of a subsidiary, are no longer allocated to the owners of the parent except to the extent that the Group has a binding obligation to cover the losses.
- Annual Improvements to IFRS (issued in April 2009) introduce a number of minor changes including revised disclosures under IFRS 8. As a result of this amendment, the Group no longer presents a measure of total assets for each reportable segment as information on total assets and liabilities is not reported to the chief operating decision maker.
- In addition, a number of other interpretations and revisions to existing standards have been issued and endorsed which have had no effect on reported profit or equity or on the disclosures in the financial statements.

The preparation of this condensed consolidated financial information requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities at the date of the condensed consolidated financial information. 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 judgment at the date of the financial statements. In the future, actual experience may deviate from these estimates and assumptions, which could affect these financial statements as the original estimates and assumptions are modified, as appropriate, in the period in which the circumstances change.

NON-GAAP MEASURES

In the reporting of financial information, the Group uses certain measures that are not required under IFRS, the generally accepted accounting principles (GAAP) under which the Group reports. The Group believes that these additional measures, which are used internally, are useful to users of the financial information in helping them understand underlying business performance.

The principal non-GAAP measure which the Group uses is adjusted diluted earnings per share, which is reconciled to diluted earnings per share. The adjusting items that mainly drive the adjustments made are separately disclosed as memorandum information on the face of the Income Statement and are used to calculate the additional non-GAAP measures of adjusted profit from operations and adjusted share of post-tax results of associates and joint ventures. All adjustments to profit from operations and diluted earnings per share are explained in this announcement.

The Management Board as the chief operating decision maker, reviews current and prior year segmental income statement information of subsidiaries and associates at constant rates of exchange which provides an approximate guide to performance in the current year had they been translated at last year's rate of exchange. The constant rate comparison provided for reporting segment information is based on a retranslation, at prior year exchange rates, of the current year results of the Group's overseas entities but other than in exceptional circumstances, does not adjust for the normal transactional gains and losses in operations which are generated by movements in exchange rates.

In the presentation of financial information, the Group also uses another measure, organic growth, to analyse underlying business performance. Organic growth is the growth after adjusting for mergers and acquisitions and discontinued activities. Adjustments are made to current and prior year numbers, based on the 2010 Group position.

The Group also prepares an alternative cash flow, which includes a measure of 'free cash flow', to illustrate the cash flows before transactions relating to borrowings, and provides gross turnover as an additional disclosure to indicate the impact of duty, excise and other taxes.

Due to the secondary listing of the ordinary shares of British American Tobacco p.l.c. on the main board of the JSE Limited (JSE) in South Africa, the Group is required to present headline earnings per share and diluted headline earnings per share, as alternative measures of earnings per share, calculated in accordance with Circular 8/2007 'Headline Earnings' issued by the South African Institute of Chartered Accountants. These are shown on pages 31 and 32.

FOREIGN CURRENCIES

The income and cash flow statements of overseas subsidiaries and associates have been translated at the average rates for the respective periods. Assets and liabilities have been translated at the relevant period end rates.

The principal exchange rates used were as follows:

	Average		Closing	
	2010	2009	2010	2009
US dollar	1.546	1.566	1.566	1.615
Canadian dollar	1.592	1.779	1.556	1.693
Euro	1.166	1.123	1.167	1.126
South African rand	11.300	13.091	10.358	11.891
Brazilian real	2.719	3.108	2.599	2.815
Australian dollar	1.682	1.990	1.527	1.796
Russian rouble	46.945	49.535	47.795	48.952

HALF-YEARLY ANALYSES OF PROFIT

The figures shown below have been produced using average rates of exchange on a half-yearly basis since the beginning of the year. Thus the discrete half-year to 30 June has not been restated for subsequent movements in foreign exchange rates during the year, which are reflected in the results for the subsequent half-year to 31 December.

	6 months to		Year to
	30.6.10	31.12.10	31.12.10
	£m	£m	£m
Revenue	7,298	7,585	14,883
Adjusted profit from operations			
Asia-Pacific	651	681	1,332
Americas	694	688	1,382
Western Europe	548	506	1,054
Eastern Europe	124	234	358
Africa and Middle East	443	415	858
	<u>2,460</u>	<u>2,524</u>	<u>4,984</u>
Restructuring and integration costs	(158)	(153)	(311)
Amortisation of trademarks	(31)	(31)	(62)
Impairment of trademarks	-	(44)	(44)
Goodwill impairment	-	(249)	(249)
Profit from operations	2,271	2,047	4,318
Net finance costs	(231)	(249)	(480)
Share of post-tax results of associates and joint ventures	239	311	550
Profit before taxation	<u>2,279</u>	<u>2,109</u>	<u>4,388</u>
Taxation on ordinary activities	(624)	(624)	(1,248)
Profit for the period	1,655	1,485	3,140
Earnings per share			
Basic	<u>76.9p</u>	<u>68.3p</u>	<u>145.2p</u>
Diluted	<u>76.5p</u>	<u>67.9p</u>	<u>144.4p</u>
Adjusted diluted	<u>87.1p</u>	<u>88.6p</u>	<u>175.7p</u>

	6 months to		Year to
	30.6.09	31.12.09	31.12.09
	£m	£m	£m
Revenue	6,780	7,428	14,208
Adjusted profit from operations			
Asia-Pacific	557	591	1,148
Americas	579	607	1,186
Western Europe	509	485	994
Eastern Europe	183	226	409
Africa and Middle East	336	388	724
	<u>2,164</u>	<u>2,297</u>	<u>4,461</u>
Restructuring and integration costs	(29)	(275)	(304)
Amortisation of trademarks	(26)	(32)	(58)
Gains on disposal of businesses and trademarks	2	-	2
Profit from operations	<u>2,111</u>	<u>1,990</u>	<u>4,101</u>
Net finance costs	(219)	(285)	(504)
Share of post-tax results of associates and joint ventures	231	252	483
Profit before taxation	<u>2,123</u>	<u>1,957</u>	<u>4,080</u>
Taxation on ordinary activities	(534)	(590)	(1,124)
Profit for the period	1,589	1,367	2,956
Earnings per share			
Basic	<u>73.2p</u>	<u>63.8p</u>	<u>137.0p</u>
Diluted	<u>72.8p</u>	<u>63.5p</u>	<u>136.3p</u>
Adjusted diluted	<u>77.3p</u>	<u>75.7p</u>	<u>153.0p</u>

SEGMENTAL ANALYSES OF REVENUE AND PROFIT

The five geographic regions are the reportable segments for the Group as they form the focus of the Group's internal reporting systems and are the basis used by the chief operating decision maker, identified as the Management Board, for assessing performance and allocating resources.

The Management Board as the chief operating and decision maker, reviews current and prior year segmental adjusted revenue, profit from operations of subsidiaries and adjusted post-tax results of associates and joint ventures at constant rates of exchange. As a result, the 2010 segmental results are translated using the 2009 average rates of exchange. The 2009 comparative figures are also stated at the 2009 actual average rates of exchange.

The analyses of **revenue** for the 12 months to 31 December 2010 and 31 December 2009, based on location of sales, are as follows:

	2010			2009
	Revenue Constant rates £m	Translation exchange £m	Revenue Current rates £m	Revenue £m
Asia-Pacific	3,448	311	3,759	3,270
Americas	3,202	296	3,498	3,156
Western Europe	3,486	(67)	3,419	3,884
Eastern Europe	1,726	(40)	1,686	1,628
Africa and Middle East	2,401	120	2,521	2,270
Total	<u>14,263</u>	<u>620</u>	<u>14,883</u>	<u>14,208</u>

Segmental analyses of revenue and profit cont...

The analyses of profit from operations and the Group's share of the **post-tax results of associates and joint ventures** for the year ended 31 December 2010, reconciled to profit before tax, are as follows:

	2010				
	Adjusted* segment result Constant rates £m	Translation exchange** £m	Adjusted* segment result Current rates £m	Adjusting items £m	Segment result Current rates £m
Asia-Pacific	1,195	137	1,332	(56)	1,276
Americas	1,248	134	1,382	(36)	1,346
Western Europe	1,081	(27)	1,054	(236)	818
Eastern Europe	428	(70)	358	-	358
Africa and Middle East	793	65	858	(338)	520
Profit from operations	4,745	239	4,984	(666)	4,318
Net finance costs					(480)
Asia-Pacific	194	14	208	(9)	199
Americas	407	5	412	(63)	349
Africa and Middle East	2	-	2	-	2
Share of post-tax results of associates and joint ventures	603	19	622	(72)	550
Profit before taxation					4,388

*The adjustments to profit from operations and the Group's share of the post-tax results of associates and joint ventures are explained on pages 28 and 30, respectively.

**Translation exchange in Eastern Europe includes exceptional transitional exchange losses in respect of the Group's subsidiary in Uzbekistan.

Segmental analyses of revenue and profit cont...

The analyses of profit from operations and the Group's share of the **post-tax results of associates and joint ventures** for the year ended 31 December 2009 are as follows:

	2009		
	Adjusted* segment result £m	Adjusting items £m	Segment result £m
Asia-Pacific	1,148	(59)	1,089
Americas	1,186	(51)	1,135
Western Europe	994	(188)	806
Eastern Europe	409	(16)	393
Africa and Middle East	724	(46)	678
Profit from operations	<u>4,461</u>	<u>(360)</u>	<u>4,101</u>
Net finance costs			<u>(504)</u>
Asia-Pacific	148	-	148
Americas	391	(58)	333
Africa and Middle East	<u>2</u>	<u>-</u>	<u>2</u>
Share of post-tax results of associates and joint ventures	<u>541</u>	<u>(58)</u>	<u>483</u>
Profit before taxation			<u>4,080</u>

*The adjustments to profit from operations and the Group's share of the post-tax results of associates and joint ventures are explained on pages 28 and 30, respectively.

REBASED REGIONAL ANALYSIS

As part of the plans to reduce complexity and drive efficiency in our management structures and achieve a better balance in the scale of our regions, it was decided to reduce the management structure from five regions to four regions from 1 January 2011. Markets which currently comprise the Eastern European region will be merged into the Africa and Middle East region and the Western Europe region. Russia, Ukraine, Moldova, Belarus, Caucasus and Central Asia will form part of the new Eastern Europe, Middle East and Africa region (EEMEA) while Romania, Bulgaria, Serbia, Montenegro, Albania and Kosovo will become part of the Western Europe Region. The following analysis of revenue and adjusted profit from operations is being provided as additional information and will be the comparative information used by the Management Board in 2011 to evaluate segment performance and allocate resources.

	2010 Revenue £m
Asia-Pacific	3,759
Americas	3,498
Western Europe	3,695
Eastern Europe, Middle East and Africa	3,931
Total	<u>14,883</u>

	2010		
	Adjusted* segment result £m	Adjusting items £m	Segment result £m
Asia-Pacific	1,332	(56)	1,276
Americas	1,382	(36)	1,346
Western Europe	1,103	(236)	867
Eastern Europe, Middle East and Africa	<u>1,167</u>	<u>(338)</u>	<u>829</u>
Profit from operations	<u>4,984</u>	<u>(666)</u>	<u>4,318</u>
Net finance costs			(480)
Asia-Pacific	208	(9)	199
Americas	412	(63)	349
Western Europe	-	-	-
Eastern Europe, Middle East and Africa	<u>2</u>	<u>-</u>	<u>2</u>
Share of post-tax results of associates and joint ventures	<u>622</u>	<u>(72)</u>	<u>550</u>
Profit before taxation			<u>4,388</u>

*The adjustments to profit from operations and the Group's share of the post-tax results of associates and joint ventures are explained on pages 28 and 30, respectively.

ADJUSTING ITEMS INCLUDED IN PROFIT FROM OPERATIONS

Adjusting items are significant items in the profit from operations which individually or, if of a similar type, in aggregate, are relevant to an understanding of the Group's underlying financial performance. These items are separately disclosed as memorandum information on the face of the income statement and in the segmental analyses, and are used to derive the Group's principal non-GAAP measure which is adjusted diluted earnings per share.

(a) Restructuring and integration costs

Restructuring costs reflect the costs incurred as a result of initiatives to improve the effectiveness and the efficiency of the Group as a globally integrated enterprise. These initiatives include a review of the Group's manufacturing operations, overheads and indirect costs, organisational structure and systems and software used. The costs of these initiatives together with the costs of integrating acquired businesses into existing operations are included in profit from operations under the following headings:

	2010 £m	2009 £m
Employee benefit costs	163	143
Impairment of tangible and intangible assets	100	107
Other operating expenses	68	61
Other operating income	(20)	(7)
Total	<u>311</u>	<u>304</u>

Restructuring and integration costs in 2010 principally relate to: the continuation of factory closure and downsizing activities in Denmark and Australia respectively; the closure of the Jawornik factory in Poland, the Tire factory in Turkey and the Lecce factory in Italy; a voluntary separation scheme and closure of the printing unit in Argentina and the continued integration of Bentoel into existing operations; as well as other restructuring initiatives directly related to improving the efficiency and effectiveness of the Group as a globally integrated enterprise. These include the combining of the Group's businesses in Belgium, Luxembourg and the Netherlands and charges for bringing employee benefits costs in the Group's subsidiary in Canada in line with the Group's global practices. In addition, the Group has recognised impairment charges as a result of the continued review of its software assets in light of the development of global software solutions.

Restructuring and integration costs in 2010 also include a payment of US\$21 million to Reynolds American relating to the early termination and settlement of all disputes at issue in respect of the Contract Manufacturing Agreement dated 30 July 2004, as explained on page 30.

Restructuring and integration costs in 2009 principally relate to: costs in respect of the planned closure of the Soeborg factory in Denmark; the planned downsizing of the manufacturing plant in Australia; the continued integration of ST, Tekel and Bentoel with existing operations; as well as other restructuring initiatives, directly related to improving the efficiency and effectiveness of the Group as a globally integrated enterprise. The costs for these other initiatives include redundancies, principally in respect of restructuring activities in the Group's subsidiary in Canada, and impairment charges for certain software assets where the development of global software solutions has resulted in these assets having minimal or limited future economic benefits.

Other operating income in 2010 includes gains from sales of surplus land and buildings in Turkey and Croatia as well as the release of deferred income from a disposal in 2007. In 2009, other operating income also includes gains on property disposals and the release of deferred income from a disposal in 2007.

(b) Amortisation of trademarks

The acquisitions of Bentoel, Tekel and ST resulted in the capitalisation of trademarks which are amortised over their expected useful lives, which do not exceed 20 years. The amortisation charge of £62 million (2009: £58 million) is included in depreciation, amortisation and impairment costs in profit from operations.

Adjusting items included in profit from operations cont...

(c) Impairment of goodwill and trademarks

Goodwill and trademarks recognised as a result of the Tekel acquisition in 2008 have been impaired by £249 million and £44 million respectively. Turkey remains an important strategic market for the Group. Although cost saving initiatives in the acquisition plan have been delivered successfully, the impairment charge arises from intense pricing competition in 2010 following unforeseen and significant excise increases in Turkey during 2009 and further increases effective from January 2010, which resulted in the growth of illicit trade and a loss of volumes and market share.

(d) Gains on disposal of businesses and trademarks

The acquisition of the cigarette and snus businesses of Skandinavisk Tobakskompagni (ST) in 2008 was subject to regulatory approval which was received on the condition that the Group divest a small number of local trademarks, primarily in Norway. The disposal of the trademarks was dealt with in two packages, with the first package sold and completed in February 2009. In March 2009, contracts were exchanged in respect of the second package with completion in May 2009. The total proceeds from the two packages resulted in a gain of £2 million which is included in other operating income in profit from operations for the year ended 31 December 2009.

OTHER CHANGES IN THE GROUP

(a) Lyfra NV

On 7 April 2010, the Group announced that it had agreed to sell its Belgium distribution business, Lyfra NV, to Landewyck Group S.a.r.l. The transaction was completed on 25 June 2010 for a consideration of €16 million and resulted in a gain of £5 million. Lyfra contributed £215 million to revenue (£473 million for the year to 31 December 2009) and £1 million to profit from operations to 25 June 2010 (£1 million for the year to 31 December 2009) in the Western Europe Region.

(b) PT Bentoel Internasional Investama Tbk

On 17 June 2009, the Group acquired an 85 per cent stake in Indonesia's fourth largest cigarette maker PT Bentoel Internasional Investama Tbk (Bentoel). A public tender offer for the remaining shares was completed on 26 August 2009, resulting in the acquisition of a further 14 per cent share in the company, bringing the total shareholding in the Bentoel Group to 99.7 per cent. This transaction resulted in goodwill of £188 million.

On 20 October 2009, it was announced that Bentoel and BAT Indonesia would enter into a merger plan whereby BAT Indonesia would merge into Bentoel. This was completed with an effective date of 1 January 2010. The Bentoel name has been retained and the company remains listed on the Indonesian Stock Exchange. As part of the merger, certain non-controlling interests were acquired for £3 million and the total shareholding in the merged group is 99.14%.

NET FINANCE COSTS

Net finance costs comprise:

	2010 £m		2009 £m
Finance costs	507		581
Finance income	(27)		(77)
	<u>480</u>		<u>504</u>
Comprising:			
Interest payable	583		602
Interest and dividend income	(60)		(85)
Fair value changes - derivatives	209	4	
Exchange differences	<u>(252)</u>	<u>(17)</u>	<u>(13)</u>
	<u>480</u>		<u>504</u>

Net finance costs cont...

Net finance costs at £480 million were £24 million lower than last year, principally reflecting the net impact of interest related changes in the fair value of derivatives and reduced borrowings.

The net £43 million gain (2009: £13 million) of fair value changes and exchange differences reflects a £nil position (2009: loss of £9 million) from the net impact of exchange rate movements and a gain of £43 million (2009: gain of £22 million) principally due to interest related changes in the fair value of derivatives.

The Group targets interest cover, as calculated under its key central banking facilities, of greater than five. For 2010 it was 11.2 times (2009: 9.9 times) with the higher cover reflecting increased profit from operations, lower net debt and the contribution of Bentoel for the whole of 2010, offset by an increase in finance costs as a result of the acquisition of Bentoel.

ASSOCIATES AND JOINT VENTURES

The Group's share of the post-tax results of associates and joint ventures increased by £67 million to £550 million after net adjusting charges of £72 million (2009: £58 million) and after tax of £322 million (2009: £291 million). Excluding the adjusting items, the Group's share of the post-tax results increased by 15 per cent to £622 million (2009: £541 million). The following adjusting items are excluded from the calculation of adjusted diluted earnings per share (page 32).

In the year ended 31 December 2010, Reynolds American recognised a trademark impairment charge of US\$6 million as well as trademark amortisation of US\$4 million. The Group's share of these charges amounted to £1 million (net of tax).

In the year ended 31 December 2010, a subsidiary of Reynolds American, R.J. Reynolds Tobacco Company Inc. (RJRTC), entered into a comprehensive settlement agreement with the Canadian federal, provincial and territorial governments to resolve all the governments' civil claims related to smuggling in Canada during the 1980s and 1990s. As part of the civil settlement, RJRTC agreed to pay the governments CA\$325 million. In a separate matter, a subsidiary of R.J. Reynolds Tobacco Holdings Inc., Northern Brands International Inc., entered into a plea agreement with the Ministry of the Attorney General of Ontario. As a result of its plea to one count of conspiracy to aid others in the sale and possession of contraband cigarettes in the early 1990s, Northern Brands paid a fine of CA\$75 million. The Group's share of these charges amounted to £59 million (net of tax).

Reynolds American also recognised restructuring charges in the year ended 31 December 2010 from the closure of one factory in August 2010 and the planned closure of another in mid 2011. As a result of these actions, Reynolds American has recorded charges mostly relating to asset impairment and to a lesser extent, severance costs. The Group's share of these charges amounted to £6 million (net of tax).

In the year ended 31 December 2010, RJRTC received a payment of US\$21million as a result of the agreement to terminate early the Contract Manufacturing Agreement dated 30 July 2004 between RJRTC and BATUS Japan Inc., a wholly owned Group subsidiary, and settle all disputes at issue between the parties, as explained on page 65. The Group's share of this receipt amounted to £3 million (net of tax) and is treated as an adjusting item. The receipt (net of tax) is presented as part of restructuring costs in the post-tax results of associates and joint ventures in the Group income statement.

During the year, the Group's interest in ITC decreased from 31.92 per cent to 31.43 per cent as a result of ITC issuing ordinary shares under the Company's Employee Stock Option Scheme. This dilution in the Group's share of ITC results in a charge of £9 million, which under IAS 28 Revised (Investments in associates) is treated as a potential disposal and included in the income statement.

Associates and joint ventures cont...

In the year ended 31 December 2009, Reynolds American recognised a trademark impairment charge of US\$394 million, triggered by the increase in federal excise taxes on tobacco products and changes in pricing. It also has an amortisation charge of US\$5 million in respect of brands. The Group's share of this charge amounted to £65 million (net of tax).

During 2009, Reynolds American reviewed its post-retirement medical plans, resulting in a past service credit which is amortised under US GAAP, but under IFRS it must be recognised in full in the income statement in 2009. The Group's share of this credit amounted to £16 million (net of tax).

Reynolds American also recognised a charge of US\$56 million in 2009 in connection with severance and related costs of around 400 employees in order to better align staffing levels with business requirements and enable Reynolds American's manufacturing operations to phase in new productivity programs. The Group's share of this charge amounted to £9 million (net of tax).

TAXATION

	2010 £m	2009 £m
UK		
- adjustment in respect of prior periods	(16)	16
Overseas		
- overseas tax	1,270	1,104
- adjustment in respect of prior periods	24	43
Current tax	1,278	1,163
Deferred tax	(30)	(39)
	<u>1,248</u>	<u>1,124</u>

The tax rates in the income statement of 28.4 per cent in 2010 and 27.5 per cent in 2009 are affected by the inclusion of the share of associates' post-tax profit in the Group's pre-tax results and by adjusting items. The underlying tax rate for subsidiaries reflected in the adjusted earnings per share below was 30.2 per cent in 2010 and 30.3 per cent in 2009.

EARNINGS PER SHARE

	2010 pence	2009 pence
Earnings per share		
- basic	145.2	137.0
- diluted	144.4	136.3
Adjusted earnings per share		
- basic	176.7	153.8
- diluted	175.7	153.0
Headline earnings per share		
- basic	160.9	144.1
- diluted	160.0	143.3

Basic earnings per share are based on the profit for the year attributable to ordinary shareholders and the weighted average number of ordinary shares in issue during the year (excluding treasury shares).

Earnings per share cont...

For the calculation of the diluted earnings per share, the weighted average number of shares reflects the potential dilutive effect of employee share schemes.

The presentation of headline earnings per share, as an alternative measure of earnings per share, is mandated under the JSE Listing Requirements. It is calculated in accordance with Circular 3/2009 'Headline Earnings', as issued by the South African Institute of Chartered Accountants.

Earnings have been affected by a number of adjusting items which impact profit from operations (see page 28) and share of post-tax results of associates and joint ventures (see page 30). It was also affected by the write-off of deferred tax assets of £35 million in respect of unutilised losses in Turkey, which has also been treated as an adjusting item. In order to illustrate the impact of these items, the adjusted diluted earnings per share are shown below:

	Adjusted diluted earnings per share	
	2010	2009
	pence	pence
Unadjusted earnings per share	144.4	136.3
Effect of restructuring and integration costs	11.8	11.7
Effect of impairment of goodwill and trademarks	11.8	-
Effect of deferred tax asset written off	1.8	-
Effect of amortisation of trademarks	2.3	2.1
Effect of associates' adjusting items	3.6	2.9
Adjusted diluted earnings per share	<u>175.7</u>	<u>153.0</u>

Similar types of adjustments would apply to basic earnings per share.

The earnings per share are based on:

	2010		2009	
	Earnings	Shares	Earnings	Shares
	£m	£m	£m	£m
Earnings per share				
- basic	2,879	1,983	2,713	1,980
- diluted	2,879	1,994	2,713	1,991
Adjusted earnings per share				
- basic	3,504	1,983	3,046	1,980
- diluted	3,504	1,994	3,046	1,991
Headline earnings per share				
- basic	3,191	1,983	2,853	1,980
- diluted	3,191	1,994	2,853	1,991

Headline earnings per share are calculated by taking the following adjustments into account:

	Diluted headline earnings per share	
	2010	2009
	pence	pence
Unadjusted earnings per share	144.4	136.3
Effect of impairment of intangibles and property, plant and equipment	15.6	4.3
Effect of gains on disposal of property, plant and equipment	-	(0.2)
Effect of gains on disposal of non-current assets held-for-sale	(0.7)	-
Effect of gains on disposal of businesses and trademarks	(0.2)	(0.2)
Effect of gains reclassified from the available-for-sale reserve	-	(0.2)
Effect of share of associates' trademark and other asset impairments	0.4	3.3
Effect of dilution in shareholding in associate	0.5	-
Headline earnings per share	<u>160.0</u>	<u>143.3</u>

CASH FLOW AND NET DEBT MOVEMENTS

a) Alternative cash flow

The IFRS cash flow statement on page 20 includes all transactions affecting cash and cash equivalents, including financing. The alternative cash flow statement below is presented to illustrate the cash flows before transactions relating to borrowings.

	2010 £m	2009 £m
Adjusted profit from operations before adjusting items (page 15)	4,984	4,461
Depreciation, amortisation and impairment	442	446
Other non cash items in operating profit	59	25
Profit from operations before depreciation and impairment	5,485	4,932
Increase in working capital	(61)	(100)
Net capital expenditure	(523)	(515)
Gross capital expenditure	(584)	(554)
Sale of fixed assets	61	39
Operating cash flow	4,901	4,317
Net interest paid	(491)	(499)
Tax paid	(1,178)	(1,095)
Dividends paid to non-controlling interests	(234)	(234)
Restructuring costs	(219)	(187)
Dividends from associates	461	328
Free cash flow	3,240	2,630
Dividends paid to shareholders	(2,093)	(1,798)
Net investment activities	-	(196)
Purchases of subsidiaries and non-controlling interests	(12)	(383)
Disposal of subsidiaries and trademarks	12	187
Net flow from share schemes and other	(77)	(203)
Net cash flow	1,070	433
External movements on net debt		
Exchange rate effects*	(41)	672
Net debt disposed/(acquired)	11	(84)
Change in accrued interest and other	(39)	28
Change in net debt	1,001	1,049
Opening net debt	(8,842)	(9,891)
Closing net debt	(7,841)	(8,842)

* Including movements in respect of debt related derivatives.

Free cash flow is the Group's cash flow before dividends and investing activities. Operating cash flow increased by £584 million or 14 per cent to £4,901 million, reflecting growth in underlying operating performance. Taking into account outflows relating to taxation, which were £83 million higher than last year due to higher taxable profits, an increase in restructuring costs due to the timing of payments and an increase in restructuring activities, as well as an increase in inflows relating to dividends received from associates, the Group's free cash flow was £610 million or 23 per cent higher at £3,240 million.

The ratio of free cash flow per share to adjusted diluted earnings per share was 92 per cent (2009: 86 per cent), with free cash flow per share increasing by 23 per cent (2009: increasing by 2 per cent).

Cash flow and net debt movements cont...

Below free cash flow, the principal cash outflows for 2010 comprise the payment of the prior year final dividend and the 2010 interim dividend. Also reflected below free cash flow are cash flows in respect of investing activities. Proceeds on disposal of subsidiaries of £12 million which arose from the sale of the Group's Belgian distribution business, Lyfra NV, as explained on page 29, have been offset by a cash outflow of £12 million arising from the acquisition of non-controlling interests in Bentoel and subsidiaries in the Eastern Europe Region. The year ended 31 December 2009 included a net outflow of £382 million in respect of the purchase of Bentoel and Tekel, net proceeds of £185 million from the ST trademark disposals and £2 million refunded from the original purchase consideration paid in 2008, as explained on page 35. The other net flows principally relate to the impact of the level of shares purchased by the employee share ownership trusts and outflows in respect of certain derivative financial instruments.

The above flows resulted in net cash inflows of £1,070 million (2009: £433 million inflow). After taking account of exchange rate movements, net debt disposed, and the change in accrued interest and other, total net debt was £7,841 million at 31 December 2010, down £1,001 million from £8,842 million on 31 December 2009.

b) Net debt/financing

The Group defines net debt as borrowings including related derivatives, less cash and cash equivalents and current available-for-sale investments. The maturity profile of net debt is as follows:

	2010 £m	2009 £m
Net debt due within one year:		
Borrowings	(1,334)	(1,370)
Related derivatives	(29)	33
Cash and cash equivalents	2,329	2,161
Current available-for-sale investments	58	57
	<u>1,024</u>	<u>881</u>
Net debt due beyond one year:		
Borrowings	(8,916)	(9,712)
Related derivatives	51	(11)
	<u>(8,865)</u>	<u>(9,723)</u>
Total net debt	<u>(7,841)</u>	<u>(8,842)</u>

The Group remains confident about its ability to access successfully the debt capital markets and reviews its options on a continuing basis.

Cash flow and net debt movements cont...

c) IFRS Cash generated from operations

The cash generated from operating activities in the IFRS cash flows on page 20 include the following items:

	2010	2009
	£m	£m
Profit from operations	4,318	4,101
Adjustments for:		
Amortisation and impairment of trademarks	106	58
Amortisation and impairment of other intangible assets	322	120
Gains on disposal of businesses and trademarks	(5)	(2)
Depreciation and impairment of property, plant and equipment	469	433
Increase in inventories	(280)	(125)
(Increase) / decrease in trade and other receivables	(127)	30
Increase in trade and other payables	497	174
Decrease in net retirement benefit liabilities	(153)	(127)
Increase / (decrease) in provisions for liabilities and charges	17	(38)
Other non-cash items	43	21
Cash generated from operations	<u>5,207</u>	<u>4,645</u>

d) IFRS Investing and financing activities

The investing and financing activities in the IFRS cash flows on page 20 include the following items:

The purchases and disposals of investments (which comprise available-for-sale investments and loans and receivables) comprises a net cash outflow in respect of current investments of £1 million (2009: £37 million inflow).

In 2009, the net cash outflow of £370 million on the purchase of Bentoel reflects the settlement of the purchase consideration for an initial 85 per cent stake followed by the acquisition of a further 14 per cent from non-controlling interests, together with related acquisition costs and the acquired cash and cash equivalents and overdrafts.

The £12 million outflow in 2009 in respect of the acquisition of Tekel cigarette assets reflected the final payment made at the conclusion of the acquisition.

The cash outflow in 2009 reflected proceeds of £188 million from the disposal of a small number of ST trademarks in Norway, the payment of the related disposal costs of £3 million and a £2 million refund of the original purchase price.

In 2009, the £1 million outflow from purchases of other subsidiaries and associates principally arises from equity investments in associate companies.

The proceeds on disposal of subsidiaries in 2010 reflects the consideration received, less cash and cash equivalents disposed of, from the sale of the Group's Belgian distribution business, Lyfra NV, as explained on page 29.

Cash flow and net debt movements cont...

The cash outflow of £12 million in 2010 for the purchases of non-controlling interests arises from the acquisition of non-controlling interests from shareholders who did not want to participate in the merger of Bentoel and BAT Indonesia, as well as non-controlling interests acquired in subsidiaries in the Eastern Europe region.

The movement relating to derivative financial instruments is in respect of derivatives taken out to hedge cash and cash equivalents and external borrowings, derivatives taken out to hedge inter company loans and derivatives treated as net investment hedges. Derivatives taken out as cash flow hedges in respect of financing activities are also included in the movement relating to derivative financial instruments, while other such derivatives in respect of operating and investing activities are reflected along with the underlying transactions.

e) IFRS net cash and cash equivalents

The net cash and cash equivalents in the IFRS cash flows on page 20 comprise:

	2010 £m	2009 £m
Cash and cash equivalents per balance sheet	2,329	2,161
Accrued interest	(1)	(1)
Overdrafts	(145)	(181)
Net cash and cash equivalents	<u>2,183</u>	<u>1,979</u>

f) Liquidity

The Central Treasury Department is responsible for managing, within an overall policy framework, the Group's exposure to funding and liquidity, interest rate, foreign exchange and counterparty risk arising from the Group's underlying operations.

The Group has a target, average centrally managed debt maturity, of at least 5 years with no more than 20 per cent of centrally managed debt maturing in a single rolling year. As at 31 December 2010, the average centrally managed debt maturity was 7.4 years (2009: 6.6 years) and the highest proportion of centrally managed debt maturing in a single rolling year was 12.5 per cent (2009: 18.4 per cent).

In May 2010, the Group repaid a €525 million bond. The repayment was financed from debt issued in November 2009.

On 25 June 2010, the terms of €470 million of the €1 billion bond maturing in 2011 were modified by extending the maturity to 2020; at the same time, the Group issued an additional €130 million bond with a maturity of 2020. In addition, €413 million of the Group's €750 million bond maturing in 2012 was purchased and cancelled. At the same time, the Group issued a new £275 million bond with a maturity of 2040.

During the year, the Group's subsidiary in Brazil received proceeds of £410 million (2009: £293 million) from short-term borrowings in respect of advance payments on leaf export contracts and repaid £297 million (2009: £241 million) in the year.

It is Group policy that short-term sources of funds (including drawings under the £1 billion euro commercial paper (ECP) programme) are backed by undrawn committed lines of credit and cash. The ECP programme was undrawn at 31 December 2010 whereas, at 31 December 2009, £187 million of ECP was outstanding.

In December 2010, the Group negotiated a new central banking facility of £2 billion with a final maturity date of December 2015. The facility is provided by 22 banks. The existing central banking facility of £1.75 billion, with a final maturity date of March 2012 was cancelled at the same time. The facilities were undrawn at the end of both years.

Cash flow and net debt movements cont...

In February 2009, the Group repaid a €900 million bond which was financed by bond issues during 2008 and cash generated from operations.

In May 2009, the Group repaid Malaysian ringgit (MYR) 100 million which was refinanced in August 2009 by a new MYR250 million bond, due 2014. The additional proceeds were used to repay MYR150 million in November 2009. During June 2009, the Group also issued a new £250 million bond maturing in June 2022.

In September 2009 and October 2009, the Group repaid its €359 million and €759 million credit facilities used to finance the acquisition of Tekel in 2008. The €759 million was refinanced by a new €700 million term loan facility with a maturity date of 31 October 2012 with an option to extend it to October 2013, at the discretion of the banking participants in the syndicated facility. In December 2010, the €700 million term loan facility was partly repaid and the remaining term loan facility of €450 million was extended to October 2013 with the Group able to negotiate improved pricing.

In November 2009, the terms of €481 million of the €1 billion bond maturing in 2013 were modified by extending the maturity to 2021. At the same time, the Group issued an additional €169 million bond with a maturity of 2021. In addition, £199 million of the £350 million bond maturing in 2013 was purchased and cancelled; at the same time the Group issued a new £500 million bond with a maturity of 2034.

RETIREMENT BENEFIT SCHEMES

The Group's subsidiaries operate around 180 retirement benefit arrangements worldwide. The majority of the scheme members belong to defined benefit schemes, most of which are funded externally and many of which are closed to new entrants. The Group also operates a number of defined contribution schemes.

The present total value of funded scheme liabilities was £5,365 million (2009: £5,250 million), while unfunded scheme liabilities amounted to £337 million (2009: £282 million). The scheme assets increased from £4,634 million in 2009 to £5,134 million in 2010.

After accounting for minimum funding obligations of £29 million (2009: £75 million), excluding unrecognised scheme surpluses of £51 million (2009: £52 million) and £1 million for unrecognised past service cost in 2009, the overall net liability for all pension schemes and healthcare schemes amounted to £648 million at the end of 2010, down from £1,024 million at the end of 2009.

Contributions to the defined benefit schemes are determined after consultation with the respective trustees and actuaries of the individual externally funded schemes, taking into account the regulatory requirements.

LITIGATION: FRANKED INVESTMENT INCOME GROUP LITIGATION ORDER

British American Tobacco is the principal test claimant in an action in the United Kingdom against HM Revenue and Customs in the Franked Investment Income Group Litigation Order (FII GLO). There are 26 corporate groups in the FII GLO. The case concerns the treatment for UK corporate tax purposes of profits earned overseas and distributed to the UK. The claim was filed in 2003 and the case was heard in the European Court of Justice (ECJ) in 2005 and a decision of the ECJ received in December 2006. In July 2008, the case reverted to a trial in the UK High Court for the UK Court to determine how the principles of the ECJ decision should be applied in a UK context.

The High Court judgment in November 2008 concluded, amongst many other things, that dividends received from EU subsidiaries should be, and should have been, exempt from UK taxation. It also concluded that certain dividends received before 5 April 1999 from the EU and, in some limited circumstances after 1993 from outside the EU, should have been treated as franked investment income with the consequence that advance corporation tax need not have been paid. Claims for the repayment of UK tax incurred where the dividends were from the EU can be made back to 1973. The tentative conclusion reached by the High Court would, if upheld, produce an estimated receivable of about £1.2 billion for British American Tobacco.

Litigation: Franked investment income Group litigation order cont...

The case was heard by the Court of Appeal in October 2009 and the judgment handed down on 23 February 2010. The Court of Appeal has determined that various questions should be referred back to the ECJ for further clarification. In addition, the Court determined that the claim should be restricted to six years and not cover claims dating back to 1973. This time restriction would, if upheld, reduce the value of the claim to between zero and £10 million. Based on advice received, the Company believes it has realistic prospects of success on further appeal. The Company sought leave to appeal from the Supreme Court in the UK and the Supreme Court has agreed to hear the appeal on time limits although no date has yet been set for the hearing. Several questions are to be referred back to the ECJ for further clarification.

No potential receipt has been recognised in the current year or the prior year, in the results of the Group, due to the uncertainty of the amounts and eventual outcome.

CONTINGENT LIABILITIES AND FINANCIAL COMMITMENTS

The Group is subject to contingencies pursuant to requirements that it complies with relevant laws, regulations and standards. Failure to comply could result in restrictions in operations, damages, fines, increased tax, increased cost of compliance, interest charges, reputational damage, or other sanctions. These matters are inherently difficult to quantify.

In cases where the Group has an obligation as a result of a past event existing at the balance sheet date, it is probable that an outflow of economic resources will be required to settle the obligation and the amount of the obligation can be reliably estimated, a provision would be recognised based on best estimates and management judgment.

There are, however, contingent liabilities in respect of litigation, taxes in some countries and guarantees for which no provisions were made.

The Group has exposures in respect of the payment or recovery of a number of taxes. The Group is and has been subject to a number of tax audits covering amongst others, excise tax, value added taxes, sales taxes, corporate taxes, withholding taxes and payroll taxes.

The estimated costs of known tax obligations have been provided in these accounts in accordance with the Group's accounting policies. In some countries, tax law requires that full or part payment of disputed tax assessments be made pending resolution of the dispute. To the extent that such payments exceed the estimated obligation, they would not be recognised as an expense. In some cases disputes are proceeding to litigation.

While the amounts that may be payable or receivable could be material to the results or cash flows of the Group in the period in which they are recognised, the Board does not expect these amounts to have a material effect on the Group's financial condition.

Product liability litigation

Group companies, notably Brown & Williamson Holdings, Inc. (formerly Brown & Williamson Tobacco Corporation) (B&W) as well as other leading cigarette manufacturers, are defendants, principally in the United States, in a number of product liability cases. In a number of these cases, the amounts of compensatory and punitive damages sought are significant.

Indemnity

In 2004, B&W completed the combination of the assets, liabilities and operations of its US tobacco business with R.J. Reynolds Tobacco Company (RJRT), a wholly-owned subsidiary of R.J. Reynolds Tobacco Holdings, Inc., pursuant to which Reynolds American Inc. was formed (the Business Combination). As part of the Business Combination, B&W contributed to RJRT all of the assets and liabilities of its US cigarette and tobacco business, subject to specified exceptions, in exchange for a 42 per cent equity ownership interest in Reynolds American Inc. As a result of the Business Combination:

- B&W discontinued the active conduct of any tobacco business in the United States;
- B&W contributed to RJRT all of its assets other than the capital stock of certain subsidiaries engaged in non-US businesses and other limited categories of assets;
- RJRT assumed all liabilities of B&W (except liabilities to the extent relating to businesses and assets not contributed by B&W to RJRT and other limited categories of liabilities) and contributed

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subsidiaries or otherwise to the extent related to B&W's tobacco business as conducted in the United States on or prior to 30 July 2004; and

- RJRT agreed to indemnify B&W and each of its associates (other than Reynolds American Inc. and its subsidiaries) against, among other matters, all losses, liabilities, damages, expenses, judgments, attorneys' fees, etc., to the extent relating to or arising from such assumed liabilities or the assets contributed by B&W to RJRT (the RJRT Indemnification).

The scope of the RJRT Indemnification includes all expenses and contingent liabilities in connection with litigation to the extent relating to or arising from B&W's US tobacco business as conducted on or prior to 30 July 2004, including smoking and health tobacco litigation, whether the litigation is commenced before or after 30 July 2004 (the Tobacco Litigation).

Pursuant to the terms of the RJRT Indemnification, RJRT is liable for any possible judgments, the posting of appeal bonds or security, and all other expenses of and responsibility for managing the defence of the Tobacco Litigation. RJRT has assumed control of the defence of the Tobacco Litigation involving B&W, to which RJRT is also a party in most (but not all) of the same cases. Accordingly, RJRT uses or plans to use the same law firm or firms to represent both B&W and RJRT in any single or similar case (except in certain limited circumstances) as RJRT's interests are typically aligned with B&W's interests, as RJRT has substantial experience in managing recognised external legal counsel in defending the Tobacco Litigation, and external counsel have independent professional responsibilities to represent the interests of B&W. In addition, in accordance with the terms of the RJRT Indemnification, associates of B&W have retained control of the defence in certain Tobacco Litigation cases with respect to which such associates are entitled to indemnification.

Included in the US litigation section below are all significant cases where B&W and/or a UK company is named as a defendant and all cases where RJRT is named as a defendant as a successor to B&W (the RJRT Successor Cases). The RJRT Successor Cases are covered by the indemnity explained above. Of the RJRT Successor Cases, the section below includes details of all cases where there has been an adverse judgment and also notes favourable judgments.

US litigation

The total number of US product liability cases pending at 31 December 2010 naming B&W was approximately 9,458 (2009: approximately 9,991). Of these, 6,303 cases are RJRT Successor Cases. For all of these cases, British American Tobacco Group companies have the protection of the indemnity above. British American Tobacco (Investments) Limited (Investments) has been served as a co-defendant in five of those cases (2009: six). No other UK-based Group company has been served as a co-defendant in any US product liability case pending as at 31 December 2010. In 2010, there were no US product liability cases tried to verdict against B&W. No product liability case in which a UK-based Group company is a defendant was tried in 2010, and one case in which a UK-based Group company is a defendant started trial in January 2011 (City of St. Louis - see below). Since many of these pending cases seek unspecified damages, it is not possible to quantify the total amounts being claimed, but the aggregate amounts involved in such litigation are significant, possibly totalling in the billions of US dollars. The cases fall into four broad categories:

(a) Medical reimbursement cases

These civil actions seek to recover amounts spent by government entities and other third party providers on healthcare and welfare costs claimed to result from illnesses associated with smoking. Although B&W continues to be a defendant in healthcare cost recovery cases involving plaintiffs such as hospitals and Native American tribes (see below), the vast majority of such cases have been dismissed on legal grounds.

Further, on 23 November 1998, the major US cigarette manufacturers (including B&W and RJRT) and the attorneys general of 46 US states and five US territories executed the Master Settlement Agreement (MSA), which settled medical reimbursement lawsuits that had been brought by these states and territories. Under the terms of the MSA, the settling cigarette manufacturers agreed, among other things, to pay approximately US\$246 billion to the settling states and territories (and to four states that reached separate settlements of their medical reimbursement actions) over 25 years, and agreed to various restrictions on US tobacco advertising and marketing. The MSA includes a credit for any amounts paid by participating manufacturers in subsequent suits brought by the states' political subdivisions.

At 31 December 2010, three US medical reimbursement suits were pending against B&W (2009: two). One of these suits was brought by an Indian tribe in the Indian Tribal Court in South Dakota. Another reimbursement suit (City of St. Louis) is pending against B&W, Investments and several other

defendants in the state court in Missouri. In City of St. Louis, the plaintiffs, approximately 40 public and non-profit hospitals in Missouri, are seeking reimbursement of past and future alleged smoking-related healthcare costs. On 26 October 2007, the plaintiffs filed a motion requesting the court to give collateral estoppel effect to the factual findings in the US Department of Justice case, which motion was denied on 2 June 2010. On 1 December 2009, certain defendants, including B&W and Investments, filed additional motions for summary judgment. In a series of orders issued from April 2010 through October 2010, the court granted summary judgment as to the plaintiffs' claims for fraudulent misrepresentation, negligent misrepresentation, failure to warn (whether sounding in strict liability or negligence) and improper marketing, and entered judgment in favour of the defendants, including B&W and Investments, on these claims. The court also dismissed the plaintiffs' claims for prejudgment interest, future damages, and damages allegedly arising out of exposure to environmental tobacco smoke (ETS), thus reducing the damages claims from the US\$2 billion originally sought to approximately US\$600 million. The claims remaining for trial are product defect (whether sounding in strict liability or negligence), restitution, civil conspiracy, aiding and abetting and punitive damages. The trial of this case began on 31 January 2011, and is expected to last approximately four to six months.

In another recoupment suit (National Committee to Preserve Social Security & Medicare), the plaintiffs, two taxpayer advocacy groups and a Medicare recipient diagnosed with lung cancer, alleged that the defendants (including B&W) are liable for the payment of Medicare beneficiaries' medical costs for diseases attributable to smoking, pursuant to the Medicare as Secondary Payer Statute (MSP). On 5 March 2009, the district court in the Eastern District of New York issued an order granting the defendants' motion to dismiss the plaintiffs' complaint in its entirety, and denying the plaintiffs' cross motion for summary judgment. The district court ruled that MSP plaintiffs can only recover Medicare funds where an alleged tortfeasor's liability has been established prior to the plaintiffs' seeking relief under the MSP, and that the plaintiffs in National Committee had failed to establish such liability. The plaintiffs filed a notice of appeal to the US Court of Appeals for the Second Circuit on 20 May 2009. On 4 February 2010, the defendants filed a motion to dismiss the appeal. On 23 June 2010, the Second Circuit denied the defendants' motion to dismiss the appeal. On 8 October 2010, a summary order was entered by the Second Circuit that vacated the judgment of the district court and remanded the case with instructions to dismiss the complaint for lack of subject matter jurisdiction. On 22 December 2010, the district court entered an order of dismissal for lack of subject matter jurisdiction and directed the Clerk of Court to enter judgment in accordance with the instructions from the Second Circuit. The Clerk of Court entered judgment in defendants' favour on 23 December 2010.

(b) Class actions

At 31 December 2010, B&W was named as a defendant in eight (2009: eight) separate actions attempting to assert claims on behalf of classes of persons allegedly injured or financially impacted through smoking or where classes of tobacco claimants have been certified. If the classes are or remain certified and the possibility of class-based liability is eventually established, it is likely that individual trials will be necessary to resolve any claims by individual plaintiffs. Class action suits have been filed in a number of states against individual cigarette manufacturers and their parent corporations, alleging that the use of the terms 'lights' and 'ultralights' constitutes unfair and deceptive trade practices.

The Schwab class-action complaint (Schwab) was filed in the US District Court for the Eastern District of New York on 11 May 2004 against several defendants, including B&W and certain UK-based Group companies. The complaint challenges the defendants' practices with respect to the marketing, advertising, promotion and sale of 'light' cigarettes. After six years of litigation, including before appellate courts, the parties on 13 July 2010 filed a stipulation of dismissal.

The Cleary class action complaint was filed in the state court in Chicago, Illinois on 3 June 1998 against several defendants, including B&W, B.A.T Industries p.l.c. (Industries) and Investments. Industries was dismissed on jurisdictional grounds by an intermediate appellate court on 17 March 2000. The Third Amended Complaint, filed on 3 March 2009, alleged that all defendants fraudulently concealed facts regarding the addictive nature of nicotine, that certain US defendants (but not Investments) marketed tobacco products to underage consumers, and that defendant Philip Morris fraudulently marketed Marlboro Lights cigarettes. The plaintiffs sought disgorgement of profits. The case was removed to the federal district court on 13 March 2009, and the federal district court denied the plaintiffs' motion to remand the case back to the state court via order dated 1 July 2009. On 1 February 2010, the court granted summary judgment dismissing the plaintiffs' fraudulent concealment claim, and permitted the plaintiffs to reinstate that claim via a new plaintiff. The court also granted summary judgment dismissing the plaintiffs' youth marketing claims and permitted the Marlboro Lights claim to proceed against defendant Philip Morris. On 22 February 2010, the court

denied the plaintiffs' motion for class certification of all three putative classes, but granted the plaintiffs leave to reinstate the certification motion as to the putative class alleging the fraudulent concealment claim if the plaintiffs identified a new plaintiff to represent that putative class. On 18 April 2010, the plaintiffs filed a motion for leave to file a Fourth Amended Complaint, which was granted on 22 April 2010. The Fourth Amended Complaint alleged that all defendants fraudulently concealed facts regarding the addictive nature of nicotine, and that defendant Philip Morris fraudulently marketed Marlboro Lights cigarettes. The plaintiffs sought disgorgement of profits. On 7 May 2010, the defendants filed a motion to dismiss the plaintiffs' Fourth Amended Complaint, which motion was granted on 22 June 2010. On 20 August 2010, the plaintiffs filed a notice of appeal in the US Court of Appeals for the Seventh Circuit. Briefing on the plaintiffs' appeal commenced in December 2010 and is expected to conclude in February 2011.

In a medical monitoring class action brought on behalf of Louisiana smokers (Scott) the jury returned a verdict on 28 July 2003 in favour of the defendants on the plaintiffs' claim for medical monitoring and found that cigarettes were not defectively designed. However, the jury also made certain findings against the defendants on claims relating to fraud, conspiracy, marketing to minors and smoking cessation. Notwithstanding these findings, this portion of the trial did not determine liability as to any individual class member or class representative. On 21 May 2004, the jury returned a verdict in the amount of US\$591 million, requiring the defendants to fund a cessation programme to help eligible class members stop smoking. On 29 September 2004, the defendants posted a US\$50 million bond, pursuant to legislation that limits the amount of the bond to US\$50 million collectively for MSA signatories, and noticed their appeal. RJRT posted US\$25 million (the portions for RJRT and B&W) towards the bond. On 7 February 2007, the Louisiana Court of Appeals upheld the class certification and found the defendants responsible for funding smoking cessation for eligible class members. The appellate court also ruled, however, that no class member who began smoking after 1 September 1988 could receive any relief, and that only those smokers whose claims accrued on or before 1 September 1988 would be eligible for the smoking cessation programme. In addition, the appellate court rejected the award of prejudgment interest, and struck eight of the twelve components of the smoking cessation programme. The defendants' application to the Louisiana Supreme Court for a writ of certiorari was denied on 7 January 2008. The defendants' petition to the US Supreme Court for a writ of certiorari was denied on 10 June 2008. On 21 July 2008, the trial court entered an amended judgment in the case. The court found that the defendants are jointly and severally liable for funding the cost of a court-supervised smoking cessation program and ordered the defendants to deposit approximately US\$263 million together with interest from 30 June 2004, into a trust for the funding of the programme. On 23 April 2010, the Louisiana Court of Appeals amended but largely affirmed the trial court's amended judgment. Pursuant to the judgment, the defendants are required to deposit US\$242 million with the court, with interest from 21 July 2008 until paid. In September 2010, the defendants' application for writ of certiorari or review by the Supreme Court of Louisiana along with the defendants' motion to stay execution of the judgment was denied. On 24 September 2010, the US Supreme Court granted the defendants' motion to stay the judgment pending the US Supreme Court's disposition of the defendants' petition for a writ of certiorari, which was filed on 2 December 2010.

Black is a 'lights' class action filed in November 2000 in the Circuit Court, City of St. Louis, Missouri. B&W removed the case to the US District Court for the Eastern District of Missouri on 23 September 2005. On 25 October 2005, the plaintiffs filed a motion to remand, which was granted on 17 March 2006. On 16 April 2008, the court stayed the case pending US Supreme Court review in *Good v. Altria Group, Inc.* A nominal trial date of 10 January 2011 was scheduled, but trial did not proceed at that time. No new date has been set.

Brown is a case filed in June 1997 in the Superior Court, San Diego County, California. On 11 April 2001, the court granted in part the plaintiffs' motion for certification of a class composed of residents of California who smoked at least one of the defendants' cigarettes from 10 June 1993 through 23 April 2001, and who were exposed to the defendants' marketing and advertising activities in California. The plaintiffs seek to recover restitution, disgorgement of profits and other equitable relief under the California Business and Professions Code. Certification was granted as to the plaintiffs' claims that the defendants violated the section of the California Business and Professions Code pertaining to unfair competition. The court, however, refused to certify the class under the California Legal Remedies Act and on the plaintiffs' common law claims. On 7 March 2005, the court granted the defendants' motion to decertify the class. On 5 September 2006, the California Court of Appeal affirmed the judge's order decertifying the class. On 1 November 2006, the plaintiffs' petition for review with the California Supreme Court was granted. On 18 May 2009, the California Supreme Court reversed the decision issued by the trial court and affirmed by the California Court of Appeal that decertified the class to the extent that it was based upon the conclusion that all class members were required to demonstrate standing, and remanded the case to the trial court for further proceedings regarding whether the class

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representatives have, or can demonstrate, standing. On 10 March 2010, the California Superior Court found that the plaintiffs' 'lights' claims were not pre-empted by the Federal Cigarette Labelling and Advertising Act, rendered the court's 30 September 2004 ruling on the issue no longer viable, and denied the defendants' second motion for summary judgment. The plaintiffs filed a tenth amended complaint on 10 September 2010. Certain defendants, including RJRT and B&W, filed answers to the tenth amended complaint on 12 October 2010. Trial is scheduled to begin on 6 May 2011.

Howard is a 'lights' class action filed in February 2000 in the Circuit Court, Madison County, Illinois. A judge certified a class on 18 December 2001. On 6 June 2003, the trial judge issued an order staying all proceedings pending resolution of Price v. Philip Morris, Inc., a 'lights' class action against Philip Morris, Inc. in the Illinois state court. The plaintiffs appealed this stay order to the Illinois Fifth District Court of Appeals, which affirmed the Circuit Court's stay order on 19 August 2005. There is currently no activity in the case.

Jones is a case filed in December 1998 in the Circuit Court, Jackson County, Missouri. The defendants removed the case to the US District Court for the Western District of Missouri on 16 February 1999. The action was brought by tobacco product users and purchasers on behalf of all similarly situated Missouri consumers. The plaintiffs allege that their use of the defendants' tobacco products has caused them to become addicted to nicotine. The plaintiffs seek to recover an unspecified amount of compensatory and punitive damages. The case was remanded to the Circuit Court on 17 February 1999. There has been limited activity in this case.

Parsons is a case filed in February 1998 in the Circuit Court, Ohio County, West Virginia. The plaintiff sued asbestos manufacturers, US cigarette manufacturers, including B&W, among other defendants, seeking to recover US\$1 million in compensatory and punitive damages individually and an unspecified amount for the class in both compensatory and punitive damages. The class was brought on behalf of persons who allegedly have personal injury claims arising from their exposure to respirable asbestos fibres and cigarette smoke. The case has been stayed pending a final resolution of the plaintiffs' motion to refer tobacco litigation to the judicial panel on multidistrict litigation filed in In Re: Tobacco Litigation in the Supreme Court of Appeals of West Virginia. On 26 December 2000, three defendants, Niral Liquidators, Inc., Desseaux Corporation of North American and Armstrong World Industries, filed bankruptcy petitions in the US Bankruptcy Court for the District of Delaware. Pursuant to the Bankruptcy Code, Parsons is automatically stayed with respect to all defendants.

Young is a case filed in November 1997 in the Circuit Court, Orleans Parish, Louisiana. The plaintiffs brought an ETS class action on behalf of all residents of Louisiana who, though not themselves cigarette smokers, have been exposed to second-hand smoke from cigarettes which were manufactured by the defendants, and who allegedly suffered injury as a result of that exposure. The plaintiffs seek to recover an unspecified amount of compensatory and punitive damages. On 13 October 2004, the trial court stayed this case pending the outcome of appellate review in the Scott class action in Louisiana (discussed above).

In Engle (a case in Florida), a jury awarded a total of US\$12.7 million to three class representatives, and in a later stage of the three-phase trial procedure adopted in this case, a jury assessed US\$17.6 billion in punitive damages against B&W. On 21 May 2003, the intermediate appellate court reversed the trial court's judgment and remanded the case to the trial court with instructions to de-certify the class. On 16 July 2003, the plaintiffs filed a motion for rehearing which was denied on 22 September 2003. On 12 May 2004, the Florida Supreme court agreed to review this case and, on 6 July 2006, it upheld the intermediate appellate court's decision to decertify the class and vacated the jury's punitive damages verdict. Further, the Florida Supreme Court permitted the judgments entered for two of the three Engle class representatives to stand, but dismissed the judgment entered in favour of the third Engle class representative. Finally, the Florida Supreme Court has permitted putative Engle class members to file individual lawsuits against the Engle defendants within one year of the court's decision (subsequently extended to 11 January 2008). The court's order precludes defendants from litigating certain issues of liability against the putative Engle class members in these individual actions. On 7 August 2006, the defendants filed a motion for rehearing before the Florida Supreme Court, which was granted in part and denied in part, on 21 December 2006. The Florida Supreme Court's 21 December 2006 ruling did not amend any of the earlier decisions' major holdings, which included decertifying the class, vacating the punitive damages judgment, and permitting individual members of the former class to file separate suits. Instead, the ruling addressed the claims on which the Engle jury's phase one verdict will be applicable to the individual lawsuits that were permitted to stand. On 1 October 2007, the United States Supreme Court denied the defendants' request for certiorari review of the Florida Supreme Court's decision.

As at 31 December 2010, B&W have been served in approximately 49 Engle progeny cases in both state and federal courts in Florida. These cases include approximately 105 plaintiffs. RJRT as a

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successor to B&W are named in approximately 6,286 Engle progeny cases. The plaintiffs' counsel included multiple plaintiffs in most of the cases filed, so case totals have increased over the past year as Florida courts ordered cases originally filed as multi-plaintiff actions to be severed.

In the first 'phase three' trial of an individual Engle class member (Lukacs), the jury awarded the plaintiff US\$37.5 million in compensatory damages (B&W's share: US\$8.4 million) on 11 June 2002. On 1 April 2003, the jury award was reduced to US\$25.1 million (B&W's share: US\$5.6 million) but no final judgment was entered into because the trial court postponed the entry of final judgment until the Engle appeal was fully resolved. The trial court, on 14 August 2008, issued an order entering judgment for the plaintiff that awarded US\$24.8 million to the plaintiff (plus interest), for which the defendants would be jointly and severally liable. On 17 October 2008, the plaintiff withdrew her request for punitive damages. On 12 November 2008, the trial court entered final judgment. On 1 December 2008, the defendants filed a notice of appeal. On 17 March 2010, the Third District Court of Appeal affirmed the ruling of the trial court. The defendants' motion for rehearing and petition for rehearing en banc was denied on May 18, 2010. RJRT expensed and paid the final judgment in the amount of approximately US\$15.2 million on 18 June 2010.

As at 31 December 2010, there have been 10 additional phase three Engle trials naming RJRT as successor to B&W, which proceeded to verdict. Of these ten trials, three resulted in the plaintiffs' verdicts (Douglas, Putney, Grossman). In Douglas, the jury awarded US\$5 million in compensatory damages against all defendants on 10 March 2010, allocating US\$250,000 of the award to RJRT. The defendants filed notice of appeal on 28 June 2010. On 29 June 2010, RJRT posted a supersedeas bond in the amount of US\$250,000. In Putney, the jury awarded US\$15,086,688 in compensatory damages and US\$5 million in punitive damages on 26 April 2010, allocating US\$4,526,000 in compensatory damages and US\$2.5 million in punitive damages to RJRT. The defendants filed a notice of appeal on 30 August 2010, and the plaintiff filed a notice of cross appeal on 31 August 2010. On 20 December 2010, RJRT posted a supersedeas bond in the amount of US\$2,372,765. In Grossman, the jury awarded US\$1,934,727 in compensatory damages on 29 April 2010, allocating US\$483,682 to RJRT. The defendants filed a notice of appeal on 14 July 2010. The plaintiff filed a notice of cross appeal on 19 July 2010. On 19 July 2010, RJRT posted a supersedeas bond in the amount of US\$483,682.

In June 2009, the Florida legislature amended its existing bond cap statute by adding a US\$200 million bond cap that applies to all phase three Engle cases in the aggregate, and establishes individual bond caps for individual cases in amounts that vary depending on the number of judgments in effect at a given time. In the absence of further legislative action, this bond cap will remain in effect until 31 December 2012.

(c) Individual cases

Approximately 3,161 cases were pending against B&W at 31 December 2010 (2009: 3,191) filed by or on behalf of individuals in which it is contended that diseases or deaths have been caused by cigarette smoking or by exposure to ETS. Of these cases, approximately: (a) 2,590 are ETS cases brought by flight attendants who were members of a class action (Broin) that was settled on terms that allow compensatory but not punitive damages claims by class members; (b) 429 of the individual cases against B&W are cases brought in consolidated proceedings in West Virginia, where the first phase of the trial is scheduled to begin on 17 October 2011; (c) 49 are Engle progeny cases that have been filed directly against B&W, and (d) 93 are cases filed by other individuals (76 of which name B&W and 17 of which name RJRT as successor to B&W). As mentioned above there are a further 6,286 Engle progeny cases which name RJRT as successor to B&W. These cases are subject to the indemnity set out above and are not detailed here.

There were three individual cases that resulted in verdicts against B&W and which remained on appeal during 2010 (not including Lukacs, see above):

In December 2003, a New York jury (Frankson) awarded US\$350,000 in compensatory damages against B&W and two industry organisations. In January 2004, the same jury awarded US\$20 million in punitive damages. On 22 June 2004, the trial judge granted a new trial unless the parties agreed to an increase in compensatory damages to US\$500,000 and a decrease in punitive damages to US\$5 million, of which US\$4 million would be awarded against B&W. The plaintiff agreed to a decrease in punitive damages, but B&W has not agreed to an increase in compensatory damages. On 25 January 2005, B&W appealed to an intermediate New York State appellate court. Oral argument was heard on 8 May 2006. The appellate court affirmed the judgment on 5 July 2006, except insofar as it dismissed the plaintiff's design defect claims. B&W filed a motion for leave to reargue, or in the alternative, for leave to appeal to the New York Court of Appeals, on 3 August 2006. The intermediate appellate court denied this motion on 5 October 2006. On 8 December 2006, the trial judge granted the plaintiff's

application for entry of judgment in the amounts of US\$5 million in punitive damages and US\$175,000 in compensatory damages. The trial court also granted the plaintiff's motion to vacate that part of the 2004 order granting a new trial unless the parties agreed to an increase in compensatory damages to US\$500,000. RJRT posted a bond in the approximate amount of US\$8.018 million on 3 July 2007. B&W appealed from final judgment on 3 July 2007 to an intermediate New York State appellate court. Oral argument was heard on 28 January 2009. On 29 September 2009, the appellate court issued a decision modifying the final judgment by deleting the award of punitive damages, and remanding the case to the trial court for a new trial on the issue of punitive damages. On 22 December 2009, the plaintiff requested an extension of time to move for leave to appeal to the New York Court of Appeals, and for leave to reargue the case to the appellate court. On 15 January 2010, the appellate court denied the plaintiff's motion for additional time to seek leave to appeal to the New York Court of Appeals, but granted the plaintiff more time to file a motion for leave to reargue to the appellate court. The plaintiff's motion for leave to reargue was denied by the appellate court on 12 March 2010. As at 31 December 2010, no date has been set for a new trial on the issue of punitive damages.

On 1 February 2005, a Missouri jury (Lincoln Smith) awarded US\$500,000 in compensatory damages against B&W and then, on 2 February 2005, awarded US\$20 million in punitive damages, also against B&W. On 1 June 2005, B&W filed its notice of appeal. Oral argument was heard on 31 August 2006. On 31 July 2007, an intermediate Missouri appellate court affirmed the compensatory damages award, but it reversed the punitive damages award, reasoning that the plaintiffs failed to produce sufficient evidence to justify the verdict. The majority of the court would have remanded the case for a second trial, limited to punitive damages, but a dissenting judge transferred the case to the Missouri Supreme Court, as permitted by Missouri law. Oral argument was heard by the Missouri Supreme Court on 13 February 2008. On 31 July 2008, the Missouri Supreme Court transferred the case back to the intermediate appellate court for further proceedings. In a decision entered on 16 December 2008, the intermediate appellate court again upheld the award of compensatory damages and reversed the jury's award of US\$20 million in punitive damages, sending the case back to the trial court for a new trial on punitive damages. Following a new trial, on 20 August 2009, a Missouri jury returned a verdict awarding US\$1.5 million in punitive damages against B&W. On 24 September 2009, B&W filed a motion for a new trial and a motion for judgment notwithstanding the verdict. On the same date, the plaintiffs filed a motion for additur, asking the court to increase the amount of punitive damages from US\$1.5 million to US\$20 million, and a motion to vacate, modify or set aside judgment, or in the alternative, for a new trial. On 21 December 2009, the court denied the plaintiffs' and B&W's post-trial motions. On 30 December 2009, B&W filed a notice of appeal. On 31 December 2009, the plaintiffs filed a notice of appeal. Both appeals remain pending.

On 18 March 2005, a New York jury (Rose) awarded US\$1.7 million in compensatory damages against B&W. On 18 August 2005, B&W filed its notice of appeal. RJRT posted a bond in the approximate amount of US\$2.058 million on 7 February 2006. Oral argument on this appeal was heard on 12 December 2006 by an intermediate New York appellate court. On 10 April 2008, the appellate court reversed the judgment in the plaintiff's favour and ordered that the case be dismissed. On 8 May 2008, the plaintiff filed a notice of appeal to New York's Court of Appeals. On 16 December 2008, the New York Court of Appeals affirmed the decision of the appellate court dismissing the plaintiff's complaint. On 14 January 2009, the plaintiff filed a motion seeking leave to reargue the 16 December 2008 decision and order of the New York Court of Appeals, which was denied by an order dated 26 March 2009. The plaintiff filed a petition for a writ of certiorari in the US Supreme Court in June 2009, which was denied on 5 October 2009.

(d) Other claims

The Flintkote Company (Flintkote), a US asbestos production and sales company, was included in the acquisition of Genstar Corporation by Imasco Limited's subsidiary, Imasco Enterprises, Inc., in 1986 and became a Group subsidiary following the restructuring of Imasco Limited (now Imperial Tobacco Canada Limited (Imperial), the Group's operating company in Canada) in 2000. Soon after this acquisition, and as part of the acquisition plan, Genstar Corporation began to sell most of its assets, including the non-asbestos related operations and subsidiaries of Flintkote. The liquidation of Flintkote assets produced cash proceeds and, having obtained advice from the law firm of Sullivan & Cromwell LLP and other advice that sufficient assets would remain to satisfy liabilities, Flintkote authorised the payment of a dividend of US\$170.2 million in 1986 and a further dividend of US\$355 million in 1987. In 2003, Imperial's subsidiary, Genstar Pacific Corporation, divested Flintkote and then, in 2004, Flintkote filed for bankruptcy in the United States Bankruptcy Court for the District of Delaware. In 2006, Flintkote, representatives of both the present and future asbestos claimants, and individual asbestos claimants were permitted by the bankruptcy court to file a complaint against Imperial and numerous other defendants including Sullivan & Cromwell LLP, for the recovery of the dividends, plus interest, and other compensation under various legal and equitable theories, including seeking a

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determination that Imperial is Flintkote's 'alter ego' and is responsible for all of Flintkote's asbestos tort liabilities. Sullivan & Cromwell LLP and Imperial have since filed cross complaints against each other. The parties are presently engaged in case management discussions to establish the scope and manner of discovery in this case. Although the Flintkote litigation is at a preliminary stage, the judge has stated an intention to determine several discrete issues for resolution in a series of bifurcated bench trials in an effort to simplify or clarify the determinative issues in the litigation. The first issue is whether Flintkote's claim for malpractice against Sullivan & Cromwell LLP is time barred. On 31 January 2011, the court entered a preliminary ruling stating that the complaint was time barred and that Sullivan & Cromwell LLP is entitled to dismissal. The second issue involves an enquiry into the two dividends and the circumstances surrounding them, including issues involving fraudulent conveyance. Certain legal issues regarding fraudulent conveyance were briefed and, at hearings held on 22 December 2010 and 2 February 2011, the court further refined the list of issues involving fraudulent conveyance. In addition, two other issues have emerged: (1) whether Flintkote or certain asbestos tort claimants are able to pursue 'alter ego' claims against Imperial, and (2) whether Flintkote should be judicially estopped from asserting certain fraudulent conveyance remedies in light of prior inconsistent statements it made during the course of the litigation. While it is expected that bench trials on all of these issues will occur in 2011, it is unclear when the court might rule on the issues.

In Wisconsin, the authorities have identified potentially responsible parties (PRPs) to fund the clean up of river sediments in the lower Fox River, Wisconsin. The pollution was caused by discharges of PCBs from paper mills and other facilities operating close to the river. The cost of the clean up work has been estimated to be in excess of US\$900 million. Among the potentially responsible parties are NCR Corporation (NCR) and Appleton Papers Inc. (Appleton) who are liable for the clean up costs in a large portion of the river under the terms of a consent decree. In 1978, Industries purchased what was then NCR's Appleton Papers Division from NCR. In 1978, Industries also incorporated a US entity by the name of BATUS, Inc. (BATUS), which in 1980 became the holding company for all of Industries' US subsidiaries, including Appleton. As the holding company, BATUS obtained insurance policies for itself and its subsidiaries that included coverage for certain environmental liabilities. Industries/BATUS spun off the Appleton business in 1990 to Wiggins Teape Appleton p.l.c. and Wiggins Teape Appleton (Holdings) p.l.c., now known as Arjo Wiggins Appleton Ltd. and Arjo Wiggins US Holdings Ltd. (collectively, the AWA Entities), obtaining full indemnities from AWA Entities for past and future environmental claims. Disputes between NCR, Appleton, the AWA Entities, and Industries as to the indemnities given and received under the purchase agreement in 1978 have been the subject of arbitrations in 1998 and 2006. Under the terms of the arbitration awards, Industries and Appleton/the AWA Entities have an obligation to share the costs of environmental claims with NCR (60:40), but Industries has never been required to pay any sums in this regard because Appleton and the AWA Entities have paid the non-NCR (60 per cent) share of the clean-up costs to date, and the authorities have not identified Industries or BATUS as PRPs. However, there is a risk for Industries that Appleton and the AWA Entities will exhaust the recoverable insurance policies prior to the completion of the mandated clean-up work and that Appleton and the AWA Entities will not have sufficient assets of their own to pay the clean-up obligations, leaving Industries with the responsibility to pay the non-NCR share of the remaining clean-up costs. There is a further risk that the clean-up costs for the project will increase beyond current estimates.

UK-based Group companies

Investments has been served in the following US cases pending at 31 December 2010: a medical reimbursement case, City of St. Louis, and Cleary, a class action (see above under medical reimbursement cases and class actions respectively); the US Department of Justice case (see below); an anti-trust case, Daric Smith (see below); and two individual actions, Eiser and Perry, which are currently dormant. No other UK-based Group company has been served in a US product liability case pending as at 31 December 2010.

Conduct-based claims

On 22 September 1999, the US Department of Justice brought an action in the US District Court for the District of Columbia against various industry members, including RJRT, B&W, Industries and Investments. Industries was dismissed for lack of personal jurisdiction on 28 September 2000. The government sought to recover federal funds expended in providing healthcare to smokers who have developed diseases and injuries alleged to be smoking-related, and, in addition, sought, pursuant to RICO, disgorgement of profits the government contends were earned as a consequence of a RICO 'enterprise'. On 28 September 2000, the district court dismissed the portion of the claim which sought recovery of federal funds expended in providing healthcare to smokers who have developed diseases and injuries alleged to be smoking-related. The non-jury trial of the RICO portion of the claim began on

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21 September 2004, and ended on 9 June 2005. On 17 November 2004, the US Court of Appeals for the DC Circuit heard an appeal by the defendants against an earlier district court decision that disgorgement of profits is an appropriate remedy for the RICO violations alleged by the government. On 4 February 2005, the DC Circuit allowed the appeal, ruling that the government could not claim disgorgement of profits. On 17 October 2005, the US Supreme Court declined to hear the appeal by the US government in respect of the claim for disgorgement of US\$280 billion of past profits from the defendants.

On 17 August 2006, the district court issued its final judgment, consisting of some 1,600 pages of factual findings and legal conclusions. The court found in favour of the government, and against certain defendants, including B&W and Investments. The court also ordered a wide array of injunctive relief, including a ban on the use of 'lights' and other similar descriptors. Compliance with the court-ordered remedies may cost RJRT and Investments millions of dollars, although remedial compliance has been stayed over the last several years pending appellate review. In addition, the government is seeking the recovery of roughly US\$1.9 million (plus accruable interest) in litigation costs, with RJRT having already paid approximately US\$780,000 in costs on behalf of itself and B&W. Investments filed a praecipe with the district court on 28 September 2010 stating that it is not yet obligated to pay costs inasmuch as there has not been final resolution of all appeals in this matter (including the extraterritorial reach, if any, of the RICO statute based on an intervening change in law).

On 10 August 2007, the defendants filed their initial appellate briefs to the Court of Appeals for the DC Circuit. All defendants filed a joint appellate brief, and Investments also filed its own brief which raised the issue of whether Congress intended for RICO to apply to extraterritorial conduct by a foreign defendant. On 19 November 2007, the government filed its opposition and cross-appeal brief, seeking to reinstate certain remedial relief, including its disgorgement claims. On 22 May 2009, a three-judge appellate panel unanimously affirmed the district court's RICO liability judgment against Investments, Altria, Philip Morris, RJRT and Lorillard, ordered the dismissal of CTR and TI (two defunct US trade associations that were not covered by the district court's injunctive remedies), and remanded for further factual findings and clarification as to whether liability should be imposed against B&W, based on changes in the nature of B&W's business operations. The panel also remanded on four discrete issues relating to the remedies, including for the district court "to reformulate" the injunction on the use of low-tar descriptors "to exempt foreign activities that have no substantial, direct, and foreseeable domestic effects". The government's cross-appeal seeking disgorgement of past profits and the funding of smoking education and cessation programmes was denied. Investments' petition for panel rehearing and rehearing en banc were filed on 31 July 2009 and was denied on 22 September 2009 by the DC Circuit.

On 19 February 2010, the defendants and the government filed certiorari petitions with the US Supreme Court. On 28 June 2010, the US Supreme Court declined to grant certiorari on all petitions. On 23 July 2010, Investments filed a petition for rehearing before the US Supreme Court, on the basis of an intervening decision by the High Court that invalidated the "effects" test the district court and DC Circuit both used in concluding that the RICO statute applied to Investments' foreign conduct. The US Supreme Court denied Investments' rehearing petition on 3 September 2010.

On 7 July 2010, the DC Circuit issued its remand returning the case to the district court for further proceedings. On 22 December 2010, the district court ordered, among other things, that B&W is no longer a defendant and is therefore not subject to the court's injunction. On 28 December 2010, the government filed a motion to compel Investments' compliance with the district court's 17 August 2006 order. Investments' opposition to the government's motion to compel compliance along with Investments' motion for reconsideration of the liability judgment against it on the basis of an intervening change in controlling law was filed on 21 January 2011.

In the Daric Smith case, purchasers of cigarettes in the State of Kansas brought a class action in the Kansas State Court against B&W, Investments and certain other tobacco companies seeking injunctive relief, treble damages, interest and costs. The allegations are that the defendants participated in a conspiracy to fix or maintain the price of cigarettes sold in the US, including the State of Kansas, in violation of the Kansas Restraint of Trade Act. Following a hearing on 8 December 2008 on the plaintiff's motion to compel Investments to produce documents, Investments identified relevant documents for discovery and Judge Smith (now retired) issued an order compelling disclosure of all of Investments' documents without an in camera review. On 15 October 2009, Investments filed a motion for reconsideration of Judge Smith's order. A decision on this is awaited. Following the appointment of a new judge, in October and November 2010, all defendants moved for summary judgment. Those motions have not yet been fully briefed.

Product liability outside the United States

At 31 December 2010, active claims against the Group's companies existed in 22 markets outside the US (2009: 22) but the only markets with more than five claims were Argentina, Brazil, Canada, Chile, Italy, Nigeria, and the Republic of Ireland (2009: five). Medical Reimbursement actions are being brought in Canada, Argentina, Brazil, Colombia, Israel, Nigeria, Saudi Arabia and Spain.

(a) Medical reimbursement cases

Brazil

In August 2007, the São Paulo Public Prosecutors office filed a medical reimbursement claim against Souza Cruz. A similar claim was lodged against Philip Morris. Souza Cruz's motion to consolidate the two claims was rejected and instead this case was removed to a different lower court. Souza Cruz filed a motion to reconsider the refusal for consolidation and an interlocutory appeal against assignment to the lower court. At the same time, the Public Prosecutor filed a motion challenging the connection between the two cases, which argument the State Court of Appeals accepted in August 2010 and ordered the two cases to progress independently. Souza Cruz subsequently filed a motion for clarification opposing the ruling, which is now pending review with the reporting justice. The lower court proceedings against Souza Cruz are expected to resume in due course.

Canada

In Canada there are three statutory actions for recovery of healthcare costs arising from the treatment of smoking and health related diseases. These proceedings name various group companies. Legislation enabling provincial governments to recover the healthcare costs has been enacted in British Columbia, New Brunswick, Ontario and Quebec. Actions have begun against various Group companies in British Columbia, New Brunswick and Ontario. In Quebec, the Group companies are challenging the legislation, and the Quebec has not filed its own action. Newfoundland is in the process of referring legislation to the Newfoundland Court of Appeals. Similar legislation has also been passed and is also being considered by other Canadian provinces.

The government of British Columbia brought a claim pursuant to the provisions of the Tobacco Damages and Health Care Costs Recovery Act 2000 (the Recovery Act) against domestic and foreign 'manufacturers' seeking to recover the plaintiff's costs of health care benefits. Imperial, Investments, Industries and other former Rothmans Group companies are named as defendants. The constitutionality of the Recovery Act was challenged by certain defendants and, on 5 June 2003, the British Columbia Supreme Court found the Recovery Act to be beyond the competence of the British Columbia legislature and, accordingly, dismissed the government's claim. The government appealed the decision to the British Columbia Court of Appeal which, on 20 May 2004, overturned the lower court's decision and declared the Recovery Act to be constitutionally valid. The defendants appealed to the Supreme Court of Canada in June and the court gave its judgment in September 2005 dismissing the appeals and declaring the Act to be constitutionally valid.

The federal government was enjoined by a Third Party Notice, and presented a Motion to Strike the claim out. The hearing took place during the week of 3 March 2008 and the court found in favour of the federal government. The defendants appealed that decision and the hearing was held during the week of 1 June 2009. On 8 December 2009, the British Columbia Court of Appeal handed down its decision in both this case and the Knight class action. This appeal was granted in part. The Court of Appeal held that it was not "plain and obvious" that the federal government did not owe a duty of care to tobacco manufacturers or consumers when it implemented its tobacco control strategy.

On 8 February 2010, the federal government sought leave to appeal this decision to the Supreme Court of Canada. On 10 March, the defendant filed response materials and a cross appeal. The government of British Columbia sought leave to oppose the defendants' cross appeal in part. On 20 May, the Supreme Court of Canada granted leave to appeal both in respect of the federal government's application and the defendants' conditional cross applications. The appeal is scheduled to be heard on 24 February 2011.

The underlying medical reimbursement action remains at a preliminary case management stage. Damages have not yet been quantified by the plaintiff. Given the Supreme Court application, and a number of other factors including delay on the part of the plaintiff in producing his damages modelling materials, the trial date has been postponed.

Non-Canadian defendants challenged the personal jurisdiction of the British Columbia Court and those motions were heard in the Supreme Court of British Columbia. On 23 June 2005, the court dismissed all defendants' motions, finding that there is a "real and substantial connection" between British

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Columbia and the foreign defendants. Subsequently, the defendants were granted leave to appeal that ruling to the Court of Appeal of British Columbia. The appeal was dismissed on 15 September 2006. The defendants filed leave to appeal to the Supreme Court on 10 November 2006, and that application was denied on 5 April 2007.

The government of New Brunswick has brought a medical reimbursement claim against domestic and foreign tobacco "manufacturers", pursuant to the provisions of the Recovery Act passed in that Province in June 2006. The Company, Investments, Industries, Imperial and Carreras Rothmans Limited (the UK Companies) have all been named as defendants. The government filed a statement of claim on 13 March 2008. The Group defendants were served with the Notice of Action and Statement of Claim on 2 June 2008. A case management conference was held on 8 January 2009 so that other defendants could challenge the use of a contingent fee arrangement (CFA) for the plaintiff's lawyer. This challenge was refused at first instance. Leave to appeal was granted on limited grounds. These grounds, upon which leave was denied, were appealed directly to the Supreme Court of Canada. On May 13, 2010, the New Brunswick Court of Appeal dismissed Imperial's appeal. The Supreme Court of Canada subsequently denied leave on all aspects of the CFA challenge, thus ending this preliminary challenge. The appeal was dismissed and an application to appeal to the Supreme Court was denied on 21 October 2010. The UK Companies have challenged the court's jurisdiction and in November 2010 all four challenges were refused. Appeals are ongoing. No damages have yet been quantified by the plaintiff.

The government of the Province of Ontario has also filed a C\$50 billion medical reimbursement claim against domestic and foreign tobacco "manufacturers", pursuant to the provisions of the Tobacco Damages and Health Care Costs Recovery Act 2009. The UK Companies have all been named as defendants. Imperial was served on 30 September 2009 and the UK Companies were served on 8 October 2009. A case management judge has been appointed and the jurisdiction motions filed by the UK Companies will be heard first. The hearing is scheduled for April 2011.

Colombia

British American Tobacco (South America) Limited (BAT South America) was served on 18 July 2008 in a public interest action that has a medical reimbursement component. The case was brought by two Colombian citizens alleging that the defendant violated numerous "collective" interests and rights of the Colombian population. In addition to equitable and injunctive relief being sought, the plaintiffs are seeking 25 per cent of smoking-related healthcare costs since the time that British American Tobacco has been operating in Colombia. Thereafter, the plaintiffs also request that the company contribute US\$50 million a year to a fund. BAT South America initially filed preliminary objections to the action, with a view to joining the claim with another class action, the Sandra Florez action (which made substantially similar allegations and sought similar relief). However, as the Florez case was decided in BAT South America's favour in September 2009, BAT South America will submit a full defence in due course.

Israel

In Israel, a medical reimbursement claim was brought against Industries, B&W, Investments and B.A.T (U.K. and Export) Limited (BATUKE), amongst others, by Clalit Health Services. The plaintiff claims damages of NIS 7.6 billion and seeks injunctive relief. On 29 March 2005, B&W, Investments and BATUKE argued for leave to appeal the denial of their application to dismiss the action on the grounds of remoteness and a decision from the Supreme Court on this issue is still awaited.

Nigeria

Health care recoupment actions have also been brought by five Nigerian states (Lagos, Kano, Gombe, Oyo, Ogun) and by the federal government of Nigeria, each seeking the equivalent of billions of US dollars for costs allegedly incurred by the state and federal governments in treating smoking-related illnesses. British American Tobacco (Nigeria) Limited (BAT Nigeria) has been named as a defendant in each of the cases; the Company and Investments have been named as defendants in six of the cases.

As at 31 December 2010, the actions that had been filed by the Attorneys-General of Ondo State and of Ekiti State were voluntarily discontinued by the plaintiffs without prejudice to re-file on 5 October 2009 and 18 June 2009, respectively. The action filed by the Attorney-General of Akwa Ibom State was struck out without prejudice for lack of prosecution on 19 October 2009.

On 21 February 2008, the Lagos action was voluntarily discontinued by the plaintiffs. On 13 March 2008, the Lagos Attorney General filed a substantially similar action which was marked as 'qualified' under Lagos State's 'Fast-Track' system. The 'Fast-Track' system provides for resolution of the dispute within an eight-month time-period after filing. BAT Nigeria, the Company and Investments

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have all been served in the new action, and have filed preliminary objections. At a hearing on 16 September 2008, because service was yet to be completed on all defendants, the court directed that the case no longer qualified to be heard on the 'Fast Track'. On 18 September 2009, the court issued a ruling denying the preliminary objections filed by the Company and Investments on the basis that the court was competent to hear the case as it related to those defendants, that the Company and Investments are necessary parties to the action and that the suit therefore was not liable to be struck out as against those defendants. On 2 October 2009, the Company and Investments filed notices of appeal from the entirety of the court's ruling as it related to their respective objections. On 15 October and 19 October 2009, respectively, the Company and Investments filed motions to stay all proceedings pending the resolution of their appeals, which motion was granted by the High Court on 20 September 2010. On 26 November 2010, the Lagos Attorney General filed a motion for leave to appeal the High Court's order granting a stay, which motion remains pending before the Court of Appeal.

On 8 July 2008, the High Court of Gombe State issued a ruling on the preliminary objections filed by the Company, Investments and other defendants in the case, setting aside the service on all defendants and striking out the Gombe suit. In its decision, the court held that the writs served on the defendants were invalid, the plaintiff had failed to pay the requisite filing fees, and that based on these filing defects, the court was not competent to assume jurisdiction. The court also stated, however, that the plaintiff, through its statement of claim and affidavit evidence filed in support of its *ex parte* motion for leave to serve outside the jurisdiction, had satisfied the requirements for service outside the jurisdiction. Although the plaintiff has not appealed from the court's decision, the plaintiff has filed a renewed action in the High Court of Gombe State. BAT Nigeria, the Company and Investments have filed notices of preliminary objection in the renewed action. On 16 December 2010, the Gombe High Court heard argument on the defendants' service and jurisdictional objections.

In the Oyo State case the British American Tobacco companies filed preliminary objections. These were partially granted on 22 June 2010 and service was set aside. The issuance of the writ was, however, not set aside and the Company and Investments are appealing this decision based on their jurisdictional objections. As at 31 December 2010, the appeals remain pending, and the plaintiff has not re-served the writ on the British American Tobacco defendants.

In Kano, the preliminary objections filed by the Company and Investments were dismissed on 16 April 2010. The Company and Investments have appealed the decision and sought a stay of proceedings. On 13 May 2010, the plaintiff filed a motion for preliminary injunction which seeks *inter alia* to prevent the defendants from marketing tobacco products or causing them to be sold to underage purchasers or near any primary or secondary school in Kano State. At a hearing on 8 December 2010 the court heard argument concerning the order in which the stay application, injunction motion, and other pending matters will be heard, and adjourned to 20 January 2011 for ruling. On 20 January 2011, the court ruled that it would first hear Nigeria's preliminary objections to the court's jurisdiction, and subsequently would hear the defendants' stay applications together with the plaintiff's injunction motion, and adjourned to 22 February 2011 for a hearing on BAT Nigeria's objections.

In Ogun, preliminary objections were filed by BAT Nigeria, the Company and Investments, but were rejected by the court on 20 May 2010. All three British American Tobacco defendants have filed appeals. On 24 May 2010, the plaintiff filed a motion for preliminary injunction which seeks *inter alia* to prevent the defendants from marketing tobacco products or causing them to be sold to underage purchasers or near any primary or secondary school in Ogun State. On 15 and 19 October 2010, the Company and Investments, respectively, filed motions in the Court of Appeal for a stay of proceedings pending their appeals. On 21 October 2010, the High Court adjourned proceedings without date pending resolution of the stay motions. As at 31 December 2010, the stay motions remain pending before the Court of Appeal and a hearing is scheduled for 31 March 2011.

Saudi Arabia

In Saudi Arabia, in 2007, there were reports that the Ministry of Health was pursuing a healthcare recoupment action in the Riyadh General Court against a number of distributors and agents. As at 31 December 2010, no Group company has been served with process. The Ministry of Health is reportedly seeking damages of at least 127 billion Saudi Riyals. Hearings take place on average every six months.

In addition, a separate medical reimbursement action has reportedly been filed by the King Faisal Specialist Hospital in the Riyadh General Court, naming 'BAT Company Limited' as a defendant. As at 31 December 2010, no Group company had been served with process in the action.

Spain

In early 2006, the Junta de Andalucia, in Spain, filed a medical reimbursement action against the State and tobacco companies (including BAT Espana S.A.) before the contentious-administrative courts. The State filed preliminary objections to the Junta's claim, with tobacco companies filing supporting briefs. The court upheld these preliminary objections and dismissed the claim in November 2007. The Junta's appeal of this ruling to the Supreme Court was dismissed in September 2009. However, in May 2009, the Junta also filed a new contentious-administrative claim following inactivity on their previous claim, which proceedings are still progressing. Preliminary objections were made in May 2010 and the parties are awaiting the court's ruling.

(b) Class actions

Brazil

There are five class actions being brought in Brazil. One is also a medical reimbursement, and is therefore discussed above.

In 1995, the Associação de Defesa da Saúde do Fumante (ADESF) class action was filed against Souza Cruz S.A. (Souza Cruz) and Philip Morris in the São Paulo Lower Civil Court alleging that the defendants are liable to a class of smokers and former smokers for failing to warn of cigarette addiction. The case was stayed in 2004 pending the defendants' appeal from a decision issued by the lower civil court on 7 April 2004. That lower court decision held that the defendants had not met their burden of proving that cigarette smoking was not addictive or harmful to health, notwithstanding an earlier interlocutory order that the São Paulo Court of Appeals had issued, which directed the trial court to allow more evidence to be taken before rendering its decision. On 12 November 2008, the São Paulo Court of Appeals overturned the lower court's unfavourable decision of 2004, finding that the lower court had failed to provide the defendants with an opportunity to produce evidence. The case now returns to the lower court for production of evidence and a new judgment. On 19 March 2009, the Lower Civil Court ordered the previous court-appointed medical expert to be replaced and a new advertising expert appointed. The parties have submitted questions to these court-appointed experts who have both delivered their reports. The plaintiff has provided comments on both expert reports. Souza Cruz responded with its comments and submissions from its own experts on 26 November 2010.

The Brazilian Association for the Defense of Consumers' Health (Saudecon) filed a class action against Souza Cruz in the City of Porto Alegre, Brazil on 3 November 2008. The plaintiff purports to represent all Brazilian smokers whom, it alleges, are unable to quit smoking and lack access to cessation treatments. The plaintiff is seeking an order requiring the named defendants to fund, according to their market share, the purchase of cessation treatments for these smokers over a minimum period of two years. Souza Cruz was served with this complaint on 19 November 2008. On 18 May 2009, the case was dismissed with judgment on the merits. The plaintiffs appealed in August 2009 and Souza Cruz and Philip Morris both responded. The parties are now awaiting judgment from the State Court of Appeal's 10th Civil Chamber.

A class action was filed against Souza Cruz by the Association of Exploited Consumers of the federal District, requesting a court order to prevent Souza Cruz selling cigarettes in Brazil. In December 2006, the federal District Court of Appeals confirmed a favourable lower court decision which had found the claim groundless and unlawful. The plaintiff appealed that ruling, but on 12 March 2009 the Superior Court affirmed the ruling and rejected the plaintiff's appeal. The plaintiff appealed again, but on 23 March 2009, in a unanimous decision, the Superior Court rejected the plaintiff's appeal. An appeal is now pending before the federal Supreme Court.

In 2004, the State of Sergipe instigated a class action seeking compensation for smokers in Sergipe State who purportedly sought to quit smoking. The lower court denied the plaintiffs' request for early relief and determined ANVISA (a federal government health agency) be ordered to join the case as co-defendants. As ANVISA is a federal agency, the case was removed to the federal court where ANVISA successfully argued that it lacked standing to be sued. The claim against ANVISA was dismissed and the federal court sent the case back to the lower state court for proceedings to continue, however, the action was stayed on 18 December 2009 pending a decision by the Superior Court on which court has jurisdiction. On 26 March 2010 the Superior Court determined that it has jurisdiction of the matter and a decision from the court is now pending.

Bulgaria

In March 2008, a smoking-related consumer fraud class action was filed in the Sofia City Court of Bulgaria against 21 defendants, including the following British American Tobacco-affiliated companies: British-American Tobacco Polska S.A., British-American Tobacco (Romania) Investments SRL, House of Prince A/S, and Scandinavian Tobacco S.A. On 24 September 2008, the claim was dismissed on procedural grounds, and the plaintiff appealed this ruling. On 11 November 2008, the Court of Appeal granted the plaintiff's appeal and on 2 December 2008, the Sofia City Court ordered the plaintiff to meet various evidentiary and procedural conditions before proceeding further with this claim. An ex parte hearing took place on 18 November 2010 to allow the plaintiff to present evidence on his ability to bring the claim and on the viability of the claim itself. On 24 November 2010, the Sofia City Court issued an order denying plaintiff the right to proceed with the claim on the grounds that the class members could not be accurately identified and because plaintiff lacked adequate funding to pursue the litigation on behalf of the proposed class. The plaintiff appealed that ruling and on 20 January 2011, the Court of Appeal affirmed the dismissal of the case.

Canada

There are 10 class actions being brought in Canada against Group companies.

In the Knight class action, a claim has been brought against Imperial under the Trade Practices Act and the Business Practices and Consumer Protection Act. The claim includes alleged deceptive practices in relation to the use of 'light' and 'mild' descriptors. The Supreme Court of British Columbia certified a class of all consumers of cigarettes bearing 'light' or 'mild' descriptors since 1974 manufactured in British Columbia by Imperial. Imperial filed an appeal against the certification which was heard in February 2006. The Appeal Court confirmed the certification of the class but has limited any financial liability, if proved, to the period from 1997. This is a 'lights' class action in which the plaintiff alleges that the marketing of light and mild cigarettes is deceptive because it conveys a false and misleading message that those cigarettes are less harmful than regular cigarettes. Although the claim arises from health concerns, it does not seek compensation for personal injury. Instead it seeks compensation for amounts spent on 'light and mild' products and a disgorgement of profits from Imperial. The motion of the federal government to strike out the third party notice issued against them by Imperial was heard in February 2006 and was granted but was appealed by Imperial and the appeal was heard in June 2009 in conjunction with the British Columbia medical reimbursement. The Court of Appeal went so far as to say that it was not "plain and obvious" that the federal government did not owe a duty of care to manufacturers or indeed to the class itself. Therefore, the government of Canada faces potential liability to claims of product liability or misrepresentation. The government has appealed this decision and the appeal will be heard on 24 February 2011.

On 9 December 2009, Imperial was served with a class action filed by Ontario tobacco farmers and the Provincial Marketing Board. The plaintiffs allege that, during the timeframe, the companies improperly paid lower prices for tobacco leaf destined for duty-free products, as opposed to the higher domestic leaf price. Imperial deposited the amount owing to the government of Ontario pursuant to the Comprehensive Agreement into an escrow account, as Imperial believes that the Growers' claim could fall within the definition of a released claim according to the Comprehensive Agreement. In response, the Ontario government filed an action against Imperial, seeking a declaration to the effect that the Growers' action is valid in its own right, and that it is not a Released Claim. No monetary damages are being claimed against Imperial by the government of Ontario.

On 26 July 2010, Imperial argued its preliminary motion in the Ontario claim. Imperial was successful in its application and the court ordered that the Ontario claim be stayed in favour of the arbitration provisions stipulated in the Comprehensive Agreement and raised by Imperial in its Notice of Arbitration. The Province of Ontario has appealed this decision but no hearing date has been set.

There are currently two class actions in Quebec. On 21 February 2005, the Quebec Superior Court granted certification in two class actions against Imperial and two domestic manufacturers, which have a combined value of C\$22 billion plus interest and costs. The court certified two classes, which include residents of Quebec who suffered from lung, throat and laryngeal cancer or emphysema, and residents who were addicted to nicotine at the time the proceedings were filed and who have since remained addicted. In Quebec, there is no right of appeal for a defendant upon certification. The plaintiffs have served a Statement of Claim. Trial in this matter has been set for 17 October 2011 and discovery is currently under way.

In June 2009, four new smoking and health class actions were filed in Nova Scotia, Manitoba, Saskatchewan and Alberta, against Canadian manufacturers and foreign companies, including the UK Companies and Imperial. In June 2010, two further suits were filed in British Columbia. Proceedings in these smoking and health class actions have also been served on Imperial. A jurisdiction motion has

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been filed in British Columbia. In Saskatchewan, a number of UK companies have been released from the action. In Nova Scotia the proceedings have not progressed. There are service issues in relation to the UK Companies for Alberta and Manitoba.

Israel

In May 2008, a 'lights' class action was brought in Israel against a number of parties including British American Tobacco's distributor, which was dismissed on 16 May 2010. The plaintiff's time to appeal that order has expired.

Venezuela

The Venezuelan Federation of Associations of Users and Consumers filed a class action against the Venezuelan government seeking regulatory controls on tobacco and recovery of medical expenses for future expenses of treating smoking-related illnesses in Venezuela. On 19 January 2009, C.A Cigarrera Bigott Sucs. (Cigarrera Bigott) notified the court of its intention to appear as a third party. The court adjourned a public hearing, initially scheduled for 28 July 2009, where Cigarrera Bigott's status as a third party would be determined and parties would present evidence and make arguments. On 16 September 2009, the Venezuelan Republic ordered the court to continue the judicial process. A new date has yet to be scheduled by the court.

(c) Individual personal injury claims

Aside from the US there are approximately 353 individual smoking cases pending world-wide as at 31 December 2010 against Group companies that are not detailed here. Over three-quarters of these cases are in Brazil.

At 31 December 2010, there were only five (2009: approximately 634) individual 'lights' cases in Italy pending against British American Tobacco Italia S.p.A before the justice of the peace courts. As at 31 October 2010, approximately 4,390 cases had been withdrawn, suspended or resulted in decisions given in favour of British American Tobacco Italia S.p.A. There are 34 smoking and health cases pending before Italian civil courts, filed by or on behalf of individuals in which it is contended that diseases or deaths have been caused by cigarette smoking. There are two labour cases for alleged occupational exposure pending in Italy. There are also seven smoking and health cases and two labour cases on appeal related to the same decision but based on different grounds (Serafini case).

In 2008, three individual smoking and health actions were brought against British American Tobacco Finland Oy, collectively seeking a total of approximately €349,329 plus interest in damages for smoking related diseases. On 10 October 2008, the Helsinki District Court dismissed the plaintiffs' claims in their entirety. Two of the original plaintiffs have appealed the respective judgments of the District Court. A joint de novo trial of the appeals was heard on 31 August 2009 before the Helsinki Court of Appeal. These appeals were dismissed. A further appeal to the Supreme Court was withdrawn on 9 November 2010. The parties agreed to bear their own costs.

Conclusion

While it is impossible to be certain of the outcome of any particular case or of the amount of any possible adverse verdict, the Group believes that the defences of the Group's companies to all these various claims are meritorious on both the law and the facts, and a vigorous defence is being made everywhere. If an adverse judgment is entered against any of the Group's companies in any case, an appeal will be made. Such appeals could require the appellants to post appeal bonds or substitute security in amounts which could in some cases equal or exceed the amount of the judgment. In any event, with regard to US litigation, the Group has the benefit of the RJRT Indemnification. At least in the aggregate, and despite the quality of defences available to the Group, it is not impossible that the Group's results of operations or cash flows in particular quarterly or annual periods could be materially affected by this and by the final outcome of any particular litigation.

Having regard to all these matters, the Group (i) does not consider it appropriate to make any provision in respect of any pending litigation and (ii) does not believe that the ultimate outcome of this litigation will significantly impair the Group's financial condition.

RELATED PARTY DISCLOSURES

The Group's related party transactions and relationships for 2010 and 2009 are disclosed as Appendix 3 to this announcement.

RESUMPTION OF THE SHARE BUY-BACK PROGRAMME

At the beginning of 2009, the Board suspended the Group's on-market share buy-back programme for the time being, in order to preserve the Group's financial flexibility during the period of economic uncertainty. Consequently, in the year ended 31 December 2010, no shares were bought back (2009: none). The Board has approved the resumption of the on-market share buy-back programme in 2011 with a value of up to £750 million, excluding costs.

POST BALANCE SHEET EVENTS

Disposal of a business by an associate company

On 14 January 2011, Reynolds American Inc. (RAI), announced that it had reached an agreement to sell Lane Limited to Scandinavian Tobacco Group A/S (STG). Under the terms of the transaction, STG has agreed to pay US\$205 million in cash for Lane. Lane manufactures other tobacco products and contributes approximately US\$0.04 per share to RAI's annual earnings which equates to earnings of US\$10 million (£6 million) for the Group. The Group disposed of Lane Limited to RAI in 2004. The transaction is expected to close in the first half of 2011, pending anti-trust review and approval.

ANNUAL REPORT

The financial information set out above does not constitute the Company's statutory accounts for the years ended 31 December 2010 or 2009. Statutory accounts for 2009 have been delivered to the Registrar of Companies and those for 2010 will be delivered following the Company's Annual General Meeting. The auditor's reports on both the 2009 and 2010 accounts were unqualified, did not draw attention to any matters by way of emphasis and did not contain statements under s498(2) or (3) of Companies Act 2006 or equivalent preceding legislation.

The Annual Report will be published on www.bat.com on 28 March 2011. At that time, a printed copy will be mailed to shareholders on the UK main register who have elected to receive it. Otherwise, such shareholders will be notified that the Annual Report is available on the website and will, at the time of that notification, receive a Performance Summary (which sets out an overview of the Group's performance, headline facts and figures and key dates in the Company's financial calendar) together with a Proxy Form and Notice of Annual General Meeting. Specific local mailing and/or notification requirements will apply to shareholders on the South African branch register.

SHAREHOLDER INFORMATION

FINANCIAL CALENDAR 2011

28 April	Interim Management Statement
28 April	Annual General Meeting The Mermaid Conference & Events Centre London EC4V 3DB
27 July	Half-Yearly Report
26 October	Interim Management Statement

CALENDAR FOR THE FINAL DIVIDEND 2010

2011

24 February	Dividend announced (including amount of dividend per share in both sterling and rand; applicable exchange rate and conversion date)
4 March	Last day to trade (JSE)
7 March to 11 March	No transfers between UK main register and South African branch register; no shares may be dematerialised or rematerialised.
7 March	Ex-dividend date (JSE)
9 March	Ex-dividend date (LSE)
11 March	Record date (LSE and JSE)
5 May	Payment date (sterling and rand)

Details of the applicable exchange rate can be found under the heading 'Dividends' above.

For holders of American Depositary Receipts (ADRs), the record date is also 11 March 2011 with an ADR payment date of 10 May 2011.

For the Dividend Reinvestment Plan (DRIP), the last date for elections is 8 April 2011.

CORPORATE INFORMATION

Premium listing

London Stock Exchange (Share Code: BATS; ISIN: GB0002875804)

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share dealing: www.computershare.com/dealing/uk
web-based enquiries: www.investorcentre.co.uk/contactus

Corporate information cont...

Secondary listing

JSE (Share Code: BTI)

Shares are traded in electronic form only and transactions settled electronically through Strate

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PO Box 61051, Marshalltown 2107, South Africa

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e-mail enquiries: web.queries@computershare.co.za

American Depositary Receipts (ADRs)

NYSE Amex Equities (Symbol: BTI; CUSIP No. 110448107)

Sponsored ADR programme; each ADR represents two ordinary shares of British American Tobacco p.l.c.

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British American Tobacco Publications

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DISCLAIMERS

This announcement does not constitute an invitation to underwrite, subscribe for, or otherwise acquire or dispose of any British American Tobacco p.l.c. shares or other securities.

This announcement contains certain forward looking statements which are subject to risk factors associated with, among other things, the economic and business circumstances occurring from time to time in the countries and markets in which the Group operates. It is believed that the expectations reflected in this announcement are reasonable but they may be affected by a wide range of variables which could cause actual results to differ materially from those currently anticipated.

Past performance is no guide to future performance and persons needing advice should consult an independent financial adviser.

DISTRIBUTION OF ANNOUNCEMENT

This announcement is released to the London Stock Exchange and the JSE Limited. It may be viewed and downloaded from our website www.bat.com

Copies of this announcement may also be obtained during normal business hours from (1) the Company's registered office; (2) the Company's representative office in South Africa; and (3) British American Tobacco Publications, as above.

Nicola Snook
Secretary
23 February 2011

ANALYSIS OF REVENUE AND PROFIT FROM OPERATIONS

REVENUE

	2010					2009		
	Reported revenue £m	Impact of exchange £m	Revenue at CC ⁽¹⁾ £m	Organic adjust- ments ⁽³⁾ £m	Organic revenue at CC ⁽¹⁾ £m	Reported revenue £m	Organic adjust- ments ⁽³⁾ £m	Organic revenue £m
Asia-Pacific	3,759	311	3,448	(112)	3,336	3,270	-	3,270
Americas	3,498	296	3,202	(117)	3,085	3,156	(170)	2,986
Western Europe	3,419	(67)	3,486	(220)	3,266	3,884	(594)	3,290
Eastern Europe	1,686	(40)	1,726	-	1,726	1,628	-	1,628
Africa and Middle East	2,521	120	2,401	-	2,401	2,270	-	2,270
Total	14,883	620	14,263	(449)	13,814	14,208	(764)	13,444

PROFIT FROM OPERATIONS

	2010							2009		
	Profit ⁽²⁾ £m	Adjusting items £m	Adjusted Profit ⁽²⁾ £m	Impact of exchange £m	Adjusted Profit ⁽²⁾ at CC ⁽¹⁾ £m	Organic adjust- ments ⁽³⁾ £m	Adjusted Profit ⁽²⁾ at CC ⁽¹⁾ £m	Adjusted Profit ⁽²⁾ £m	Organic adjust- ments ⁽³⁾ £m	Adjusted Profit ⁽²⁾ £m
Asia-Pacific	1,276	(56)	1,332	137	1,195	(19)	1,176	1,148	-	1,148
Americas	1,346	(36)	1,382	134	1,248	(3)	1,245	1,186	(6)	1,180
Western Europe	818	(236)	1,054	(27)	1,081	(1)	1,080	994	(15)	979
Eastern Europe	358	-	358	(70)	428	-	428	409	-	409
Africa and Middle East	520	(338)	858	65	793	-	793	724	-	724
Total	4,318	(666)	4,984	239	4,745	(23)	4,722	4,461	(21)	4,440

Notes:

(1) CC: Constant currencies

(2) Profit: Profit from operations

(3) Organic adjustments: Mergers and acquisitions and discontinued activities - adjustments are made to the 2009 and 2010 numbers, based on the 2010 Group position

KEY GROUP RISK FACTORS

This section identifies the main risk factors that may affect the British American Tobacco Group's finances and operations.

The following table provides a brief description of the key risks to which the Group's operations are exposed and identifies, in each case, their potential impact on the Group and the principal activities in place to manage the risk. Each risk is considered in the context of the Group strategy by identifying the principal strategic element to which it relates, although other elements may also be relevant.

It is not the intention to provide an extensive analysis of all risks affecting the Group. Not all of the factors listed are within the control of the Group and other factors besides those listed may affect the performance of its businesses. Some risks may be unknown at present and other risks, currently regarded as immaterial, could turn out to be material in the future.

This section should also be read in the context of the cautionary statement regarding forward-looking statements on page 56.

Risk registers are used at Group, regional, area and individual market levels. They are based on a standardised methodology, which was updated during 2010 to include information on prevailing trends in relation to each risk and to simplify and standardise the analysis of their impact and likelihood, which are now assessed at three levels (high/medium/low), instead of four previously. The Group risk register provides the basis for the assessment of the key Group risk factors identified below. It is reviewed by the Audit Committee twice yearly and one or more key risks are considered in detail at each Audit Committee meeting. The Board reviews the Group risk register annually.

The number of risks identified in this section has been reduced in comparison with previous years. This reflects both the updated risk management methodology and the Board's continuing reappraisal of Group risks. It also ensures that the list identifies only those risks and uncertainties that the Directors believe to be the principal ones facing the business, consistent with the guidance issued recently by the Financial Reporting Review Panel.

Illicit trade

Competition from Illicit trade

Illicit trade in the form of counterfeit products, smuggled genuine products and locally manufactured products on which applicable taxes are evaded, represents a significant and growing threat to the legitimate tobacco industry. Increasing excise rates can encourage more consumers to switch to illegal cheaper tobacco products and provide greater rewards for smugglers. The risk is exacerbated where current economic conditions have resulted in high unemployment and/or reduced disposable incomes.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Sudden and disproportionate excise increases and widening excise differentials between markets.
- Ineffective regulatory environment.
- Economic downturn.
- Lack of law enforcement and weak border controls.

Potential impact on Group

- Erosion of brand equity.
- Reduced ability to take price increases.
- Investment in trade marketing and distribution is undermined.
- Product is commoditised.
- Lower volumes and reduced profits.

Principal activities in place to address risk

- Dedicated Anti-Illicit Trade (AIT) teams operating at global, regional, area and key market levels.

Key Group risk factors cont...

- Active engagement with key stakeholders.
- Global AIT strategy development supported by a research programme to further the understanding of the size and scope of the problem.
- AIT Intelligence Unit (including a dedicated analytical laboratory) cooperates with law enforcement agencies in pursuit of priority targets and capacity building.
- Strong internal business conduct and customer approval policies.

Excise and tax

Excise shocks from tax rate increases or structure changes

Tobacco products are subject to substantial excise and sales taxes in most countries in which the Group operates. In many of these countries, taxes are generally increasing but the rate of increase varies between countries and between different types of tobacco products.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Government initiatives to raise revenues.
- Increases advocated within context of national health policies.
- Insufficient capacity to engage with stakeholders in meaningful dialogue

Potential impact on Group

- Consumers reject the Group's legitimate tax-paid products for products from illicit sources.
- Reduced sales volume or alteration of sales mix.

Principal activities in place to address risk

- Requirement for Group companies to have in place formal pricing and excise strategies including contingency plans.
- Pricing and excise committees at regional, area and individual market levels.
- Engagement with local tax and customs authorities where appropriate.
- Annual management review of brand portfolio, brand health and equity.

Onerous disputed taxes, interest and penalties

Principal relevance to Group strategy: Potential impact on **Productivity** (capital effectiveness)

Principal potential causes

- Non-filing or late filing of tax returns or incorrect filings.
- Non-payment or late payments of taxes.
- Unfavourable ruling by tax authorities in disputed areas and aggressive auditing and/or pursuit of tax claims.

Potential impact on Group

- Significant fines and penalties.
- Disruption and loss of focus on the business due to diversion of management time.
- Impact on profit and dividend.

Principal activities in place to address risk

- Tax committees.
- Specialist resources available internally to provide advice and guidance and external advice sought where appropriate.

Financial

The Group's underlying operations give rise to certain financial risks. The principal risks in this regard, and the controls in place to address them, are identified below and further details of the Group's financial management and treasury operations can be found within the Financial review.

Management of cost base

The Group continues to implement measures to reduce its overall cost base. There is a risk that targeted reductions will not be achieved and/or that productivity programmes do not achieve their objectives.

Principal relevance to Group strategy: Potential impact on **Productivity** (cost management)

Principal potential causes

- Insufficient resources devoted to productivity programmes due to other priorities.
- Low prioritisation or resistance to change to overhead focus and targets.

Potential impact on Group

- Inability to manage cost savings leads to lower profits and reduced funds for investment in long term growth.
- Reduced shareholder confidence.

Principal controls in place to address risk

- Programme in place to achieve costs savings of £800 million by 2012.
- Development of a formal structure to integrate, drive and orchestrate the delivery of productivity programmes by providing visibility, establishing targets and enabling benefits tracking.
- Regular tracking of actual productivity savings and forecast improvements in operating margin and supply chain, overheads and indirects projects.

Translational foreign exchange rate exposures

The Group faces translational foreign exchange (FX) rate exposures for earnings/cash flows from its global business.

Principal relevance to Group strategy: Potential impact on **Productivity** (capital effectiveness)

Principal potential causes

- FX rate exposures arise from exchange rate movements against sterling, the Group's reporting currency.

Potential impact on Group

- Fluctuations in translational FX rates of key currencies against sterling introduce volatility in reported results.

Principal activities in place to address risk

- While translational FX exposure is not hedged, its impact is identified in results presentations and financial disclosures and earnings are restated at constant rates for comparability.
- Debt and interest are matched to assets and cash flows to mitigate volatility where possible.

Marketplace

The Group has substantial operations in over 180 countries. Its results are influenced by the economic, regulatory and political situations in the countries and regions in which it has operations, as well as by the actions of competitors.

Inability to obtain required price increases

To the extent that price increases are required to cover cost rises and deliver profit growth, there is a risk that the Group will be unable to achieve these.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Changes in the global economy reduce consumers' disposable income.
- Consumer down-trading.
- Competitors seek volume growth by price discounts or by not taking full price increases.

Potential impact on Group

- Reduction in volumes.
- Profit growth in the short term falls below shareholders' expectations.
- Reduction in funds for investment in long-term growth.

Principal activities in place to address risk

- Regular regional and management reviews of budgeted pricing scenarios.
- Pricing and excise committees at regional, area and individual market levels.
- Routine brand price trade-off exercises conducted in key markets.

Key Group risk factors cont...

- Competitor analysis and price war simulations.

Geopolitical tensions

Geopolitical tensions, including terrorism have the potential to disrupt the Group's business operations.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Regional and/or global conflicts.
- Terrorism and political violence.
- Violent organised crime.
- The implementation of trade sanctions.
- Economic policy changes, including nationalisation of assets and withdrawal from international and bilateral trade agreements.

Potential impact on Group

- Potential loss of life, loss of assets and disruption to normal business processes.
- Increased costs due to more complex supply chain arrangements and/or the cost of building new facilities or maintaining inefficient facilities.
- Reduced volumes and impact on profits.
- Reputational impact of inability to protect staff and assets from serious harm.

Principal activities in place to address risk

- Globally integrated sourcing strategy and contingency sourcing arrangements.
- Security risk modelling, including external risk assessments and the monitoring of geopolitical and economic policy developments world wide.
- Insurance cover and business continuity planning, including scenario planning and testing and risk awareness training.
- Security controls for field force, direct store sales, supply chain, with an emphasis on the protection of Group employees.

Major impact of climate change

Climatic instability and degradation may lead to loss of traditional growing areas, relocation of office/factory sites, and supply chain disruption.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Increased production of CO₂ and other greenhouse gases as a result of human activity.
- Alteration of the earth's global energy.
- Changes in ocean circulation or atmospheric composition.
- Natural disasters.

Potential impact on Group

- Loss of major leaf growing area, market and/or major transportation facilities, including ports.
- Inability to obtain adequate supply of leaf and other production materials.
- Scarcity of skilled staff due to population migration.
- Potential loss of market share to competitors with changes in the geographical footprint.

Principal activities in place to address risk

- Group-wide sales and operational planning, including a globally integrated sourcing strategy and contingency sourcing arrangements.
- Group-wide environmental risk modelling and supporting insurance to cover financial exposure.
- Biodiversity risk and opportunity assessments specific to leaf growing areas.
- Sustainability implementation plan covering the management and reduction of the Group's impact on natural resources and CO₂ generation.
- Research and development, including on drought-resistant tobacco types.

Legal and compliance

Breach of legal and contractual obligations

Key Group risk factors cont...

Non-compliance with any of the laws applicable to group companies that could expose the Group to liabilities and reputational risks.

Principal relevance to Group strategy: Potential impact on **Productivity** (capital effectiveness)

Principal potential causes

- Lack of understanding of applicable national and international laws and legal principles.
- Lack of understanding of contractual obligations or inconsistent contractual risks and assumptions.
- Dependency on third parties.

Potential impact on Group

- Unfavourable outcome or settlement of pending or future litigation.
- Material impact on consolidated results of operations, cash flows and financial position in a particular fiscal quarter or fiscal year.

Principal activities in place to address risk

- Comprehensive policies and procedures to promote legal compliance.
- Development of template contracts and standard provisions.
- Specialist resources available internally to provide advice and guidance and external advice sought where appropriate.

Regulation

The Group's businesses operate under increasingly stringent regulatory regimes around the world. Further regulation is expected, particularly as a result of the World Health Organisation's Framework Convention on Tobacco Control (FCTC) and, increasingly, active tobacco control activities outside the FCTC.

Regulation risks covering: packaging and labelling; advertising and promotion; design, contents and emissions of products; testing and measuring; and public place smoking.

Strict and restrictive regulation in these areas may impair the Group's ability to communicate with adult smokers and/or to meet consumer expectations and may also impact on its ability to communicate with its corporate stakeholders. In addition, increased regulation may lead to increased operating costs and reduced sales.

Principal relevance to Group strategy: Potential impact on **Growth** (organic revenue growth)

Principal potential causes

- Strict adoption of FCTC guidelines.
- Adoption of more stringent national regulations, such as point of sale display bans and plain packaging.
- Adoption of differing regulatory regimes in different countries/groups of countries and/or lack of consensus on interpretation/application.

Potential impact on Group

- Cost complexity of meeting regulations.
- Generic or plain packaging leads to loss of brand equity.
- Reduced ability to communicate brand portfolio and innovations, contributing to an increase in illicit trade.
- Contribution to the denormalisation of smoking.
- Reduced consumer acceptability of new product specifications, leading to loss of volume.
- Loss of reputation, penalties and closure of production as a result of non-compliance.

Principal activities in place to address risk

- Group companies have regulatory strategies in place in order to identify issues material to their operating environment and develop plans to address them in a manner consistent with local law and Group policy.
- Engagement is sought with scientific and regulatory communities and stakeholder engagement takes place at global, regional and individual market levels.
- Global monitoring of regulatory trends and developments and analysis of regulatory proposals to determine impacts, if any, on business.

Key Group risk factors cont...

- Development of dedicated technical and advocacy capabilities, corporate positions and best practice examples, supported by training, for markets to address regulation.
- Development of strategies and capabilities to develop and launch competitive, consumer-acceptable, fit-for-purpose products and new product initiatives within the changing regulatory environment.

Regulations are passed without the voice of the industry being taken into account

There is a risk that industry participation in the regulation discussion is reduced due to inability to engage with authorities and put its points across effectively.

Principal relevance to Group strategy: Potential impact on **Responsibility** (balanced regulation)

Principal potential causes

- Stringent adoption of FCTC guidelines on industry participation.
- National governments fail to take into account the views of tobacco industry
- The Group's advocacy of balanced regulation is not considered when regulation is formulated.

Potential impact on Group

- Exclusion of industry from participating in engagement with regulators and policy makers.
- Increased cost of business for legitimate industry, lower turnover and reduced profits
- Diminished shareholder confidence leading to a reduced share price.

Principal activities in place to address risk

- Continued social dialogue.
- Regulatory and stakeholder engagement at global, regional and individual market levels, including the promotion of best practice in the formulation of regulation.

Data risks

Loss of confidential information or malicious manipulation of data

The loss or misuse of sensitive information, or its disclosure to outsiders, including competitors and trading partners, could potentially have a significant adverse impact on the Group's business operations and/or give rise to legal liability.

Principal relevance to Group strategy: Potential impact on **Productivity** (cost management)

Principal potential causes

- Inadequate controls regarding the creation, storage and sharing of confidential information.
- Inadequate access controls to key systems and data.

Potential impact on Group

- Loss of revenue and/or profit due to use of inaccurate data, loss of trade secrets and/or competitors gaining advantage.
- Increased costs in restoring lost data and/or reversing inaccurate transactions.
- Regulatory action, civil action and/or criminal prosecution for breach of legal obligations.
- Damage to corporate reputation and loss of shareholder confidence.
- Negative impact on share price.

Principal activities in place to address risk

- Information technology controls.
- Established information security and information technology policies and procedures.
- Promotion of awareness and understanding of information security issues.

As noted in the introduction to this section, as a result of the Group's updated risk management methodology and in consequence of the Board's continuing reappraisal of Group risks, a number of risks previously considered as key Group risks are no longer assessed as such in terms of their impact and likelihood, and so are not addressed in the table above. Nevertheless, they remain on the Group risk register and continued to be reviewed in accordance with the Group's risk management procedures. They include:

- Liquidity risk, including capital structure and leverage;
- Transactional foreign exchange exposures;
- Financial counterparty risks;

Key Group risk factors cont...

- Wrongly valued acquisition opportunities;
- Retirement benefits;
- Economic crisis impact on secondary supply chain;
- Trading performance in key markets;
- Loss of a smoking and health-related court case; and
- Disruption to the Group's information technology systems.

Cautionary statement

The Business Review and certain other sections of this document contain forward-looking statements which are subject to risk factors associated with, among other things, the economic and business circumstances occurring from time to time in the countries and markets in which the Group operates. It is believed that the expectations reflected in these statements are reasonable but they may be affected by a wide range of variables which could cause actual results to differ materially from those currently anticipated.

RELATED PARTY DISCLOSURES

The Group has a number of transactions and relationships with related parties, as defined in IAS 24 (Related Party Disclosures), all of which are undertaken in the normal course of business.

Transactions and balances with associates relate mainly to the sale and purchase of cigarettes and tobacco leaf. Amounts receivable from associates in respect of dividends included in the table below were £77 million (2009: £68 million). The Group's share of dividends from associates was £466 million (2009: £331 million). Legal fees recovered from Reynolds American Inc. included in other net income amounted to £1 million (2009: £nil).

	2010	2009
	£m	£m
Transactions		
- revenue	38	47
- purchases	(442)	(365)
- other net income	460	329
Amounts receivable at 31 December	99	78
Amounts payable at 31 December	(21)	(34)

On 26 May 2010, a wholly owned subsidiary of the Group, BATUS Japan Inc., entered into an American blend Cigarette Manufacturing Agreement (referred to as the 2010 Agreement) with a wholly owned subsidiary of Reynolds American, R.J. Reynolds Tobacco Company (referred to as RJRTC), with an effective date of 1 January 2010. Under this Agreement, RJRTC has been appointed BATUS Japan's exclusive manufacturer of all BATUS Japan's requirements for certain American-blend cigarettes intended to be distributed and sold in Japan for the five year period expiring on 31 December 2014, subject to the early termination and extension provisions set out in the agreement. The 2010 Agreement is based on arm's length terms and conditions.

On the same date, RJRTC and BATUS Japan entered into a letter agreement terminating the existing Contact Manufacturing Agreement dated 30 July 2004 (referred to as the 2004 Agreement), as amended between the parties, with effect from midnight on 31 December 2009. The 2004 Agreement was scheduled to expire on 31 December 2014, subject to early termination and extension provisions. Under the terms of the letter agreement, certain sections and sub-sections of the 2004 Agreement will survive the termination, and, in consideration for RJRTC agreeing to terminate the agreement and in settlement of all disputes at issue between the parties, BATUS Japan agreed to pay RJRTC US\$21 million. The payment has been presented as an adjusting item and is included within the Group's restructuring and integration costs on page 28. The Group's share of the income net of tax included within the post-tax results of Reynolds American is also presented as an adjusting item and is credited against restructuring costs (see page 30).

In 2010, the Group acquired non-controlling interests of shareholders in Indonesia and Eastern Europe for £3 million and £9 million respectively. These transactions are shown as a £12 million reduction to reserves.

The Group sold its Belgian distribution business, Lyfra NV, to Landewyck Group S.a.r.l in 2010 for a consideration of €16 million. The Group's German subsidiary has an available-for-sale investment in Landewyck Group S.a.r.l.

A capital injection was made into BAT Algeria in 2009 where a shareholder SOCALTA (Societe Algerienne de Trading Alimentaire) contributed £16 million. This contribution by a non-controlling interest was assisted by a loan from another Group subsidiary of £4 million.

Related party disclosures cont...

The key management personnel of British American Tobacco consist of the members of the Board of Directors of British American Tobacco p.l.c. and the members of the Management Board. No such person had any material interest during the year in a contract of significance (other than a service contract) with the Company or any subsidiary company. The term key management personnel in this context includes the respective members of their households.

	2010 £m	2009 £m
The total compensation for key management personnel, including Directors, was:		
- salaries and other short term employee benefits	22	18
- post-employment benefits	3	3
- share based payments	12	9
	<u>37</u>	<u>30</u>

There were no other long term benefits applicable in respect of key personnel other than those disclosed in the Remuneration Report in the Annual Report.