Agenda of
Annual General Meeting of Shareholders
for the 29th Fiscal Year

Date: 10:00 a.m. on Friday, 18th March, 2016 (Korea Standard Time)

Place: Vision Hall of Human Resources Development Institute of KT&G Corporation located at 71, Beotkkok-Gil, Daedeok-gu, Daejeon-si, Rep. of Korea

KT&G Corporation

Matters Requiring Resolution

I. Approval of Financial Statements(Consolidated and Separate) and Statements of Appropriation of Retained Earnings for the 29th Fiscal Year

II. Amendment of Articles of Incorporation

III. Appointment of (Four)Members of Board of Directors

III-1. Appointment of Independent Non-Executive Director(Ko, Sang-Kon)

III-2. Appointment of Independent Non-Executive Director(Youn, Hai-Su)

III-3. Appointment of Independent Non-Executive Director(Lee, Eun-Kyung)

III-4. Appointment of Inside Director(Kim, Heung-Ryul)

IV. Appointment of (Two) Members of the Audit Committee

IV-1. Appointment of Member of the Audit Committee (Ko, Sang-Kon)

IV-2. Appointment of Member of the Audit Committee(Lee, Eun-Kyung)

V. Approval of Annual Cap on Directors' Remuneration

I. Agendum No. 1

Approval of Financial Statements(Consolidated and Separate) and Statement of Appropriation of Retained Earnings for the 29th Fiscal Year

Pursuant to Article 449 of the Korean Commercial Code and Article 41 of the Articles of Incorporation of the Company, the Consolidated and Separate Financial Statements and Statement of Appropriation of Retained Earnings for the 29th Fiscal Year (2015. 1. 1 ~ 2015. 12. 31) are required to be approved.

(The financial statements below are audited by the Independent Auditor with opinion of 'unqualified' and the audit report was filed on Feb. 25th, 2016)

1. Consolidated Financial Statements

1) Consolidated Statements of Financial Position(Consolidated Balance Sheet)

29th Fiscal Year: As of December 31, 2015
28th Fiscal Year: As of December 31, 2014

□ Assets

KT&G Corporation and Subsidiaries

(Unit: billion KRW, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
1. Total non-current assets	**3,102.5**	**3,010.1**	**92.4**	**3.1**
1) Property, plant and equipment	1,789.8	1,753.4	36.4	2.1
2) Intangible assets	105.4	154.9	-49.5	-32.0
3) Long term trade and other receivables	75.1	86.7	-11.6	-13.4
4) Investment property	164.5	168.0	-3.5	-2.1
5) Equity accounted investment	51.5	57.9	-6.4	-11.1
6) Available-for-sale financial assets	364.7	325.8	38.9	11.9
7) Other financial assets	0.0	0.3	-0.3	-100.0
8) Long term deposits	404.0	301.8	102.2	33.9
9) Long term prepaid expenses	7.1	4.7	2.4	51.1
10) Long term advance payments	107.7	127.9	-20.2	-15.8
11) Deferred income tax asset	32.7	28.7	4.0	13.9
2. Total current assets	**5,564.2**	**4,408.2**	**1,156.0**	**26.2**
1) Inventories	2,119.1	1,982.5	136.6	6.9
2) Trade and other receivables	1,217.9	989.8	228.1	23.0
3) Other financial assets	1,136.9	668.4	468.5	70.1
4) Prepaid tobacco excise and other taxes	447.8	260.8	187.0	71.7
5) Current Available-for-sale financial assets	0.0	1.0	-1.0	-100.0
6) Advance payments	75.7	68.5	7.2	10.5
7) Prepaid expenses	20.6	20.8	-0.2	-1.0
8) Cash and cash equivalents	546.2	416.4	129.8	31.2
3. Non-current asset held for sale	**6.7**	**0.4**	**6.3**	**1,575.0**
Total assets	**8,673.4**	**7,418.7**	**1,254.7**	**16.9**

□ Equities and liabilities

KT&G Corporation and Subsidiaries

(Unit: billion KRW, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
Total equities	**6,275.5**	**5,708.1**	**567.4**	**9.9**
1. Capital stock	955.0	955.0	0.0	0.0
2. Treasury shares	-337.1	-339.1	2.0	-
3. Gain on reissuance of treasury shares	494.6	492.0	2.6	0.5
4. Other capital surplus	-9.9	-4.5	-5.4	-
5. Reserves	3,704.3	3,426.3	278.0	8.1
6. Retained earnings	1,402.0	1,100.9	301.1	27.4
7. Non-controlling interests	66.6	77.5	-10.9	-14.1
Total liabilities	**2,397.9**	**1,710.6**	**687.3**	**40.2**
1. Total non-current liabilities	**526.2**	**586.0**	**-59.8**	**-10.2**
1) Long term borrowing	102.3	137.8	-35.5	-25.8
2) Long term trade and other payables	13.6	32.2	-18.6	-57.8
3) Long term advance receipts	10.4	14.6	-4.2	-28.8
4) Provision for other liabilities and charges	2.8	2.9	-0.1	-3.4
5) Defined benefit liabilities	120.6	132.2	-11.6	-8.8
6) Deferred income tax liabilities	276.5	266.3	10.2	3.8
2. Total current liabilities	**1,871.7**	**1,124.6**	**747.1**	**66.4**
1) Trade and other payables	606.4	503.9	102.5	20.3
2) Short term borrowings	206.4	141.9	64.5	45.5
3) Advance receipts	28.6	37.5	-8.9	-23.7
4) Current portion of long term borrowings	27.7	1.2	26.5	2,208.3
5) Other financial liabilities	0.0	0.0	0.0	-
6) Income taxes payable	224.8	180.8	44.0	24.3
7) Tobacco excise and other taxes payables	777.8	259.3	518.5	200.0
Total equities and liabilities	**8,673.4**	**7,418.7**	**1,254.7**	**16.9**

2) Consolidated Statements of Comprehensive Income
(Consolidated Income Statements)

29th Fiscal Year: From January 1, 2015 to December 31, 2015

28th Fiscal Year: From January 1, 2014 to December 31, 2014

KT&G Corporation and Subsidiaries

(Unit: billion Won, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
1.Sales	**4,169.8**	**4,112.9**	**56.9**	**1.4**
1) Manufactured cigarettes	2,751.5	2,812.4	-60.9	-2.2
2) Red ginseng	942.3	820.7	121.6	14.8
3) Pharmaceuticals	159.0	158.1	0.9	0.6
4) Real estate	136.7	154.2	-17.5	-11.3
5) Others	180.3	167.5	12.8	7.6
2.Cost of sales	**1,630.6**	**1,840.9**	**-210.3**	**-11.4**
1) Manufactured cigarettes	896.4	1,160.2	-263.8	-22.7
2) Red ginseng	448.3	391.7	56.6	14.4
3) Pharmaceuticals	95.8	98.1	-2.3	-2.3
4) Real estate	85.3	96.6	-11.3	-11.7
5) Others	104.8	94.3	10.5	11.1
3. Gross profit	**2,539.2**	**2,272.0**	**267.2**	**11.8**
4. Selling and Administration Expenses	**1,173.3**	**1,100.1**	**73.2**	**6.7**
5. Profit from operations	**1,365.9**	**1,171.9**	**194.0**	**16.6**
6. Net other income	**-41.4**	**-61.3**	**19.9**	**-**
7. Net finance income	**74.8**	**44.1**	**30.7**	**69.6**
8. Net income from jointly controlled entities and associates	**15.1**	**3.2**	**11.9**	**371.9**
9. Profit before income taxes	**1,414.4**	**1,157.9**	**256.5**	**22.2**
10. Income tax expense	**382.2**	**344.1**	**38.1**	**11.1**
11. Profit for the period	**1,032.2**	**813.8**	**218.4**	**26.8**
12. Earnings per share	**8,222 KRW**	**6,558 KRW**		
13. Other comprehensive income for the period	**-30.8**	**-68.4**	**37.6**	**-**
14. Total comprehensive income for the period	**1,001.4**	**745.4**	**256.0**	**34.3**

3) Consolidated Statements of Change in Equity

KT&G Corporation and Subsidiaries

(Unit: billion Won)

	Capital stock	Other capital Surplus	Treasury Shares	Gain on Reissuance of Treasury Shares	Reserve	Retained Earnings	Controlling Interest	Non-controlling Interest	Total Equity
Ⅰ. 2014. 1. 1	955.0	-4.5	-339.1	492.0	3,368.8	802.8	5,275.0	90.5	5,365.5
Comprehensive income									
Profit for the period						825.6	825.6	-11.8	813.8
Other comprehensive income					-47.0	-20.1	-67.1	-1.3	-68.4
Total comprehensive income					-47.0	805.5	758.5	-13.1	745.4
Transaction with equity holders of the Company									
Cash Dividend						-402.9	-402.9		-402.9
Other Reserve					152.0	-152.0			
Reserve for research and human resources development					-47.5	47.5			
Granting for Right of Stock Option								0.1	0.1
Total transaction with equity holders of the Company					104.5	-507.4	-402.9	0.1	-402.8
Ⅱ. 2014. 12. 31	**955.0**	**-4.5**	**-339.1**	**492.0**	**3,426.3**	**1,100.9**	**5,630.6**	**77.5**	**5,708.1**

(Unit: billion Won)

	Capital stock	Other capital Surplus	Treasury Shares	Gain on Reissuance of Treasury Shares	Reserve	Retained Earnings	Controlling Interest	Non-controlling Interest	Total Equity
Ⅰ. 2015. 1. 1	955.0	-4.5	-339.1	492.0	3,426.3	1,100.9	5,630.6	77.5	5,708.1
Comprehensive income									
Profit for the period						1,035.7	1,035.7	-3.5	1,032.2
Other comprehensive income					-30.4	1.9	-28.5	-2.3	-30.8
Total comprehensive income					-30.4	1,037.6	1,007.2	-5.8	1,001.4
Transaction with equity holders of the Company									
Cash Dividend						-428.1	-428.1		-428.1
Other Reserve					320.9	-320.9	0.0		0.0
Reserve for research and human resources development					-12.5	12.5	0.0		0.0
Reissuance of Treasury Shares			2.0	2.6			4.6		4.6
Redeemable Convertible Preference Shares		-5.4					-5.4	-5.1	-10.5
Total transaction with equity holders of the Company		-5.4	2.0	2.6	308.4	-736.5	-428.9	-5.1	-434.0
Ⅱ. 2015. 12. 31	**955.0**	**-9.9**	**-337.1**	**494.6**	**3,704.3**	**1,402.0**	**6,208.9**	**66.6**	**6,275.5**

4) Consolidated Statements of Cash Flows

KT&G Corporation and Subsidiaries

(Unit: billion Won)

	FY2015		FY2014	
	Amount		Amount	
Ⅰ. Net cash generated from operating activities		**1,259.2**		**765.2**
1. Profit for the period	**1,032.2**		**813.8**	
2. Total Adjustments	**540.6**		**561.1**	
Adjustment for Income tax expense	382.2		344.1	
Adjustment for Finance costs	9.6		11.0	
Adjustment for Finance income	-84.3		-55.1	
Adjustment for Depreciation/Amortization	161.9		162.0	
Adjustment for Retirement and termination benefits	67.2		51.3	
Adjustment for Foreign currency translations loss	34.1		30.2	
Adjustment for Loss and Reversal on the write-down of inventories	-0.6		1.5	
Adjustment for Impairment Loss and Reversal of impairment on trade and other receivables	-5.5		-8.2	
Adjustment for Loss on sales of property, plant and equipment/intangible assets	1.0		4.7	
Adjustment for Other expense and etc.	57.1		77.2	
Adjustment for Share of gain/loss of associates	-15.1		-3.2	
Adjustment for Gain on foreign currency translations gain	-53.3		-45.8	
Adjustment for Gain on sales of property, plant and equipment/intangible assets and etc	-13.7		-8.6	
3. Changes in working capital	**12.8**		**-315.8**	
4. Income tax paid	**-326.4**		**-293.9**	

(Unit: billion Won)

II. Net cash used in investing activities		**-747.5**		**-342.9**
Interest received	30.2		32.1	
Proceeds from sale of property, plant and equipment/intangible assets	13.2		11.7	
Proceeds from sale of non-current asset held for sale	4.3		0.1	
Proceeds from sale of available-for-sale financial assets	0.2		14.5	
Decrease in loans	11.9		13.4	
Decrease in guarantee deposits	28.4		27.4	
Investment income received from long-term deposits in MSA Escrow Fund	1.5		1.3	
Dividends received	19.2		20.3	
Decrease(Increase) in other financial assets	-468.2		17.3	
Acquisition of property, plant and equipment/intangible assets	-216.3		-332.5	
Acquisition of investment property	-0.1		-0.2	
Acquisition sale of available-for-sale financial assets	-34.2		-53.6	
Increase in loans	-51.3		-0.4	
Increase in guarantee deposits	-21.4		-24.2	
Increase in long-term deposits in MSA Escrow Fund	-78.5		-70.1	
Acquisition of jointly controlled entities and associates and etc	13.6		0.0	
Ⅲ. Net cash used in financing activities		**-381.0**		**-353.8**
Interest paid	-6.9		-3.2	
Dividends paid	-428.1		-402.9	
Increase(Decrease) in borrowing and others	54.0		52.3	
Ⅳ. Net change in cash and cash equivalents (Ⅰ+Ⅱ+Ⅲ)		**130.7**		**68.5**
Ⅴ. Cash and cash equivalents at the beginning of period		**416.4**		**347.9**
Exchange gains(losses) on cash and cash equivalents		**-0.9**		**0.0**
Ⅵ. Cash and cash equivalents at the end of period		**546.2**		**416.4**

5) Notes to Consolidated Financial Statements

KT&G CORPORATION AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

For the years ended December 31, 2015 and 2014

1. Reporting Entity

(a) Description of the Controlling Company

KT&G Corporation (the "Parent Company"), which is engaged in manufacturing and selling tobaccos, was established on April 1, 1987 as Korea Monopoly Corporation, a wholly-owned enterprise of the Korean government, pursuant to the Korea Monopoly Corporation Act, in order to secure financing and to promote and develop, through efficient management, the monopoly business of red ginseng and tobacco. On April 1, 1989, the Parent Company changed its name to Korea Tobacco and Ginseng Corporation pursuant to the Korea Tobacco and Ginseng Corporation Act. Also, pursuant to the Act on Management Reform and Privatization of Public Enterprises, proclaimed on August 28, 1997 and enforced on October 1, 1997, the Parent Company was excluded from the application of the Act for the Management of Government Invested Enterprises. Accordingly, the Parent Company became an entity existing and operating under the Commercial Act of Korea. The Korean government sold 28,650,000 shares of the Parent Company to the public during 1999 and the Parent Company listed its shares on the Korea Exchange (formerly, the Korea Stock Exchange) on October 8, 1999. On December 27, 2002, the Parent Company changed its name again to KT&G Corporation from Korea Tobacco and Ginseng Corporation.

As of December 31, 2015, the Parent Company has three manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 123 branches for the sale of tobacco throughout the country. Also,the Parent Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printingplant for the manufacturing of packaging. The head office of the Parent Company is located in 71, Beotkkot-gil,Daedeok-gu, Daejeon.

Pursuant to the Korean government's privatization program and management reorganization plan, on December 28, 1998, the shareholders approved a plan to separate the Parent Company into two companies by setting up a subsidiary for its red ginseng business segment effective January 1, 1999. The separation was accomplished by the Parent Company's contribution of the assets and liabilities in the red ginseng business segment into a wholly-owned subsidiary, Korea Ginseng Corporation.

On October 17, 2002 and October 31, 2001, the Parent Company listed 35,816,658 and 45,400,000 Global Depositary Receipts ("GDR") (each GDR representing the right to receive one-half share of an ordinary share of the Parent Company), respectively, on the Luxembourg Stock Exchange pursuant to the Korean government's privatization program. Also, on June 25, 2009,the market of the Parent Company's GDR was changed from the BdLmarket to the Euro MTF in theLuxembourg Stock Exchange.

The ownership of the Parent Company's issued ordinary sharesas of December 31, 2015 is held as follows:

Shareholder	Number of shares	Percentage of ownership
National Pension Service	11,098,167	8.08%
Industrial Bank of Korea	9,510,485	6.93%

Employee Share Ownership Association	2,603,918	1.90%
Treasury shares	11,326,605	8.25%
Others	102,753,322	74.84%
	137,292,497	100.00%

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries

(i) List of consolidated subsidiaries

Next most senior parent	Subsidiary	Principal operation	Percentage of ownership	Reporting date	Location
KT&G Corporation	Korea Ginseng Corporation	Manufacturing and selling ginseng	100.00%	Dec. 31	Korea
	Yungjin Pharm. Ind.Co., Ltd.	Manufacturing and selling pharmaceuticals	53.00%	Dec. 31	Korea
	Tae-a Industry Co., Ltd.	Manufacturing tobacco materials	100.00%	Dec. 31	Korea
	KT&G TutunMamulleri SanayiveTicaret A.S.	Manufacturing and selling tobaccos	99.99%	Dec. 31	Turkey
	Korea Tabacos do Brasil Ltda.	Processing leaf tobaccos	99.90%	Dec. 31	Brazil
	KT&G Pars	Manufacturing and selling tobaccos	99.99%	Dec. 31	Iran
	KT&G Rus L.L.C.	Manufacturing and selling tobaccos	100.00%	Dec. 31	Russia
	KGC Life & Gin Co., Ltd.	Selling ginseng door-to-door	100.00%	Dec. 31	Korea
	Global Trading, Inc.	Selling tobaccos	100.00%	Dec. 31	USA
	Somang Cosmetics Co., Ltd.[(*)]	Manufacturing and selling cosmetics	97.73%	Dec. 31	Korea
	RenzolucPte., Ltd. [(*)]	Manufacturing and selling tobaccos	100.00%	Dec. 31	Singapore
	KT&G Life Sciences Corporation[(*)]	Research and development medicine	73.94%	Dec. 31	Korea
	KGC Yebon Corporation	Manufacturing and selling medical herbs	100.00%	Dec. 31	Korea

	K-Q HongKong I, Limited(*)	Manufacturing and selling ginseng	100.00%	Dec. 31	Hongkong
	PT KT&G Indonesia	Manufacturing and selling tobaccos	99.99%	Dec. 31	Indonesia
	K&I HK Co., Ltd.	Selling cosmetics	100.00%	Dec. 31	Hongkong
	K&I China Co., Ltd.	Selling cosmetics	100.00%	Dec. 31	China
	SangSang Stay, Inc.	Hotel	100.00%	Dec. 31	Korea
RenzolucPte., Ltd.	PT TrisaktiPurwosariMakmur	Manufacturing and selling tobaccos	60.17%	Dec. 31	Indonesia
	PT MandiriMahaMulia	Manufacturing and selling tobaccos	66.47%	Dec. 31	Indonesia
PT Trisakti PurwosariMakmur	PT SentosaAbabiPurwosari	Manufacturing and selling tobaccos	99.24%	Dec. 31	Indonesia
	PT PurindoIlufa	Manufacturing and selling tobaccos	100.00%	Dec. 31	Indonesia
Korea Ginseng Corporation	Cheong Kwan Jang Taiwan Corporation	Manufacturing and selling ginseng	100.00%	Dec. 31	Taiwan
	Korean Red Ginseng Corp., Inc.	Manufacturing and selling ginseng	100.00%	Dec. 31	USA
	Korea Ginseng (China) Corp.	Manufacturing and selling ginseng	100.00%	Dec. 31	China
	Korea Ginseng Corporation Japan	Manufacturing and selling ginseng	100.00%	Dec. 31	Japan
	PT CKJ INDONESIA	Manufacturing and selling ginseng	99.88%	Dec. 31	Indonesia
	Jilin Hanzheng Ginseng Co., Ltd.	Manufacturing and selling ginseng	100.00%	Dec. 31	China

(*) The Group’s percentage of ownership, shown above, excludes preferred shares. As of December 31, 2015, the Group’s percentage of ownership would be 97.76%, 68.91%, 59.48% and 50.00% if preferred shares are included.

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries, Continued

For the year ended December 31, 2015, the Parent Company purchased shares of Somang Cosmetics Co., Ltd. for ₩49,755 million, resulting in an increase of the Parent Company's percentage of ownership in Somang Cosmetics Co., Ltd. by 97.73%.

For the year ended December 31, 2015, the Parent Company made an additional investment of ₩2,356 million and ₩5,096 million in Korean Tobacos do Brasil Ltda. and K&I China Co., Ltd, respectively.

(ii) Financial information of subsidiaries

In millions of won

Subsidiary		Total assets	Total liabilities	Revenue	Net profit(loss)	Total comprehensive income (loss)
Korea Ginseng Corporation	₩	1,761,926	299,561	917,786	69,256	67,909
Yungjin Pharm. Ind.Co., Ltd.		193,695	93,271	170,203	3,386	(365)
Tae-a Industry Co., Ltd.		14,897	4,134	13,727	606	547
KT&G TutunMamulleriSanayiveTicaret A.S.		54,318	44,442	22,802	3,933	2,708
Korea Tabacos do Brasil Ltda.		2,615	6	-	(481)	(835)
KT&G Pars		30,166	48,108	5,792	1,483	1,447
KT&G Rus L.L.C.		108,993	56,844	50,825	3,266	(8,986)
KGC Life & Gin Co., Ltd.		27,959	8,831	52,468	(1,901)	(1,937)
Global Trading, Inc.		40,652	21,990	126,200	2,445	3,540
Somang Cosmetics Co., Ltd.		80,716	46,157	76,037	(1,529)	(2,616)
RenzolucPte., Ltd.		46,178	75,262	-	(40,190)	(44,705)
KT&G Life Sciences Corporation		19,235	18,334	1,237	(6,971)	(6,980)
KGC Yebon Corporation		49,860	2,798	13,072	719	704
K-Q HongKong I, Limited		41,792	-	-	(80)	2,518
PT KT&G Indonesia		16,023	36,533	15,217	(14,519)	(14,358)
K&I HK Co., Ltd.		744	571	1,562	25	35
K&I China Co., Ltd.		5,026	243	879	(467)	(652)
SangSang Stay, Inc.		19,611	37	-	(138)	(138)
PT TrisaktiPurwosariMakmur, etc.		84,349	65,214	35,808	(2,543)	(3,397)
PT MandiriMahaMulia		10,612	6,857	8,682	(28)	(175)
Cheong Kwan Jang Taiwan Corporation		14,545	13,137	20,256	12	44
Korean Red Ginseng Corp., Inc.		9,634	6,056	15,864	125	336
Korea Ginseng (China) Corp.		59,257	59,226	36,249	(5,998)	(5,908)

Korea Ginseng Corporation Japan	4,416	3,469	8,956	185	233
PT CKJ INDONESIA	987	1,067	-	(125)	(127)
Jilin Hanzheng Ginseng Co., Ltd.	72,426	49,352	6,253	(18,027)	(18,154)

(c) Change in Consolidated Group

For the year ended December 31, 2015, the Parent Company establishedSangSang Stay, Inc.

2. Basis of Preparation

(a) Statement of Compliance

The consolidated financial statements have been prepared in accordance with Korean International Financial Reporting Standards (“K-IFRS”).

The consolidated financial statements were authorized for issue by the Board of Directors on January21, 2016, which will be submitted for approval to the shareholders’ meeting to be held on March 18, 2016.

(b) Basis of Measurement

The consolidated financial statements have been prepared on the historicalcost basis, except for the following material items in the consolidated statements of financial position:

- Derivative financial instruments measured at fair value
- Available-for-sale financial assets measured at fair value
- Liabilities for defined benefit plans recognized at the net of the total present value of defined benefit obligations less the fair value of plan assets

(c) Functional and Presentation Currency

These consolidated financial statements are presented in Korean won, which is the Group’s functional currency and the currency of the primary economic environment in which the Group operates.

(d) Use of Estimates and Judgments

The preparation of the consolidated financial statements in conformity with K-IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

(i) Judgements

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following notes:

- Note 4 – classification of financial instruments

(ii) Assumptions and estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are included in the following notes:

- Note 8 – impairment test: key assumptions underlying recoverable amounts
- Note 25 – measurement of defined benefit obligations: key actuarial assumptions
- Note 29 –Recognition of deferred tax assets: availability of future taxable profit against which temporary differences can be utilized
- Notes 34 – recognition and measurement of contingencies: key assumptions about likelihood and magnitude of an outflow of resources

2. Basis of Preparation, Continued

(d) Use of Estimates and Judgments, Continued

(iii) Measurement of fair value

A number of the Group's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities. The Group has an established control framework with respect to the measurement of fair values. This includes a valuation team that has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values, and reports directly to the CFO.

The valuation team regularly reviews significant unobservable inputs and valuation adjustments. If third party information, such as broker quotes or pricing services, is used to measure fair values, then the valuation team assesses the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of K-IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

Significant valuation issues are reported to the Group's Audit Committee.

When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs)

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. The Group recognizes transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values is included in the following notes:

- Note9 –investment property
- Note32 –financial instruments

3. Changes in Accounting Policies

The accounting policies applied in these consolidated financial statements are the same as those applied in the Group's consolidated financial statements as of and for the year ended December 31, 2014, except for the adoption of amendments to K-IFRS 1019 *Employee Benefits*.

Amendments to K-IFRS 1019 introduced a practical expedient to accounting for defined benefit plan, when employees or third parties pay contributions if certain criteria are met. According to the amendments, the entity is permitted to recognize those contributions as a reduction of the service cost in the period in which the related service is rendered, instead of forecast future contributions from employees or third parties and attribute them to periods or service as negative benefits.

The Group retrospectively applied the amendments in accordance with the transitional requirements of K-IFRS 1019. The changes do not have a significant impact on the Group's consolidated financial statements.

4. Significant Accounting Policies

The significant accounting policies applied by the Group in preparation of its consolidated financial statements are included below. The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements except for the changes in accounting policies as explained in note 3.

(a) Basis of Consolidation

(i) Non-controlling interests

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the acquisition date.

Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

(ii) Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

(iii) Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognized in profit or loss. Any interest retained in the former subsidiary is measured at fair value when control is lost.

(iv) Interests in equity-accounted investees

Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. A joint venture is an arrangement in which the Group has joint control, whereby the Group has rights to the net assets of the arrangement, rather than rights to its assets and obligations for its liabilities.

Interests in associates and joint venture are accounted for using the equity method. They are recognized initially at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and other comprehensive income of equity-accounted investees, until the date on which significant influence or joint control ceases.

(v) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated. Unrealised gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

4. Significant Accounting Policies, Continued

(b) Property, Plant and Equipment

All property, plant and equipment are stated at historical cost less depreciation and accumulated impairment loss. Historical cost includes expenditures directly attribute to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Property, plant and equipment, except for land and other tangible fixed assets, are depreciated on a straight-line basis over estimated useful lives that appropriately reflect the pattern in which the asset's future economic benefits are expected to be consumed.

The estimated useful lives of the Group's assets are as follows:

	Useful lives (years)		Useful lives (years)
Buildings	10 ~ 60	Vehicles	4 ~ 10
Structures	5~ 40	Tools	4~ 5
Machinery	5~ 20	Furniture and fixtures	2~ 5

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in other income and expense in the statement of comprehensive income.

(c) Borrowing Costs

The Group capitalizes borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Other borrowing costs are recognized in expense as incurred. A qualifying asset is an asset that requires a substantial period of time to get ready for its intended use or sale. Financial assets and inventories that are manufactured or otherwise produced over a short period of time are not qualifying assets. Assets that are ready for their intended use or sale when acquired are not qualifying assets.

To the extent that the Group borrows funds specifically for the purpose of obtaining a qualifying asset, the Group determines the amount of borrowing costs eligible for capitalization as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings. The Group immediately recognizes other borrowing costs as an expense. To the extent that the Group borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the Group determines the amount of borrowing costs eligible for capitalization by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the Group that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that the Group capitalizes during a period does not exceed the amount of borrowing costs incurred during that period.

4. Significant Accounting Policies, Continued

(d) Government Grants

Government grants are not recognized unless there is reasonable assurance that the Group will comply with the grant's conditions and that the grant will be received.Government grants which are intended to compensate the Group for expenses incurred are recognized as other income in profit or loss over the periods in which the Group recognizes the related costs as expenses.

(e) Intangible Assets except for Goodwill

Intangible assets are measured initially at cost and, subsequently, are carried at cost less accumulated amortization and accumulated impairment losses. Intangible assets consist of industrial property rights, facility usage rights andintangible assets under development. Intangible assets are amortized on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The residual value of intangible assets is assumed to be zero. However, as there are no foreseeable limits to the periods over which some of industrial property rights and facility usage rights are expected to be available for use, these intangible assets are regarded as having indefinite useful lives and not amortized.

The estimated useful lives were as follows:

	Useful lives (years)

Industrial property rights	5 ~ 20 or indefinite
Facility usage rights	indefinite
Other intangible assets	3 ~ 5 or indefinite

Amortization periods and amortization methods for intangible assetswith finite useful lives are reviewed at the end of each reporting period. The useful lives of intangible assets that are not being amortized are reviewed at the end of each reporting period to determine whether events and circumstances continue to support indefinite useful life assessment for those assets.The change is accounted for as a change in an accounting estimate.

(f) Investment Property

Property held for the purpose of earning rentals or benefiting from capital appreciation is classified as investment property. Investment property is initially measured at its cost. Transaction costs are included in the initial measurement. Subsequently, investment property is carried at depreciated cost less any accumulated impairment losses.

Subsequent costs are recognized in the carrying amount of investment property at cost or, if appropriate, as separate items if it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing are recognized in profit or loss as incurred.

Investment property except for land, are depreciated on a straight-line basis over 10 ~ 60 years as estimated useful lives.

Depreciation methods, useful lives and residual values are reviewed at the end of each reporting date and adjusted, if appropriate. The change is accounted for as a change in an accounting estimate.

4. Significant Accounting Policies, Continued

(g) Non-current Assets Held for Sale

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. In order to be classified as held for sale, the asset (or disposal group) must be available for immediate sale in its present condition and its sale must be highly probable. The assets or disposal group that are classified as non-current assets held for sale are measured at the lower of their carrying amount and fair value less cost to sell.

The Group recognizes an impairment loss for any initial or subsequent write-down of an asset (or disposal group) to fair value less costs to sell, and a gain for any subsequent increase in fair value less costs to sell, up to the cumulative impairment loss previously recognized in accordance with K-IFRS No. 1036 *Impairment of Assets*.

A non-current asset that is classified as held for sale or part of a disposal group classified as held for sale is not depreciated (or amortized).

(h) Inventories

Inventories are measured at the lower of cost and net realizable value.The cost of inventories comprises all costs of purchase, costs of conversionand other costs incurred in bringing the inventories to their present location andcondition.

The costof inventories is determined by the weighted-average method for merchandise, finished goods, by-products, work-in-progress and tobacco leaf in raw materials, by the moving-average method for raw materials and supplies; and by thespecific identification method for all other inventories.

When inventories are sold, the carrying amount of those inventories is recognized as an expense in the period in which the related revenue is recognized.The amount of any write-down of inventories to net realizable value and all lossesof inventories are recognized as an expense in the period the write-down orloss occurs. The amount of any reversal of any write-down of inventories, arisingfrom an increase in net realizable value, is recognized as a reduction in theamount of inventories and recognized as an expense in the period in which thereversal occurs.

Tobaccoleaf inventories which have an operating cycle that exceeds12 months are classified as current assets, consistent withrecognized industry practice.The estimated amounts of inventories in current assets which are not expected to berealized within 12 months are ₩310,043million and ₩272,649million, respectively, as of December 31, 2015 and 2014.

(i) Impairment of Non-financial Assets

The carrying amounts of the Group's non-financial assets, other than inventories, deferred tax assets,assets arising from employee benefits and non-current assets held for sale, are reviewed at the end of the reporting period to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and intangible assets that have indefinite useful lives or that are not yet available for use, irrespective of whether there is any indication of impairment, are tested for impairment annually by comparing their recoverable amount to their carrying amount.

The Group estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the Groupestimates the recoverable amount of cash-generating unit ("CGU"). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. The value in use is estimated by applying a pre-tax discount rate that reflect current market assessments of the time value of money and the risks specific to the asset or CGU for which estimated future cash flows have not been adjusted, to the estimated future cash flows expected to be generated by the asset or CGU.

An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

(j) Non-derivative Financial Assets

The Group recognizes and measures non-derivative financial assets by the following four categories: financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables and available-for-sale financial assets. The Group recognizes financial assets in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument.

Upon initial recognition, non-derivative financial assets are measured at their fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the asset's acquisition or issuance.

(i) Financial assets at fair value through profit or loss

A financial asset is classified as financial assets are classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Upon initial recognition, transaction costs are recognized in profit or loss when incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

(ii) Held-to-maturity investments

A non-derivative financial asset with a fixed or determinable payment and fixed maturity, for which the Group has the positive intention and ability to hold to maturity, are classified as held-to-maturity investments. Subsequent to initial recognition, held-to-maturity investments are measured at amortized cost using the effective interest method.

(iii) Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method except for loans and receivables of which the effect of discounting is immaterial.

4. Significant Accounting Policies, Continued

(j) Non-derivative Financial Assets, Continued

(iv) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as financial assets at fair value through profit or loss, held-to-maturity investments or loans and receivables. Subsequent to initial recognition, they are measured at fair value, which changes in fair value, net of any tax effect, recorded in other comprehensive income in equity. Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments are measured at cost.

(v) De-recognition of financial assets

The Group derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognized as a separate asset or liability.

If the Group retains substantially all the risks and rewards of ownership of the transferred financial assets, the Groupcontinues to recognize the transferred financial assets and recognizes financial liabilities for the consideration received.

(vi) Offsetting between financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position only when the Group currently has a legally enforceable right to offset the recognized amounts, and there is the intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

(k) Derivative financial instruments

Derivatives are initially recognized at fair value. Subsequent to initial recognition, derivatives are measured at fair value, and changes inthe fair value of derivative financial instrumnets are recognized immediately in profit or loss.

Embedded derivatives are separated from the host contract and accounted for separately only if the following criteria have been met:

- The economic characteristics and risks of the embedded derivative are not closely related to those of the host contract;
- A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
- The hybrid instrument is not measured at fair value with changes in fair value recognized in profit or loss.

4. Significant Accounting Policies, Continued

(l) Impairment of Financial Assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably. However, losses expected as a result of future events, regardless of likelihood, are not recognized.

If financial assets have objective evidence that they are impaired, impairment losses should be measured and recognized.

(i) Financial assets measured at amortized cost

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of its estimated future cash flows discounted at the asset's original effective interest rate. If it is not practicable to obtain the instrument's estimated future cash flows, impairment losses would be measured by using prices from any observable current market transactions. The Group can recognize impairment losses directly or establish a provision to cover impairment losses. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed either directly or by adjusting an allowance account.

(ii) Financial assets carried at cost

If there is objective evidence that an impairment loss has occurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses are not reversed.

(iii) Available-for-sale financial assets

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from other comprehensive income to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized. Impairment losses recognized in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss.For an investment in an equity security, objective evidence of impairment includes a significant or prolonged decline in its fair value below its cost. The Group considers a decline of 20% to be significant and a period of nine months to be prolonged.

(m) Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and call deposits with maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preferred shares when it has a short maturity with a specified redemption date.

4. Significant Accounting Policies, Continued

(n) Non-derivative Financial Liabilities

The Group classifies non-derivative financial liabilities into financial liabilities at fair value through profit or loss, financial guarantee liabilities and other financial liabilities in accordance with the substance of the contractual arrangement and the definitions of financial liabilities. The Group recognizes financial liabilities in the statement of financial position when the Group becomes a party to the contractual provisions of the financial liability.

(i) Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading or designated as such upon initial recognition. Subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss. Upon initial recognition, transaction costs that are directly attributable to the acquisition are recognized in profit or loss as incurred.

(ii) Financial guarantee liabilities

Financial guarantee liability is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified term of a debt instrument. Upon initial recognition, financial guarantee liabilities are measured at their fair value plus, transaction costs that are directly attributable to the acquisition or issue of the financial guarantee liability.

After initial recognition, an issuer of such a contract measures it at the higher ofthe amount determined in accordance with K-IFRS No. 1037*Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognized less, when appropriate, cumulative amortisation recognized in accordance with K-IFRS No. 1018 *Revenue.*

(iii) Other financial liabilities

Non-derivative financial liabilities other than financial liabilities at fair value through profit or loss or financial guarantee liabilities are classified as other financial liabilities. At the date of initial recognition, other financial liabilities are measured at fair value minus transaction costs that are directly attributable to the acquisition. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

The Group derecognizes a financial liability from the statement of financial position when it is extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

(o) Employee Benefits

(i) Short-term employee benefits

Short-term employee benefits are employee benefits that are due to be settled within 12 months after the end of the period in which the employees render the related service. When an employee has rendered service to the Group during an accounting period, the Group recognizes the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

(ii) Retirement benefits: defined contribution plans

When an employee has rendered service to the Group during a period, the Grouprecognizes the contribution payable to a defined contribution plan in exchange for that service as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, the Group recognizes that excess as an asset (prepaid expense) to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(iii) Retirement benefits: defined benefit plans

The calculation of defined benefit obligations is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for the Group, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. To calculate the present value of economic benefits, consideration is given to any applicable minimum fundingrequirements.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognized immediately in other comprehensive income. The Group determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognized in profit or loss.

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognized immediately in profit or loss. The

Group recognizes gains and losses on the settlement of a defined benefit plan when the settlement occurs.

(iv) Termination benefits

Termination benefits are expensed at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognizes costs for a restructuring. If benefits are not expected to be settled wholly within 12months of the end of the reporting period, then they are discounted.

(p) Provisions

Provisions are recognized when theGroup has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Where the effect of the time value of money is material, provisions are determined at the present value of the expected future cash flows.

Where some or all of the expenditures required to settle a provision are expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset.

Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimates. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision is reversed.

(q) Equity Capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of ordinary shares and share options are recognized as a deduction from equity, net of any tax effects.

When the Group repurchases its share capital, the amount of the consideration paid is recognized as a deduction from equity and classified as treasury shares. The profits or losses from the purchase, disposal, reissue, or retirement of treasury shares are not recognized as current profit or loss. If the Group acquires and retains treasury shares, the consideration paid or received is directly recognized in equity.

(r) Revenue Recognition

TheGroup’s revenue categories consist of goods sold, services and other income.

Revenue from sale of goods is measured at the fair value of the consideration received or receivable, net of tobacco excise and other taxes, trade discounts and volume rebates. Revenue from the sale of goods is recognized when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods, the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Tobacco excise and other taxes deducted from revenue for the years ended December 31, 2015 and 2014were ₩5,514,613million and ₩3,732,429million, respectively.

Revenue from the construction of real estate includes the initial amount agreed in the contract plus any variations in contract work, claims and incentive payments, to the extent that it is probable that they will result in revenue and can be measured reliably. As soon as the outcome of a construction contract can be estimated reliably, contract revenue is recognized in profit or loss in proportion to the stage of completion of the contract. The stage of completions is assessed by reference to surveys of work performed. Meanwhile, profits from an apartment house for self-instalment sales is recognized on percentage-of-completion method according to Q&A of Korea Accounting Institute, called 2011-I-KQA. This accounting standard is effective upon Korean Corporation Financial Reporting Standards of Laws on External Audit of Corporation (Article 13, Section 1, Paragraph 1)

Revenue from rendering of services is recognized by reference to the stage of completion of the transaction at the end of the reporting period when the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group, the stage of completion of the transaction at the end of the reporting period can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably. When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue is recognized only to the extent of the expenses recognized that are recoverable.

Rental income from investment property, net of lease incentives granted, is recognized in profit or loss on a straight-line basis over the term of the lease.

4. Significant Accounting Policies, Continued

(s) Finance Income and Finance Costs

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income and interest income on long-term deposits in MSA Escrow Fund. Interest income is recognized as it accrues in profit or loss, using the effective interest method. Dividend income is recognized in profit or loss on the date that the Group’s right to receive payment is established.

Finance costs is interest expense on borrowings and unwinding of the discount on trade and other payables which is recognized in profit or loss using the effective interest method.

(t) Income Taxes

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

(i) Current tax

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the end of the reporting period and any adjustment to tax payable in respect of previous years. The taxable profit is different from the accounting profit for the period since the taxable profit is calculated excluding the temporary differences, which will be taxable or deductible in determining taxable profit (tax loss) of future periods, and non-taxable or non-deductible items from the accounting profit.

(ii) Deferred tax

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the Groupexpects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. The Group recognizes a deferred tax asset for all deductible temporary differences to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

The carrying amount of a deferred tax asset is reviewed at the end of each reporting period and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of that deferred tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period to recover or settle the carrying amount of its assets and liabilities.

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

4. Significant Accounting Policies, Continued

(u) Foreign Currencies

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of the Group at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated to the functional currency using the reporting date's exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

Foreign currency differences arising on retranslation are recognized in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments, a financial liability designated as a hedge of the net investment in a foreign operation, or qualifying cash flow hedges, which are recognized in other comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

(ii) Foreign operations

If the presentation currency of the Group is different from a foreign operation's functional currency, the financial statements of the foreign operation are translated into the presentation currency using the following methods:

The assets and liabilities of foreign operations, whose functional currency is not the currency of a hyperinflationary economy, are translated to presentation currency at exchange rates at the reporting date. The income and expenses of foreign operations are translated to functional currency at exchange rates at the dates of the transactions. Foreign currency differences are recognized in other comprehensive income.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation is treated as assets and liabilities of the foreign operation. Thus they are expressed in the functional currency of the foreign operation and translated at the closing rate.

When a foreign operation is disposed of, the relevant amount in the translation is transferred to profit or loss as part of the profit or loss on disposal.

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which in substance is considered to form part of the net investment in the foreign operation, are recognized in other comprehensive income in the translation reserve.On the partial disposal of a subsidiary that includes a foreign operation,the entity re-attribute the proportionate share of the cumulativeamount of the exchange differences recognised in other comprehensiveincome to the non-controlling interests in that foreign operation. In anyother partial disposal of a foreign operation the entity reclassify toprofit or loss only the proportionate share of the cumulative amount ofthe exchange differences recognised in other comprehensive income.

(v) Earnings per Share

The Group presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Group by the weighted average number of ordinary shares outstanding during the period, adjusted for own shares held. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding, adjusted for own shares held, for the effects of all dilutive potential ordinary shares.

5. Basis of Translating Financial Statements

The consolidated financial statements are expressed in Korean wonand have been translated into U.S. dollars at the rate of ₩1,172.00to $1, the basic exchange rate on December 31, 2015 posted by Seoul Money Brokerage Services,solely for the convenience of the reader. This translation should not be construed as a representation that any or all of the amounts shown could be converted into U.S. dollars at this or any other rate.

6. Operating Segments

(a) The Group's operating segments are summarized as follows:

Operating segments	Principal operation
Tobacco	Manufacturing and selling tobaccos
Ginseng	Manufacturing and selling red ginseng
Real estate	Selling and renting real estate
Others	Manufacturing and selling pharmaceuticals, cosmetics and others

(b) Segment information on sales and operating profit for the year ended December 31, 2015 was as follows:

In millions of won	Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:							

Total segment sales	₩	2,879,091	1,007,593	143,619	391,242	4,421,545	(251,706)	4,169,839
Less: Inter-segment sales		127,575	65,263	6,864	52,004	251,706	(251,706)	-
External sales	₩	2,751,516	942,330	136,755	339,238	4,169,839	-	4,169,839
Depreciation and amortization:								
Depreciation	₩	107,388	29,202	6,277	8,226	151,093	-	151,093
Amortization		4,012	1,548	-	5,199	10,759	-	10,759
Segment profit:								
Operating profit	₩	1,074,722	114,952	30,481	152,130	1,372,285	(6,381)	1,365,904
Other expense,net								(41,409)
Net finance income								74,762
Share of gain of associates								15,137
Income tax expense								(382,174)
Profit for the year	₩							1,032,220

6. Operating Segments, Continued

(c) Segment information on sales and operating profit for the year ended Decemner 31, 2014 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:								
Total segment sales	₩	2,899,357	887,778	161,112	381,165	4,329,412	(216,557)	4,112,855
Less: Inter-segment sales		87,001	67,070	6,957	55,529	216,557	(216,557)	-
External sales	₩	2,812,356	820,708	154,155	325,636	4,112,855	-	4,112,855
Depreciation and amortization:								
Depreciation	₩	108,234	26,478	6,168	8,537	149,417	-	149,417
Amortization		4,056	2,091	-	6,484	12,631	-	12,631
Segment profit:								
Operating profit	₩	1,002,760	117,748	38,689	19,749	1,178,946	(7,084)	1,171,862
Other expense,net								(61,335)
Net finance income								44,139
Share of gain of associates								3,245
Income tax expense								(344,110)
Profit for the year	₩							813,801

(d) Segment information on assets and liabilities as of December 31, 2015 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	3,990,313	1,831,157	149,522	365,152	6,336,144	(319,032)	6,017,112
Investments in associates		-	-	48,800	2,721	51,521	-	51,521
Non-current assets held for sale		1,542	-	-	5,150	6,692	-	6,692
		3,991,855	1,831,157	198,322	373,023	6,394,357	(319,032)	6,075,325
Unallocated assets								2,598,032
Total assets	₩							8,673,357
Acquisition of non-current assets	₩	144,008	55,708	-	16,671	216,387	-	216,387
Liabilities:								
Segment liabilities	₩	1,443,132	161,563	-	84,536	1,689,231	(155,384)	1,533,847
Unallocated liabilities								864,011
Total liabilities	₩							2,397,858

(e) Segment information on assets and liabilities as of December 31, 2014 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	3,620,656	1,682,186	141,938	347,494	5,792,274	(278,945)	5,513,329
Investments in associates		-	-	55,842	2,061	57,903	-	57,903
Non-current assets held for sale		426	-	-	-	426	-	426
		3,621,082	1,682,186	197,780	349,555	5,850,603	(278,945)	5,571,658
Unallocated assets								1,847,004
Total assets	₩							7,418,662
Acquisition of non-current assets	₩	239,599	80,533	-	12,958	333,090	(354)	332,736
Liabilities:								
Segment liabilities	₩	867,391	184,385	-	77,175	1,128,951	(173,338)	955,613
Unallocated liabilities								754,969
Total liabilities	₩							1,710,582

6. **Operating Segments, Continued**

(f) Geographical informationdetermined by customer's and branch's location as of and for the year ended December 31, 2015were as follows:

In millions of won		Korea	Foreign country	Total
External sales	₩	3,138,878	1,030,961	4,169,839
Non-current assets		2,125,865	100,203	2,226,068

(g) Revenues from major customers which amount to more than 10 percent of the details of the Group's consolidated total revenues for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Alokozay International Limited	₩	443,183	385,338

7. **Property, Plant and Equipment**

(a) Details of property, plant and equipment as of December 31, 2015 and 2014 are summarized as follows:

		2015			2014		
In millions of won		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	583,481	-	583,481	574,429	-	574,429
Buildings		963,700	(389,526)	574,174	878,145	(357,630)	520,515
Structures		72,949	(39,770)	33,179	66,192	(37,624)	28,568
Machinery		1,278,124	(933,159)	344,965	1,224,507	(875,701)	348,806
Vehicles		12,907	(10,572)	2,335	13,383	(10,533)	2,850
Tools		63,467	(52,664)	10,803	59,753	(50,097)	9,656
Furniture and fixtures		245,349	(195,912)	49,437	230,065	(176,229)	53,836
Others		1,508	-	1,508	1,454	-	1,454
Construction-in-progress		189,897	-	189,897	213,298	-	213,298
	₩	3,411,382	(1,621,603)	1,789,779	3,261,226	(1,507,814)	1,753,412

(b) Changes in property, plant and equipment for the year ended December 31, 2015 were as follows:

In millions of won		January 1 2015	Acquisition	Disposal	Depreciation	Transfer of construction -in-progress	Net exchange difference and others	December 31 2015
Land	₩	574,429	7,271	(823)	-	5,293	(2,689)	583,481
Buildings		520,515	19,685	(398)	(34,617)	76,931	(7,942)	574,174
Structures		28,568	3,722	(86)	(3,455)	4,588	(158)	33,179
Machinery		348,806	29,847	(740)	(74,567)	48,891	(7,272)	344,965
Vehicles		2,850	481	(107)	(982)	156	(63)	2,335
Tools		9,656	5,502	(144)	(4,568)	351	6	10,803
Furniture and fixtures		53,836	22,493	(384)	(26,629)	108	13	49,437
Others		1,454	54	-	-	-	-	1,508
Construction-in-progress		213,298	112,914	-	-	(136,318)	3	189,897
	₩	1,753,412	201,969	(2,682)	(144,818)	-	(18,102)	1,789,779

7. Property, Plant and Equipment, Continued

For the year ended December 31, 2015, land and buildings with a carrying amount of ₩2,732 million were transferred to investment property and land, buildings and structures with a carrying amount of ₩6,692 million were transferred to non-current assets held for sale.

For the year ended December 31, 2015, borrowing costs of ₩82 million were capitalized as part of the cost of machinery and others with the capitalization rate of 3.75%.

(c) Changes in property, plant and equipment for the year ended December 31, 2014 were as follows:

In millions of won		January 1 2014	Acquisition	Disposal	Depreciation	Transfer of construction -in-progress	Net exchange difference and others	December 31 2014
Land	₩	528,983	1,643	(716)	-	75,028	(30,509)	574,429
Buildings		535,055	3,201	(1,132)	(32,481)	30,313	(14,441)	520,515
Structures		29,299	2,264	(75)	(3,281)	826	(465)	28,568
Machinery		348,643	10,476	(2,258)	(73,891)	70,553	(4,717)	348,806
Vehicles		3,392	439	(61)	(1,023)	208	(105)	2,850
Tools		8,710	4,037	(86)	(3,993)	1,015	(27)	9,656
Furniture and fixtures		60,254	20,651	(3,088)	(28,580)	4,799	(200)	53,836

Others		1,304	150	-	-	-	-	1,454
Construction-in-progress		106,649	293,893	(58)	-	(182,742)	(4,444)	213,298
	₩	1,622,289	336,754	(7,474)	(143,249)	-	(54,908)	1,753,412

For the year ended December 31, 2014, land and construction-in-progress with a carrying amount of ₩32,682 million was transferred to inventories.

8. Intangible Assets

(a) Details of intangible assets as of December 31, 2015 and 2014 are summarized as follows:

				2015			2014
In millions of won		Cost	Accumulated amortization and impairment	Carrying amount	Cost	Accumulated amortization and impairment	Carrying amount
Goodwill	₩	87,902	(72,841)	15,061	87,061	(54,900)	32,161
Industrial property rights		46,806	(32,015)	14,791	46,203	(29,203)	17,000
Facility usage rights		28,282	(2,731)	25,551	27,230	(3,680)	23,550
Other intangible assets		116,349	(70,150)	46,199	116,230	(37,144)	79,086
Intangible assets under development		6,180	(2,354)	3,826	5,480	(2,340)	3,140
	₩	285,519	(180,091)	105,428	282,204	(127,267)	154,937

8. Intangible Assets, Continued

(b) Changes in intangible assets for the year ended December 31, 2015 were as follows:

In millions of won		January 1 2015	Acquisition	Disposal	Transfer of Intangible assets under development	Amortization	Impairment	Net exchange difference	December31 2015
Goodwill	₩	32,161	-	-	-	-	(17,941)	841	15,061
Industrial property rights		17,000	1,030	(104)	82	(1,330)	(1,575)	(312)	14,791
Facility usage rights		23,550	4,042	(2,041)	-	-	-	-	25,551
Other intangible assets		79,086	221	-	-	(9,429)	(23,694)	15	46,199
Intangible assets under development		3,140	783	-	(82)	-	(14)	(1)	3,826

	₩	154,937	6,076	(2,145)	-	(10,759)	(43,224)	543	105,428

For the year ended December 31, 2015, the Group recognized ₩43,224 million of impairment losses on goodwill, industrial property rights, other intangible assets and intangible assets under development since the carrying amounts exceeded their recoverable amounts.

(c) Changes in intangible assets for the year ended December 31, 2014 were as follows:

In millions of won		January 1 2014	Acquisition	Disposal	Transfer of Intangible assets under development	Amortization	Impairment	Net exchange difference	December 31 2014
Goodwill	₩	83,370	-	-	-	-	(54,900)	3,691	32,161
Industrial property rights		31,733	397	(6)	326	(2,652)	(12,654)	(144)	17,000
Facility usage rights		25,757	455	(4)	-	-	(2,658)	-	23,550
Other intangible assets		89,285	261	(177)	-	(9,979)	(433)	129	79,086
Intangible assets under development		2,485	981	-	(326)	-	-	-	3,140
	₩	232,630	2,094	(187)	-	(12,631)	(70,645)	3,676	154,937

For the year ended December 31, 2014, the Group recognized ₩70,645 million of impairment losses on goodwill, industrial property rights, facility usage rights and other intangible assetssince the carrying amounts exceeded their recoverable amounts.

(d) Expenditures not capitalized for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Cost of sales	₩	1,972	925
Selling, general and administrative expenses		36,032	35,747
	₩	38,004	36,672

8. Intangible Assets, Continued

(e) The following is a summary of impairment tests for goodwill allocation for each operating segment as of December 31, 2015 and 2014.

In millions of won		2015	2014
Tobacco	₩	-	17,100

Others		15,061	15,061
	₩	15,061	32,161

The recoverable amounts of all CGUs have been determined based on value-in-use calculations, and the key assumptions used for value-in-use calculations for the years ended December 31, 2015 and 2014 are as follows:

	2015	2014
Gross margin	6.3%	5.4~28.7%
Perpetual growth rate	2.0%	0.0~2.0%
Discount rate (weighted average cost of capital)	12.2%	8.8~12.1%

As a result of the impairmenttest, the Group recognized ₩17,941 million and ₩54,900 million of impairment loss on goodwill for the years ended December 31, 2015 and 2014, respectively.

9. Investment Property

(a) Details of investment property as of December 31, 2015 and 2014 are summarized as follows:

		2015			2014		
In millions of won		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	49,123	-	49,123	48,293	-	48,293
Buildings		179,948	(64,583)	115,366	177,315	(57,640)	119,675
	₩	229,071	(64,583)	164,489	225,608	(57,640)	167,968

(b) Changes in investment property for the years ended December 31, 2015 and 2014were as follows:

		2015			2014		
In millions of won		Land	Buildings	Total	Land	Buildings	Total
Beginning balance	₩	48,293	119,675	167,968	48,303	125,672	173,975
Acquisition		-	64	64	-	248	248
Depreciation		-	(6,275)	(6,275)	-	(6,168)	(6,168)
Transfer from (to)							
property, plant and equipment		830	1,902	2,732	(10)	(77)	(87)

Ending balance	₩	49,123	115,366	164,489	48,293	119,675	167,968

(c) The amounts recognized in profit or loss from investment property for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Rental income	₩	34,764	33,839
Direct operating expense		(6,377)	(6,477)
	₩	28,387	27,362

9. Investment Property, Continued

(d) The carrying amount and the fair value of investment propertyas of December 31, 2015 and 2014 were as follows:

		2015		2014	
In millions of won		Fair value	Carrying amount	Fair value	Carrying amount
Land	₩	435,034	49,123	309,002	48,293
Buildings		177,756	115,366	186,337	119,675
	₩	612,790	164,489	495,339	167,968

The fair value of investment property was determined based on the yield capitalization method by external, independent valuers. The fair value measurement for all of the investment properties has been categorized as a level 3 fair value based on the inputs to the valuation techniques used.

10. Investments in Associates

(a) Investments in associates as of December 31, 2015 and 2014 are summarized as follows:

In millions of won, except percentage of ownership			2015			2014		
Associate	Location	Principal operation	Percentage of ownership		Carrying amount	Percentage of ownership		Carrying amount
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	20.24%	₩	2,720	25.34%	₩	2,061
JR CR-REIT IV Co., Ltd.	Korea	Renting of real estate	-		-	49.02%		12,900
KVG REIT 1 Co., Ltd.	Korea	Renting of real estate	29.67%		6,635	29.67%		6,848
KOCREF REIT 17 Co., Ltd.	Korea	Renting of real estate	22.06%		13,208	22.06%		6,619

JR REIT V Co., Ltd.	Korea	Renting of real estate	34.63%	5,470	34.63%	5,524
JR REIT VIII Co., Ltd.	Korea	Renting of real estate	21.74%	9,693	21.74%	9,858
LSK Global Pharma Services Co., Ltd.	Korea	Research and development medicine	23.15%	-	23.15%	-
JR REIT X Co., Ltd.	Korea	Renting of real estate	28.79%	8,907	28.79%	9,114
JR REIT XIII Co., Ltd.	Korea	Renting of real estate	27.03%	4,888	27.03%	4,979
				₩ 51,521		₩ 57,903

In 2015, the Group received₩13,625 million of dividend related with liquidation of JR CR-REIT IV Co., Ltd.

In 2015, the Group's ownership of Lite Pharm Tech, Inc. has decreased to 20.24% due to theirpaid-in capital increase.

10. Investments in Associates, Continued

(b) Financial information of associates, which represents 100% of the entities' balancesas of and for the year ended December 31, 2015are summarized as follows:

In millions of won

Associate		Total assets	Total liabilities	Revenue	Total comprehensive income
Lite Pharm Tech, Inc.	₩	14,638	1,199	9,405	2,255
JR CR-REIT IV Co., Ltd.		-	-	3,235	8,208
KVG REIT 1 Co., Ltd.		50,386	28,023	5,892	1,678
KOCREF REIT 17 Co., Ltd.		72,473	12,601	5,875	32,677
JR REIT V Co., Ltd.		30,967	15,170	2,508	1,555
JR REIT VIII Co., Ltd.		107,646	63,060	7,167	3,007
LSK Global Pharma Services Co., Ltd.		5,078	7,562	15,703	(251)
JR REIT X Co., Ltd.		87,412	56,473	3,962	272
JR REIT XIII Co., Ltd.		47,178	29,097	2,887	777

(c) Financial information of associates, which represents 100% of the entities' balancesas of and for the year ended December 31, 2014 are summarized as follows:

In millions of won

	Total	Total	Revenue	Total

Associate		assets	liabilities		comprehensive income
Lite Pharm Tech, Inc.	₩	9,028	894	9,795	2,734
JR CR-REIT IV Co., Ltd.		63,325	35,139	3,540	196
KVG REIT 1 Co., Ltd.		51,094	28,016	5,784	1,661
KOCREF REIT 17 Co., Ltd.		66,270	36,266	5,457	1,820
JR REIT V Co., Ltd.		31,127	15,175	2,412	1,494
JR REIT VIII Co., Ltd.		108,441	63,097	7,619	3,093
LSK Global Pharma Services Co., Ltd.		5,322	6,007	13,988	1,892
JR REIT X Co., Ltd.		87,739	56,095	4,223	130
JR REIT XIII Co., Ltd.		46,965	28,543	2,911	921

(d) Changes in investments in associatesfor the year ended December 31, 2015were as follows:

In millions of won

Associate		January 1 2015	Disposal	Share of gain	Dividends	December 31 2015
Lite Pharm Tech, Inc.	₩	2,061	-	659	-	2,720
JR CR-REIT IV Co., Ltd.		12,900	(13,625)	4,955	(4,230)	-
KVG REIT 1 Co., Ltd.		6,848	-	519	(732)	6,635
KOCREF REIT 17 Co., Ltd.		6,619	-	7,208	(619)	13,208
JR REIT V Co., Ltd.		5,524	-	758	(812)	5,470
JR REIT VIII Co., Ltd.		9,858	-	654	(819)	9,693
LSK Global Pharma Services Co., Ltd.		-	-	-	-	-
JR REIT X Co., Ltd.		9,114	-	126	(333)	8,907
JR REIT XIII Co., Ltd.		4,979	-	258	(349)	4,888
	₩	57,903	(13,625)	15,137	(7,894)	51,521

10. Investments in Associates, Continued

(e) Changes in investments in associatesfor the year ended December 31, 2014were as follows:

In millions of won

Associate	January 1 2014	Share of gain	Dividends	December 31 2014

Lite Pharm Tech, Inc.	₩	1,476	585	-	2,061
JR CR-REIT IV Co., Ltd.		12,953	27	(80)	12,900
KVG REIT 1 Co., Ltd.		7,047	511	(710)	6,848
KOCREF REIT 17 Co., Ltd.		6,745	387	(513)	6,619
JR REIT V Co., Ltd.		5,573	735	(784)	5,524
JR REIT VIII Co., Ltd.		9,948	669	(759)	9,858
LSK Global Pharma Services Co., Ltd.		-	-	-	-
JR REIT X Co., Ltd.		9,334	79	(299)	9,114
JR REIT XIII Co., Ltd.		5,000	252	(273)	4,979
	₩	58,076	3,245	(3,418)	57,903

(f) Reconciliation of the summarized financial information presented to the carrying amount of the Group's interest in the associate as of December 31, 2015 are summarized as follows:

In millions of won

Associate	Percentage of ownership		Equity attributable to owners of the parent	Share of netassets	Share of lossnot recognized	Carrying amount
Lite Pharm Tech, Inc.	20	₩	13,439	2,720	-	2,720
KVG REIT 1 Co., Ltd.	29		22,363	6,635	-	6,635
KOCREF REIT 17 Co., Ltd.	22		59,872	13,208	-	13,208
JR REIT V Co., Ltd.	34		15,797	5,470	-	5,470
JR REIT VIII Co., Ltd.	21		44,586	9,693	-	9,693
LSK Global Pharma Services Co., Ltd.	23		(2,484)	(575)	575	-
JR REIT X Co., Ltd.	28		30,939	8,907	-	8,907
JR REIT XIII Co., Ltd.	27		18,081	4,888	-	4,888
		₩				51,521

11. Available-for-sale Financial Assets

(a) Changes in available-for-sale financial assets for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	326,833	296,601

Acquisitions		63,190	56,392
Net changes in fair value		3,881	(11,655)
Disposals and exercise of convertible right		(29,223)	(14,505)
Ending balance	₩	364,681	326,833
Statement of financial position:			
Current	₩	-	1,000
Non-current		364,681	325,833
	₩	364,681	326,833

In 2015, the Group acquired ₩28,990 million of ordinary shares of U&I Corporation by exercising conversion options embedded in their convertible bonds and convertible preference shares. The Group recognized ₩24,990 million of difference between the fair value of ordinary shares acquired and the carrying amount of bonds and preference shares converted as gain on sale of available-for-sale financial assets for the year ended December 31, 2015.

(b) Available-for-sale financial assets as of December 31, 2015 and 2014 are summarized as follows:

In millions of won		2015	2014
Available-for-sale debt instruments:			
Government and municipal bonds	₩	96	96
Corporate bonds		1,500	2,500
Total available-for-sale debt instruments		1,596	2,596
Available-for-sale equity instruments:			
Listed			
– YTN Co., Ltd.		24,428	22,291
– Oscotech, Inc.		3,696	1,030
–Shinhan Financial Group Co., Ltd.		158,530	178,171
–Rexahn Pharmaceuticals, Inc.		2,696	4,917
–U&I Corporation		22,564	-
		211,914	206,409
Unlisted		151,171	117,828
Total available-for-sale equity instruments		363,085	324,237
Total available-for-sale financial assets	₩	364,681	326,833

The fair value of listed available-for-sale equity instruments is principally based on quoted prices in an active market.

As of December 31, 2015 and 2014, ₩37,659 million and ₩29,698 million of available-for-sale financial assets that do not have a market price in an active market and whose fair value cannot be reliably measured or is similar to their carrying amount are measured at cost, respectively.

12. Long-term Deposits in MSA Escrow Fund

Long-term depositsin MSA Escrow Fund as of December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
MMF	₩	43,309	19,269
Treasury note		360,657	282,539
	₩	403,966	301,808

As discussed in note 34 to the consolidated financial statements, long-term deposits in MSA Escrow Fund are deposited to the United States government related to the export of tobacco to the United States. The payments of long-term depositsin MSA Escrow Fundfor the years ended December 31, 2015 and 2014 are ₩78,492 million and ₩70,094million, respectively.

Interest income on long-term depositsin MSA Escrow Fundfor the years ended December 31, 2015 and 2014 are ₩1,287 million and ₩877million, respectively.

13. Trade and Other Receivables

(a) Trade and other receivables as of December 31, 2015 and 2014are summarized as follows:

		2015		2014	
In millions of won		Current	Non-current	Current	Non-current
Loans to employees	₩	15,774	52,275	7,816	20,221
Loans		2,504	315	645	3,707
Other receivables		127,369	323	77,067	276
Guarantee deposits		34,730	22,158	-	62,531
Accrued income		5,943	-	5,595	-
Trade receivables		1,031,618	-	898,654	-
	₩	1,217,938	75,071	989,777	86,735

(b) Trade and other receivablesas of December 31, 2015 and 2014have been reported in the consolidated statements of financial position net of allowances as follows:

	2015		2014	
In millions of won	Current	Non-current	Current	Non-current

Gross trade and other receivables	₩	1,251,180	75,071	1,029,436	86,735
Allowance:					
Loans		(197)	-	(197)	-
Other receivables		(2,296)	-	(2,286)	-
Trade receivables		(30,749)	-	(37,176)	-
		(33,242)	-	(39,659)	-
Net trade and other receivables	₩	1,217,938	75,071	989,777	86,735

13. Trade and Other Receivables, Continued

(c) Changes in the allowance account for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Beginning balance	₩	39,659	51,838
Impairment loss		12	509
Reversal of impairment loss		(5,465)	(8,664)
Net exchangedifference		(964)	(4,024)
Ending balance	₩	33,242	39,659

Impairment loss (reversal of impairment loss) on trade and other receivables is included as part of selling,general and administrative expenses and other expense (income) in the consolidated statements of comprehensive income.

(d) The agingschedule of trade and other receivables which were past due but not impaired as of December 31, 2015 and 2014 is as follows:

In millions of won		2015	2014
Within 1 month	₩	67,309	80,369
Between 1 and 2 months		64,851	42,870
Beyond 2 months		198,982	239,153
	₩	331,142	362,392

There is no significant concentration of credit risk with respect to trade and other receivables sincetrade and other receivables, excluding export trade receivables, are widely dispersed amongst a number of customers. The Group holds pledged assets and guarantees in respect of some of the past due debtor balances.

(e) Details of trade and other receivables that are measured at amortized cost as of December 31, 2015 and 2014were as follows:

	2015	2014

In millions of won	Effective interest rate		Current	Non-current	Effective interest rate		Current	Non-current
Loans to employees	1.89~5.68%	₩	15,774	52,275	3.00~5.68%	₩	7,816	20,221
Loans	1.70~7.29%		1,863	315	1.70~7.29%		-	3,665
Other receivables	-		-	-	3.79%		8,300	-
Guarantee deposits	1.70~8.47%		33,787	20,260	1.70~8.47%		-	60,123
		₩	51,424	72,850		₩	16,116	84,009

14. Inventories

(a) Inventoriesas of December 31, 2015 and 2014aresummarized as follows:

In millions of won		2015	2014
Merchandise, net of loss on the write-down of inventories	₩	7,677	12,271
Finished goods, net of loss on the write-down of inventories		610,309	503,761
Work-in-progress, net of loss on the write-down of inventories		608,280	545,090
Raw materials, net of loss on the write-down of inventories		770,561	797,696
Supplies		27,367	26,936
By-products		7,051	8,646
Buildings under construction		3,618	1,185
Sites for lotting-out construction		25,815	31,179
Goods-in-transit		58,436	55,739
	₩	2,119,114	1,982,503

(b) The amount of inventories recognized as an expensefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Cost of sales:			
Write-down (reversal of write-down) of inventories	₩	(565)	1,540
Loss on retirement of inventories		4,706	7,143
Other expense:			
Loss on retirement of inventories		3,798	1,379
	₩	7,939	10,062

15. Cash and Cash Equivalents and Other Financial Assets

(a) Cash and cash equivalentsas of December 31, 2015 and 2014 aresummarized as follows:

In millions of won		2015	2014
Cash on hand	₩	2,788	11,854
Demand deposits		161,627	157,138
Short-term investment assets		381,798	247,402
	₩	546,213	416,394

(b) Other financial assets as of December 31, 2015 and 2014 aresummarized as follows:

		2015		2014	
In millions of won		Current	Non-current	Current	Non-current
Time deposits	₩	120,141	-	35,337	11
Certificates of deposit		31,406	-	31,099	-
Money trust		985,359	-	602,000	236
Security deposits for checking accounts		-	12	-	12
	₩	1,136,906	12	668,436	259

15. Cash and Cash Equivalents and Other Financial Assets, Continued

(c) Financial assets restricted in use as of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Long-term other financial assets	₩	12	12
Current other financial assets		1,406	3,209
	₩	1,418	3,221

16. Non-current Assets Held for Sale

Changes in non-current assets held for sale for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	426	153

Transfer from property, plant and equipment		6,692	426
Disposal		(426)	(153)
Ending balance	₩	6,692	426

17. Pledged Assets

(a) The followings assets were pledged as collateral for borrowings as of December 31, 2015.

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Holder
Investment property	₩	70,769	Leasehold deposits received	₩	8,975	9,225	Metlife Insurance Korea Co.,Ltd., etc.
Property, plant and equipment and investment property		81,465	Short-term borrowings		12,000	48,009	KEB Hana Bank
			Long-term borrowings		14,936	16,991	KEB Hana Bank, etc.
Property, plant and equipment		28,780	Investment subsidy		-	660	Chungju-si
			Short-term borrowings		1,500	4,440	KEB Hana Bank
Other financial assets		1,406	ACH pledged		-	1,406	Bank of Oklahoma
	₩	182,420		₩	37,411	80,731	

(b) The followings assets were pledged as collateral for borrowings as of December 31, 2014.

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Holder
Investment property	₩	71,677	Leasehold deposits received	₩	7,901	8,683	Metlife Insurance Korea Co.,Ltd., etc.
Property, plant and equipment and investment property		71,005	Short-term borrowings		12,000	28,934	KEB Hana Bank
			Long-term borrowings		6,890	20,466	KEB Hana Bank, etc.
Property, plant and equipment		28,882	Investment subsidy		-	660	Chungju-si
			Short-term borrowings		1,554	3,000	KEB Hana Bank, etc.
Property, plant and equipment		56	Long-term borrowings		204	294	The Korea Development Bank
Property, plant and equipment			Long-term borrowings		5,000	5,000	KEB Hana Bank
and other financial assets		18,213	Short-term borrowings		8,423	8,052	KEB Hana Bank
Other financial assets		100	Short-term borrowings		1,500	110	KEB Hana Bank

Other financial assets	1,410	Contract fulfilment	-	1,410	Haitai Beverage Co.,Ltd., etc.
Other financial assets	1,099	ACH pledged	-	1,099	Bank of Oklahoma
	₩ 192,442		₩ 43,472	77,708	

18. Share Capital and Other Capital Surplus

(a) Details of sharecapital as of December 31, 2015 and 2014 were as follows:

In won, except number of shares	2015	2014
Number of ordinaryshares:		
Authorized	800,000,000	800,000,000
Issued	137,292,497	137,292,497
Outstanding	125,965,892	125,898,800
Par value	₩ 5,000	5,000

The Parent Company has, thus far, reacquired and retired 53,699,400 shares of treasury share. Accordingly, as of December 31, 2015, the Parent Company's ordinary share differs from the aggregate par value of issuedshares by ₩268,497 million.

(b) Changes in the number of shares for the years ended December 31, 2015 and 2014were as follows:

	2015			2014		
Number of share	Ordinary shares	Treasury shares	Total	Ordinary shares	Treasury shares	Total
Beginning balance	137,292,497	(11,393,697)	125,898,800	137,292,497	(11,393,697)	125,898,800
In-kind donation of treasury shares	-	67,092	67,092	-	-	-
Ending balance	137,292,497	(11,326,605)	125,965,892	137,292,497	(11,393,697)	125,898,800

(c) Changes in other capital surplusfor the years ended December 31, 2015 and 2014were as follows:

In millions of won	2015	2014
Beginning balance	₩ (4,573)	(4,573)
Extinguishment of equity conversion options	(5,483)	-
Paid-in capital increase of subsidiary	128	-
Ending balance	₩ (9,928)	(4,573)

For the year ended December 31, 2015, the Group early redeemed theredeemable convertible preferred shares issued by Somang Cosmetics Co., Ltd.With regard to the early redemption, the Group recognized the consideration paid for the repurchase of equity conversion options as other capital surplus.

For the year ended December 31, 2015, the Group recognized changes in controlling interests in other surplus due to paid-in capital increase of Somang Cosmetics Co., Ltd.

19. Treasury Shares

(a) Changes in the treasury sharesfor the years ended December 31, 2015 and 2014were as follows:

	2015			2014		
In millions of won, except number of shares	Number of shares		Carrying amount	Number of shares		Carrying amount
Beginning balance	11,393,697	₩	339,059	11,393,697	₩	339,059
In-kind donation of treasury shares	(67,092)		(1,997)	-		-
Ending balance	11,326,605	₩	337,062	11,393,697	₩	339,059

19. Treasury Shares, Continued

(b) Changes in gain on reissuance of treasury shares for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	492,032	492,032
In-kind donation of treasury shares,net of tax		2,616	-
Ending balance	₩	494,648	492,032

20. Reserves

(a) Details of reservesas of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Available-for-sale financial assets - net change in fair value	₩	(30,378)	(14,303)
Foreign operations - foreign currency translation differences		(95,110)	(80,729)
Legal reserve		603,145	603,145
Voluntary reserve		3,226,658	2,918,254
	₩	3,704,315	3,426,367

(b) Available-for-sale financial assets - net change in fair valueas of December 31, 2015 and 2014 aresummarized as follows:

In millions of won		2015	2014
Available-for-sale financial assets - net change in fair value before tax	₩	(40,077)	(18,869)
Tax effect		9,699	4,566
	₩	(30,378)	(14,303)

(c) Legal Reserve

The Korean Commercial Act requires the Parent Company to appropriate a legal reserve in an amount equal to at least 10% of cash dividends for each accounting period until the reserve equals 50% of stated capital. The legal reserve may be used to reduce a deficit or may be transferred to ordinary shares in connection with a free issue of shares.

(d) Details of voluntary reserve as of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Reserveforbusinessrationalization	₩	12,851	12,851
Reserveforresearchandhumanresourcedevelopment		30,000	42,522
Reservefor business expansion		698,881	698,881
Unconditionalreserve		2,484,926	2,164,000
	₩	3,226,658	2,918,254

Reserve for business rationalization

Until December 10, 2002 under *the Special Tax Treatment Control Act*, investment tax credits were allowed for certain investments. The Parent Company was, however, required to appropriate from retained earnings, the amount of tax benefits received, and transfer such amount into a reserve for business rationalization.

20. Reserves, Continued

Effective December 11, 2002, the Parent Company was no longer required to establish a reserve for business rationalization despite tax benefits received for certain investments and, consequently, the existing balance is now regarded as a voluntary reserve.

Reserve for research and human resource development

Reserve for research and human resource development was appropriated in order to utilize certain tax deduction benefits through the early recognition of future expenditures. This reserve is restored to retained earnings in accordance with the relevant tax laws. Such reserves are taken back into taxable income in the year of restoration.

Reserve for business expansion and other reserves

Reserves without specific purposes are restored to retained earnings by the Parent Company. Those reserves can be used for other purposes afterwards upon a resolution at a general meeting of shareholders.

21. Retained Earnings

(a) Changes in retained earnings for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Beginning balance	₩	1,100,876	802,755
Dividends		(428,056)	(402,876)
Transfer from reserve for research and human resource development		12,522	47,478
Transfer to unconditional reserve		(320,926)	(152,000)
Profit for the year		1,032,220	813,801
-Less: non-controlling interests		3,497	11,805
Remeasurements of net defined benefit liability, net of tax		38	(21,655)
-Less: non-controlling interests		1,804	1,568
Ending balance	₩	1,401,975	1,100,876

(b) Statements of appropriation of retained earnings of the Parent Company for the years ended December 31, 2015 and 2014 are as follows:

Date of appropriation for 2015: March18, 2016

Date of appropriation for 2014: February 27, 2015

In millions of won		2015	2014
Unappropriated retained earnings:			
Balance at beginning of year	₩	-	2,422
Profit for the year		987,924	747,054
Remeasurements of net defined benefit liability, net of tax		7,962	(13,016)
		995,886	736,460
Transfer from voluntary reserves		10,000	12,522
Unappropriated retained earnings available for appropriation		1,005,886	748,982
Appropriation of retained earnings:			
Dividends		(428,284)	(428,056)
Unconditionalreserve		(577,602)	(320,926)
		(1,005,886)	(748,982)
Unappropriated retained earningsto be carried over to subsequent year	₩	-	-

22. Dividends

The following dividends were declared and paid by the Parent Company for the years ended December 31, 2015 and 2014 are as follows:

		2015	2014
Dividends in millions of won	₩	428,056	402,876
Dividends per share in won		3,400	3,200
		68.0	64.0
Dividend rate as a percentage of par value		0%	0%

Dividends of ₩428,284 million (₩3,400 per share) will be proposed at the shareholders' meeting to be held on March 18, 2016. The dividends have not been recognized as liabilities.

23. Trade and Other Payables

Trade and other payables as of December 31, 2015 and 2014 are summarized as follows:

		2015		2014	
In millions of won		Current	Non-current	Current	Non-current
Leasehold deposits received	₩	19,404	7,030	-	27,007
Trade payables		103,591	-	95,936	-
Withholdings		212,891	171	158,480	258
Accrued expenses		180,172	-	156,231	-
Other payables		90,297	6,446	93,206	4,979
	₩	606,355	13,647	503,853	32,244

24. Borrowings

(a) Short-term borrowings as of December 31, 2015 and 2014 are summarized as follows:

In millions of won	Lender	Annual interest rate		2015	2014
Borrowings	Kookmin Bank	2.12% ~ 2.49%	₩	23,469	87,231
	KEB Hana Bank	2.78% ~ 3.32%		13,500	28,420
	KEB Hana Bank	3M LIBOR+1.45%		44,252	-
	The Korea Development Bank	2.23%		100,000	-

	PT Bank Woori Saudara	10.66%		2,550	-
Customer credit contracts(*)	Nonghyup Bank, etc.	6.64%,etc.		22,602	26,210
			₩	206,373	141,861

(*) The Group has entered into a customer credit contract with Nonghyup Bank, etc. The financial institutions pay trade receivables on behalf of customers and the Group has provided guarantees to the financial institutions for customers.

24. Borrowings, Continued

(b) Long-term borrowings as of December 31, 2015 and 2014 are summarized as follows:

In millions of won	Lender	Maturity	Annual interest rate		2015	2014
Borrowings	Nonghyup Bank	Jun.2020	0.00%	₩	34,514	23,852
	KEB Hana Bank	Sep.2017	1.98%~4.20%		1,936	8,096
	Kookmin Bank	Sep.2023	2.60%~3.15%		13,000	3,794
	The Korea Development Bank	-	-		-	204
Convertible bond					8,500	8,326
Redeemable convertible preferred shares					53,340	76,890
Redeemable preferred shares					18,611	17,851
				₩	129,901	139,013
Statement of financial position:						
Current				₩	27,659	1,218
Non-current					102,242	137,795
				₩	129,901	139,013

Details of convertible bond and preferred shares as of December 31, 2015are summarized as follows:

Description	*Issuing company*	*Details*
Convertible bond(*)	PT TrisaktiPurwosariMakmur	Issue date: Dec.2011
		Par value: IDR 100,000 million
		Issued value: IDR 100,000 million
		Carrying amount: ₩8,500 million (IDR 100,000 million)
		Interest rate: 9.5%

		The bonds will mature four years from the issue date and become convertible into shares at the rate of IDR 9,659 per share.
Redeemable convertible preferred shares	KT&G Life Sciences Corporation	Issue date: Nov.2011 Issued value: ₩18,000 million Carrying amount: ₩18,000 million The convertible instrument will mature ten years from the issue date. The instrument can be converted into 1,090,909 ordinary shares at any time, and automatically converts upon maturity. If KT&G Life Sciences Corporation will be not listed by the end of 2015, recourse is available.
	Renzoluc Pte, Ltd.	Issue date: Sep.2012 Issued value: ₩35,340 million Carrying amount: ₩35,340 million The convertible instrument will mature ten years from the date of establishment of QCP 2011 Corporate Partnership Private Equity Fund (the “PEF”). The instrument can be converted into 6,978,948 ordinary shares at any time after five years from the issue date. Payable on demandfrom 270 days prior to the expiration of the PEF
Redeemable preferred shares	K-Q HongKong I, Limited	Issue date: Aug.2012, Sep.2012, Dec.2012 Issued value: ₩18,611 million Carrying amount: ₩18,611 million The convertible instrument will mature ten years from the date of establishment of the PEF. Payable on demand from 270 days prior to the expiration of the PEF

(*) The fair value of the liability component was calculated using the market interest rate for an equivalent non-convertible bond. The fair value of the equity component was determined by deducting the fair value of the liability component from the fair value of the compound financial instrument as a whole.

24. Borrowings, Continued

For the year ended December 31, 2015, the Group early redeemed theredeemable convertible preferred shares issued by Somang Cosmetics Co., Ltd. With regard to the early redemption, the Group recognized ₩11,962 million of gain on debt redemption and ₩(5,483) million of other capital surplus, respectively.

(c) As discussed in note 17 to the consolidated financial statements, the Group provided collateral for the above borrowings as of December 31, 2015.

25. RetirementBenefits Plan

(a) The components of retirement benefits for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Defined benefit plans:			
Current service cost	₩	44,227	42,430
Net Interest on the net defined benefit liability		3,351	3,882
Past service cost and loss on settlement		-	(19)
		47,578	46,293
Defined contribution plans:			
Contributions recognized as expense		4,300	3,219
	₩	51,878	49,512

The Group recognized termination benefits amounting to ₩15,332million and ₩5,318million as an expense for the years ended December 31, 2015 and 2014, respectively.

(b) Changes in net defined benefit liabilitiesfor the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Balance at beginning of year	W	132,247	111,137
Current service cost		44,227	42,411
Net interest on the net defined benefit liabilities		3,351	3,882
Remeasurements of the net defined benefit liabilities before tax		(553)	28,196
Payments		(9,224)	(11,059)
Payments into plan assets		(49,224)	(42,440)
Net exchange difference		(176)	120
Balance at end of year	W	120,648	132,247
Statements of financial position:			
-Present value of definedbenefit obligations	W	373,590	364,717
-Fair value of plan assets		(252,942)	(232,470)
Net Defined benefit liabilities	W	120,648	132,247

25. RetirementBenefits Plan, Continued

(c) Changes in defined benefit obligations for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Balance at beginning of year	W	364,717	315,593
Current service costs		44,227	42,430
Interest costs		9,230	11,054
Past service cost and any gains or losses on settlement		-	(19)
Remeasurements before tax		(1,075)	26,868
Payments		(43,333)	(31,329)
Net exchange difference		(176)	120
Balance at end of year	W	373,590	364,717

(d) Changes in plan assets for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Balance at beginning of year	W	232,470	204,456
Interest income		5,879	7,172
Remeasurements before tax		(522)	(1,328)
Payments		(34,109)	(20,270)
Payments into plan assets		49,224	42,440
Balance at end of year	W	252,942	232,470

Actual returns on plan assets for the years ended December 31, 2015 and 2014 are ₩5,357 million and ₩5,844 million, respectively.

(e) The amount ofremeasurementsof the net defined benefit liabilitiesfor the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Actuarial gains and lossesbefore tax:			
- Demographic assumptions	W	1,705	-
- Financial assumptions		(9,170)	(3,172)
- Experience adjustments		8,540	(23,696)
The return on plan assets, excluding interest income on plan assets		(522)	(1,328)
Remeasurements of the net defined benefit liabilities before tax		553	(28,196)
Tax effect		(515)	6,541

Remeasurements of the net defined benefit liabilities, net of tax	W	38	(21,655)

(f) The components of plan assets as of December 31, 2015 and 2014are as follows:

In millions of won		2015	2014
Deposits	W	27,551	54,310
Other		225,391	178,160
	W	252,942	232,470

25. RetirementBenefits Plan, Continued

(g) The principal actuarial assumptions as of December 31, 2015 and 2014were as follows:

	2015	2014
Discount rate	1.93%~ 2.54%	2.24%~ 3.70%
Rate of salary increases	3.00%~ 5.00%	2.00%~ 5.38%

For the purpose of calculating present value of the defined benefit obligations, the Group used the discount rate determined by reference to market yields at the end of thereporting period on high quality corporate bondsconsistent with the currency and estimated term of the defined benefit obligations.

As of December 31, 2015 and 2014,the weighted average duration of the defined benefit obligations were 9.46 and 11.49 years, respectively.

(h) Sensitivities in respect of the key assumptions used to measure the defined benefit obligationswere as follows:

In millions of won		1 percentage point increase	1 percentage point decrease
Discount rate	W	(32,745)	38,092
Rate of salary increases		37,321	(32,804)

The effect on defined benefit obligations is as of December 31, 2015.

26. Result from Operating Activities

(a) Details of expenses classified by nature for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Changes in inventories	₩	(136,611)	(88,650)
Raw materials and consumables purchased		1,299,921	1,664,086
Salaries		517,604	515,539
Retirement and termination benefits		67,210	54,830
Depreciation		151,093	149,417
Amortization		10,759	12,631
Employee welfare		94,725	64,866
Advertising		248,137	232,042
Commissions		264,302	248,535
Other expenses		286,795	87,697
	₩	2,803,935	2,940,993

26. Result from Operating Activities, Continued

(b) Details of selling, general and administrative expensesfor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Salaries	₩	346,393	339,238
Retirement and termination benefits		46,263	34,491
Employee welfare		67,978	45,806
Travel		11,338	10,714
Communications		5,226	5,500
Utilities		9,044	8,867
Taxes and dues		19,293	18,407
Supplies		3,683	3,575
Rent		22,872	25,093
Depreciation		43,609	45,585
Amortization		10,561	12,436
Repairs and maintenance		4,476	7,112
Vehicles		6,606	8,723

Insurance		1,928	1,807
Commissions		228,990	210,817
Freight and custody		52,510	48,365
Conferences		3,493	3,632
Advertising		247,985	232,432
Training		6,465	6,304
Prizes and rewards		3,238	2,337
Cooperation		813	1,328
Normal research and development		36,032	35,747
Impairment loss (reversal of impairment loss) on trade receivables		(5,462)	(8,142)
	₩	1,173,334	1,100,174

27. Other Income and Expenses

(a) Details of other income for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Foreign currency transaction gain	₩	32,055	17,337
Foreign currency translation gain		53,337	45,809
Reversal of impairment loss on other receivables		3	522
Gain on sale of property, plant and equipment		12,912	8,584
Gain on sale of intangible assets		789	54
Others		19,656	18,126
	₩	118,752	90,432

(b) Details of other expenses for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Foreign currency transaction loss	₩	14,022	16,771
Foreign currency translation loss		34,087	30,177
Impairment loss on other receivables		12	509
Donations		46,189	13,578
Loss on sale of property, plant and equipment		963	4,645
Loss on sale of intangible assets		57	17
Impairment loss on intangible assets		43,224	70,645
Others		21,607	15,425

	₩	160,161	151,767

28. Net Finance Income

(a) Details of net finance incomefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Finance income:			
Interest income	₩	33,803	37,372
Dividend income		12,098	16,842
Interest income on long-term depositsin MSA Escrow Fund		1,287	877
Gain on sale of available-for-sale financial assets		25,184	11
Gain on transactions of derivative instruments		7	-
Gain on debt redemption		11,962	-
		84,341	55,102
Finance costs:			
Interest expense		(9,482)	(10,949)
Impairment loss onavailable-for-sale financialassets		(95)	-
Loss on transactions of derivative instruments		(2)	(14)
		(9,579)	(10,963)
Net finance costs	₩	74,762	44,139

(b) Details of interest income for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Deposits	₩	30,597	31,841
Available-for-sale financial assets		40	112
Trade and other receivables		3,166	5,419
	₩	33,803	37,372

(c) Details of interest expensefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Borrowings	₩	4,261	4,998

Trade and other payables		2,168	1,632
Others		3,053	4,319
	₩	9,482	10,949

29. Income Tax

(a) The components of income tax expense for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Current income tax expense	₩	368,953	307,635
Adjustments recognized in the period for current tax of prior periods		216	5,695
Changes in temporary difference		6,219	16,518
Cash reserve tax		2,881	-
Total income tax expense		378,269	329,848
Tax expense recognized outside profit or loss		3,905	14,262
Income tax expense	₩	382,174	344,110

29. Income Tax, Continued

(b) Current and deferred tax expense (benefit) that were recognized outside profit or loss for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Current:			
- Gain on reissuance of treasury shares	₩	835	-
Deferred:			
-Net changes in fair value of available-for-sale financial assets		(5,133)	(7,720)
-Remeasurements of the net defined benefit liabilities		515	(6,542)
-Exchange differences on translating foreign operations		(122)	-
		(4,740)	(14,262)
Tax expenserecognized outside profit or loss	₩	(3,905)	(14,262)

Income tax related to gain on reissuance of treasury shares was recognized directly in equity and income tax related to remeasurements of the net defined benefit liabilities, net changes in fair value of available-for-sale financial assets and exchange differences on translating foreign operations was recognized in other comprehensive income.

(c) The income tax expensecalculated by applying statutory tax rates to the Group’s profit before taxfor the year differs from the actual tax expense in the statements ofcomprehensive incomefor the years ended

December 31, 2015 and 2014 for the following reasons:

In millions of won, except tax rate information		2015	2014
Profitbefore tax	₩	1,414,394	1,157,911
Statutory tax rate		24.7%	24.3%
Expense for income taxes at statutory tax rate		349,489	281,018
Adjustment:			
Non-taxable income		(353)	(1,888)
Non-deductible expenses		7,966	7,870
Changes in unrecognized deferred tax		24,206	20,114
Tax credits and deduction		(1,250)	(1,197)
Adjustments recognized in the period for current tax of prior periods		216	4,535
Other		1,900	33,658
Income tax expense	₩	382,174	344,110
Effective tax rate		27.0%	29.7%

29. Income Tax, Continued

(d) Changes in deferred tax assets(liabilities) for the years ended December 31, 2015 and 2014 were as follows:

(i) For the year ended December 31, 2015

In millions of won		January 1 2015	Profit or loss	Other comprehensive income	December 31 2015
Accumulated depreciation	₩	3,140	8,173	-	11,313
Allowance for bad debts		11,481	(2,281)	-	9,200
Available-for-sale financial assets		15,339	(10,720)	5,133	9,752
Accrued expense		28,847	3,200	-	32,047
Defined benefit liability		9,700	9,380	(515)	18,565
Treasury shares		(8,808)	52	-	(8,756)
Investments in associates		(283,739)	(24,723)	122	(308,340)
Provision for advanced depreciation		(14,493)	(4,763)	-	(19,256)
Reserve		(12,320)	4,818	-	(7,502)
Others		13,296	5,905	-	19,201

	₩	(237,557)	(10,959)	4,740	(243,776)

(ii) For the year ended December 31, 2014

In millions of won		January 1 2014	Profit or loss	Other comprehensive income	December 31 2014
Accumulated depreciation	₩	4,999	(1,859)	-	3,140
Allowance for bad debts		15,627	(4,146)	-	11,481
Available-for-sale financial assets		16,524	(8,905)	7,720	15,339
Accrued expense		26,422	2,425	-	28,847
Defined benefit liability		3,609	(451)	6,542	9,700
Treasury shares		(8,808)	-	-	(8,808)
Investments in Associates		(263,625)	(20,114)	-	(283,739)
Provision for advanced depreciation		(14,493)	-	-	(14,493)
Reserve		(17,689)	5,369	-	(12,320)
Others		16,395	(3,099)	-	13,296
	₩	(221,039)	(30,780)	14,262	(237,557)

(e) As of December 31, 2015 and 2014, the aggregate amounts of temporary differences associated with undistributed earnings of subsidiaries and associates for which deferred tax liabilities have not been recognized were ₩391,655 million and ₩290,242 million, respectively.

(f) Details of deductible temporarydifferences, unused tax losses, and unused tax credits for which no deferred tax asset is recognized as of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Deductible temporarydifferences	₩	29,728	29,757
Unused tax losses		118,042	116,224
Unused tax credits		4,826	2,653
	₩	152,596	148,634

30. Earnings per Share

Basic and dilutedearnings pershare for the years ended December 31, 2015 and 2014were as follows:

	2015	2014

Profit for the year attributable to ownersof the parent in millions of won	₩	1,035,717	825,606
Weighted-average number of ordinary shares outstanding		125,961,848	125,898,800
Basic and diluted earnings per share in won	₩	8,222	6,558

31. Transactions and Balances with Related Companies

(a) The Group has no significant transactions,receivables andliabilities with related parties, as of and for theyear ended December 31, 2015.

(b) There is no guarantee being provided by related parties as of December 31, 2015.

(c) Details of key management personnel compensation for the years ended December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
Short-term employee benefits	₩	22,550	23,577
Post-employment benefits		3,112	2,839
	₩	25,662	26,416

32. Risk Management and Fair Value of Financial Instruments

(a) Overview

The Group has exposure to the following risks from its use of financial instruments:

- Market risk
- Credit risk
- Liquidity risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk including quantitative disclosures.

32. Risk Management and Fair Value of Financial Instruments, Continued

(b) Risk Management Framework

The purpose of managing financial risks is to identify the potential risk factors that may affect the Group's financial performance, and minimize, eliminate and avoid it to the extent that is acceptable. One of the principal responsibilities of the treasury departmentis to manage the financial risks arising from the Group's underlying operations. The treasury departmentmonitors and manages the financial risk arising from the Group's underlying operations in accordance with the risk management policies and procedures authorized by the board of directors. Also, the treasury departmentprovides an internal report analyzing the nature and exposure level of financial risks to Risk Management Committee of the

Group. The Risk Management Committee preparesthe overall strategy for financial risk management, and evaluates the effectiveness of the financial risk management strategy. In addition, the Parent Company's audit committee consistently observes the compliance of the risk management policy and procedure, and reviews the risk exposure limit of the Group.The Group applied the same financial risk management strategy that was applied in the previous period.

(c) Management of Financial Risks

(i) Market risk

Market risk is the risk that changes in market prices – such as foreign exchange rates, interest rates and equity prices – will affect the Group's income or the value of its financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

Currency risk
The Group has exposure to the risk that the fair value or future cash flows of a financialinstrument will fluctuate because of changes in foreignexchange rates arising from the export and import of tobacco. The Group's management has measured the currency risk internally and regularly, and has entered into foreign currency option contracts to hedge foreign currency risk in case of need.

The carrying amounts of monetary assets and liabilities denominated in a currency other than the functional currency as of December 31, 2015 and 2014 were as follows:

		2015		2014	
In millions of won		Assets	Liabilities	Assets	Liabilities
USD	₩	797,656	46,905	837,834	180,646
EUR		541	1,695	24,735	10,443
Others		7,645	21,151	10,878	2,036
	₩	805,842	69,751	873,447	193,125

As of December 31, 2015 and 2014, the effects of a 10% weakening or strengthening of functional currency against foreign currencies on profit before tax were as follows:

		2015		2014	
In millions of won		10% weakening	10% strengthening	10% weakening	10% strengthening
Increase (decrease) in profit before tax	₩	73,609	(73,609)	68,032	(68,032)

32. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

Equity price risk

The Grouphas exposure to the risk that the fair value or future cash flows of a financialinstrument will fluctuate because of changes in market prices. Other market price risk arises from available-for-sale equity instruments held for investments. The Group's management has monitored the mix of debt and equity instruments in its investment portfolio based onmarket indices. Material investments within the portfolio are managed on an individual basisand all buy and sell decisions are approved by the Group's management.

As of December 31, 2015 and 2014, the effects of a 5% fluctuation of the price index of stocks on other comprehensive income were as follows:

		2015		2014	
In millions of won		5% increase	5% decrease	5% increase	5% decrease
Increase (decrease) in comprehensive incomebefore tax	₩	1,780	(1,780)	5,676	(5,676)

Interest rate risk

The Group has exposure to the risk that the fair value or future cash flows of a financialinstrument will fluctuate because of changes in marketinterest rates.The Group's management has monitored the level of interest rates regularly and hasmaintained the balance of borrowings at variable rates and fixed rates. As of December 31, 2015, there is no significant effect on cash flows or the fair value of financial liabilities from the interest rate fluctuation, considering the amounts of interest bearing liabilities.

(ii) Credit risk

The Group has exposure to the risk that one party to a financial instrument will cause afinancial loss for the other party by failing to discharge anobligation. The Group has transacted with customers with high credit ratings to manage credit risk, and has implemented and operated policies and procedures for credit enhancements of the financial assets. Counterparty credit risk is managed by evaluating its credit rating and limiting the aggregate amount and duration of exposurebefore sales commence, and the Grouphas been provided collateral and guarantees. The credit ratings of all counterparties and the level of collateral and guarantees are reviewed regularly. Analysis of financial assets past due has been reported quarterly and appropriate measures have been taken to secure the Group's assets.

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit riskas of December 31, 2015 and 2014is as follows:

In millions of won		2015	2014
Available-for-sale debt instruments	₩	1,596	2,596
Long-term deposits in MSA Escrow Fund		403,966	301,808
Trade and other receivables		1,293,009	1,076,512
Other financial assets		1,136,918	668,695
Cash and cash equivalents (excluding cash on hand)		543,425	404,540
Financial guarantee contract		76,566	150,063

₩	3,455,480	2,604,214

32. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

(iii) Liquidity risk

The Grouphas exposure to the risk that an entity will encounter difficulty in meetingobligations associated with financial liabilities.The Group’s management has established short-term and long-term financial management plans to manage the liquidity risk,and analyzed cash outflows occurred and cash outflows budgeted, so as to match the maturity structure of financial assets and financial liabilities.The Group’s management determines whether or not the financial liabilities are repayable with the operating cash flows and cash inflows from financial assets.

The maturity analysis with a residual contractual maturity of financial liabilities as of December 31, 2015 and 2014 is as follows:

				Residual contractual maturity			
In millions of won		Carrying amount	Contractual cash flow	Within 3 months	Between 3 months and 1 year	Between 1 and 5 years	Beyond 5 years
As of December 31, 2015:							
Trade and other payables	₩	406,940	408,593	368,074	27,043	11,042	2,434
Long-term borrowings		102,242	104,044	98	293	43,557	60,096
Current portion of long-term borrowings		27,659	27,676	296	27,380	-	-
Short-term borrowings		206,373	208,593	122,917	85,676	-	-
Financial guarantee contract		-	76,566	-	-	76,566	-
	₩	743,214	825,472	491,385	140,392	131,165	62,530
As of December 31, 2014:							
Trade and other payables	₩	377,359	379,047	328,406	17,414	33,227	-
Long-term borrowings		137,795	144,266	720	2,171	33,953	107,422
Current portion of long-term borrowings		1,218	1,248	302	946	-	-
Short-term borrowings		141,861	143,438	115,604	27,834	-	-
Financial guarantee contract		-	150,063	-	150,063	-	-
	₩	658,233	818,062	445,032	198,428	67,180	107,422

The above financial liabilities are presented at the nominal value of undiscounted future cash flows as of the earliest period at which the Group can be required to pay.

32. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair value of Financial Instruments

The carrying amount of each category of financial assets and liabilitiesas of December 31, 2015 and 2014 are as follows:

In millions of won		2015	2014
Financial assets:			
Available-for-sale financial assets	₩	364,681	326,833
Loans and receivables			
- Trade and other receivables		403,966	301,808
- Long-term deposits in MSA Escrow Fund		1,293,009	1,076,512
- Other financial assets		1,136,918	668,695
- Cash and cash equivalents		546,213	416,394
		3,380,106	2,463,409
	₩	3,744,787	2,790,242
Financial liabilities:			
Financial liabilities measured at amortized cost			
- Trade and other payables	₩	406,940	377,359
- Long-term borrowings		102,242	137,795
- Current portion of long-term borrowings		27,659	1,218
- Short-term borrowings		206,373	141,861
	₩	743,214	658,233

32. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair value of Financial Instruments, Continued

The fair value measurements classified by fair value hierarchy as of December 31, 2015 and 2014 were as follows:

			Fair value		
In millions of won		Carrying amount	Level I	Level II	Level III
As of December 31, 2015:					
Financial assets					
Available-for-sale financial assets	₩	327,022	211,914	-	115,108
As of December 31, 2014:					

Financial assets					
Available-for-sale financial assets	₩	297,135	206,409	-	90,726

There is no transfer between fair value hierarchy levels of recurring fair value measurements for the years ended December 31, 2015 and 2014.

The fair value measurements for available-for-sale equity instruments in real estate trust fund have been categorized as a level 3 fair value based on the inputs to the valuation techniques used. Changes in fair value classified as level 3 for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	90,726	62,467
Acquisition		22,200	38,992
Disposal		-	(14,411)
Changes in fair value		2,182	3,678
Ending balance	₩	115,108	90,726

32. Risk Management and Fair Value of Financial Instruments, Continued

(e) Finance income (costs)

(i) Details of finance income (costs) by categories for the years ended December 31, 2015 were as follows:

In millions of won		Financial assets at fair value through profit or loss	Available-for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	₩	-	40	33,763	-	33,803
Dividend income		-	12,098	-	-	12,098
Interest income on long-term depositsin MSAEscrow Fund		-	-	1,287	-	1,287
Gain on sale of available-for-sale financial assets		-	25,184	-	-	25,184
Gain on transactions of derivative instruments		7	-	-	-	7
Gain on debt redemption		-	-	-	11,962	11,962
Interest expense		-	-	-	(9,482)	(9,482)

Impairment loss on						
available-for-sale financial assets		-	(95)	-	-	(95)
Loss on transactions of derivative instruments		(2)	-	-	-	(2)
	₩	5	37,227	35,050	2,480	74,762
Comprehensive loss before tax						
Net change in fair value	₩	-	3,881	-	-	3,881
Disposal		-	(25,184)	-	-	(25,184)
Impairment		-	95	-	-	95
	₩	-	(21,208)	-	-	(21,208)

(ii) Details of finance income (costs) by categories for the year ended December 31, 2014 were as follows:

In millions of won		Financial assets at fair value through profit or loss	Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	₩	-	112	37,260	-	37,372
Dividend income		-	16,842	-	-	16,842
Interest income on						
long-term depositsin MSAEscrow Fund		-	-	877	-	877
Gain on sale of						
available-for-sale financial assets		-	11	-	-	11
Interest expense		-	-	-	(10,949)	(10,949)
Loss on transactions of derivative instruments		(14)	-	-	-	(14)
	₩	(14)	16,965	38,137	(10,949)	44,139
Comprehensive income before tax						
Net change in fair value	₩	(14)	(11,510)	-	-	(11,510)
Disposal		-	(11)	-	-	(11)
	₩	-	(11,521)	-	-	(11,521)

33. Capital Management

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The board of directors seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

The Group monitors capital using net debt deducting cash and cash equivalents and current financial instruments from borrowings and equity. The Group applied the same capital management strategy that was applied in the previous year.

As of December 31, 2015 and 2014, the Group's capital structure was as follows:

In millions of won		2015	2014
Net debt:			
Debt(borrowings)	₩	336,274	280,874
Less:			
Cash and cash equivalents		(546,213)	(416,394)
Current other financial assets		(1,136,906)	(668,436)
		(1,346,845)	(803,956)
Equity	₩	6,275,499	5,708,080

34. Contingent Liabilities and Commitments

(a) Each year the Groupdeposits a proportion of sales of tobacco products in the United States in accordance with the Tobacco Master Settlement Agreement ("MSA") under the Escrow Statute of the United States government. The MSA Escrow Funds are maintained to pay the medical expenses of tobacco purchasers who have suffered health effects as a result of smoking. The unused portion of this fund will be refunded to the Group 25 years from the date of each annual funding. The Group recorded as long-term deposits the amounts paid into the MSA Escrow Funds of State governments in the United States against potential litigation and damages related to the export of tobacco into the United States.

(b) As of December 31, 2015, the tobacco lawsuits claiming damages of ₩100 million and a lawsuit by National Health Insurance Service claiming damages of ₩53,742 million are filed against the Group. Additionally, as of December 31, 2015, the Group is involved in thirteen lawsuits as a plaintiff for alleged damages totalling ₩15,479 million and ten lawsuits as a defendant for alleged damages totalling ₩2,851 million. The amount of the liability the Group may ultimately be liable for with respect to the litigation cannot be reasonably estimated as of December 31, 2015.

(c) As of December 31, 2015, the Group has entered into letter of credit agreements with KEB Hana Bankand other banks with limits in the aggregate of USD63,800 thousand.

(d) As of December 31, 2015, the Group's trade receivables from the export of cigarettes are insured against non-payment up to USD20,380 thousand by an export guarantee insurance with the Korea Export Insurance Corporation.

34. Contingent Liabilities and Commitments, Continued

(e) The Group has been provided with a foreign currency payment guarantee for local dealers in Russia and other countries up to USD 40,000 thousand by KEB Hana Bank. Details of guarantees exercised as of

December 31, 2015, are summarized as follows:

In thousands of USD, THB and millions of IDR		Exercised amount
Customs bond and L/C opening of Global Trading, Inc.	USD	14,222
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB	8,142
Payment guarantee for purchase of certificate stamp of PT MandiriMahaMulia	IDR	128,410

(f) The Group has maintained a contract with the farmers who grow six-year old green ginseng for purchasevolume guarantees and recorded contractual amounts paid to the farmers as advance payments in the amountof₩151,783million and ₩170,524 million as of December 31, 2015 and 2014, respectively.

(g) As of December 31, 2015, the Group has an accounts receivable loan agreement with a limit of₩107,000 million with KEB Hana Bank and other financial institutions.

(h) As of December 31, 2015, the Group has a trade bill loan agreement with a limit of ₩10,000 millionwith KEB Hana Bank and other financial institutions.

(i) As of December 31, 2015, the Group has a loan agreement with a limit of ₩162,652million withShinhan Bank and other financial institutions.

(j) As of December 31, 2015, the Group has provided one blank note, five notes amounting to ₩4,000millionand two blank checks to Nara Credit and other financial institutions. Besides, as of December 31, 2015, the Group lost seven blank notes and one blank check and expects to proceed a judgment of nullification.

(k) On March 17, 2011, the Group signed the memorandum of understanding ("MOU") on global investment partnership with National Pension Serviceto jointly invest in foreign assets with a limit of ₩800,000 million.

(l) With relation to the acquisition of KT&G Life Sciences Corporation, the Parent Company entered into a contract with a former owner of the acquiree, Gwak, Tae-Hwan ("Individual Shareholder"). Details of the contract are as follows:

Description	Details
Restriction of disposal	Individual Shareholder shall not be permitted to dispose of its shares, in whole or in part, within one year after KT&G Life Sciences Corporation is listed.

Right of first refusal held by the Parent Company	Individual Shareholder shall not be permitted to make any transfer of its shares, in whole or in part, unless Individual Shareholder has offered them first to the Parent Company.
Tag-along right held by Individual Shareholder	In the event that the Parent Company proposes to enter into a transaction or a series of related transactions with a third party purchaser to dispose of its shares, then Individual Shareholder shall elect to participate in such disposition upon the terms and conditions no less favorable than those applicable to the Parent Company.

34. Contingent Liabilities and Commitments, Continued

(m) As of December 31, 2015, the Group has provided guarantees up to ₩225,600 million with an exercised amount of ₩76,566 million for the buyers of apartments in respect of their borrowings from Shinhan Bank.

(n) As of December 31, 2015, the Group is insured by performance guarantee insurance up to ₩2,281 millionwith the Seoul Guarantee Insurance.

(o) The Group sold its property, plant and equipment and intangible assetsrelating to the drink business of Iksan factory to Haitai Beverage Co.,Ltd. and LG Household& Health CareCo., Ltd., as approved by the Board of Directors on October 16, 2013. In connection, the Group entered into an agreement to refrain from engaging in a business such as beverage manufacture or pharmacy distribution, that could result in a competition with the buyer for three years from the transaction date.

35. Cash Flows from Operating Activities

(a) Details of cash generated from operations for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Profit for the year	₩	1,032,220	813,801
Adjustments for:			
Income tax expense		382,174	344,110
Finance costs		9,579	10,963
Finance income		(84,341)	(55,102)
Depreciation		151,093	149,417
Amortization		10,759	12,631
Retirement and termination benefits		67,210	51,313
Foreign currency translations loss		34,087	30,177
Impairment loss on trade and other receivables		12	509

Write-down (reversal of write-down) of inventories		(565)	1,540
Loss on sale of property, plant and equipment		963	4,645
Loss on sale of intangible assets		57	17
Impairment loss on intangible assets		43,224	70,645
Other expense		13,952	6,624
Share of gain of associates		(15,137)	(3,245)
Foreign currency translations gain		(53,337)	(45,809)
Reversal of impairment loss on trade and other receivables		(5,465)	(8,664)
Gain on sale of property, plant and equipment		(12,912)	(8,584)
Gain on sale of intangible assets		(789)	(54)
		1,572,784	1,374,934
Changes in working capital:			
Trade and other receivables		(185,672)	(71,383)
Advance payments		12,626	29,412
Prepaid expenses		(2,522)	1,387
Prepaid tobacco excise and other taxes		(187,086)	1,883
Inventories		(145,968)	(65,640)
Trade and other payables		88,086	(72,032)
Advance receipts		(10,942)	4,414
Tobacco excise and other taxes payable		521,234	(89,803)
Payment of retirement and termination benefits		(76,940)	(54,050)
Cash generated from operations	₩	1,585,600	1,059,122

(b) Details of material transactions without cash inflow and outflow for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Increase in accrued expenses related with payment of retirement and termination benefits	₩	1,140	-
Decrease in other payables related with acquisition of property, plant and equipment		8,360	
Decrease in advance receipts related with disposal of property, plant and equipment and non-current assets held for sale		2	-
Increase in other receivables related with disposal of property, plant and equipment		184	-

(c) The Group presented cash flows arising from short-term financial instruments on a net basis.

2. Separate Financial Statements

1) Separate Statements of Financial Position(Balance Sheet)

29th Fiscal Year: As of December 31, 2015
28th Fiscal Year: As of December 31, 2014

□ Assets

KT&G Corporation

(Unit: billion Won, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
1. Total non-current assets	**3,469.0**	**3,311.6**	**157.4**	**4.8**
1) Property, plant and equipment	1,309.6	1,279.7	29.9	2.3
2) Intangible assets	22.5	19.6	2.9	14.8
3) Long term trade and other receivables	78.6	120.7	-42.1	-34.9
4) Investment property	136.8	140.2	-3.4	-2.4
5) Investments in associates	46.2	60.2	-14.0	-23.3
6) Investments in subsidiaries	1,124.4	1,081.8	42.6	3.9
7) Available-for-sale financial assets	340.2	303.4	36.8	12.1
8) Long term deposits	404.0	301.8	102.2	33.9
9) Long term prepaid expenses	6.7	4.2	2.5	59.5
2. Total current assets	**3,978.7**	**2,982.9**	**995.8**	**33.4**
1) Inventories	889.0	910.4	-21.4	-2.4
2) Current trade and other receivables	1,074.9	824.9	250.0	30.3
3) Current Available-for-sale financial assets	0.0	1.0	-1.0	-
4) Prepaid tobacco excise and other taxes	447.8	260.8	187.0	71.7
5) Advance payments	26.5	20.3	6.2	30.5
6) Prepaid expenses	4.1	3.9	0.2	5.1
7) Other financial assets	1,092.0	640.0	452.0	70.6
8) Cash and cash equivalents	444.4	321.6	122.8	38.2
3. Non-current asset held for sale	**1.5**	**0.4**	**1.1**	**-**
Total assets	**7,449.2**	**6,294.9**	**1,154.3**	**18.3**

□ Equities and liabilities

KT&G Corporation

(Unit: billion Won, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
Total equities	**5,896.5**	**5,341.7**	**554.8**	**10.4**
1. Capital stock	955.0	955.0	0.0	0.0
2. Treasury shares	-337.1	-339.0	1.9	-0.6
3. Gain on reissuance of treasury shares	494.6	492.0	2.6	0.5
4. Other capital surplus	3.6	3.6	0.0	0.0
5. Reserves	3,784.5	3,493.6	290.9	8.3
6. Retained earnings	995.9	736.5	259.4	35.2
Total liabilities	**1,552.7**	**953.2**	**599.5**	**62.9**
1. Total non-current liabilities	**123.0**	**167.1**	**-44.1**	**-26.4**
1) Long term trade and other payables	8.1	28.3	-20.2	-71.4
2) Long term advance receipts	0.5	2.3	-1.8	-78.3
3) Defined benefit liabilities	42.2	67.3	-25.1	-37.3
4) Deferred income tax liabilities	72.2	69.2	3.0	4.3
2. Total current liabilities	**1,429.7**	**786.1**	**643.6**	**81.9**
1) Trade and other payables	433.8	347.2	86.6	24.9
2) Short term borrowings	5.0	5.6	-0.6	-10.7
3) Advance receipts	26.0	26.3	-0.3	-1.1
4) Income taxes payable	199.8	157.5	42.3	26.9
5) Tobacco excise and other taxes payable	765.1	249.5	515.6	206.7
Total equities and liabilities	**7,449.2**	**6,294.9**	**1,154.3**	**18.3**

2) Separate Statements of Comprehensive Income(Income Statements)

29th Fiscal Year: From January 1, 2015 to December 31, 2015
28th Fiscal Year: From January 1, 2014 to December 31, 2014

KT&G Corporation

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(Unit: billion Won, %)

	29th Fiscal Year	28th Fiscal Year	Increase or Decrease	
			Amount	%
1. Sales	**2,821.7**	**2,742.6**	**79.1**	**2.9**
1) Manufactured cigarettes	2,607.7	2,500.0	107.7	4.3
2) Real estate	142.8	160.3	-17.5	-10.9
3) Exports of leaf tobacco and others	71.2	82.3	-11.1	-13.5
2. Cost of sales	**946.7**	**1,063.8**	**-117.1**	**-11.0**
1) Manufactured cigarettes	813.7	914.4	-100.7	-11.0
2) Real estate	84.9	96.0	-11.1	-11.6
3) Exports of leaf tobacco and others	48.1	53.4	-5.3	-9.9
3. Gross profit	**1,875.0**	**1,678.8**	**196.2**	**11.7**
4. Selling and administration expenses	**637.7**	**624.2**	**13.5**	**2.2**
5. Profit from operations	**1,237.3**	**1,054.6**	**182.7**	**17.3**
6. Net other income	**1.1**	**-85.4**	**86.5**	**-**
7. Net finance income	**81.0**	**76.3**	**4.7**	**6.2**
8. Profit before income taxes	**1,319.4**	**1,045.5**	**273.9**	**26.2**
9. Income tax expense	**331.5**	**298.4**	**33.1**	**11.1**
10. Profit for the period	**987.9**	**747.1**	**240.8**	**32.2**
11. Earnings per share	**7,843 KRW**	**5,934 KRW**		
12. Other comprehensive income for the period	**-9.7**	**-34.9**	**25.2**	**-**
13. Total comprehensive income for the period	**978.2**	**712.2**	**266.0**	**37.3**

3) Separate Statements of Change in Equity

KT&G Corporation

(Unit: billion Won)

	Capital stock	Other capital Surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained Earnings	Total Equity
Ⅰ. 2014. 1. 1	955.0	3.6	-339.1	492.0	3,411.1	509.8	5,302.4
Comprehensive income							
Profit for the period						747.1	747.1
Other comprehensive income							
Change in value of available for sales financial assets					-21.9		-21.9
Remeasurement of the net defined benefit liability						-13.0	-13.0
Total other comprehensive income					-21.9	-13.0	-34.9
Total comprehensive income					-21.9	734.1	712.2
Transaction with equity holders of the Company							
Cash Dividend						-402.9	-402.9
Reserve for research and human resource development					-47.5	47.5	0.0
Other Reserve					152.0	-152.0	0.0
Total transaction with equity holders of the Company					104.5	-507.4	-402.9
Ⅱ. 2014. 12. 31	**955.0**	**3.6**	**-339.1**	**492.0**	**3,493.7**	**736.5**	**5,341.7**

(Unit: billion Won)

	Capital stock	Other capital Surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained Earnings	Total Equity
Ⅰ. 2015. 1. 1	955.0	3.6	-339.1	492.0	3,493.7	736.5	5,341.7
Comprehensive income							
Profit for the period						987.9	987.9
Other comprehensive income							
Change in value of available for sales financial assets					-17.6		-17.6
Remeasurement of the net defined benefit liability						8.0	8.0
Total other comprehensive income					-17.6	8.0	-9.6
Total comprehensive income					-17.6	995.9	978.3
Transaction with equity holders of the Company							
Reissuance of Treasury Shares			2.0	2.6			4.6
Cash Dividend						-428.1	-428.1
Reserve for research and human resource development					-12.5	12.5	0.0
Other Reserve					320.9	-320.9	0.0
Total transaction with equity holders of the Company			2.0	2.6	308.4	-736.5	-423.5
Ⅱ. 2015. 12. 31	**955.0**	**3.6**	**-337.1**	**494.6**	**3,784.5**	**995.9**	**5,896.5**

4) Separate Statements of Cash Flows

KT&G Corporation

(Unit: billion Won)

	FY2015		FY2014	
Ⅰ. Net cash generated from operating activities		**1,316.8**		**751.6**
1. Profit for the period	987.9		747.1	
2. Total Adjustments	386.8		439.4	
Adjustment for Income tax expense	331.5		298.4	
Adjustment for Finance cost	0.9		0.8	
Adjustment for Finance income	-81.9		-77.1	
Adjustment for Depreciation & Amortization	105.4		104.2	
Adjustment for Retirement and termination benefits	47.1		29.7	
Adjustment for Foreign currency translation loss	3.3		3.2	
Adjustment for Loss(Reversal) on the write-down of inventories	-0.2		-1.9	
Adjustment for Loss on sale of property, plant, equipment and intangible assets	0.5		1.3	
Adjustment for Foreign currency translation gain	-39.8		-31.2	
Adjustment for Gain on sale of property, plant and equipment and intangible assets	-13.1		-8.1	
Adjustment for Other expense and etc.	33.1		120.1	
3. Changes in working capital	226.1		-184.3	
4. Income tax paid	-284.0		-250.6	
Ⅱ. Net cash used in investing activities		**-764.8**		**-273.7**
Interest received	29.4		30.1	
Investment income received from long-term deposits in MSA Escrow Fund	1.5		1.3	
Dividend received	20.2		20.5	
Proceeds from sale of available-for-sale financial assets	0.2		10.0	
Proceeds from sale of investment in associates	13.6		0.0	
Decrease in guarantee deposits	18.2		19.8	
Decrease in loans	11.2		13.6	
Proceeds from sale of property, plant, equipment and intangible assets	11.2		8.8	
Proceeds from sale of asset held for sale	4.3		0.1	
Decrease(Increase) in other financial assets	-440.0		20.0	
Increase in loans	-59.9		-9.9	
Acquisition of investment in subsidiaries	-77.2		-8.1	
Acquisition of investment in associates	0.0		0.0	
Acquisition of redeemable convertible preference shares	-26.0		0.0	
Acquisition of available-for-sale financial assets	-34.2		-52.0	
Increase in long-term deposits in MSA Escrow Fund	-78.5		-70.1	
Acquisition of property, plant, equipment	-142.2		-237.0	
Acquisition of investment property	-0.1		-0.2	
Increase in guarantee deposits and etc	-16.5		-20.6	
Ⅲ. Net cash used in financing activities		**-429.2**		**-402.2**

Decrease in deposits received	-4.6		-2.8	
Dividend paid	-428.0		-402.9	
Increase in deposits received	3.4		3.5	
Ⅳ. Net change in cash and cash equivalents (Ⅰ+Ⅱ+Ⅲ)		**122.8**		**75.7**
Ⅴ. Cash and cash equivalents at the beginning of period		**321.6**		**245.8**
Exchange gains(losses) on cash and cash equivalents		**0.0**		**0.1**
Ⅵ. Cash and cash equivalents at the end of period		**444.4**		**321.6**

5) Notes to Separate Financial Statements

KT&G CORPORATION

Notes to the Separate Financial Statements

For the years ended December 31, 2015 and 2014

1. Organization and Description of Business

KT&G Corporation (the "Company"), which is engaged in manufacturing and selling tobaccos, was established on April 1, 1987 as Korea Monopoly Corporation, a wholly-owned enterprise of the Korean government, pursuant to the Korea Monopoly Corporation Act, in order to secure financing and to promote and develop, through efficient management, the monopoly business of red ginseng and tobacco. On April 1, 1989, the Company changed its name to Korea Tobacco and Ginseng Corporation pursuant to the Korea Tobacco and Ginseng Corporation Act. Also, pursuant to the Act on Management Reform and Privatization of Public Enterprises, proclaimed on August 28, 1997 and enforced on October 1, 1997, the Company was excluded from the application of the Act for the Management of Government Invested Enterprises. Accordingly, the Company became an entity existing and operating under the Commercial Act of Korea. The Korean government sold 28,650,000 shares of the Company to the public during 1999 and the Company listed its shares on the Korea Exchange (formerly, the Korea Stock Exchange) on October 8, 1999. On December 27, 2002, the Company changed its name again to KT&G Corporation from Korea Tobacco and Ginseng Corporation.

As of December 31, 2015, the Company has three manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 123 branches for the sale of tobacco throughout the country. Also,the Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printingplant for the manufacturing of packaging. The head office of the Company is located in 71, Beotkkot-gil,Daedeok-gu, Daejeon.

Pursuant to the Korean government's privatization program and management reorganization plan, on December 28, 1998, the shareholders approved a plan to separate the Company into two companies by setting up a subsidiary for its red ginseng business segment effective January 1, 1999. The separation was accomplished by the Company's contribution of the assets and liabilities in the red ginseng business segment into a wholly-owned subsidiary, Korea Ginseng Corporation.

On October 17, 2002 and October 31, 2001, the Company listed 35,816,658 and 45,400,000 Global Depositary Receipts ("GDR") (each GDR representing the right to receive one-half share of an ordinary share of the Company), respectively, on the Luxembourg Stock Exchange pursuant to the Korean government's privatization program. Also, on June 25, 2009,the market of the Company's GDR was changed from the BdLmarket to the Euro MTF in theLuxembourg Stock Exchange.

The ownership of the Company's issued ordinary sharesas of December 31, 2015 is held as follows:

Shareholder	Number of shares	Percentage of ownership
National Pension Service	11,098,167	8.08%
Industrial Bank of Korea	9,510,485	6.93%
Employee Share Ownership Association	2,603,918	1.90%
Treasury shares	11,326,605	8.25%
Others	102,753,322	74.84%
	137,292,497	100.00%

2. Basis of Preparation

(a) Statement of Compliance

The separate financial statements have been prepared in accordance with Korean International Financial Reporting Standards ("K-IFRS"), as prescribed in *the Act on External Audits of Corporations* in the Republic of Korea.

These financial statements are separate financial statements prepared in accordance with K-IFRS No.1027 *Separate Financial Statements* presented by a parent, an investor in an associate or a venture in a jointly controlled entity, in which the investments are accounted for on the basis of the direct equity interest rather than on the basis of the reported results and net assets of the investees.

The separate financial statements were authorized for issue by the Board of Directors on January 21, 2016, which will be submitted for approval to the shareholders' meeting to be held on March 18, 2016.

(b) Basis of Measurement

The separate financial statements have been prepared on the historicalcost basis, except for the following material items in the separate statements of financial position:

- Derivative financial instruments measured at fair value
- Available-for-sale financial assets measured at fair value
- Liabilities for defined benefit plans recognized at the net of the total present value of defined benefit obligations less the fair value of plan assets

(c) Functional and Presentation Currency

These separate financial statements are presented in Korean won, which is the Company's functional currency and the currency of the primary economic environment in which the Company operates.

(d) Use of Estimates and Judgments

The preparation of the separate financial statements in conformity with K-IFRS requiresmanagement to make judgements, estimates and assumptions that affect the applicationof accounting policies and the reported amounts of assets, liabilities, income and expenses.Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following note:

- Note 4 – classification of financial instruments;

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are included in the following notes:

- Note 10 – impairment test: key assumptions underlying recoverable amounts;
- Note 25 – measurement of defined benefit obligations: key actuarial assumptions; and
- Notes 34– recognition and measurement of contingencies: key assumptions about likelihood and magnitude of an outflow of resources.

2. Basis of Preparation, Continued

(e) Measurement of Fair Values

A number of the Company's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities. The Company has an established control framework with respect to the measurement of fair values. This includes a valuation team that has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values, and reports directly to the CFO.

The valuation team regularly reviews significant unobservable inputs and valuation adjustments. If third party information, such as broker quotes or pricing services, is used to measure fair values, then the valuation team assesses the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of K-IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

Significant valuation issues are reported to the Company's Audit Committee.

When measuring the fair value of an asset or a liability, the Company uses market observable data as far as possible. Fair values are categorized into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability fall into different levels of the fair value hierarchy, then the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.The Company recognizes transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values is included in following notes:

- Note 8 – investment property
- Note 32 – financial instruments

3. Changes in Accounting Policies

The accounting policies applied in these separate financial statements are the same as those applied in the Company's separate financial statements as of and for the year ended December 31, 2014, except for the adoption of amendments to K-IFRS 1019 *Employee Benefits*.

Amendments to K-IFRS 1019 introduced a practical expedient to accounting for defined benefit plan, when employees or third parties pay contributions if certain criteria are met. According to the amendments, the entity is permitted to recognize those contributions as a reduction of the service cost in the period in which the related service is rendered, instead of forecast future contributions from employees or third parties and attribute them to periods or service as negative benefits.

The Company retrospectively applied the amendments in accordance with the transitional requirements of K-IFRS 1019.The changesdo not have a significant impact on the Company's separate financial statements.

4. Significant Accounting Policies

The significant accounting policies applied by the Company in preparation of its separate financial statements are included below. The accounting policies set out below have been applied consistently to all periodspresented in these separate financial statements except for the changes in accounting policies as explained innote 3.

(a) Subsidiaries and Associates in the Separate Financial Statements

These separate financial statements are prepared and presented in accordance with K-IFRS No.1027. The Company applied the cost method to investments in subsidiaries, associates and joint ventures in accordance with K-IFRS No. 1027. Dividends from a subsidiaries, associates and joint ventures are recognized in profit or loss when the right to receive the dividend is established.

(b) Property, Plant and Equipment

All property, plant and equipment are stated at historical cost less depreciation and accumulated impairment loss. Historical cost includes expenditures directly attribute to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Property, plant and equipment, except for land and other tangible fixed assets, are depreciated on a straight-line basis over estimated useful lives that appropriately reflect the pattern in which the asset's future economic benefits are expected to be consumed.

The estimated useful lives of the Company's assets are as follows:

	Useful lives (years)		Useful lives (years)
Buildings	10 ~ 60	Vehicles	4
Structures	10~ 40	Tools	4
Machinery	10~ 12	Furniture and fixtures	4

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in other income and expense in the statement of comprehensive income.

4. Significant Accounting Policies, Continued

(c) Borrowing Costs

The Company capitalizes borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Other borrowing costs are recognized in expense as incurred. A qualifying asset is an asset that requires a substantial period of time to get ready for its intended use or sale. Financial assets and inventories that are manufactured or otherwise produced over a short period of time are not qualifying assets. Assets that are ready for their intended use or sale when acquired are not qualifying assets.

To the extent that the Company borrows funds specifically for the purpose of obtaining a qualifying asset, the Company determines the amount of borrowing costs eligible for capitalization as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings. The Company immediately recognizes other borrowing costs as an expense. To the extent that the Company borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the Company determines the amount of borrowing costs eligible for capitalization by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the Company that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that the Company capitalizes during a period does not exceed the amount of borrowing costs incurred during that period.

(d) Government Grants

Government grants are not recognized unless there is reasonable assurance that the Company will comply with the grant's conditions and that the grant will be received.Government grants which are intended to compensate the Company for expenses incurred are recognized as other income in profit or loss over the periods in which the Company recognizes the related costs as expenses.

(e) Intangible Assets

Intangible assets are measured initially at cost and, subsequently, are carried at cost less accumulated amortization and accumulated impairment losses. Intangible assets consist of industrial property rights, facility usage rights andintangible assets under development. Intangible assets are amortized on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The residual value of intangible assets is assumed to be zero. However, as there are no foreseeable limits to the periods over which some of industrial property rights and facility usage rights are expected to be available for use, these intangible assets are regarded as having indefinite useful lives and not amortized.

The estimated useful lives are as follows:

	Useful lives (years)
Industrial property rights	10 ~ 20 or indefinite
Facility usage rights	indefinite

Amortization periods and amortization methods for intangible assetswith finite useful lives are reviewed at the end of each reporting period. The useful lives of intangible assets that are not being amortized are reviewed at the end of each reporting period to determine whether events and circumstances continue to support indefinite useful life assessment for those assets.The change is accounted for as a change in an accounting estimate.

4. Significant Accounting Policies, Continued

(f) Investment Property

Property held for the purpose of earning rentals or benefiting from capital appreciation is classified as investment property. Investment property is initially measured at its cost. Transaction costs are included in the initial measurement. Subsequently, investment property is carried at depreciated cost less any accumulated impairment losses.

Subsequent costs are recognized in the carrying amount of investment property at cost or, if appropriate, as separate items if it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing are recognized in profit or loss as incurred.

Investment property except for land, are depreciated on a straight-line basis over 10 ~ 60 years as estimated useful lives.

Depreciation methods, useful lives and residual values are reviewed at the end of each reporting date and adjusted, if appropriate. The change is accounted for as a change in an accounting estimate.

(g) Non-current Assets Held for Sale

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. In order to be classified as held for sale, the asset (or disposal group) must be available for immediate sale in its present condition and its sale must be highly probable. The assets or disposal group that are classified as non-current assets held for sale are measured at the lower of their carrying amount and fair value less cost to sell.

The Company recognizes an impairment loss for any initial or subsequent write-down of an asset (or disposal group) to fair value less costs to sell, and a gain for any subsequent increase in fair value less costs to sell, up to the cumulative impairment loss previously recognized in accordance with K-IFRS No. 1036*Impairment of Assets*.

A non-current asset that is classified as held for sale or part of a disposal group classified as held for sale is not depreciated (or amortized).

(h) Inventories

Inventories are measured at the lower of cost and net realizable value.The cost of inventories comprises all costs of purchase, costs of conversionand other costs incurred in bringing the inventories to their present location andcondition.

The costof inventories is determined by the weighted-average method for finished goods, by-products, work-in-progress and tobacco leaf in raw materials, by the moving-average method for raw materials and supplies; and by thespecific identification method for all other inventories.

4. Significant Accounting Policies, Continued

(h) Inventories, Continued

When inventories are sold, the carrying amount of those inventories is recognized as an expense in the period in which the related revenue is recognized.The amount of any write-down of inventories to net realizable value and all lossesof inventories are recognized as an expense in the period the write-down orloss occurs. The amount of any reversal of any write-down of inventories, arisingfrom an increase in net realizable value, is recognized as a reduction in theamount of inventories and recognized as an expense in the period in which thereversal occurs.

Tobaccoleaf inventories which have an operating cycle that exceeds12 months are classified as current assets, consistent withrecognized industry practice.The estimated amounts of inventories in current assets which are not expected to berealized within 12 months are ₩310,043million and ₩272,649million, respectively, as of December 31, 2015 and 2014.

(i) Impairment of Non-financial Assets

The carrying amounts of the Company's non-financial assets, other than inventories, deferred tax assets,assets arising from employee benefits and non-current assets held for sale, are reviewed at the end of the reporting period to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and intangible assets that have indefinite useful lives or that are not yet available for use, irrespective of whether there is any indication of impairment, are tested for impairment annually by comparing their recoverable amount to their carrying amount.

The Company estimates the recoverable amount of an individual asset. If it is impossible to measure the individual recoverable amount of an asset, then the Company estimates the recoverable amount of cash-generating unit ("CGU"). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. The value in use is estimated by applying a pre-tax discount rate that reflect current market assessments of the time value of money and the risks specific to the asset or CGU for which estimated future cash flows have not been adjusted, to the estimated future cash flows expected to be generated by the asset or CGU.

An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

(j) Non-derivative Financial Assets

The Company recognizes and measures non-derivative financial assets by the following four categories: financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables and available-for-sale financial assets. The Company recognizes financial assets in the statement of financial position when the Company becomes a party to the contractual provisions of the instrument.

Upon initial recognition, non-derivative financial assets are measured at their fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the asset's acquisition or issuance.

4. Significant Accounting Policies, Continued

(j) Non-derivative Financial Assets, Continued

(i) Financial assets at fair value through profit or loss

A financial asset is classified as financial assets are classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Upon initial recognition, transaction costs are recognized in profit or loss when incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

(ii) Held-to-maturity investments

A non-derivative financial asset with a fixed or determinable payment and fixed maturity, for which the Company has the positive intention and ability to hold to maturity, are classified as held-to-maturity investments. Subsequent to initial recognition, held-to-maturity investments are measured at amortized cost using the effective interest method.

(iii) Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method except for loans and receivables of which the effect of discounting is immaterial.

(iv) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as financial assets at fair value through profit or loss, held-to-maturity investments or loans and receivables. Subsequent to initial recognition, they are measured at fair value, which changes in fair value, net of any tax effect, recorded in other comprehensive income in equity. Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments are measured at cost.

(v) De-recognition of financial assets

The Company derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Company is recognized as a separate asset or liability.

If the Company retains substantially all the risks and rewards of ownership of the transferred financial assets, the Company continues to recognize the transferred financial assets and recognizes financial liabilities for the consideration received.

4. Significant Accounting Policies, Continued

(j) Non-derivative Financial Assets, Continued

(vi) Offsetting between financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position only when the Company currently has a legally enforceable right to offset the recognized amounts, and there is the intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

(k) Derivative Financial Instruments

Derivatives are initially recognized at fair value. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are recognized immediately in profit or loss.

Embedded derivatives are separated from the host contract and accounted for separately only if the following criteria have been met:

- the economic characteristics and risks of the embedded derivative are not closely related to those of the host contract
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative and
- the hybrid instrument is not measured at fair value with changes in fair value recognized in profit or loss.

Changes in the fair value of separable embedded derivatives are recognized immediately in profit or loss.

(l) Impairment of Financial Assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably. However, losses expected as a result of future events, regardless of likelihood, are not recognized.

If financial assets have objective evidence that they are impaired, impairment losses should be measured and recognized.

(i) Financial assets measured at amortized cost

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of its estimated future cash flows discounted at the asset’s original effective interest rate. If it is not practicable to obtain the instrument’s estimated future cash flows, impairment losses would be measured by using prices from any observable current market transactions. The Company can recognize impairment losses directly or establish a provision to cover impairment losses. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed either directly or by adjusting an allowance account.

4. Significant Accounting Policies, Continued

(l) Impairment of Financial Assets, Continued

(ii) Financial assets carried at cost

If there is objective evidence that an impairment loss has occurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses are not reversed.

(iii) Available-for-sale financial assets

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized in other comprehensive income is reclassified from other comprehensive income to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized. Impairment losses recognized in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss.For an investment in an equity security, objective evidence of impairment includes a significant or prolonged decline in its fair value below its cost. The Company considers a decline of 20% to be significant and a period of nine months to be prolonged.

(m) Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and call deposits with maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Company in the management of its short-term commitments. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preferred shares when it has a short maturity with a specified redemption date.

(n) Non-derivative Financial Liabilities

The Company classifies non-derivative financial liabilities into financial liabilities at fair value through profit or loss, financial guarantee liabilities and other financial liabilities in accordance with the substance of the contractual arrangement and the definitions of financial liabilities. The Company recognizes financial liabilities in the statement of financial position when the Company becomes a party to the contractual provisions of the financial liability.

(i) Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading or designated as such upon initial recognition. Subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss. Upon initial recognition, transaction costs that are directly attributable to the acquisition are recognized in profit or loss as incurred.

4. Significant Accounting Policies, Continued

(n) Non-derivative Financial Liabilities, Continued

(ii) Financial guarantee liabilities

Financial guarantee liability is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified term of a debt instrument. Upon initial recognition, financial guarantee liabilities are measured at their fair value plus, transaction costs that are directly attributable to the acquisition or issue of the financial guarantee liability.

After initial recognition, an issuer of such a contract measures it at the higher ofthe amount determined in accordance with K-IFRS No. 1037*Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognized less, when appropriate, cumulative amortisation recognized in accordance with K-IFRS No. 1018 *Revenue.*

(iii) Other financial liabilities

Non-derivative financial liabilities other than financial liabilities at fair value through profit or loss or financial guarantee liabilities are classified as other financial liabilities. At the date of initial recognition, other financial liabilities are measured at fair value minus transaction costs that are directly attributable to the acquisition. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

The Company derecognizes a financial liability from the statement of financial position when it is extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

(o) Employee Benefits

(i) Short-term employee benefits

Short-term employee benefits are employee benefits that are due to be settled within 12 months after the end of the period in which the employees render the related service. When an employee has rendered service to the Company during an accounting period, the Company recognizes the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

(ii) Retirement benefits: defined contribution plans

When an employee has rendered service to the Company during a period, the Company recognizes the contribution payable to a defined contribution plan in exchange for that service as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, the Company recognizes that excess as an asset (prepaid expense) to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

4. Significant Accounting Policies, Continued

(o) Employee Benefits, Continued

(iii) Retirement benefits: defined benefit plans

The calculation of defined benefit obligations is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for the Company, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. To calculate the present value of economic benefits, consideration is given to any applicable minimum funding requirements.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognized immediately in other comprehensive income. The Company determines the net interest expense (income) on the net defined benefit liability (asset) for the year by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognized in profit or loss.

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognized immediately in profit or loss. The Company recognizes gains and losses on the settlement of a defined benefit plan when the settlement occurs.

(iv) Termination benefits

Termination benefits are expensed at the earlier of when the Company can no longer withdraw the offer of those benefits and when the Company recognizes costs for a restructuring. If benefits are not expected to be settled wholly within 12months of the end of the reporting period, then they are discounted.

(p) Provisions

Provisions are recognized when the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Where the effect of the time value of money is material, provisions are determined at the present value of the expected future cash flows.

Where some or all of the expenditures required to settle a provision are expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset.

Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimates. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision is reversed.

4. Significant Accounting Policies, Continued

(q) Equity Capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of ordinary shares and share options are recognized as a deduction from equity, net of any tax effects.

When the Company repurchases its share capital, the amount of the consideration paid is recognized as a deduction from equity and classified as treasury shares. The profits or losses from the purchase, disposal, reissue, or retirement of treasury shares are not recognized as current profit or loss. If the Company acquires and retains treasury shares, the consideration paid or received is directly recognized in equity.

(r) Revenue Recognition

The Company’s revenue categories consist of goods sold, services and other income.

Revenue from sale of goods is measured at the fair value of the consideration received or receivable, net of tobacco excise and other taxes, trade discounts and volume rebates. Revenue from the sale of goods is recognized when the Company has transferred to the buyer the significant risks and rewards of ownership of the goods, the Company retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Company and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Tobacco excise and other taxes deducted from revenue for the yearsended December 31, 2015 and 2014were ₩5,179,692million and ₩3,536,343million, respectively.

Revenue from the construction of real estate includes the initial amount agreed in the contract plus any variations in contract work, claims and incentive payments, to the extent that it is probable that they will result in revenue and can be measured reliably. As soon as the outcome of a construction contract can be estimated reliably, contract revenue is recognized in profit or loss in proportion to the stage of completion of the contract. The stage of completions is assessed by reference to surveys of work performed. Meanwhile, profits from an apartment house for self-installment sales is recognized on percentage-of-completion method according to Q&A of Korea Accounting Institute, called 2011-I-KQA. This accounting standard is effective upon Korean Corporation Financial Reporting Standards of Laws on External Audit of Corporation (Article 13, Section 1, Paragraph 1)

Revenue from rendering of services is recognized by reference to the stage of completion of the transaction at the end of the reporting period when the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Company, the stage of completion of the transaction at the end of the reporting period can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably. When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue is recognized only to the extent of the expenses recognized that are recoverable.

Rental income from investment property, net of lease incentives granted, is recognized in profit or loss on a straight-line basis over the term of the lease.

4. Significant Accounting Policies, Continued

(s) Finance Income and Finance Costs

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income and interest income on long-term deposits in MSA Escrow Fund. Interest income is recognized as it accrues in profit or loss, using the effective interest method. Dividend income is recognized in profit or loss on the date that the Company's right to receive payment is established.

Finance costs is interest expense on unwinding of the discount on trade and other payables which is recognized in profit or loss using the effective interest method.

(t) Income Taxes

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

(i) Current tax

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the end of the reporting period and any adjustment to tax payable in respect of previous years. The taxable profit is different from the accounting profit for the year since the taxable profit is calculated excluding the temporary differences, which will be taxable or deductible in determining taxable profit (tax loss) of future periods, and non-taxable or non-deductible items from the accounting profit.

(ii) Deferred tax

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. The Company recognizes a deferred tax asset for all deductible temporary differences to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

The carrying amount of a deferred tax asset is reviewed at the end of each reporting period and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of that deferred tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset only if there is a legally enforceable right to offset the related current tax liabilities and assets, and they relate to income taxes levied by the same tax authority and they intend to settle current tax liabilities and assets on a net basis

4. Significant Accounting Policies, Continued

(u) Foreign Currencies

Transactions in foreign currencies are translated to the respective functional currencies of the Company at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated to the functional currency using the reporting date's exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

Foreign currency differences arising on retranslation are recognized in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments, a financial liability designated as a hedge of the net investment in a foreign operation, or qualifying cash flow hedges, which are recognized in other comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

(v) Earnings per Share

The Company presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period, adjusted for own shares held. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding, adjusted for own shares held, for the effects of all dilutive potential ordinary shares.

(w) Operating Segment

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components. All operating segments' operating results are reviewed regularly by the Company's chief executive officer to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Operating segment disclosures are included in the consolidatedfinancial statements in accordance with K-IFRS No.1108 *Operating Segments*.

5. Basis of Translating Financial Statements

The separate financial statements are expressed in Korean wonand have been translated into U.S. dollars at the rate of ₩1,172.00 to $1, the basic exchange rate on December 31, 2015 posted by Seoul Money Brokerage Services,solely for the convenience of the reader. This translation should not be construed as a representation that any or all of the amounts shown could be converted into U.S. dollars at this or any other rate.

6. Property, Plant and Equipment

(a) Details of property, plant and equipment as of December 31, 2015 and 2014are summarized as follows:

		2015			2014		
In millions of won		Cost	Accumulated depreciation	Carrying amount	Cost	Accumulated depreciation	Carrying amount
Land	₩	467,590	-	467,590	457,890	-	457,890
Buildings		696,569	(311,151)	385,418	690,661	(286,158)	404,503
Structures		44,962	(29,061)	15,901	44,422	(27,272)	17,150
Machinery		991,848	(775,864)	215,984	972,679	(735,831)	236,848
Vehicles		2,211	(1,855)	356	2,304	(2,033)	271
Tools		37,753	(32,199)	5,554	36,425	(31,978)	4,447
Furniture and fixtures		169,422	(135,913)	33,509	158,793	(123,346)	35,447
Others		1,366	-	1,366	1,312	-	1,312
Construction-in-progress		183,954	-	183,954	121,792	-	121,792
	₩	2,595,675	(1,286,043)	1,309,632	2,486,278	(1,206,618)	1,279,660

(b) Changes in property, plant and equipment for the year endedDecember 31, 2015were as follows:

In millions of won		January 1 2015	Acquisition	Disposal	Depreciation	Transfer of construction-in-progress	Other changes	December 31 2015
Land	₩	457,890	7,158	(773)	-	5,293	(1,978)	467,590
Buildings		404,503	1,238	(398)	(26,812)	9,124	(2,237)	385,418
Structures		17,150	836	(41)	(2,159)	174	(59)	15,901
Machinery		236,848	4,649	(411)	(50,716)	25,614	-	215,984
Vehicles		271	263	(14)	(193)	29	-	356
Tools		4,447	3,005	(144)	(2,101)	347	-	5,554
Furniture and fixtures		35,447	15,276	(6)	(17,236)	28	-	33,509
Others		1,312	54	-	-	-	-	1,366
Construction-in-progress		121,792	102,771	-	-	(40,609)	-	183,954
	₩	1,279,660	135,250	(1,787)	(99,217)	-	(4,274)	1,309,632

For the yearended December 31, 2015, land and buildingswith a carrying amount of ₩2,732million were transferred to investment property and land, buildings and structures with a carrying amount of ₩1,542million were transferred to non-current assets held for sale.

6. Property, Plant and Equipment, Continued

(c) Changes in property, plant and equipment for the year ended December 31, 2014 were as follows:

In millions of won		January 1 2014	Acquisition	Disposal	Depreciation	Transfer of construction-in-progress	Other changes	December 31 2014
Land	₩	410,763	1,611	(652)	-	75,028	(28,860)	457,890
Buildings		400,314	1,552	(1,182)	(26,351)	30,093	77	404,503
Structures		16,973	1,946	(21)	(2,105)	357	-	17,150
Machinery		234,926	7,410	(60)	(50,666)	51,140	(5,902)	236,848
Vehicles		362	109	-	(200)	-	-	271
Tools		3,135	2,000	(85)	(1,611)	1,008	-	4,447
Furniture and fixtures		34,524	14,220	(5)	(17,151)	3,859	-	35,447
Others		1,162	150	-	-	-	-	1,312
Construction-in-progress		80,604	207,079	(58)	-	(161,485)	(4,348)	121,792
	₩	1,182,763	236,077	(2,063)	(98,084)	-	(39,033)	1,279,660

For the year ended December 31, 2014, land and construction-in-progress with a carrying amount of ₩32,682 million were transferred to inventories and machinery with a carrying amount of ₩5,902 million wascontributedto KGC YebonCorporation as in-kind capital contribution.

7. Intangible Assets

(a) Details of intangible assets as of December 31, 2015 and 2014are summarized as follows:

		2015			2014		
In millions of won		Cost	Accumulated amortization	Carrying amount	Cost	Accumulated amortization	Carrying amount
Industrial property rights	₩	6,997	(5,535)	1,462	7,163	(5,596)	1,567
Facility usage rights		19,180	(1,708)	17,472	17,701	(2,658)	15,043
Intangible assets under development		3,560	-	3,560	3,026	-	3,026
	₩	29,737	(7,243)	22,494	27,890	(8,254)	19,636

(b) Changes in intangible assets for the year endedDecember 31, 2015 were as follows:

In millions of won		January 1 2015	Acquisition	Disposal	Amortization	December 31 2015
Industrial property rights	₩	1,567	23	(104)	(24)	1,462
Facility usage rights		15,043	3,195	(766)	-	17,472
Intangible assets under development		3,026	534	-	-	3,560
	₩	19,636	3,752	(870)	(24)	22,494

7. Intangible Assets, Continued

(c) Changes in intangible assets for the year ended December 31, 2014 were as follows:

In millions of won		January 1 2014	Acquisition	Disposal	Impairment	Amortization	December 31 2014
Industrial property rights	₩	1,625	-	-	-	(58)	1,567
Facility usage rights		17,357	347	(3)	(2,658)	-	15,043
Intangible assets under development		2,209	817	-	-	-	3,026
	₩	21,191	1,164	(3)	(2,658)	(58)	19,636

(d) Expenditures not capitalized for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Cost of sales	₩	296	250
Selling, general and administrative expenses		12,273	14,042
	₩	12,569	14,292

8. Investment Property

(a) Details of investment property as of December 31, 2015 and 2014are summarized as follows:

		2015			2014		
In millions of won		Cost	Accumulated depreciation	Carrying amount	Cost	Accumulated depreciation	Carrying amount
Land	₩	23,066	-	23,066	22,236	-	22,236
Buildings		172,757	(59,022)	113,735	170,124	(52,219)	117,905
	₩	195,823	(59,022)	136,801	192,360	(52,219)	140,141

(b) Changes in investment property for the years ended December 31, 2015 and 2014were as follows:

		2015			2014		
In millions of won		Land	Buildings	Total	Land	Buildings	Total
Beginning balance	₩	22,236	117,905	140,141	22,246	123,788	146,034
Acquisition		-	64	64	-	222	222
Depreciation		-	(6,136)	(6,136)	-	(6,028)	(6,028)
Transfer from (to) property, plant and equipment		830	1,902	2,732	(10)	(77)	(87)
Ending balance	₩	23,066	113,735	136,801	22,236	117,905	140,141

8. Investment Property, Continued

(c) The amounts recognized in profit or loss from investment propertyfor the yearsended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Rental income	₩	33,992	33,069
Direct operating expense		(6,136)	(6,028)
	₩	27,856	27,041

(d) The carrying amount and the fair value of investment propertyas of December 31, 2015 and 2014were as follows:

		2015		2014	
In millions of won		Fair value	Carrying amount	Fair value	Carrying amount
Land	₩	406,600	23,066	281,106	22,236
Buildings		171,979	113,735	180,272	117,905
	₩	578,579	136,801	461,378	140,141

The fair value of investment property was determined based on the yield capitalization method by external, independent valuers. The fair value measurement for all of the investment properties has been categorized as a level 3 fair value based on the inputs to the valuation techniques used.

9. Investments in Associates

Investments in associates as of December 31, 2015 and 2014are summarized as follows:

In millions of won			2015			2014		
Company	Location	Principal operation	Percentage of ownership		Carrying amount	Percentage of ownership		Carrying amount
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	20.24%	₩	1,830	25.34%	₩	1,830
JR CR-REIT IV Co., Ltd.	Korea	Renting real estate	-		-	49.02%		13,995
KVG REIT 1 Co., Ltd.	Korea	Renting real estate	29.67%		7,300	29.67%		7,300
KOCREF REIT 17 Co., Ltd.	Korea	Renting real estate	22.06%		7,000	22.06%		7,000
JR REIT V Co., Ltd.	Korea	Renting real estate	34.63%		5,600	34.63%		5,600
JR REIT VIII Co., Ltd.	Korea	Renting real estate	21.74%		10,000	21.74%		10,000
LSK Global Pharma Services Co., Ltd.	Korea	Researching and developing medicine	23.15%		-	23.15%		-
JR REIT X Co., Ltd.	Korea	Renting real estate	28.79%		9,500	28.79%		9,500
JR REIT XIII Co., Ltd.	Korea	Renting real estate	27.03%		5,000	27.03%		5,000
				₩	46,230		₩	60,225

In 2015, the Company’s ownership in Lite Pharm Tech, Inc. has decreased to 20.24% due to their paid-in capital increase.

In 2015, the Company recognized ₩370million of loss on disposal of investments in associates as JR CR-REIT IV Co., Ltd. was liquidated.

10. Investments in Subsidiaries

Investments in subsidiaries as of December 31, 2015 and 2014are summarized as follows:

In millions of won

Company	Location	Principal operation	2015 Percentage of ownership	2015 Carrying amount	2014 Percentage of ownership	2014 Carrying amount
Korea Ginseng Corporation	Korea	Manufacturing and sellingginseng	100.00%	₩ 672,048	100.00%	₩ 672,048
Yungjin Pharm. Ind. Co., Ltd.	Korea	Manufacturing and selling pharmaceutical	53.00%	66,355	53.00%	66,355
Tae-a Industry Co., Ltd.	Korea	Manufacturing tobacco materials	100.00%	15,698	100.00%	15,698
KT&G TutunMamulleri SanayiveTicaret A.S.	Turkey	Manufacturing and selling tobaccos	99.99%	30,049	99.99%	30,049
Korea Tabacos do Brasil Ltda.	Brazil	Processing leaf tobaccos	99.99%	2,891	99.90%	535
KT&G Pars	Iran	Manufacturing and selling tobaccos	99.99%	-	99.99%	-
KT&G Rus L.L.C.	Russia	Manufacturing and selling tobaccos	100.00%	110,297	100.00%	110,297
KGC Life & Gin Co., Ltd.	Korea	Selling ginseng door-to-door	100.00%	44,100	100.00%	44,100
Global Trading, Inc.	USA	Selling tobaccos	100.00%	4,913	100.00%	4,913
Somang Cosmetics Co., Ltd.(*)	Korea	Manufacturing and selling cosmetics	97.73%	70,676	60.00%	20,921
RenzolucPte., Ltd.(*)	Singapore	Manufacturing and selling tobaccos	100.00%	-	100.00%	22,156
KT&G Life Sciences Corporation(*)	Korea	Researching and developing medicine	73.94%	14,287	73.94%	15,332
KGC Yebon Corporation	Korea	Manufacturing and selling medical herbs	100.00%	49,828	100.00%	49,828
K-Q HongKong I, Limited(*)	HongKong	Manufacturing and selling ginseng	100.00%	17,761	100.00%	17,761
PT KT&G Indonesia	Indonesia	Manufacturing and selling tobaccos	99.99%	-	99.99%	11,400
K&I HK Co., Ltd.	HongKong	Selling cosmetics	100.00%	11	100.00%	11
K&I China Co., Ltd.	China	Selling cosmetics	100.00%	5,532	100.00%	436
SangSang Stay, Inc.	Korea	Hotel	100.00%	20,000	-	-
				₩ 1,124,446		₩ 1,081,840

(*) The Company's percentage of ownership, shown above, excludes preferred shares. As of December 31, 2015, the Company's percentage of ownership would be 97.76%, 68.91%, 59.48%and 50.00%, respectively, if preferred shares are included.

10. Investments in Subsidiaries, Continued

For the year ended December 31, 2015, the Company acquired additional shares of Somang Cosmetics Co., Ltd. for ₩49,775 million, increasing its ownership from 60.00% to 97.73%.

For the year ended December 31, 2015, the Company made an additional investment of ₩2,356 million and ₩5,096 million in Korean Tobacos do Brasil Ltda. and K&I China Co., Ltd, respectively.

For the year ended December 31, 2015, the Company established SangSang Stay, Inc.

For the year ended December 31, 2015, the Company recognized ₩34,601 million of impairment losses on investments in RenzolucPte., Ltd., KT&G Life Sciences Corporation and PT KT&G Indonesiasince the carrying amounts exceeded their recoverable amounts.

For the year ended December 31, 2014, the Company made an additional investment of ₩7,654 million in PT KT&G Indonesia and established K&I HK Co., Ltd. and K&I China Co., Ltd.

For the year ended December 31, 2014, the Company acquired ₩73,025 million of additional interest in Korea Ginseng Corporation through an in-kind capital contribution of its interest in Jilin Hanzheng Ginseng Co., Ltd. and other available-for-sale financial assets with a carrying amount of ₩47,675 million and ₩25,350 million, respectively.

For the year ended December 31, 2014, the Company acquired ₩5,902 million of interest in KGC Yebon through an in-kind capital contribution.

For the year ended December 31, 2014, the Company recognized ₩5million of loss on disposal of investments in subsidiaries as YebonNongwon Agriculture Co., Ltd. was liquidated.

For the year ended December 31, 2014, the Company recognized ₩123,900 million of impairment losses on investments in KT&G TutunMamulleriSanayiveTicaret A.S., Somang Cosmetics Co., Ltd., Renzoluc Pte, Ltd. and KT&G Life Sciences Corporation since the carrying amounts exceeded their recoverable amounts.

11. Available-for-sale Financial Assets

(a) Changes in available-for-sale financial assets for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	304,438	296,391
Acquisitions		63,190	51,992
Net changes in fair value		1,744	(28,844)
Reclassification to investments in subsidiaries		-	(24,930)
Net gain reclassified from equity		-	19,829
Disposals		(29,223)	(10,000)
Ending balance	₩	340,149	304,438
Statement of financial position:			
Current	₩	-	1,000
Non-current		340,149	303,438
	₩	340,149	304,438

In 2015, the Company acquired ₩28,990 million of ordinary shares of U&I Corporationby exercising conversion optionsembedded in their convertible bonds and convertible preference shares. The Company recognized ₩24,990 million of difference between the fair value of ordinary shares acquired and the carrying amount of bonds and preference shares converted as gain on sale of available-for-sale financial assets for the year ended December 31, 2015.

(b) Available-for-sale financial assets as of December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
Available-for-sale debt instruments:			
Corporate bonds	₩	1,500	2,500
Available-for-sale equity instruments:			
Listed			
– Oscotech, Inc.		3,696	1,030
–Shinhan Financial Group Co., Ltd.		158,530	178,171
–Rexahn Pharmaceuticals, Inc.		2,696	4,917
–U&I Corporation		22,564	-
		187,486	184,118
Unlisted		151,163	117,820
Total available-for-sale equity instruments		338,649	301,938
Total available-for-sale financial assets	₩	340,149	304,438

The fair value of listed available-for-sale equity instruments is principally based on quoted prices in an active market.

As of December 31, 2015 and 2014, ₩37,555million and ₩29,594 million of available-for-sale financial assets that do not have a market price in an active market and whose fair value cannot be reliably measured or is similar to their carrying amount are measured at cost, respectively.

12. Long-term Deposits in MSA Escrow Fund

Long-term depositsin MSA Escrow Fund as of December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
MMF	₩	43,309	19,269
Treasury note		360,657	282,539
	₩	403,966	301,808

As discussed in note 34 tothe separate financial statements, long-term depositsin MSA Escrow Fund are deposited to the United States governmentrelated to the export of tobacco to the United States.For the years ended December 31, 2015 and 2014, ₩78,492million and ₩70,094million were paid into long-term depositsin MSA Escrow Fund, respectively.

Long-term deposits in MSA Escrow Fund are invested in demand deposits of financial institutions or government and public bonds.Interest income on long-term depositsin MSA Escrow Fundfor the years ended December 31, 2015 and 2014 are ₩1,287million and ₩877million, respectively.

13. Trade and Other Receivables

(a) Trade and other receivables as of December 31, 2015 and 2014are summarized as follows:

		2015		2014	
In millions of won		Current	Non-current	Current	Non-current
Loans to employees	₩	15,767	51,976	7,811	19,885
Loans		69,813	8,204	8,612	61,711
Other receivables		142,130	1,551	72,964	1,697
Guarantee deposits		19,070	16,869	-	37,409
Accrued income		8,912	-	7,808	-
Trade receivables		819,170	-	727,753	-
	₩	1,074,862	78,600	824,948	120,702

(b) Trade and other receivablesas of December 31, 2015 and 2014have been reported in the separate statements of financial position net of allowances as follows:

		2015		2014	
In millions of won		Current	Non-current	Current	Non-current
Gross trade and other receivables	₩	1,121,048	78,600	869,457	131,276
Allowance:					
Loans		(12,447)	-	(1,099)	(10,574)
Other receivables		(7,570)	-	(7,673)	-
Accrued income		(2,264)	-	(2,126)	-
Trade receivables		(23,905)	-	(33,611)	-
		(46,186)	-	(44,509)	(10,574)
Net trade and other receivables	₩	1,074,862	78,600	824,948	120,702

13. Trade and Other Receivables, Continued

(c) Changes in the allowance account for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Beginning balance	₩	55,083	65,357
Impairment loss		2,569	510
Reversal of impairment loss		(11,466)	(10,784)
Ending balance	₩	46,186	55,083

Impairment loss (reversal of impairment loss) on trade and other receivables is included as part of selling,general and administrative expenses and other expense (income) in the separate statements of comprehensive income.

(d) The agingschedule of trade and other receivables which were past due but not impaired as of December 31, 2015 and 2014 is as follows:

In millions of won		2015	2014
Within 1 month	₩	48,107	46,952
Between 1 and 2 months		39,921	35,915
Beyond 2 months		245,788	210,237
	₩	333,816	293,104

There is no significant concentration of credit risk with respect to trade and other receivables sincetrade and other receivables, excluding export trade receivables, are widely dispersed amongst a number of customers.The Company holds pledged assets and guarantees in respect of some of the past due debtor balances.

(e) Details of trade and other receivables that are measured at amortized cost as of December 31, 2015 and 2014were as follows:

	2015				2014			
In millions of won	Effective interest rate		Current	Non-current	Effective interest rate		Current	Non-current
Loans to employees	1.89~5.68%	₩	15,767	51,976	3.00~5.68%	₩	7,811	19,885
Other receivables	-		-	-	3.79%		8,300	-
Guarantee deposits	1.89~5.68%		19,070	16,869	3.00~5.68%		-	37,409
		₩	34,837	68,845		₩	16,111	57,294

14. Inventories

(a) Inventoriesas of December 31, 2015 and 2014aresummarized as follows:

In millions of won		2015	2014
Finished goods, net of loss on the write-down of inventories	₩	72,394	83,387
Work-in-progress		15,294	7,645
Raw materials		685,101	699,260
Supplies		25,959	25,319
By-products		5,515	7,138
Buildings under construction		3,618	1,185
Sites for lotting-out construction		25,815	31,180
Goods-in-transit		55,339	55,324
	₩	889,035	910,438

(b) The amount of inventories recognized as an expensefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Cost of sales:			
Reversal of write-down of inventories	₩	(183)	(1,911)
Loss on retirement of inventories		825	3,367
Other expense:			
Loss on retirement of inventories		844	588
	₩	1,486	2,044

15. Cash and Cash Equivalents and Other Financial Assets

(a) Cash and cash equivalentsas of December 31, 2015 and 2014 aresummarized as follows:

In millions of won		2015	2014
Cash on hand	₩	2,623	883
Demand deposits		71,753	80,679
Short-term investment assets		370,000	240,000
	₩	444,376	321,562

(b) Other financial assets as of December 31, 2015 and 2014 aresummarized as follows:

In millions of won		2015	2014
Time deposits	₩	100,000	10,000
Money trust		950,000	600,000
Certificates of deposit		30,000	30,000
Derivative financial instruments		11,976	-
	₩	1,091,976	640,000

During the year ended December 31, 2015, the Company acquired redeemable convertible preference shares of Somang Cosmetics Co., Ltd. and recognized embedded derivatives as other financial assets separately from the host contract. The fair value of derivative financial instruments was determined based on the DCF and option pricing model by external, independent valuers.

16. Non-current Assets Held for Sale

Changes in non-current assets held for sale for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	426	3
Transfer from property, plant and equipment		1,542	426
Disposal		(426)	(3)
Ending balance	₩	1,542	426

17. Pledged Assets

(a) Investment property pledged as collateralas of December 31, 2015was as follows:

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Leaseholder
Investment property	₩	70,769	Leasehold deposits received	₩	8,975	9,225	Metlife Insurance Korea Co.,Ltd. and others

(b) Investment property pledged as collateral as of December 31, 2014 was as follows:

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Leaseholder
Investment property	₩	71,677	Leasehold deposits received	₩	7,901	8,683	Metlife Insurance Korea Co.,Ltd. and others

18. ShareCapital and Other Capital Surplus

(a) Details of sharecapital as of December 31, 2015 and 2014 were as follows:

		2015	2014
Number of ordinaryshares:			
Authorized		800,000,000	800,000,000
Issued		137,292,497	137,292,497
Outstanding		125,965,892	125,898,800
Par value in won	₩	5,000	5,000

The Company has, thus far, reacquired and retired 53,699,400 shares of treasury share. Accordingly, as of December 31, 2015, the Company's ordinary share differs from the aggregate par value of issuedshares by ₩268,497 million.

(b) Changes in the number of shares for the years ended December 31, 2015 and 2014were as follows:

	2015			2014		
	Ordinary shares	Treasury shares	Total	Ordinary shares	Treasury shares	Total
Beginning balance	137,292,497	(11,393,697)	125,898,800	137,292,497	(11,393,697)	125,898,800
In-kind donation of treasury shares	-	67,092	67,092	-	-	-
Ending balance	137,292,497	(11,326,605)	125,965,892	137,292,497	(11,393,697)	125,898,800

(c) There was no change in other capital surplus for the years ended December 31, 2015 and 2014.

19. Treasury Shares

(a) Changes in the treasury sharesfor the years ended December 31, 2015 and 2014were as follows:

	2015			2014		
In millions of won, except number of shares	Number of shares		Carrying amount	Number of shares		Carrying amount
Beginning balance	11,393,697	₩	339,059	11,393,697	₩	339,059
In-kind donation of treasury shares	(67,092)		(1,997)	-		-
Ending balance	11,326,605	₩	337,062	11,393,697	₩	339,059

(b) Changes in gain on reissuance of treasury shares for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Beginning balance	₩	492,032	492,032
In-kind donation of treasury shares,net of tax		2,616	-
Ending balance	₩	494,648	492,032

20. Reserves

(a) Details of reservesas of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Available-for-sale financial assets - net change in fair value	₩	(45,128)	(27,434)
Legal reserve		602,937	602,937
Voluntary reserve		3,226,658	2,918,255
	₩	3,784,467	3,493,758

20. Reserves, Continued

(b) Available-for-sale financial assets - net change in fair valueas of December 31, 2015 and 2014aresummarized as follows:

In millions of won		2015	2014
Available-for-sale financial assets - net change in fair value before tax	₩	(59,536)	(36,192)
Tax effect		14,408	8,758
	₩	(45,128)	(27,434)

(c) Legal Reserve

The Korean Commercial Act requires the Company to appropriate a legal reserve in an amount equal to at least 10% of cash dividends for each accounting period until the reserve equals 50% of stated capital. The legal reserve may be used to reduce a deficit or may be transferred to ordinary shares in connection with a free issue of shares.

(d) Details of voluntary reserve as of December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Reserveforbusinessrationalization	₩	12,851	12,851
Reserveforresearchandhumanresourcedevelopment		30,000	42,523
Reservefor business expansion		698,881	698,881
Unconditionalreserve		2,484,926	2,164,000
	₩	3,226,658	2,918,255

Reserve for business rationalization
Until December 10, 2002 under *the Special Tax Treatment Control Act*, investment tax credits were allowed for certain investments. The Company was, however, required to appropriate from retained earnings, the amount of tax benefits received, and transfer such amount into a reserve for business rationalization.

Effective December 11, 2002, the Company was no longer required to establish a reserve for business rationalization despite tax benefits received for certain investments and, consequently, the existing balance is now regarded as a voluntary reserve.

Reserve for research and human resource development
Reserve for research and human resource development was appropriated in order to utilize certain tax deduction benefits through the early recognition of future expenditures. This reserve is restored to retained earnings in accordance with the relevant tax laws. Such reserves are taken back into taxable income in the year of restoration.

Reserve for business expansion and other reserves
Reserves without specific purposes are restored to retained earnings by the Company. Those reserves can be used for other purposes afterwards upon a resolution at a general meeting of shareholders.

21. Retained Earnings

(a) Changes in retained earnings for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Beginning balance	₩	736,460	509,820
Dividends		(428,056)	(402,876)
Transfer from reserve for research and human resource development		12,522	47,478
Transfer to unconditional reserve		(320,926)	(152,000)
Profit for the year		987,924	747,054
Remeasurements of net defied benefit liability, net of tax		7,962	(13,016)
Ending balance	₩	995,886	736,460

(b) Statements of appropriation of retained earnings for the years ended December 31, 2015 and 2014 are as follows:

Date of appropriation for 2015: March 18, 2016
Date of appropriation for 2014: February 27, 2015

In millions of won		2015	2014
Unappropriated retained earnings:			
Beginning balance	₩	-	2,422
Profit for the year		987,924	747,054
Remeasurements of net defined benefit liability, net of tax		7,962	(13,016)
		995,886	736,460
Transfer from voluntary reserves		10,000	12,522
Unappropriated retained earnings available for appropriation		1,005,886	748,982
Appropriation of retained earnings:			
Dividends		(428,284)	(428,056)
Unconditional reserve		(577,602)	(320,926)
		(1,005,886)	(748,982)
Unappropriated retained earnings to be carried over to subsequent year	₩	-	-

22. Dividends

The following dividends were declared and paid by the Company for the years ended December 31, 2015 and 2014 are as follows:

		2015	2014
Dividendsin millions of won	₩	428,056	402,876
Dividends per share in won		3,400	3,200
Dividend rate as a percentage of par value		68.00%	64.00%

Dividends of ₩428,284 million (₩3,400 per share) will be proposed at the shareholders' meeting to be held on March 18, 2016. The dividends have not been recognized as liabilities.

23. Trade and Other Payables

Trade and other payables as of December 31, 2015 and 2014are summarized as follows:

In millions of won		2015		2014	
		Current	Non-current	Current	Non-current
Leasehold deposits received	₩	19,404	8,147	-	28,310
Trade payables		65,154	-	66,448	-
Withholdings		4,749	-	4,031	-
Withholdings value added tax		184,587	-	132,173	-
Accrued expenses		125,699	-	110,155	-
Other payables		34,231	-	34,433	-
	₩	433,824	8,147	347,240	28,310

24. Short-term Borrowings

Short-term borrowings as of December 31, 2015 and 2014are summarized as follows:

In millions of won	Annual interest rate		2015	2014
Customer credit contracts:				
NonghyupBank	6.64%	₩	4,099	4,536
KEB HanaCard Co., Ltd.	3M CD rate+2.5%		932	1,016
		₩	5,031	5,552

The Company has entered into a customer credit contract with the NonghyupBankand KEB HanaCard Co., Ltd. The financial institutions pay trade receivables for customers and the Company has provided guarantees to the financial institutions for customers.

25. RetirementBenefits Plan

(a) The components of retirement benefits for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Defined benefit plans:			
Current service cost	₩	28,383	27,282
Interest cost		1,749	2,229
Expected return on plan assets		-	
Past service cost and loss on settlement		-	165
		30,132	29,676
Defined contribution plans:			
Contributions recognized as expense		4,185	2,860
	₩	34,317	32,536

The Company recognized termination benefits amounting to ₩12,741million and ₩272million as an expensefor the years ended December 31, 2015 and 2014, respectively.

25. RetirementBenefits Plan, Continued

(b) Changes in net defined benefit liability for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	67,260	60,273
Service cost		28,383	27,447
Net interest on net defined benefit liability		1,749	2,229
Remeasurements of net defined benefit liability before tax		(10,504)	17,171
Retirement benefits paid		(4,714)	(5,360)
Contributions to plan assets		(40,000)	(34,500)
Ending balance	₩	42,174	67,260
Statement of financial position:			
Present value of defined benefit obligations	₩	247,774	258,236
Fair value of plan assets		(205,600)	(190,976)
Net defined benefit liability	₩	42,174	67,260

(c) Changes in defined benefit obligations for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	258,236	227,258
Current service costs		28,383	27,282
Past service costs		-	165
Interest expense		6,590	8,083
Actuarial losses (gains) before tax		(10,952)	16,100
Retirement benefits paid		(34,483)	(20,652)
Ending balance	₩	247,774	258,236

(d) Changes in plan assets for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	190,976	166,986
Interest income		4,841	5,854
Return on plan assets, excluding interest income on plan assets		(448)	(1,071)
Retirement benefits paid		(29,769)	(15,293)
Contributions to plan assets		40,000	34,500
Ending balance	₩	205,600	190,976

Actual returns on plan assets were ₩4,393 million and ₩4,783 million for the years ended December 31, 2015 and 2014, respectively.

25. RetirementBenefits Plan, Continued

(e) Details of remeasurements of net defined benefit liability in other comprehensive income for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Actuarial gains (losses) before tax:			
Demographic assumptions	₩	9,558	-
Financial assumptions		(8,305)	(3,172)
Experience adjustments		9,699	(12,928)
		10,952	(16,100)
Return on plan assets, excluding interest income on plan assets		(448)	(1,071)
Remeasurements of net defined benefit liabilities before tax		10,504	(17,171)
Tax effect		(2,542)	4,155
Remeasurements of net defined benefit liabilities, net of tax	₩	7,962	(13,016)

(f) The components of plan assets as of December 31, 2015 and 2014 are as follows:

In millions of won		2015	2014
Deposits, cash and cash equivalents	₩	22,226	26,146
Others		183,374	164,830
	₩	205,600	190,976

(g) The principal actuarial assumptions as of December 31, 2015 and 2014 are as follows:

	2015	2014
Discount rate	2.20%	2.60%
Salary increase rate	4.00%	4.00%

For the purpose of calculating present value of the defined benefit obligations, the Company used the discount rate determined by reference to market yields at the end of the reporting period on high quality corporate bonds consistent with the currency and estimated term of the defined benefit obligations.

As of December 31, 2015 and 2014, the weighted average duration of the defined benefit obligations was 8.09years and 11.99 years, respectively.

(h) The effects of changes in each significant actuarial assumptions on defined benefit obligations as of December 31, 2015 would be as follows:

In millions of won	1% point increase	1% point decrease
Discount rate	(19,947)	22,903
Salary increase rate	22,332	(19,870)

26. Result from Operating Activities

(a) Details of expenses classified by nature for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Changes in inventories	₩	21,403	26,672
Raw materials and consumables purchased		735,999	777,874
Salaries		340,536	341,276
Retirement and termination benefits		47,058	32,808
Depreciation		105,353	104,113
Amortization		24	58
Employee welfare		62,005	40,600
Advertising		120,304	132,801
Commissions		103,012	104,172
Other expenses		48,660	127,632
	₩	1,584,354	1,688,006

(b) Details of selling, general and administrative expensesfor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Salaries	₩	232,370	229,515
Retirement and termination benefits		34,277	21,743
Employee welfare		43,819	29,198
Travel		4,736	4,212
Communications		3,407	3,589
Utilities		8,598	8,259
Taxes and dues		16,028	15,290
Supplies		1,945	1,867
Rent		12,918	13,578
Depreciation		32,682	32,369
Amortization		24	58
Repairs and maintenance		3,228	6,005
Vehicles		4,800	6,351
Insurance		284	326
Commissions		78,174	79,736
Freight and custody		28,401	27,415
Conferences		2,743	2,969
Advertising		120,152	132,647
Training		4,244	3,757
Prizes and rewards		2,312	2,070
Normal research and development		12,273	14,042
Reversal of impairment loss on trade receivables		(9,706)	(10,784)
	₩	637,709	624,212

27. Other Income and Expenses

(a) Details of other income for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Foreign currency transaction gain	₩	27,188	14,739
Foreign currency translation gain		39,761	31,247
Reversal of impairment loss on other receivables		1,760	-
Gain on sale of property, plant and equipment		12,421	8,064
Gain on sale of intangible assets		723	-
Others		22,600	17,847
	₩	104,453	71,897

(b) Details of other expenses for the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Foreign currency transaction loss	₩	9,622	10,718
Foreign currency translation loss		3,317	3,185
Impairment loss on other receivables		2,569	510
Loss on disposalof investments in associates		370	-
Loss on disposal of investments in subsidiaries		-	5
Impairment loss on investments in subsidiaries		34,601	123,900
Loss on sale of property, plant and equipment		513	1,290
Loss on sale of intangible assets		-	2
Impairment loss on intangible assets		-	2,658
Donations		43,665	6,787
Others		8,703	8,252
	₩	103,360	157,307

28. Net Finance Income

(a) Details of net finance incomefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Finance income:			
Interest income	₩	33,330	35,605
Dividend income		21,014	20,525
Interest income on long-term depositsin MSA Escrow Fund		1,287	877
Gain on sale of available-for-sale financial assets		25,183	20,132
Gain on valuation of derivatives		1,103	-
		81,917	77,139
Finance costs:			
Interest costs		(793)	(830)
Impairment loss on available-for-sale financial assets		(95)	-
		(888)	(830)
Net finance income	₩	81,029	76,309

(b) Details of interest incomefor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Deposits	₩	25,821	26,815
Available-for-sale financial assets		40	50
Trade and other receivables		7,469	8,740
	₩	33,330	35,605

(c) Details of interest expensesfor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Trade and other payables	₩	793	830

29. Income Tax

(a) The components of income tax expense for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Current income tax expense	₩	326,329	273,279
Adjustments recognized in the period for current tax of prior periods		(69)	(1,387)
Changes in temporary difference		2,983	15,373
		329,243	287,265
Less: tax expense recognized outside profit or loss		2,273	11,135
	₩	331,516	298,400

(b) Current tax and deferred tax that were recognized outside profit or loss for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Current tax:			
Gain on reissuance of treasury shares	₩	835	-
Deferred tax:			
Net changes in fair value of available-for-sale financial assets		(5,650)	(6,980)
Remeasurements of the net defined benefit liabilities		2,542	(4,155)
		(3,108)	(11,135)
Tax expense recognized outside profit or loss	₩	(2,273)	(11,135)

Income tax related to gain on reissuance of treasury shares was recognized directly in equity and income tax related to net changes in fair value of available-for-sale financial assets and remeasurements of the net defined benefit liabilitieswere recognized in other comprehensive income.

(c) Reconciliation of income tax expense based on statutory tax rate to actual income tax expense for the years ended December 31, 2015 and 2014 are as follows:

In millions of won		2015	2014
Profit before income tax	₩	1,319,440	1,045,454
Normal tax rate		24.20%	24.20%
Income taxes at statutory tax rate		319,278	252,538
Adjustment:			
Non-taxable income		(314)	(1,664)
Non-deductible expenses		5,447	3,578
Changes in unrecognized deferred tax		8,373	44,403
Tax credits and deduction		(544)	(855)
Adjustments recognized in the period for current tax of prior periods		(69)	(1,387)
Other		(655)	1,787
Income tax expense	₩	331,516	298,400
Effective tax rate		25.10%	24.40%

29. Income Tax, Continued

(d) Changes in deferred income tax assets (liabilities) for the years ended December 31, 2015 and 2014 are as follows:

(i) For the year ended December 31, 2015

In millions of won		January 1 2015	Profit or loss	Other comprehensive income (loss)	December 31 2015
Accumulated depreciation	₩	7,117	459	-	7,576
Allowance		11,324	(2,613)	-	8,711
Available-for-sale financial assets		14,600	(6,024)	5,650	14,226
Accrued expenses		23,254	3,072	-	26,326
Defined benefit liability		9,191	(1,945)	(2,542)	4,704
Treasury Shares		(8,808)	52	-	(8,756)
Investments in subsidiaries		(106,837)	-	-	(106,837)
Advanced depreciation provision		(14,493)	-	-	(14,493)
Reserve		(7,260)	2,420	-	(4,840)
Other		2,716	(1,512)	-	1,204
	₩	(69,196)	(6,091)	3,108	(72,179)

(ii) For the year ended December 31, 2014

In millions of won		January 1 2014	Profit or loss	Other comprehensive income	December 31 2014
Accumulated depreciation	₩	8,248	(1,131)	-	7,117
Allowance		13,970	(2,646)	-	11,324
Available-for-sale financial assets		16,525	(8,905)	6,980	14,600
Accrued expenses		21,526	1,728	-	23,254
Defined benefit liability		6,061	(1,025)	4,155	9,191
Treasury Shares		(8,808)	-	-	(8,808)
Investments in subsidiaries		(89,976)	(16,861)	-	(106,837)
Advanced depreciation provision		(14,493)	-	-	(14,493)
Reserve		(10,290)	3,030	-	(7,260)
Other		3,414	(698)	-	2,716
	₩	(53,823)	(26,508)	11,135	(69,196)

29. Income Tax, Continued

(e) As of December 31, 2015 and 2014, deferred tax liability of ₩163,818million and ₩129,217million for temporary differences related to investments in subsidiaries and associates was notrecognized, respectively, because the Company controls the timing of reversal of the temporary differences and management is satisfied that they will not reverse in the foreseeable future.

30. Earnings per Share

Basic and dilutedearnings pershare for the years ended December 31, 2015 and 2014were as follows:

		2015	2014
Profit for the year in millions of won	₩	987,924	747,054
Weighted-average number of ordinary shares outstanding		125,961,848	125,898,800
Basic and diluted earnings per sharein won	₩	7,843	5,934

The weighted-average number of ordinary shares outstanding is the number of ordinary shares outstanding at the beginning of the period, adjusted by the number of ordinary shares bought back or issued during the period multiplied by a time-weighting factor.

31. Transactions and Balances with Related Companies

(a) Details of parent and subsidiary relationships as of December 31, 2015 and 2014 were as follows:

			Percentage of ownership					
			2015			2014		
Subsidiary	Location	Immediate parent company	Parent	Sub-sidiary	Total	Parent	Sub-sidiary	Total
Korea Ginseng Corporation	Korea	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
Yungjin Pharm. Ind. Co., Ltd.	Korea	KT&G Corporation	53.00%	-	53.00%	53.00%	-	53.00%
Tae-a Industry Co., Ltd.	Korea	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
KT&G TutunMamulleri SanayiveTicaret A.S.	Turkey	KT&G Corporation	99.99%	-	99.99%	99.99%	-	99.99%
Korea Tabacos do Brasil Ltda.	Brazil	KT&G Corporation	99.99%	-	99.99%	99.90%	-	99.90%
KT&G Pars	Iran	KT&G Corporation	99.99%	-	99.99%	99.99%	-	99.99%
KT&G Rus L.L.C.	Russia	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
KGC Life & Gin Co., Ltd.	Korea	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
Global Trading, Inc.	USA	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
Somang Cosmetics Co., Ltd.(*1)	Korea	KT&G Corporation	97.73%	-	97.73%	60.00%	-	60.00%
RenzolucPte., Ltd.(*1)	Singapore	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
KT&G Life Sciences Corporation(*1)	Korea	KT&G Corporation	73.94%	-	73.94%	73.94%	-	73.94%
KGC Yebon Corporation	Korea	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
K-Q HongKong I, Limited(*1)	HongKong	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
PT KT&G Indonesia	Indonesia	KT&G Corporation	99.99%	-	99.99%	99.99%	-	99.99%
K&I HK Co., Ltd.(*2)	HongKong	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
K&I China Co., Ltd.(*2)	China	KT&G Corporation	100.00%	-	100.00%	100.00%	-	100.00%
SangSang Stay, Inc.(*3)	Korea	KT&G Corporation	100.00%	-	100.00%	-	-	-
Jilin Hanzheng Ginseng Co., Ltd.	China	Korea Ginseng Corporation	-	100.00%	100.00%	-	100.00%	100.00%
Cheong Kwan Jang Taiwan Corporation	Taiwan	Korea Ginseng Corporation	-	100.00%	100.00%	-	100.00%	100.00%
Korean Red Ginseng Corp., Inc.	USA	Korea Ginseng Corporation	-	100.00%	100.00%	-	100.00%	100.00%
Korea Ginseng (China) Corp.	China	Korea Ginseng Corporation	-	100.00%	100.00%	-	100.00%	100.00%
Korea Ginseng Corporation Japan	Japan	Korea Ginseng Corporation	-	100.00%	100.00%	-	100.00%	100.00%
PT CKJ INDONESIA	Indonesia	Korea Ginseng Corporation	-	99.88%	99.88%	-	99.88%	99.88%
PT TrisaktiPurwosariMakmur	Indonesia	RenzolucPte., Ltd.	-	60.17%	60.17%	-	60.17%	60.17%
PT MandiriMahamulia	Indonesia	RenzolucPte., Ltd.	-	66.47%	66.47%	-	66.47%	66.47%
PT Sentosa AbabiPurwosari	Indonesia	PT Trisakti PurwosariMakmur	-	99.24%	99.24%	-	99.24%	99.24%
PT PurindoIlufa	Indonesia	PT Trisakti PurwosariMakmur	-	100.00%	100.00%	-	100.00%	100.00%

(*1) The percentage of ownership, shown above, excludes preferred shares. As of December 31, 2015, the Company's percentage of ownership would be 97.76%, 68.91%, 59.48%and 50.00%, respectively, if preferred shares are included.

(*2) The Company established K&I HK Co., Ltd. and K&I China Co., Ltd.in 2014.

(*3) The Company established SangSang Stay, Inc. in 2015.

31. Transactions and Balances with Related Companies, Continued

(b) Significant transactions which occurred in the normal course of business with related companies for the years ended December 31, 2015 and 2014are summarized as follows:

In millions of won		2015 Sales and other income	2015 Purchase and other expenses	2014 Sales and other income	2014 Purchase and other expenses
Korea Ginseng Corporation	₩	8,674	1,706	8,872	1,846
Yungjin Pharm. Ind. Co., Ltd.		330	28	363	40
Tae-a Industry Co., Ltd.		17	13,727	15	14,987
KT&G TutunMamulleriSanayiveTicaret A.S.		8,275	22	9,687	164
KT&G Pars		1,132	-	3,301	-
KT&G Rus L.L.C.		25,173	22	31,490	-
KGC Life & Gin Co., Ltd.		819	503	1,076	649
Global Trading, Inc.		106,723	-	66,588	-
Somang Cosmetics Co., Ltd.		138	131	177	155
RenzolucPte., Ltd.		3,699	-	4,007	-
KT&G Life Sciences Corporation		30	-	68	-
KGC Yebon Corporation		538	136	253	16
PT KT&G Indonesia		1,588	-	491	-
K&I China Co., Ltd.		-	226	-	-
Korea Ginseng (China) Corp.		-	-	-	233
PT TrisaktiPurwosariMakmur		153	-	149	-
PT MandiriMahamulia		3,390	-	4,807	-
SangSang Stay, Inc.		45	-	-	-
	₩	160,724	16,501	131,344	18,090

(c) Account balances with related companies as of December 31, 2015 and 2014 were as follows:

In millions of won		2015 Receivables	2015 Payables	2014 Receivables	2014 Payables
Korea Ginseng Corporation	₩	37	2,044	764	1,795
Yungjin Pharm. Ind. Co., Ltd.		11	413	60	413
KT&G TutunMamulleriSanayiveTicaret A.S.		44,388	-	38,559	-
Korea Tabacos do Brasil Ltda.		99	-	94	-
KT&G Pars(*)		42,868	-	41,827	-
KT&G Rus L.L.C.(*)		38,425	-	27,701	-
KGC Life & Gin Co., Ltd.		-	245	109	165
Global Trading, Inc.		12,071	-	509	-
Somang Cosmetics Co., Ltd.		28,144	28	12	29
RenzolucPte., Ltd.		47,884	-	48,327	-
KT&G Life Sciences Corporation		-	1	5	814
PT KT&G Indonesia		29,112	-	18,580	-
PT TrisaktiPurwosariMakmur		156	-	156	-
PT MandiriMahamulia		3,698	-	4,167	-
	₩	246,893	2,731	180,870	3,216

(*) Above receivables are the gross amounts before ₩20,198 million and ₩19,668 million of allowance for doubtful accounts.

31. Transactions and Balances with Related Companies, Continued

(d) Details of financial transactions with related parties for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015			2014		
		Loans		Capital	Loans		Capital
		Increase	Collection	Increase	Increase	Collection	Increase
Korea Ginseng Corporation	₩	-	-	-	-	-	73,025
KT&G TutunMamulleri SanayiveTicaret A.S.		-	1,099	-	-	-	-
Korea Tabacos do Brasil Ltda.		-	-	2,356	-	-	-
Global Trading, Inc.		-	-	-	-	2,035	-
Somang Cosmetics Co., Ltd.		-	-	49,755	-	-	-
RenzolucPte., Ltd.		969	-	-	-	-	-
KGC Yebon Corporation		-	-	-	-	-	5,902
PT KT&G Indonesia		7,748	-	-	9,946	-	7,654
K&I HK Co.,Ltd.		-	-	-	-	-	11
K&I China Co.,Ltd.		-	-	5,096	-	-	436
SangSang Stay, Inc.		-	-	20,000	-	-	-

During the year ended December 31, 2015, the Company acquired 94,079 shares of redeemable convertible preference shares of Somang Cosmetics Co., Ltd. for ₩26,000 millionfrom KOFC QCP IBKC Frontier Champ 2010-2 Private Equity Fund.

(e) Details of key management personnel compensation for the years ended December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
Short-term employee benefits	₩	15,456	15,909
Retirement benefits		1,476	1,936
	₩	16,932	17,845

32. Risk Management and Fair Value of Financial Instruments

(a) Overview

The Company has exposure to the following risks from its use of financial instruments:

- Market risk
- Credit risk
- Liquidity risk

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing riskincluding quantitative disclosures.

(b) Risk Management Framework

The purpose of managing financial risks is to identify the potential risk factors that may affect the Company's financial performance, and minimize, eliminate and avoid it to the extent that is acceptable. One of the principal responsibilities of the treasury departmentis to manage the financial risks arising from the Company's underlying operations. The treasury departmentmonitors and manages the financial risk arising from the Company's underlying operations in accordance with the risk management policies and procedures authorized by the board of directors. Also, the treasury departmentprovides an internal report analyzing the nature and exposure level of financial risks to Risk Management Committee of the Company. The Risk Management Committee preparesthe overall strategy for financial risk management, and evaluates the effectiveness of the financial risk management strategy. In addition, the Company's audit committee consistently observes the compliance of the risk management policy and procedure, and reviews the risk exposure limit of the Company.The Company applied the same financial risk management strategy that was applied in the previous period.

(c) Management of Financial Risks

(i) Market risk

Market risk is the risk that changes in market prices – such as foreign exchange rates, interest rates and equity prices – will affect the Company's income or the value of its financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

32. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

Currency risk

The Company has exposure to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates arising from the export and import of tobacco. The Company's management has measured the currency risk internally and regularly, and has entered into foreign currency forward contracts to hedge foreign currency risk, if necessary.

The carrying amounts of monetary assets and liabilities denominated in a currency other than the functional currency as of December 31, 2015 and 2014 were as follows:

		2015		2014	
In millions of won		Assets	Liabilities	Assets	Liabilities
USD	₩	918,070	44,431	785,423	44,293
IDR		48,190	-	48,327	6,785
EUR		30,375	1,504	28,988	-
Others		2,177	-	2,087	-
	₩	998,812	45,935	864,825	51,078

As of December 31, 2015 and 2014, the effects of a 10% weakening or strengthening of functional currency against foreign currencies on profit before tax were as follows:

		2015		2014	
In millions of won		10% weakening	10% strengthening	10% weakening	10% strengthening
Increase (decrease) in profit before tax	₩	95,288	(95,288)	81,375	(81,375)

Equity price risk

The Company has exposure to equity price risk, which arises from listed available-for-sale equity instruments. The Company's management has monitored the proportion of equity instruments in its investment portfolio based on market indices. Material investments within the portfolio are managed on an individual basis, and all buy and sell decisions are approved by the Company's management.

As of December 31, 2015 and 2014, the effects of a 5% fluctuation in the price index of stocks on comprehensive income before tax were as follows:

		2015		2014	
In millions of won		5% increase	5% decrease	5% increase	5% decrease
Comprehensive income before tax	₩	1,627	(1,627)	5,252	(5,252)

32. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

Interest rate risk

The Company has exposure to the risk that the fair value or future cash flows of a financialinstrument will fluctuate because of changes in marketinterest rates.The Company’s management has monitored the level of interest rates regularly and hasmaintained the balance of borrowings at variable rates and fixed rates. As of December 31, 2015, there is no significant effect on cash flows or the fair value of financial liabilities from the interest rate fluctuation, considering the amounts of interest bearing liabilities.

(ii) Credit risk

The Company has exposure to the risk that one party to a financial instrument will cause afinancial loss for the other party by failing to discharge anobligation. The Company has transacted with customers with high credit ratings to manage credit risk, and has implemented and operated policies and procedures for credit enhancements of the financial assets. Counterparty credit risk is managed by evaluating its credit rating and limiting the aggregate amount and duration of exposurebefore sales commence, and the Company has been provided collateral and guarantees. The credit ratings of all counterparties and the level of collateral and guarantees are reviewed regularly. Analysis of financial assets past due has been reported quarterly and appropriate measures have been taken to secure the Company's assets.

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit riskas of December 31, 2015 and 2014is as follows:

In millions of won		2015	2014
Available-for-sale debt instruments	₩	1,500	2,500
Long-term deposits in MSA Escrow Fund		403,966	301,808
Trade and other receivables		1,153,462	945,650
Other financial assets (excluding derivatives)		1,080,000	640,000
Cash and cash equivalents (excluding cash on hand)		441,753	320,679
Financial guarantee contracts		76,566	150,063
	₩	3,157,247	2,360,700

32. Risk Management and Fair Value of Financial Instruments, Continued

(c) Management of Financial Risks, Continued

(iii) Liquidity risk

The Company has exposure to the risk that an entity will encounter difficulty in meetingobligations associated with financial liabilities.The Company's management has established short-term and long-term financial management plans to manage the liquidity risk,and analyzed cash outflows occurred and cash outflows budgeted, so as to match the maturity structure of financial assets and financial liabilities.The Company's management determines whether or not the financial liabilities are repayable with the operating cash flows and cash inflows from financial assets.

The maturity analysis with a residual contractual maturity of financial liabilities as of December 31, 2015 and 2014is as follows:

				Residual contractual maturity		
In millions of won		Carrying amount	Contractual cash flow	Within 3 months	Between 3 months and 1 year	Between 1 and 5 years
As of December 31, 2015:						
Trade and other payables	₩	252,635	253,343	225,084	19,583	8,676
Short-term borrowings		5,031	5,031	5,031	-	-
Financial guarantee liabilities		-	76,566	-	-	76,566
	₩	257,666	334,940	230,115	19,583	85,242
As of December 31, 2014:						
Trade and other payables	₩	239,346	240,489	211,036	-	29,453
Short-term borrowings		5,552	5,552	5,552	-	-
Financial guarantee liabilities		-	150,063	-	150,063	-
	₩	244,898	396,104	216,588	150,063	29,453

The above financial liabilities are presented at the nominal value of undiscounted future cash flows as of the earliest period at which the Company can be required to pay.

32. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair Value of Financial Instruments

The carrying amounts of each category of financial assets and liabilities as of December 31, 2015 and 2014are summarized as follows:

In millions of won		2015	2014
Financial assets:			
Financial assets at fair value through profit or loss			
(derivative financial instruments)	₩	11,976	-
Available-for-sale financial assets		340,149	304,438
Loans and receivables			
–Trade and other receivables		1,153,462	945,650
–Long-term deposits in MSA Escrow Fund		403,966	301,808
–Other financial assets (excluding derivatives)		1,080,000	640,000
–Cash and cash equivalents		444,376	321,562
		3,081,804	2,209,020
	₩	3,433,929	2,513,458
Financial liabilities:			
Financial liabilities measured at amortized cost			
–Trade and other payables	₩	252,635	239,346
–Short-term borrowings		5,031	5,552
	₩	257,666	244,898

The fair value measurementsclassified by fair value hierarchyas of December 31, 2015 and 2014were as follows:

In millions of won		Carrying amount	Fair value Level I	Level II	Level III
As of December 31, 2015:					
Available-for-sale financial assets	₩	302,594	187,486	-	115,108
Other financial assets					
(derivative financial instruments)		11,976	-	-	11,976
	₩	314,570	187,486	-	127,084
As of December 31, 2014:					
Available-for-sale financial assets	₩	274,844	184,118	-	90,726

There is no transfer between fair value hierarchy levels of recurring fair value measurements for the years ended December 31, 2015 and 2014.

32. Risk Management and Fair Value of Financial Instruments, Continued

(d) Fair Value of Financial Instruments, Continued

The fair value measurementsfor available-for-sale equity instruments in real estate trust fund and derivative financial instruments have been measured using the adjusted net asset method, DCF and option pricing model and categorized as a level 3 fair value based on the inputs to the valuation techniques used. Changesin fair value classified as level 3 for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Beginning balance	₩	90,726	62,467
Acquisition		33,073	38,992
Disposal		-	(14,411)
Changes in fair value		3,285	3,678
Ending balance	₩	127,084	90,726

(e) Finance Income (Costs)

(i) Details of finance income (costs) by categories for the year ended December 31, 2015 were as follows:

In millions of won		Financial assets at fair value through profit or loss	Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	₩	-	40	33,290	-	33,330
Dividend income		-	12,015	-	-	12,015
Interest income on long-term deposits in MSA Escrow Fund		-	-	1,287	-	1,287
Gain on valuation of derivative financial instruments		1,103	-	-	-	1,103
Gain on sale		-	25,183	-	-	25,183
Interest expense		-	-	-	(793)	(793)
Impairment loss		-	(95)	-	-	(95)
	₩	1,103	37,143	34,577	(793)	72,030
Other comprehensive income (loss) before tax						
Net change in fair value	₩	-	1,744	-	-	1,744
Reclassification adjustments on sale		-	(25,183)	-	-	(25,184)
Reclassification adjustments on impairment		-	95	-	-	95
	₩	-	(23,344)	-	-	(23,345)

32. Risk Management and Fair Value of Financial Instruments, Continued

(e) Finance Income (Costs), Continued

(ii) Details of finance income (costs) by categories for the year ended December 31, 2014 were as follows:

In millions of won		Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:					
Interest income	₩	50	35,555	-	35,605
Dividend income		16,842	-	-	16,842
Investment income on long-term deposits in MSA Escrow Fund		-	877	-	877
Gain on sale		20,132	-	-	20,132
Interest expense		-	-	(830)	(830)
	₩	37,024	36,432	(830)	72,626
Other comprehensive income before tax					
Net change in fair value	₩	(8,712)	-	-	(8,712)
Reclassification adjustments on sale		(20,132)	-	-	(20,132)
	₩	(28,844)	-	-	(28,844)

33. Capital Management

The Company's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The board of directors seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

The Company monitors capital using equity and net debtdeducting cash and cash equivalents and current financial instruments from borrowings. The Company applied the same capital management strategy that was applied in the previous year.

As of December 31, 2015 and 2014, the Company's capital structure was as follows:

In millions of won		2015	2014
Debt(borrowings)	₩	5,031	5,552
Less:			
Cash and cash equivalents		(444,376)	(321,562)
Current other financial assets		(1,091,976)	(640,000)
Net debt (asset)		(1,531,321)	(956,010)
Equity	₩	5,896,481	5,341,733

34. Contingent Liabilities and Commitments

(a) Each year the Company deposits a proportion of sales of tobacco products in the United States in accordance with the Tobacco Master Settlement Agreement ("MSA") under the Escrow Statute of the United States government. The MSA Escrow Funds are maintained to pay the medical expenses of tobacco purchasers who have suffered health effects as a result of smoking. The unused portion of this fund will be refunded to the Company 25 years from the date of each annual funding. The Company recorded as long-term deposits the amounts paid into the MSA Escrow Funds of State governments in the United States against potential litigation and damages related to the export of tobacco into the United States.

(b) As of December 31, 2015, the tobacco lawsuits claiming damages of ₩100 million and a lawsuit by National Health Insurance Service claiming damages of ₩53,742 million are filed against the Company. Additionally, as of December 31, 2015, the Company is involved in five lawsuits as a plaintiff for alleged damages totalling ₩14,783 million and six lawsuits as a defendant for alleged damages totalling ₩2,526million. The amount of the liability the Company may ultimately be liable for with respect to the litigation cannot be reasonably estimated as of December 31, 2015.

(c) As of December 31, 2015, the Company has entered into letter of credit agreements with Korea Exchange Bank and other banks with limits in the aggregate of USD59,000 thousand.

(d) As of December 31, 2015, the Company's trade receivables from the export of cigarettes are insured against non-payment up to USD20,380thousand by an export guarantee insurance with the KoreaExport Insurance Corporation.

(e) The Company has been provided with a foreign currency payment guarantee for local dealers in Russia and other countries up to USD 40,000 thousand by Korea Exchange Bank. Details of guarantees exercised as of December 31, 2015, are summarized as follows:

In thousands of USD, THB and millions of IDR		Exercised amount
Customs bond and L/C opening of Global Trading, Inc.	USD	14,222
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB	8,142
Payment guarantee for purchase of certificate stamp of PT MandiriMahaMulia	IDR	128,410

(f) On March 17, 2011, the Company signed the memorandum of understanding ("MOU") on global investment partnership with National Pension Serviceto jointly invest in foreign assets with a limit of ₩800,000 million.

34. Contingent Liabilities and Commitments, Continued

(g) With relation to the acquisition of KT&G Life Sciences Corporation, the Company entered into a contract with a former owner of the acquiree, Gwak, Tae-Hwan ("Individual Shareholder"). Details of the contract are as follows:

Description	Details
Restriction of disposal	Individual Shareholder shall not be permitted to dispose of its shares, in whole or in part, within one year after KT&G Life Sciences Corporationis listed.
Right of first refusal held by the Company	Individual Shareholder shall not be permitted to make any transfer of its shares, in whole or in part, unless Individual Shareholder has offered them first to the Company.
Tag-along right held by Individual Shareholder	In the event that the Company proposes to enter into a transaction or a series of related transactions with a third party purchaser to dispose of its shares, then Individual Shareholder shall elect to participate in such disposition upon the terms and conditions no less favorable than those applicable to the Company.

(h) As of December 31, 2015, the Company has provided guaranteesup to ₩225,600 million with an exercised amount of ₩76,566 million for the buyers of apartments in respect oftheir borrowings from Shinhan Bank.

(i) As of December 31, 2015, the Company is insured by performance bond insurance up to ₩1,157million with the Seoul Guarantee Insurance.

35. Cash Flows

(a) Details of cash generated from operationsfor the years ended December 31, 2015 and 2014were as follows:

In millions of won		2015	2014
Profit for the year	₩	987,924	747,054
Adjustments for:			
Income tax expense		331,516	298,400
Finance costs		888	830
Finance income		(81,917)	(77,139)
Depreciation		105,353	104,113
Amortization		24	58
Retirement and termination benefits		47,058	29,676
Foreign currency translations loss		3,317	3,185
Loss on sale of property, plant and equipment		513	1,290
Loss on sale of intangible assets		-	2
Impairment loss on intangible assets		-	2,658
Loss on disposal of investment in associates		370	-
Loss on disposalof investment in subsidiaries		-	5
Impairment loss on investment in subsidiaries		34,601	123,900
Other expense		7,117	4,064
Foreign currency translations gain		(39,761)	(31,247)
Reversal of impairment loss on trade and other receivables		(8,897)	(10,274)
Reversal of write-down of inventory		(183)	(1,911)
Gain on sale of property, plant and equipment		(12,421)	(8,064)
Gain on sale of intangible assets		(723)	-
		1,374,779	1,186,600
Changes in working capital:			
Trade and other receivables		(123,588)	(62,879)
Advance payments		(6,256)	16,395
Prepaid expenses		(1,470)	2,523
Prepaid tobacco excise and other taxes		(186,998)	1,997
Inventories		19,916	59,943
Trade and other payables		69,305	(75,874)
Advance receipts		78	6,933
Tobacco excise and other taxes payable		515,621	(93,525)
Payment of retirement and termination benefits		(60,499)	(39,860)
Cash generated from operations	₩	1,600,888	1,002,253

(b) Details of material transactions without cash inflow and outflow for the years ended December 31, 2015 and 2014 were as follows:

In millions of won		2015	2014
Increase in accrued expenses related to payment of retirement and termination benefits	₩	1,141	-
Acquisition of available-for-sale financial assets upon exercise of conversion options		28,990	-
Decrease in other payables related to acquisition of property, plant and equipment		3,166	-
Decrease in advance receipts related to disposal of property, plant and equipment and non-current assets held for sale		298	-

(c) The Company presented cash flows arising from short-term financial instruments on a net basis

3. Statements of Appropriation of Retained Earnings

29th Fiscal Year: 2015. 1. 1 ~ 2015. 12. 31 **28th Fiscal Year: 2014. 1. 1 ~ 2014. 12. 31**

Date of final decision of appropriation: 2016. 3. 18 **Date of final decision of appropriation: 2015. 2. 27**

KT&G Corporation

(Unit: billion Won)

	29th Fiscal Year		28th Fiscal Year	
	Amount		Amount	
1. Retained earnings before appropriations		**995.9**		**736.5**
1) Retained earnings carried from the previous fiscal year(loss)	0.0		2.4	
2) Profit for the period	987.9		747.1	
3) Actuarial gains	8.0		-13.0	
2. Transfer from voluntary reserves		**10.0**		**12.5**
1) Reserve for research and human resource development	10.0		12.5	
2) Reserve for loss on reissuance of treasury shares	0.0		0.0	
3. Appropriations of retained earnings		**1,005.9**		**749.0**
1) Dividends	428.3		428.1	
(1) Cash Dividends	428.3		428.1	
Common stock				
Current year: 3,400 KRW(68%)				
Common stock				
Previous year: 3,400 KRW(68%)				
2) Transfer to Reserve for research and human resource development	0.0		0.0	
3) Transfer to unconditional reserves	577.6		320.9	
4. Retained earnings to be carried forward to next fiscal year(loss)		**0.0**		**0.0**

II. Agendum No. 2

Amendment of Articles of Incorporation

Pursuant to Article 433 of the Korean Commercial Code, the Company intends to amend certain provisions of its Articles of Incorporation as follows:

Current Provisions	Proposed Amendments (Draft)	Reason for the Amendments
Article 2 (Objective) (1) The objectives of the Company shall be as follows: 1~47 (Omitted) 48. research activity incidental to the businesses described above. (The rest has been omitted)	**Article 2 (Objective)** (1) The objectives of the Company shall be as follows: 1~47 (Omitted) **<u>48. supply and development of software;</u>** **<u>49.</u>** research activity incidental to the businesses described above. (The rest has been omitted)	Added business objective
Article 33 (Qualification of Independent Non-Executive Directors) Independent non-executive directors shall be appointed among persons who are independent, well qualified and sufficiently experienced in the field of economics, business management, law, or relevant technology. Any of the following persons shall not be an independent non-executive director, and an independent non-executive director, who becomes any of the following persons, shall be disqualified. (1) a person who falls under Articles 382(3)(i)~(vii) of the Commercial Code or Articles 542-8(2)(i)~(vii) of the Commercial Code; (2) an individual who receives support from the Company for the past two (2) years, or a present or former employee or officer who works at an entity or organization, which receives support from the Company or has worked for such entity or organization in the recent two (2) years; and (3) a government official (excluding educational officials; hereinafter the same shall apply) under the relevant laws or a person who is restricted from being employed under the Public Service Ethics Act and other relevant laws.	**Article 33 (Qualification of Independent Non-Executive Directors)** Independent non-executive directors shall be appointed among persons**, <u>having no grounds for disqualification under related laws and regulations</u>,** who are independent, well qualified and sufficiently experienced in the field of economics, business management, law, or relevant technology. **<u>(1) ~(3) (Deleted)</u>**	Clarified in accordance with related laws(Korea Commercial Code)

Current Provisions	Proposed Amendments (Draft)	Reason for the Amendments
(Newly inserted)	**Addenda (March 18, 2016)** These Articles of Incorporation shall be enforced effective as of the resolution date of a general meeting of shareholders.	

III. Agendum No. 3

Appointment of (Four)Members of Board of Directors

Pursuant to Article 382 of the Korean Commercial Code and Article 26 of the Articles of Incorporation of the Company, the Company intends to appoint (Three) Independent Non-Executive Directors and (One) Inside Director as follows :

III-1. Appointment of Independent Non-Executive Director(Ko, Sang-Kon)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Ko, Sang-Kon	Nov. 23, 1953	Independent Non-Executive Director Candidate Recommendation Committee	The next day of the 29th annual general meeting of shareholders ~ the date of the 32nd annual general meeting of shareholders	Chairman of Public Relation, EDEN Welfare Foundation Invited Professor of Graduate School of Communication studies, Sung Kyun Kwan University (Former)Auditor of Korea PR Association

III-2. Appointment of Independent Non-Executive Director(Yoon, Hai-Su)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Youn, Hai-Su	Feb. 14, 1952	Independent Non-Executive Director Candidate Recommendation Committee	The next day of the 29th annual general meeting of shareholders ~ the date of the 32nd annual general meeting of shareholders	President of Seoul University of Foreign Studies (Former)Assistant administrator of ‘the 21st Century Committee’ under direct Presidential Control (Former)Professor of Political Science and Diplomacy, Myungji University

III-3. Appointment of Independent Non-Executive Director(Lee, Eun-Kyung)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Lee, Eun-Kyung	May 28, 1963	Independent Non-Executive Director Candidate Recommendation Committee	The next day of the 29th annual general meeting of shareholders ~ the date of the 32nd annual general meeting of shareholders	Managing Director of Finance & Operation(Division of ‘Calvin Klein’) , PVH Korea (Former)Director of Finance, Reebok Korea (Former)Vice President of Finance, Astrazeneca Korea (Former)Coordinator of Procurement/Export, GE Korea

III-4. Appointment of Inside Director(Kim, Heung-Ryul)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Kim, Heung-Ryul	Mar. 26, 1961	CEO(President)	The next day of the 29th annual general meeting of shareholders ~ the date of the 31st annual general meeting of shareholders	Head of Business, Executive Vice President, KT&G Corp. Head of Mgmt. Support Division, Managing Director, KT&G Corp. Head of Global Business Headquarters, Director, KT&G Corp.

Ⅳ. Agendum No. 4

Appointment of (Two) Members of the Audit Committee

Pursuant to Articles 542-11 and 542-12 of the Korean Commercial Code and Article 34-3 of the Articles of Incorporation of the Company, the Company intends to appoint Members of the Audit Committee as follows:

IV-1. Appointment of Member of the Audit Committee(Ko, Sang-Kon)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Ko, Sang-Kon	Nov. 23, 1953	Board of Directors	The next day of the 29th annual general meeting of shareholders ~ the date of the 32nd annual general meeting of shareholders	Chairman of Public Relation, EDEN Welfare Foundation Invited Professor of Graduate School of Communication studies, Sung Kyun Kwan University (Former)Auditor of Korea PR Association

IV-2. Appointment of Member of the Audit Committee(Lee, Eun-Kyung)

Name	Date of Birth	Nominator	Term of Office	Work Experience
Lee, Eun-Kyung	May 28, 1963	Board of Directors	The next day of the 29th annual general meeting of shareholders ~ the date of the 32nd annual general meeting of shareholders	Managing Director of Finance & Operation(Division of ‘Calvin Klein’) , PVH Korea (Former)Director of Finance, Reebok Korea (Former)Vice President of Finance, Astrazeneca Korea (Former)Coordinator of Procurement/Export, GE Korea

V. Agendum No. 5

Approval of the Cap on Directors' Remuneration

Pursuant to Article 388 of the Korean Commercial Code and Article 30 of the Articles of Incorporation of the Company, we intend to obtain approval of the cap on remuneration to be paid to Directors as follows:

Annual Cap on Remuneration of Directors for the 30th Fiscal Year (2016) (including Independent Non-executive Directors)	Annual Cap on Remuneration of Directors for the 29th Fiscal Year (2015) (including Independent Non-executive Directors)
4,000,000,000 Won	4,000,000,000 Won