KT&G CORPORATION

Separate Interim Financial Statements

(Unaudited)

June 30, 2011 and 2010

(With Independent Auditors' Review Report Thereon)

Contents

Independent Auditors' Review Report

Based on a report originally issued in Korean

The Board of Directors and Shareholders
KT&G Corporation:

Reviewed Financial Statements

We have reviewed the accompanying separate interim financial statements of KT&G Corporation (the "Company"), which comprise the separate statement of financial position as of June 30 2011, and the related separate statements of comprehensive income for the three- and six-month periods and changes in equity and cash flows for the six-month periods all of which ended June 30, 2011 and 2010, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility

Management is responsible for the preparation and fair presentation of these separate interim financial statements in accordance with Korean International Financial Reporting Standards No. 1034 *Interim Financial Reporting*, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Review Responsibility

Our responsibility is to issue a report on these separate interim financial statements based on our reviews. We conducted our reviews in accordance with Review Standards for Quarterly and Semiannual Financial Statements established by the Securities and Futures Commission of the Republic of Korea. A review of interim financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the Republic of Korea and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our reviews, nothing has come to our attention that causes us to believe that the accompanying separate interim financial statements referred to above are not prepared, in all material respects, in accordance with Korean International Financial Reporting Standards No. 1034 *Interim Financial Reporting*.

The following matters may be helpful to the readers in their understanding of this review report of the separate interim financial statements:

As discussed in note 28 to the separate interim financial statements, the Company and the Korean government are defendants in lawsuits claiming damages of ₩584 million for the effects of smoking. The final outcome of these lawsuits cannot be predicted.

Other Matter

The separate statement of financial position of the Company as of December 31, 2010, the related separate statements of comprehensive income, changes in equity and cash flows for the year then ended, which are not accompanying this report were audited by us and our report thereon, dated February 22, 2011, expressed an unqualified opinion. The accompanying separate statement of financial position of the Company as of December 31, 2010, presented for comparative purposes, is not different from that audited by us in all material respects.

The accompanying separate interim financial statements as of and for the three- and six-month periods ended June 30, 2011 have been translated into United States dollars solely for the convenience of the reader. We have reviewed the translation and, nothing has come to our attention to suggest that the separate interim financial statements expressed in Korean won have not been translated into dollars on the basis set forth in note 4 to the separate interim financial statements.

KPMG Samjong Accounting Corp.
Seoul, Korea
August 12, 2011

This report is effective as of August 12, 2011, the review report date. Certain subsequent events or circumstances, which may occur between the review report date and the time of reading this report, could have a material impact on the accompanying separate interim financial statements and notes thereto. Accordingly, the readers of the review report should understand that there is a possibility that the above review report may have to be revised to reflect the impact of such subsequent events or circumstances, if any.

KT&G CORPORATION
Separate Statements of Financial Position

As of June 30, 2011 and December 31, 2010

In millions of won and thousands of U.S. dollars	*Note*	2011 Korean won	2011 U.S. dollars (note 4)	2010 Korean won
Assets				
Property, plant and equipment	*5*	₩ 1,168,317	$ 1,083,681	₩ 1,196,126
Intangible assets	*6*	48,801	45,266	48,564
Investment property	*7*	124,356	115,348	98,143
Investments in associates	*8*	32,730	30,359	2,830
Investments in subsidiaries	*9*	854,621	792,710	840,121
Available-for-sale financial assets	*10,27*	284,411	263,808	313,937
Long-term deposits in MSA Escrow Fund	*11,27,28*	133,961	124,257	132,414
Long-term prepaid expenses		4,699	4,357	4,401
Long-term trade and other receivables	*12,27*	111,816	103,716	84,595
Total non-current assets		2,763,712	2,563,502	2,721,131
Inventories	*13*	934,075	866,409	990,333
Trade and other receivables	*12,26,27*	567,514	526,402	527,827
Prepaid tobacco excise and other taxes		173,334	160,777	177,043
Advance payments		39,441	36,584	5,783
Prepaid expenses		996	922	1,707
Current available-for-sale financial assets	*10,27*	-	-	1,000
Cash and cash equivalents	*14,27*	655,093	607,637	828,951
		2,370,453	2,198,731	2,532,644
Assets held for sale	*5,29*	8,955	8,307	-
Total current assets		2,379,408	2,207,038	2,532,644
Total assets		₩ 5,143,120	$ 4,770,540	₩ 5,253,775

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Financial Position, Continued

As of June 30, 2011 and December 31, 2010

In millions of won and thousands of U.S. dollars	*Note*	2011 Korean won	2011 U.S. dollars (note 4)	2010 Korean won
Equity				
Ordinary shares	*1,15*	₩ 954,959	$ 885,780	₩ 954,959
Other capital surplus	*15*	3,582	3,323	3,582
Treasury shares	*16*	(321,829)	(298,515)	(216,827)
Gain on reissuance of treasury shares	*16*	482,129	447,202	482,129
Reserve	*17*	2,715,201	2,518,506	2,184,703
Retained earnings	*18*	380,445	352,884	929,140
Total equity	*27*	4,214,487	3,909,180	4,337,686
Liabilities				
Long-term trade and other payables	*7,20,27*	25,776	23,908	22,902
Long-term advance receipts		1,025	951	515
Defined benefit liabilities	*21*	39,603	36,734	28,774
Deferred income tax liabilities	*24*	88,260	81,866	93,310
Total non-current liabilities		154,664	143,459	145,501
Short-term borrowings	*19,27*	9,349	8,672	8,618
Trade and other payables	*20,26,27*	285,596	264,907	238,587
Advance receipts		6,118	5,674	7,712
Income taxes payable	*24*	104,138	96,594	190,815
Tobacco excise and other taxes payable		368,768	342,054	324,856
Total current liabilities		773,969	717,901	770,588
Total liabilities		928,633	861,360	916,089
Total equity and liabilities		₩ 5,143,120	$ 4,770,540	₩ 5,253,775

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Comprehensive Income

For the six-month periods ended June 30, 2011 and 2010

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*	2011 Korean won	2011 U.S. dollars (note 4)	2010 Korean won
Sales:	*26*			
Manufacture of tobacco		₩ 1,118,748	$ 1,037,703	₩ 1,092,215
Real estate		13,294	12,331	47,109
Exports of leaf tobacco and others		28,621	26,548	14,231
		1,160,663	1,076,582	1,153,555
Cost of sales:	*26*			
Manufacture of tobacco		(419,853)	(389,438)	(422,941)
Real estate		(2,199)	(2,040)	(26,529)
Exports of leaf tobacco and others		(20,383)	(18,905)	(7,826)
		(442,435)	(410,383)	(457,296)
Gross profit		718,228	666,199	696,259
Other income	*22*	13,985	12,972	91,496
Selling expenses	*22*	(183,554)	(170,257)	(187,527)
General and administrative expenses	*22*	(100,023)	(92,778)	(103,574)
Other expense	*22*	(32,182)	(29,851)	(14,631)
Profit from operations		416,454	386,285	482,023
Finance income	*23*	71,246	66,085	284,604
Finance costs	*23*	(4,342)	(4,028)	(100)
Net finance income	*23*	66,904	62,057	284,504
Profit before income taxes		483,358	448,342	766,527
Income tax expense	*24*	(105,170)	(97,551)	(177,464)
Profit for the period		₩ 378,188	$ 350,791	₩ 589,063
Other comprehensive income:				
Available-for-sale financial assets, net of tax	*10,23,24*	₩ (13,502)	$ (12,523)	₩ (126,067)
Actuarial gains, net of tax	*21,24*	63	58	3,613
Other comprehensive income (expense) for the period, net of tax		(13,439)	(12,465)	(122,454)
Total comprehensive income for the period		₩ 364,749	$ 338,326	₩ 466,609
Earnings per share in won and U.S. dollars:				
Basic and diluted	*25*	₩ 2,970	$ 2.75	₩ 4,631

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Comprehensive Income, Continued

For the three-month periods ended June 30, 2011 and 2010

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*		2011 Korean won		2011 U.S. dollars (note 4)		2010 Korean won
Sales:	*26*						
Manufacture of tobacco		₩	599,857	$	556,402	₩	591,980
Real estate			7,149		6,631		14,029
Exports of leaf tobacco and others			16,626		15,421		7,191
			623,632		578,454		613,200
Cost of sales:	*26*						
Manufacture of tobacco			(227,931)		(211,419)		(233,635)
Real estate			(1,152)		(1,069)		(6,780)
Exports of leaf tobacco and others			(12,090)		(11,213)		(4,133)
			(241,173)		(223,701)		(244,548)
Gross profit			382,459		354,753		368,652
Other income	*22*		4,925		4,568		90,925
Selling expenses	*22*		(94,977)		(88,097)		(101,917)
General and administrative expenses	*22*		(50,075)		(46,447)		(59,793)
Other expense	*22*		(15,187)		(14,087)		(6,339)
Profit from operations			227,145		210,690		291,528
Finance income	*23*		10,017		9,291		248,148
Finance costs	*23*		(336)		(311)		(46)
Net finance income	*23*		9,681		8,980		248,102
Profit before income taxes			236,826		219,670		539,630
Income tax expense	*24*		(57,850)		(53,659)		(129,920)
Profit for the period		₩	178,976	$	166,011	₩	409,710
Other comprehensive income:							
Available-for-sale financial assets, net of tax	*10,23,24*	₩	157	$	146	₩	(185,466)
Actuarial gains (losses), net of tax	*21,24*		55		51		(2)
Other comprehensive income (expense) for the period, net of tax			212		197		(185,468)
Total comprehensive income for the period		₩	179,188	$	166,208	₩	224,242
Earnings per share in won and U.S. dollars:							
Basic and diluted	*25*	₩	1,408	$	1.31	₩	3,221

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Changes in Equity

For the six-month period ended June 30, 2011

In millions of won		Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Total equity
Balance at January 1, 2011	₩	954,959	3,582	(216,827)	482,129	2,184,703	929,140	4,337,686
Total comprehensive income for the period:								
Profit for the period		-	-	-	-	-	378,188	378,188
Other comprehensive income:								
Available-for-sale financial assets, net of tax		-	-	-	-	(13,502)	-	(13,502)
Actuarial gains, net of tax		-	-	-	-	-	63	63
Total other comprehensive income (expense)		-	-	-	-	(13,502)	63	(13,439)
Total comprehensive income (expense) for the period		-	-	-	-	(13,502)	378,251	364,749
Transactions with owners, recorded directly in equity:								
Dividends		-	-	-	-	-	(382,946)	(382,946)
Acquisition of treasury shares		-	-	(105,002)	-	-	-	(105,002)
Transfer to unconditional reserve		-	-	-	-	544,000	(544,000)	-
Total transactions with owners		-	-	(105,002)	-	544,000	(926,946)	(487,948)
Balance at June 30, 2011	₩	954,959	3,582	(321,829)	482,129	2,715,201	380,445	4,214,487

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Changes in Equity, Continued

For the six-month period ended June 30, 2011

In thousands of U.S. dollars	Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Total equity
Balance at January 1, 2011	$ 885,780	3,323	(201,120)	447,202	2,026,438	861,831	4,023,454
Total comprehensive income for the period:							
Profit for the period	-	-	-	-	-	350,791	350,791
Other comprehensive income:							
Available-for-sale financial assets, net of tax	-	-	-	-	(12,523)	-	(12,523)
Actuarial gains, net of tax	-	-	-	-	-	58	58
Total other comprehensive income (expense)	-	-	-	-	(12,523)	58	(12,465)
Total comprehensive income (expense) for the period	-	-	-	-	(12,523)	350,849	338,326
Transactions with owners, recorded directly in equity:							
Dividends	-	-	-	-	-	(355,205)	(355,205)
Acquisition of treasury shares	-	-	(97,395)	-	-	-	(97,395)
Transfer to unconditional reserve	-	-	-	-	504,591	(504,591)	-
Total transactions with owners	-	-	(97,395)	-	504,591	(859,796)	(452,600)
Balance at June 30, 2011	$ 885,780	3,323	(298,515)	447,202	2,518,506	352,884	3,909,180

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Changes in Equity, Continued

For the six-month period ended June 30, 2010

In millions of won		Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Total equity
Balance at January 1, 2010	₩	954,959	2,632	(226,945)	468,274	2,074,108	579,963	3,852,991
Total comprehensive income for the period:								
Profit for the period		-	-	-	-	-	589,063	589,063
Other comprehensive income:								
Available-for-sale financial assets, net of tax		-	-	-	-	(126,067)	-	(126,067)
Actuarial gains, net of tax		-	-	-	-	-	3,613	3,613
Total other comprehensive income (expense)		-	-	-	-	(126,067)	3,613	(122,454)
Total comprehensive income (expense) for the period		-	-	-	-	(126,067)	592,676	466,609
Transactions with owners, recorded directly in equity:								
Dividends		-	-	-	-	-	(356,157)	(356,157)
Transfer from reserve for research and human resource development		-	-	-	-	(15,000)	15,000	-
Transfer from reserve for loss on reissuance of treasury shares		-	-	-	-	(26,646)	26,646	-
Transfer to reserve for research and human resource development		-	-	-	-	60,000	(60,000)	-
Transfer to unconditional reserve		-	-	-	-	203,000	(203,000)	-
Total transactions with owners		-	-	-	-	221,354	(577,511)	(356,157)
Balance at June 30, 2010	₩	954,959	2,632	(226,945)	468,274	2,169,395	595,128	3,963,443

See accompanying notes to the separate interim financial statements.

KT&G CORPORATION
Separate Statements of Cash Flows

For the six-month periods ended June 30, 2011 and 2010

In millions of won and thousands of U.S. dollars	*Note*	2011 Korean won	2011 U.S. dollars (note 4)	2010 Korean won
Cash flows from operating activities				
Cash generated from operations	*30*	₩ 543,068	$ 503,727	₩ 447,102
Income tax paid		(193,106)	(179,117)	(100,423)
Net cash from operating activities		349,962	324,610	346,679
Cash flows from investing activities				
Interest received		13,946	12,936	5,979
Investment income received from long-term deposits in MSA Escrow Fund		904	839	992
Dividends received		54,607	50,651	31,855
Proceeds from sale of available-for-sale financial assets		2,570	2,384	261,959
Collection of loans		8,789	8,153	25,260
Proceeds from sale of property, plant and equipment		12,530	11,623	10,416
Proceeds from sale of intangible assets		3,754	3,482	538
Proceeds from sale of assets held for sale		-	-	59,000
Withdrawal of guarantee deposits		22,178	20,571	12,527
Proceeds from sale of other investment assets		52	48	20
Acquisition of available-for-sale financial assets		(10,000)	(9,276)	(11,623)
Increase in loans		(10,207)	(9,469)	(5,632)
Acquisition of investments in associates		(12,600)	(11,687)	-
Acquisition of investments in subsidiaries		(14,500)	(13,450)	(43,022)
Payments of guarantee deposits		(34,883)	(32,356)	(12,329)
Payments of long-term deposits in MSA Escrow Fund		(7,544)	(6,998)	(6,798)
Acquisition of property, plant and equipment		(63,968)	(59,334)	(44,515)
Acquisition of intangible assets		(3,580)	(3,320)	(3,170)
Acquisition of investment property		(1,232)	(1,142)	-
Net cash provided by (used in) investing activities		(39,184)	(36,345)	281,457
Cash flows from financing activities				
Interest paid		-	-	(5)
Dividends paid		(382,946)	(355,205)	(356,157)
Decrease in deposits received		(3,916)	(3,632)	(3,130)
Acquisition of treasury shares		(105,002)	(97,396)	-
Increase in deposits received		7,308	6,780	2,229
Net cash used in financing activities		(484,556)	(449,453)	(357,063)
Net increase in cash and cash equivalents		(173,778)	(161,188)	271,073
Cash and cash equivalents at beginning of period		828,951	768,900	268,954
Effect of exchange rate fluctuation on cash held		(80)	(75)	8
Cash and cash equivalents at end of period		₩ 655,093	$ 607,637	₩ 540,035

See accompanying notes to the separate interim financial statements.

June 30, 2011 and 2010

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 Code 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 June 30, 2011, the Company has four manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 139 branches for the sale of tobacco throughout the country. Also, the Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printing plant for the manufacturing of packaging. The head office of the Company is located in Pyeongchon-dong, 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 BdL market to the Euro MTF in the Luxembourg Stock Exchange.

The ownership of the Company's issued ordinary shares as of June 30, 2011 is held as follows:

In millions of won,
except number of shares and percentage of ownership

Shareholder	Number of shares	Percentage of ownership	Amount
Industrial Bank of Korea	9,510,485	6.93%	47,552
Employee Share Ownership Association	3,716,594	2.71%	18,583
Treasury shares	11,284,790	8.22%	56,424
Others	112,780,628	82.14%	563,903
Retirement of treasury shares	-	-	268,497
	137,292,497	100.00%	954,959

2. Basis of Preparation

(a) Statement of Compliance

The financial statements have been prepared in accordance with Korean International Financial Reporting Standards ("K-IFRS"), as prescribed in the Act on External Audit of Corporations. K-IFRS is effective from the fiscal year beginning on or after January 1, 2011 and the Company early-adopted K-IFRS from 2009.

These financial statements are separate financial statements which are those presented by a parent or an investor in an associate, 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 investee in accordance with K-IFRS No.1027 *Consolidated and Separate Financial Statements*.

These financial statements have been prepared in accordance with K-IFRS No.1034 *Interim Financial Reporting*.

(b) Basis of Measurement

The financial statements have been prepared under the historical cost basis except as described in the accounting policy below on financial instruments and inventories valued at net realizable value.

(c) Use of Estimates and Judgments

The preparation of the financial statements in conformity with K-IFRS requires management to make judgements, 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.

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

- Classification of investment property – Note 7.

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

- Measurement of defined benefit obligations – Note 21
- Provisions and contingencies – Note 28.

June 30, 2011 and 2010

3. Significant Accounting Policies

(a) Investments in Subsidiaries and Associates in the Separate Financial Statements

These financial statements are separate financial statements which are those presented by a parent or an investor in an associate in accordance with K-IFRS No.1027, 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 Company accounts for investments in subsidiaries and associates at cost. The Company measures an investment in Korea Ginseng Corporation at the deemed cost which is the previous GAAP carrying amount at the date of transition in accordance with K-IFRS No.1101 *First-time Adoption of Korean International Financial Reporting Standards*. Dividends on investments in subsidiaries and associates are recognized in profit or loss when the Company's right to receive payment is established.

(b) Foreign Currencies

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

Foreign currency transactions are initially recorded using the spot exchange rate between the functional currency and the foreign currency at the date of the transaction. At the end of each reporting period, foreign currency monetary items are translated using the closing rate. 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. Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous financial statements are recognized in profit or loss in the period in which they arise. When gains or losses on non-monetary items are recognized in other comprehensive income, exchange components of those gains or losses are recognized in other comprehensive income. Conversely, when gains or losses on non-monetary items are recognized in profit or loss, exchange components of those gains or losses are recognized in profit or loss.

(c) Property, Plant and Equipment

Property, plant and equipment are measured initially at cost and after initial recognition, are carried at cost less accumulated depreciation and accumulated impairment losses. The cost of property, plant and equipment includes expenditure arising directly from the construction or acquisition of the asset, any costs directly attributable to bringing the asset to the location and condition necessary for them to be capable of operating in the manner intended by management and the initial estimate of the costs of dismantling and removing the item and restoring the site on which they are located.

Subsequent costs are recognized in the carrying amount of property, plant and equipment 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.

3. Significant Accounting Policies, Continued

(c) Property, Plant and Equipment, Continued

Property, plant and equipment, except for land and other tangible fixed assets, are depreciated on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. The estimated useful lives were as follows:

	Useful lives (years)
Buildings and structures	10 ~ 60
Machinery and vehicles	4 ~ 12
Tools, furniture and fixtures	4

Each part of property, plant and equipment with a cost that is significant in relation to the total cost are depreciated separately.

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

(d) Intangible Assets

Intangible assets are measured initially at cost and after initial recognition, are carried at cost less accumulated amortization and accumulated impairment losses. Intangible assets consist of industrial property rights, rights to facility usage and other intangible assets. 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 rights to facility usage and some of industrial property right 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	10 ~ 20 or indefinite
Rights to facility usage	indefinite
Other intangible assets	4

The amortization period and the amortization method for intangible assets with a finite useful life are reviewed at each financial year-end. The useful lives of intangible assets that are not being amortized are reviewed each period to determine whether events and circumstances continue to support an indefinite useful life assessment for those assets. If it is appropriate to change, such a change is accounted for as a change in an accounting estimate.

3. Significant Accounting Policies, Continued

(e) Investment Property

Properties held to earn rentals or for capital appreciation are classified as investment properties. Investment properties are measured initially at its cost including transaction costs and after initial recognition, are carried at cost less accumulated depreciation and 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 properties, except for land, are depreciated on a straight-line basis over 10 ~ 60 years, the estimated useful lives. Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate. The change is accounted for as a change in an accounting estimate.

(f) Inventories

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

The cost of 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 the specific 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 losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in the amount of inventories and recognized as an expense in the period in which the reversal occurs.

Tobacco leaf inventories which have an operating cycle that exceeds 12 months are classified as current assets, consistent with recognized industry practice. The estimated amounts of inventories in current assets which are not expected to be realized within 12 months are ₩363,223 million and ₩403,082 million as of June 30, 2011 and December 31, 2010, respectively.

3. Significant Accounting Policies, Continued

(g) Non-derivative Financial Assets

The Company classifies a non-derivative financial asset into the following four categories: financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables or available-for-sale financial assets, relating to recognition and measurement of 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 financial asset. The Company derecognizes financial assets from the statement of financial position when the contractual rights to the cash flows from the financial asset expire or the Company transfers the contractual rights to receive the cash flows on the financial asset in a transaction in which all the risks and rewards of ownership of the financial asset are substantially transferred. 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 asset and recognizes financial liabilities for the consideration received.

Non-derivative financial assets comprise investments in equity and debt securities, long-term deposits in MSA Escrow Fund, trade and other receivables and cash and cash equivalents. When non-derivative financial assets are recognized initially, the Company measures it at its fair value plus, in the case of financial assets not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset.

Financial Assets at Fair Value through Profit or Loss
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.

Held-to-maturity Investments
Non-derivative financial assets with fixed or determinable payments and fixed maturity that the Company has the positive intention and ability to hold to maturity are classified as held-to-maturity investments. After initial recognition, held-to-maturity investments are measured at amortized cost using the effective interest method.

Loans and Receivables
Loans and receivables are trade receivables, loans and other receivables with fixed or determinable payments that are not quoted in an active market. After initial recognition, loans and receivables are measured at amortized cost using the effective interest method except for short-term receivables of which the effect of discounting is immaterial.

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 and changes therein are recognized directly in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary available-for-sale financial assets. Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost. When the financial asset is derecognized or impairment losses is recognized, the cumulative gain or loss previously recognized in other comprehensive income is reclassified from equity to profit or loss. Dividends on an available-for-sale equity instrument are recognized in profit or loss when the Company's right to receive payment is established.

3. Significant Accounting Policies, Continued

(g) Non-derivative Financial Assets, Continued

Cash and Cash Equivalents
Cash and cash equivalents comprise cash on hand, demand deposits and short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preferred shares acquired within a short period of their maturity and with a specified redemption date. Bank overdrafts are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(h) Non-derivative Financial Liabilities

The Company classifies non-derivative financial liabilities into financial liabilities at fair value through profit or loss or 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 and removes financial liabilities from the statement of financial position when the financial liability is extinguished.

Non-derivative financial liabilities comprise borrowings and trade and other payables. When non-derivative financial liabilities are recognized initially, the Company measures it at its fair value minus, in the case of financial liabilities not at fair value through profit or loss, transaction costs that are directly attributable to the issue of the financial liability.

Financial Liabilities at Fair Value through Profit or Loss
Financial liabilities 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 liabilities at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

Other Financial Liabilities
Other financial liabilities are those non-derivative financial liabilities that are not classified as financial liabilities at fair value through profit or loss. After initial recognition, other financial liabilities are measured at amortized cost using the effective interest method except for short-term liabilities of which the effect of discounting is immaterial.

3. Significant Accounting Policies, Continued

(i) Non-current Assets Held for Sale

The Company classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use, and measures it at the lower of its carrying amount and fair value less costs to sell.

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

The Company recognizes an impairment loss for write-down of the asset (or disposal group) to fair value less costs to sell and a gain for increase in fair value less costs to sell of an asset, but not in excess of the cumulative impairment loss that has been recognized previously in accordance with K-IFRS No.1036 *Impairment of Assets*.

(j) 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 six-month periods ended June 30, 2011 and 2010 were ₩1,610,463 million and ₩1,625,630 million, respectively.

Revenue from lotting-out construction contracts 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 and the lotting-out rate. The stage of completion is assessed by reference to surveys of work performed.

Revenue associated with the transaction involving the 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.

Revenue arising from the use by others of the Company assets yielding interest, royalties and dividends is recognized when it is probable that the economic benefits associated with the transaction will flow to the Company and the amount of the revenue can be measured reliably.

In addition, interest is recognized using the effective interest method, royalties are recognized on an accrual basis in accordance with the substance of the relevant agreement and dividends are recognized when the shareholders' right to receive is established.

3. Significant Accounting Policies, Continued

(k) Impairment of Non-financial Assets

The Company assesses at the end of each reporting period whether there is any indication that an asset may be impaired except for inventories, deferred tax assets, assets arising from employee benefits and non-current assets (or disposal groups) classified as held for sale. If any such indication exists, the Company estimates the recoverable amount of the asset. Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, irrespective of whether there is any indication that it may be impaired. If there is any indication that an asset may be impaired, recoverable amount is estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, the Company determines the recoverable amount of the cash-generating unit to which the asset belongs (the asset's cash-generating unit).

The recoverable amount is measured as the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. If the recoverable amount of an asset or cash-generating unit is less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. That reduction is recognized in profit or loss.

(l) Impairment of Financial Assets

The Company assesses at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired, except a financial asset at fair value through profit or loss. A financial asset or group of financial assets is considered to be impaired if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset. For specific financial assets such as trade receivables, if the Company determines that no objective evidence of impairment exists for an individually assessed financial asset, it collectively assesses them for impairment. The objective evidence that the group of loans and receivables is impaired includes an increased number of delayed payments and an adverse change in national or local economic conditions that correlate with defaults on the assets in the group.

The amount of the impairment loss on financial assets carried at amortized cost is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced either directly or through use of an allowance account. The amount of the loss is recognized in profit or loss. 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. The reversal does not result in a carrying amount of the financial asset that exceeds what the amortized cost would have been had the impairment not been recognized at the date the impairment is reversed. The amount of the reversal is recognized in profit or loss.

The amount of the impairment loss on financial assets carried at cost 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.

3. Significant Accounting Policies, Continued

(l) Impairment of Financial Assets, Continued

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 equity 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.

(m) Income Taxes

Income tax expense comprises current tax expense and deferred tax expense. Current and deferred taxes are recognized as an expense included in profit or loss for the period, except to the extent that the tax arises from a transaction which is recognized in other comprehensive income or directly in equity.

Current tax expense is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period. Current tax liabilities (assets) for the current and prior periods are measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and liabilities are recognized for temporary differences which are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base, the carryforward of unused tax losses and unused tax credits. 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 that have been enacted or substantively enacted by the end of the reporting period.

The Company recognizes a deferred tax liability for all taxable temporary differences associated with investments in subsidiaries and associates, except to the extent that the parent or investor is able to control the timing of the reversal of the temporary difference; and it is probable that the temporary difference will not reverse in the foreseeable future.

The Company recognizes a deferred tax asset for all deductible temporary differences arising from investments in subsidiaries and associates, to the extent that, and only 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. The Company reduces the carrying amount of a deferred tax asset 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 these deferred tax assets to be utilized. Such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Income tax expense is recognized in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

3. Significant Accounting Policies, Continued

(n) Dividends

The dividends declared to holders of equity instruments after the reporting period are not recognized as a liability at the end of the reporting period.

(o) Equity Capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the equity transaction are recognized as a deduction from equity, net of any tax effects.

If the Company reacquires its own equity instruments, those instruments ("treasury shares") are presented as a deduction from total equity. The gain or loss on the purchase, sale, issue or cancellation of treasury shares is not recognized in profit or loss but recognized directly in equity.

(p) Provisions, Contingent Assets and Contingent Liabilities

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 amount recognized as a provision is the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. 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, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation.

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

Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimate. 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.

3. Significant Accounting Policies, Continued

(q) Employee Benefits

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.

The Company recognizes the expected cost of profit-sharing and bonus payments if the Company has a present legal or constructive obligation to make such payments as a result of past events; and a reliable estimate of the obligation can be made.

Retirement Benefits: Defined Contribution Plans
With regard to the defined contribution plan, 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.

Retirement Benefits: Defined Benefit Plans
The Company classifies retirement benefits plans other than defined contribution plans as defined benefit plans. The defined benefit liabilities are calculated at the present value of the defined benefit obligations less the fair value of the plan assets at the end of the reporting period.

In determining the present value of its defined benefit obligations and the related current service cost, the Company uses the projected unit credit method.

With regard to actuarial gains and losses which arise from application of actuarial assumptions, the Company recognizes all actuarial gains and losses in other comprehensive income. Actuarial gains and losses recognized in other comprehensive income are recognized immediately in retained earnings and are not reclassified to profit or loss in a subsequent period.

Termination Benefits
The Company recognizes termination benefits as a liability and an expense when, and only when, the Company is demonstrably committed to terminating the employment of an employee or group of employees before the normal retirement date or providing termination benefits as a result of an offer made in order to encourage voluntary redundancy.

3. Significant Accounting Policies, Continued

(r) 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 for the period attributable to owners of the Company by the weighted-average number of shares outstanding during the period.

Diluted EPS is determined by adjusting the profit or loss for the period attributable to owners of the Company and the weighted-average number of shares outstanding for the effects of all dilutive potential shares, which comprise employee share options.

(s) Operating Segments

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

(t) New Standards and Interpretations Not Yet Adopted

The new and amended standards and interpretations that have been issued but are not yet effective as of June 30, 2011 have not been applied in preparing the financial statements. None of these is expected to have a significant effect on the financial statement of the Company, except for K-IFRS No. 1109 *Financial Instruments*. The extent of the impact of adopting this standard on the financial statements has not been determined.

4. Basis of Translating Financial Statements

The separate interim financial statements are expressed in Korean won and have been translated into U.S. dollars at the rate of ₩1,078.10 to $1, the basic exchange rate on June 30, 2011 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.

5. Property, Plant and Equipment

(a) Changes in property, plant and equipment for the six-month period ended June 30, 2011 were as follows:

In millions of won		Land, buildings and structures	Machinery and vehicles	Tools, furniture, fixtures and other	Construction-in-progress	Total
Cost:						
Balance at January 1, 2011	₩	1,037,073	828,046	188,894	82,475	2,136,488
Additions		697	1,712	4,543	57,016	63,968
Disposals		(6,808)	(7,107)	(557)	-	(14,472)
Others		22,084	4,669	558	(65,270)	(37,959)
Balance at June 30, 2011	₩	1,053,046	827,320	193,438	74,221	2,148,025
Accumulated depreciation and impairment:						
Balance at January 1, 2011	₩	(252,397)	(547,083)	(140,882)	-	(940,362)
Disposals		689	6,849	546	-	8,084
Depreciation		(10,906)	(29,654)	(12,938)	-	(53,498)
Others		5,313	755	-	-	6,068
Balance at June 30, 2011	₩	(257,301)	(569,133)	(153,274)	-	(979,708)
Carrying amount:						
Balance at January 1, 2011	₩	784,676	280,963	48,012	82,475	1,196,126
Balance at June 30, 2011	₩	795,745	258,187	40,164	74,221	1,168,317

Other changes for the six-month period ended June 30, 2011 include assets with a carrying amount of ₩27,739 million transferred to investment property, those of ₩8,955 million transferred to assets held for sale, those of ₩559 million transferred from investment property, and those of ₩4,244 million transferred from investment property.

For the six-month period ended June 30, 2010, the Company purchased and disposed of property, plant and equipment amounting to ₩44,515 million and ₩4,737 million, respectively.

5. Property, Plant and Equipment, Continued

(b) Changes in property, plant and equipment for the year ended December 31, 2010 were as follows:

In millions of won		Land, buildings and structures	Machinery and vehicles	Tools, furniture, fixtures and other	Construction-in-progress	Total
Cost:						
Balance at January 1, 2010	₩	1,022,347	835,754	232,769	45,447	2,136,317
Additions		4,593	10,500	18,205	91,180	124,478
Disposals		(6,493)	(44,178)	(63,456)	(123)	(114,250)
Others		16,626	25,970	1,376	(54,029)	(10,057)
Balance at December 31, 2010	₩	1,037,073	828,046	188,894	82,475	2,136,488
Accumulated depreciation and impairment:						
Balance at January 1, 2010	₩	(229,226)	(523,569)	(173,096)	-	(925,891)
Disposals		1,936	36,525	61,866	-	100,327
Depreciation		(25,004)	(60,039)	(29,652)	-	(114,695)
Others		(103)	-	-	-	(103)
Balance at December 31, 2010	₩	(252,397)	(547,083)	(140,882)	-	(940,362)
Carrying amount:						
Balance at January 1, 2010	₩	793,121	312,185	59,673	45,447	1,210,426
Balance at December 31, 2010	₩	784,676	280,963	48,012	82,475	1,196,126

Other changes for the year ended December 31, 2010 include assets with a carrying amount of ₩957 million transferred to operating expenditures, those of ₩9,449 million transferred to inventories (sites for lotting-out construction) and those of ₩247 million transferred from investment property.

6. Intangible Assets

(a) Changes in intangible assets for the six-month period ended June 30, 2011 were as follows:

In millions of won		Industrial property rights	Rights to facility usage	Other intangible assets	Intangible assets under development	Total
Cost:						
Balance at January 1, 2011	₩	6,266	16,514	4,074	31,617	58,471
Additions		-	2,713	-	867	3,580
Disposals		-	(3,322)	(1)	-	(3,323)
Others		92	-	-	(92)	-
Balance at June 30, 2011	₩	6,358	15,905	4,073	32,392	58,728
Accumulated amortization and impairment:						
Balance at January 1, 2011	₩	(5,187)	-	(4,073)	(647)	(9,907)
Amortization		(20)	-	-	-	(20)
Balance at June 30, 2011	₩	(5,207)	-	(4,073)	(647)	(9,927)
Carrying amount:						
Balance at January 1, 2011	₩	1,079	16,514	1	30,970	48,564
Balance at June 30, 2011	₩	1,151	15,905	-	31,745	48,801

For the six-month period ended June 30, 2010, the Company acquired and disposed of intangible assets amounting to ₩3,170 million and ₩694 million, respectively.

6. Intangible Assets, Continued

(b) Changes in intangible assets for the year ended December 31, 2010 were as follows:

In millions of won		Industrial property rights	Rights to facility usage	Other intangible assets	Intangible assets under development	Total
Cost:						
Balance at January 1, 2010	₩	6,175	15,316	658	29,419	51,568
Additions		3	1,711	3,416	2,657	7,787
Disposals		(200)	(513)	-	(171)	(884)
Others		288	-	-	(288)	-
Balance at December 31, 2010	₩	6,266	16,514	4,074	31,617	58,471
Accumulated amortization and impairment:						
Balance at January 1, 2010	₩	(5,233)	-	(647)	(647)	(6,527)
Disposals		94	-	-	-	94
Amortization		(48)	-	(11)	-	(59)
Impairment		-	-	(3,415)	-	(3,415)
Balance at December 31, 2010	₩	(5,187)	-	(4,073)	(647)	(9,907)
Carrying amount:						
Balance at January 1, 2010	₩	942	15,316	11	28,772	45,041
Balance at December 31, 2010	₩	1,079	16,514	1	30,970	48,564

The Company recognized ₩3,415 million of impairment loss on the intangible assets relating to the acquisition of the sales network in the United States for the year ended December 31, 2010.

(c) Expenditures not capitalized for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

			2011		2010
In millions of won		Three-month	Six-month	Three-month	Six-month
Cost of sales	₩	41	85	75	136
Selling expenses		189	237	351	377
General and administrative expenses		2,991	5,544	2,985	4,628
	₩	3,221	5,866	3,411	5,141

7. Investment Property

(a) Changes in investment property for the six-month period ended June 30, 2011 were as follows:

In millions of won		Land	Buildings	Total
Cost:				
Balance at January 1, 2011	₩	13,919	116,660	130,579
Subsequent expenditure		-	1,232	1,232
Transfer to property, plant and equipment		(268)	(464)	(732)
Transfer from property, plant and equipment		1,481	26,257	27,738
Balance at June 30, 2011	₩	15,132	143,685	158,817
Accumulated depreciation and impairment:				
Balance at January 1, 2011	₩	-	(32,436)	(32,436)
Depreciation		-	(2,199)	(2,199)
Transfer to property, plant and equipment		-	174	174
Balance at June 30, 2011	₩	-	(34,461)	(34,461)
Carrying amount:				
Balance at January 1, 2011	₩	13,919	84,224	98,143
Balance at June 30, 2011	₩	15,132	109,224	124,356

(b) Changes in investment property for the year ended December 31, 2010 were as follows:

In millions of won		Land	Buildings	Total
Cost:				
Balance at January 1, 2010	₩	13,919	117,010	130,929
Transfer to property, plant and equipment		-	(350)	(350)
Balance at December 31, 2010	₩	13,919	116,660	130,579
Accumulated depreciation and impairment:				
Balance at January 1, 2010	₩	-	(29,029)	(29,029)
Depreciation		-	(3,510)	(3,510)
Transfer to property, plant and equipment		-	103	103
Balance at December 31, 2010	₩	-	(32,436)	(32,436)
Carrying amount:				
Balance at January 1, 2010	₩	13,919	87,981	101,900
Balance at December 31, 2010	₩	13,919	84,224	98,143

7. Investment Property, Continued

(c) The amounts recognized in profit or loss from investment property for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Rental income	₩	4,835	9,158	3,989	8,359
Direct operating expense		(1,152)	(2,199)	(877)	(1,755)
	₩	3,683	6,959	3,112	6,604

(d) The carrying amount and the fair value of investment property as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		June 30 2011 Fair value	June 30 2011 Carrying amount	December 31 2010 Fair value	December 31 2010 Carrying amount
Land	₩	205,864	15,132	204,383	13,919
Buildings		134,145	109,224	109,235	84,224
	₩	340,009	124,356	313,618	98,143

(e) Investment property pledged as collateral as of June 30, 2011 was as follows:

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Leaseholder
Investment property	₩	56,346	Leasehold deposits received	₩	6,032	7,171	Metlife Insurance Korea Co., Ltd. and 24 others

(f) Investment property pledged as collateral as of December 31, 2010 was as follows:

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Leaseholder
Investment property	₩	32,722	Leasehold deposits received	₩	2,583	3,429	Korea Life Insurance Co., Ltd. and 18 others

8. Investments in Associates

Investments in associates as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won, except percentage of ownership			June 30 2011		December 31 2010	
Associate	Location	Principal operation	Percentage of ownership	Carrying amount	Percentage of ownership	Carrying amount
Cosmo Tabacco Co., Ltd.	Mongolia	Manufacturing and selling tobaccos	40.00%	₩ -	40.00%	₩ -
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	25.34%	1,830	25.34%	1,830
Korean Carbon Finance, Inc.	Korea	Emissions trading	20.00%	1,000	20.00%	1,000
JR CR-REIT IV Co., Ltd.	Korea	Selling and renting of real estate	32.68%	10,000	-	-
KVG REIT 1 Co., Ltd.	Korea	Selling and renting of real estate	29.67%	7,300	-	-
KOCREF REIT 17 Co., Ltd.	Korea	Selling and renting of real estate	22.06%	7,000	-	-
JR REIT V Co., Ltd.	Korea	Selling and renting of real estate	34.63%	5,600	-	-
				₩ 32,730		₩ 2,830

The Company reclassified ₩17,300 million of available-for-sale financial assets to investments in associates for the six-month period ended June 30, 2011.

The Company recognized ₩2,947 million of impairment loss on the investment in Cosmo Tabacco Co., Ltd. in years prior to the previous year.

9. Investments in Subsidiaries

Investments in subsidiaries as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won, except percentage of ownership			June 30 2011		December 31 2010	
Subsidiary	Location	Principal operation	Percentage of ownership	Carrying amount	Percentage of ownership	Carrying amount
Korea Ginseng Corporation	Korea	Manufacturing and selling ginseng	100.00%	₩ 559,882	100.00%	₩ 559,882
Yungjin Pharm. Ind. Co., Ltd.	Korea	Manufacturing and selling pharmaceuticals	53.00%	66,355	53.00%	66,355
Tae-a Industry Co., Ltd. (*1)	Korea	Manufacturing tobacco materials	100.00%	15,698	100.00%	14,198
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Turkey	Manufacturing and selling tobaccos	99.99%	54,049	99.99%	54,049
Korea Tabacos do Brasil Ltda.	Brazil	Processing leaf tobaccos	99.90%	394	99.90%	394
KT&G Pars	Iran	Manufacturing and selling tobaccos	99.99%	5,733	99.99%	5,733
KT&G Rus L.L.C.	Russia	Manufacturing and selling tobaccos	100.00%	110,297	100.00%	110,297
KGC Life & Gin Co., Ltd. (formerly, KGC Sales Co., Ltd.)	Korea	Selling ginseng door-to-door	100.00%	22,500	100.00%	22,500
KT&G Bio Corp.	Korea	Manufacturing and selling pharmaceuticals	100.00%	900	100.00%	900
Global Trading, Inc.	USA	Selling tobaccos	100.00%	4,913	100.00%	4,913
Purpleland Development Co., Ltd.	Korea	Selling and renting of real estate	100.00%	900	100.00%	900
Jilin Hanzheng Ginseng Co., Ltd. (*2)	China	Manufacturing and selling ginseng	100.00%	13,000	-	-
				₩ 854,621		₩ 840,121

(*1) Tae-a Industry Co., Ltd. increased paid-in capital by way of shareholder allocation and the Company's investments in subsidiaries increased by ₩1,500 million for the six-month period ended June 30, 2011.

(*2) The Company established Jilin Hanzheng Ginseng Co., Ltd. in 2011.

10. Available-for-sale Financial Assets

(a) Changes in available-for-sale financial assets for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	314,937	443,800
Acquisitions		10,000	39,923
Net changes in fair value before tax		(17,311)	(141,998)
Transfer to investments in associates		(17,300)	-
Impairment		(3,988)	-
Disposals		(1,927)	(26,788)
Balance at end of period	₩	284,411	314,937
Statements of financial position:			
- Current	₩	-	1,000
- Non-current		284,411	313,937
	₩	284,411	314,937

The Company recognized ₩3,988 million of impairment loss on the available-for-sale equity instruments of Migami, Inc. for the six-month period ended June 30, 2011.

(b) Available-for-sale financial assets as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011	December 31 2010
Available-for-sale debt instruments:			
- Government and municipal bonds	₩	44	44
- Corporate bonds		2,000	20,300
Total available-for-sale debt instruments		2,044	20,344
Available-for-sale equity instruments:			
Listed			
- YTN Co., Ltd.		20,950	30,839
- Oscotech, Inc.		1,159	1,022
- Shinhan Financial Group Co., Ltd.		204,025	212,042
- Rexahn Pharmaceuticals, Inc.		8,544	8,152
		234,678	252,055
Unlisted			
- Dream Hub PFV Co., Ltd.		12,732	12,732
- Migami, Inc.		-	3,988
- Other unlisted available-for-sale equity instruments		34,957	25,818
		47,689	42,538
Total available-for-sale equity instruments		282,367	294,593
Total available-for-sale financial assets	₩	284,411	314,937

10. Available-for-sale Financial Assets, Continued

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

The fair value of Dream Hub PFV Co., Ltd. which does not have a market price in an active market is measured at the value per share determined by the net asset valuation model.

The other unlisted available-for-sale equity instruments that do not have a market price in an active market and whose fair value cannot be reliably measured and available-for-sale debt instruments whose fair value is similar to their carrying amount, are measured at cost.

11. Long-term Deposits in MSA Escrow Fund

(a) Long-term deposits in MSA Escrow Fund as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011	December 31 2010
MMF	₩	77,626	74,167
Treasury note		56,335	58,247
	₩	133,961	132,414

(b) As discussed in note 28 to the 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 deposits in MSA Escrow Fund for the six-month periods ended June 30, 2011 and 2010 are ₩7,544 million and ₩6,798 million, respectively.

(c) Investment income on long-term deposits in MSA Escrow Fund for the six-month periods ended June 30, 2011 and 2010 are ₩2,072 million and ₩5,549 million, respectively.

(d) Long-term deposits in MSA Escrow Fund are measured at quoted prices in an active market.

12. Trade and Other Receivables

(a) Trade and other receivables as of June 30, 2011 and December 31, 2010 are summarized as follows:

		June 30 2011		December 31 2010	
In millions of won		Current	Non-current	Current	Non-current
Loans to employees	₩	17,889	35,681	19,287	42,972
Loans		1,352	29,649	14,942	7,374
Other receivables		49,645	-	70,822	-
Guarantee deposits		-	46,486	-	34,249
Accrued income		2,779	-	2,989	-
Trade receivables		495,849	-	419,787	-
	₩	567,514	111,816	527,827	84,595

(b) Trade and other receivables as of June 30, 2011 and December 31, 2010 have been reported in the statements of financial position net of allowances as follows:

		June 30 2011		December 31 2010	
In millions of won		Current	Non-current	Current	Non-current
Gross trade and other receivables	₩	572,751	111,816	533,011	84,595
Allowance account:					
- Other receivables		(1,961)	-	(1,917)	-
- Trade receivables		(3,276)	-	(3,267)	-
		(5,237)	-	(5,184)	-
Net trade and other receivables	₩	567,514	111,816	527,827	84,595

(c) Changes in the allowance account for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	5,184	5,407
Impairment loss		53	63
Write-off		-	(286)
Balance at end of period	₩	5,237	5,184

Impairment loss on trade and other receivables is included as part of other expense in the statements of comprehensive income.

12. Trade and Other Receivables, Continued

(d) The aging schedule of trade and other receivables which were past due but not impaired as of June 30, 2011 and December 31, 2010 is as follows:

In millions of won		June 30 2011	December 31 2010
Within 1 month	₩	57,983	46,679
Between 1 and 2 months		19,257	64,212
Beyond 2 months		131,268	7,226
	₩	208,508	118,117

There is no significant concentration of credit risk with respect to trade and other receivables since trade and other receivables, excluding export trade receivables, are widely dispersed amongst a number of customers. The Company holds bank guarantees, other guarantees and credit insurance 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 June 30, 2011 and December 31, 2010 were as follows:

	June 30 2011				December 31 2010			
In millions of won	Effective interest rate		Current	Non-current	Effective interest rate		Current	Non-current
Loans to employees	3.00~5.68%	₩	17,889	35,681	3.00~5.68%	₩	19,287	42,972
Guarantee deposits	3.00~5.68%		-	46,486	3.00~5.68%		-	34,249
		₩	17,889	82,167		₩	19,287	77,221

There is no material difference between the carrying amount and their fair value except the above trade and other receivables, due to the short-term duration of the majority of trade and other receivables.

13. Inventories

(a) Inventories as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011	December 31 2010
Finished goods, net of loss on the write-down of inventories	₩	91,169	70,770
Work-in-progress		14,798	14,401
Raw materials		765,430	843,286
Supplies		23,490	23,400
By-products		7,601	7,467
Buildings under construction		1,398	381
Sites for lotting-out construction		5,221	9,449
Goods-in-transit		24,968	21,179
	₩	934,075	990,333

(b) The amounts of inventories recognized as an expense for the six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011	2010
Cost of sales:			
- Loss on the write-down of inventories	₩	29	125
Other expense:			
- Loss on retirement of inventories		1,912	1,835
	₩	1,941	1,960

14. Cash and Cash Equivalents

Cash and cash equivalents as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011	December 31 2010
Cash on hand	₩	6,169	4,956
Demand deposits		98,924	53,995
Short-term investment assets		550,000	770,000
	₩	655,093	828,951

Cash equivalents mainly include short-term deposits with an original maturity of three months or less. The carrying amount of cash and cash equivalents approximates their fair value.

15. Share Capital

(a) Details of share capital as of June 30, 2011 and December 31, 2010 were as follows:

In won, except number of shares		June 30 2011	December 31 2010
Number of ordinary shares:			
- Authorized		800,000,000	800,000,000
- Issued		137,292,497	137,292,497
- Outstanding		126,007,707	127,648,800
Par value	₩	5,000	5,000

The Company has, thus far, reacquired and retired 53,699,400 shares of treasury shares. Accordingly, as of June 30, 2011, the Company's ordinary shares differ from the aggregate par value of issued shares by ₩268,497 million.

(b) Changes in the number of shares for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

	2011			2010		
Number of shares	Ordinary shares	Treasury shares	Total	Ordinary shares	Treasury shares	Total
Beginning of period	137,292,497	(9,643,697)	127,648,800	137,292,497	(10,093,697)	127,198,800
Acquisition of treasury shares	-	(1,641,093)	(1,641,093)	-	-	-
Disposal of treasury shares	-	-	-	-	450,000	450,000
End of period	137,292,497	(11,284,790)	126,007,707	137,292,497	(9,643,697)	127,648,800

(c) Changes in the other capital surplus for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	3,582	2,632
Acquisition of KGC Life & Gin Co., Ltd.		-	(3,434)
Transfer of the sports department		-	4,384
Balance at end of period	₩	3,582	3,582

In 2010, the Company acquired all the shares of KGC Life & Gin Co., Ltd. for ₩4,934 million from Korea Ginseng Corporation, which is a subsidiary of the Company. The Company recognized investments in subsidiaries at the carrying amount of ₩1,500 million in the financial statements of Korea Ginseng Corporation. Accordingly, the Company recognized a decrease in other capital surplus amounting to ₩3,434 million.

In 2010, the Company disposed of its sports department for ₩8,565 million to Korea Ginseng Corporation, which is a subsidiary of the Company. The Company recognized the difference of ₩4,384 million between the net disposal proceeds and the carrying amount of the sports department as an increase in other capital surplus.

16. Treasury Shares

(a) Changes in the treasury shares for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won, except number of shares	2011		2010	
	Number of shares	Carrying amount	Number of shares	Carrying amount
Balance at beginning of period	9,643,697	₩ 216,827	10,093,697	₩ 226,945
Acquisition of treasury shares	1,641,093	105,002	-	-
Disposal of treasury shares	-	-	(450,000)	(10,118)
Balance at end of period	11,284,790	₩ 321,829	9,643,697	₩ 216,827

(b) Changes in gain on reissuance of treasury shares for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	482,129	468,274
Gain on reissuance of treasury shares before tax		-	18,278
Less: tax at 24.2%		-	(4,423)
Gain of reissuance of treasury shares, net of tax		-	13,855
Balance at end of period	₩	482,129	482,129

17. Reserves

(a) Details of reserves as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		June 30 2011	December 31 2010
Available-for-sale financial assets reserve	₩	4,532	18,034
Legal reserve		602,937	602,937
Voluntary reserve		2,107,732	1,563,732
	₩	2,715,201	2,184,703

(b) Available-for-sale financial assets reserve as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011	December 31 2010
Available-for-sale financial assets reserve before tax	₩	5,810	23,121
Tax effect		(1,278)	(5,087)
	₩	4,532	18,034

(c) Legal Reserve

The Korean Commercial Code 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.

17. Reserves, Continued

(d) Details of voluntary reserve as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		June 30 2011	December 31 2010
Reserve for business rationalization	₩	12,851	12,851
Reserve for research and human resource development		60,000	60,000
Reserve for business expansion		698,881	698,881
Unconditional reserve		1,336,000	792,000
	₩	2,107,732	1,563,732

Reserve for Business Rationalization
Until December 10, 2002 under the Special Tax Treatment Control Law, 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 Business Expansion
Reserve for business expansion was a legal reserve under the Korea Tobacco and Ginseng Corporation Act, which was abrogated on September 1, 1997, consequently, the existing balance has been regarded as a voluntary reserve since then.

Other Reserves
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 reserve is taken back into taxable income in the year of restoration. Reserves without specific purposes are restored to retained earnings by a resolution at a general meeting of shareholders.

18. Retained Earnings

Changes in retained earnings for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	929,140	579,963
Transfer from reserve for research and human resource development		-	15,000
Transfer from reserve for loss on reissuance of treasury shares		-	26,646
Transfer to reserve for research and human resource development		-	(60,000)
Transfer to unconditional reserve		(544,000)	(203,000)
Dividends		(382,946)	(356,157)
Profit for the period		378,188	931,127
Actuarial gains (losses), net of tax		63	(4,439)
Balance at end of period	₩	380,445	929,140

19. Short-term Borrowings

Short-term borrowings as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won	Annual interest rate		June 30 2011	December 31 2010
Customer credit contracts:				
National Agricultural Cooperative Federation	7.23%	₩	7,785	6,965
Kookmin Bank	3M CD rate+2.50%		1,564	1,653
		₩	9,349	8,618

The Company has entered into a customer credit contract with the National Agricultural Cooperative Federation ("NACF") and Kookmin Bank. The financial institutions pay past-due trade receivables for customers and the Company has provided guarantees to the financial institutions for customers. The amount paid by the financial institutions is recognized as short-term borrowings in the statements of financial position.

20. Trade and Other Payables

(a) Trade and other payables as of June 30, 2011 and December 31, 2010 are summarized as follows:

		June 30 2011		December 31 2010	
In millions of won		Current	Non-current	Current	Non-current
Leasehold deposits received	₩	-	25,776	-	22,902
Trade payables		42,004	-	21,669	-
Withholdings		3,945	-	2,725	-
Withholdings taxes		122,967	-	114,727	-
Accrued expenses		95,368	-	86,548	-
Other payables		21,312	-	12,918	-
	₩	285,596	25,776	238,587	22,902

(b) Details of trade and other payables that are measured at amortized cost as of June 30, 2011 and December 31, 2010 were as follows:

	June 30 2011			December 31 2010		
In millions of won	Effective interest rate		Amortized cost	Effective interest rate		Amortized cost
Leasehold deposits received	3.00~5.68%	₩	25,776	3.00~5.68%	₩	22,902

There is no material difference between the carrying amount and their fair value except the above trade and other payables, due to the short-term duration of the majority of trade and other payables.

21. Retirement Benefits Plan

The Company operates both defined benefit and defined contribution plans. According to these plans, the Company pays retirement benefits calculated under the plan's benefit formula at the time employees leave the Company. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method.

(a) The components of retirement benefits for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Defined benefit plan:					
- Current service costs	₩	5,733	11,466	3,107	11,270
- Interest costs		1,524	3,048	1,121	3,239
- Expected returns on plan assets		(1,118)	(2,236)	(1,609)	(3,217)
- Gains (losses) on the settlement of the plan		-	-	494	(1,319)
		6,139	12,278	3,113	9,973
Defined contribution plan:					
- Contributions recognized as expense		205	549	198	525
	₩	6,344	12,827	3,311	10,498

The Company recognized contributions payable amounting to ₩83 million as trade and other payables (accrued expenses) in the statement of financial position as of December 31, 2010.

The Company recognized termination benefits amounting to ₩24 million and ₩45,526 million as an expense for the six-month periods ended June 30, 2011 and 2010, respectively. The Company recognized trade and other payables (accrued expenses) amounting to ₩1,695 million in the statement of financial position as of December 31, 2010.

(b) Changes in defined benefit liabilities for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	28,774	18,295
Retirement benefits		12,278	27,725
Actuarial losses (gains) before tax		(81)	5,692
Payments into plan assets		-	(10,758)
Transfer of the sports department		-	(451)
Payments, including the amount transferred to the defined contribution plan		(1,682)	(11,258)
Changes in accrued expenses		314	(471)
Balance at end of period	₩	39,603	28,774
Statements of financial position:			
- Present value of retirement benefit obligations	₩	142,799	133,114
- Fair value of plan assets		(103,196)	(104,340)
Defined benefit liabilities	₩	39,603	28,774

21. Retirement Benefits Plan, Continued

(c) Changes in defined benefit obligations for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	133,114	129,813
Current service costs		11,466	26,895
Interest costs		3,048	6,978
Losses on the settlement of the plan		-	286
Actuarial losses before tax		-	5,033
Transfer of the sports department		-	(599)
Payments, including the amount transferred to the defined contribution plan		(5,605)	(33,798)
Changes in accrued expenses		776	(1,494)
Balance at end of period	₩	142,799	133,114

Some of employees have transferred from the defined benefit plan to the defined contribution plan. The Company recognized ₩286 million of the losses on the settlement of the defined benefit plan in profit or loss for the year ended December 31, 2010.

(d) Changes in plan assets for the six-month period ended June 30, 2011 and the year ended December 31, 2010 were as follows:

In millions of won		2011	2010
Balance at beginning of period	₩	104,340	111,518
Expected return on plan assets		2,236	6,434
Actuarial gains (losses) before tax		81	(659)
Payments into plan assets		-	10,758
Transfer of the sports department		-	(148)
Payments, including the amount transferred to the defined contribution plan		(3,923)	(22,540)
Changes in accrued expenses		462	(1,023)
Balance at end of period	₩	103,196	104,340

Actual returns on plan assets for the six-month periods ended June 30, 2011 and 2010 are ₩2,317 million and ₩3,640 million, respectively.

Expected rates of return are determined taking into account the current level of expected returns on risk-free investments, the historical level of risk premium associated with other invested assets, and the expectations for future returns on such assets.

(e) The amount of actuarial gains (losses) for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

		2011		2010	
In millions of won		Three-month	Six-month	Three-month	Six-month
Actuarial gains (losses) before tax	₩	71	81	(2)	4,632
Tax effect		(16)	(18)	-	(1,019)
	₩	55	63	(2)	3,613

21. Retirement Benefits Plan, Continued

(f) The components of plan assets as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		June 30 2011	December 31 2010
Cash and cash equivalents	₩	14	17,532
Short-term trading financial assets		59,261	58,942
Available-for-sale financial assets		43,921	27,866
	₩	103,196	104,340

As of June 30, 2011 and December 31, 2010, short-term trading financial assets include severance insurance of ₩66 million and ₩65 million, respectively, which continues to be covered by the existing retirement benefits plan.

(g) The principal actuarial assumptions as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won	June 30 2011	December 31 2010
Rate of salary increases	5.00%	5.00%
Discount rate	4.70%	4.70%
Expected rate of return on plan assets	4.40%	4.40%

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.

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

In millions of won		1 percentage point increase	1 percentage point decrease
Rate of salary increases:			
- Increase (decrease) in defined benefit obligations	₩	13,373	(11,755)
- Increase (decrease) in retirement benefits before tax		1,519	(1,327)
Discount rate:			
- Increase (decrease) in defined benefit obligations		(12,444)	14,494
- Increase (decrease) in retirement benefits before tax		(717)	800
Expected rate of return on plan assets:			
- Increase (decrease) in retirement benefits before tax		(508)	508

The effect on defined benefit obligations is as of June 30, 2011. The effect on retirement benefits before tax is for the six-month period ended June 30, 2011.

22. Profit from Operations

(a) Employee benefit costs for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

		2011		2010	
In millions of won		Three-month	Six-month	Three-month	Six-month
Salaries	₩	71,552	147,242	68,696	132,736
Retirement benefits		6,344	12,827	3,311	10,498
Termination benefits		24	24	43,997	45,526
Employee welfare		8,167	15,346	7,188	12,754
	₩	86,087	175,439	123,192	201,514

(b) Depreciation and amortization for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

		2011		2010	
In millions of won		Three-month	Six-month	Three-month	Six-month
Depreciation	₩	29,738	55,697	28,336	59,622
Amortization		8	20	12	35
	₩	29,746	55,717	28,348	59,657

(c) Details of other income for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

		2011		2010	
In millions of won		Three-month	Six-month	Three-month	Six-month
Foreign currency transaction gain	₩	1,529	2,109	5,053	7,498
Foreign currency translation gain		-	251	25,918	16,346
Gain on sale of property, plant and equipment		1,582	6,625	57,395	62,596
Gain on sale of intangible assets		-	605	-	1
Others		1,814	4,395	2,559	5,055
	₩	4,925	13,985	90,925	91,496

22. Profit from Operations, Continued

(d) Details of selling expenses for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Salaries	₩	34,463	70,355	29,187	61,531
Retirement and termination benefits		2,845	5,762	23,543	26,309
Employee welfare		4,272	8,062	3,551	6,419
Travel		976	1,851	816	1,528
Communications		424	847	443	853
Utilities		984	2,701	1,083	2,743
Taxes and dues		3,539	6,545	3,387	6,618
Supplies		244	520	70	351
Rent		2,591	5,619	2,633	5,100
Depreciation		6,740	11,063	7,372	14,911
Repairs and maintenance		1,502	2,400	641	1,883
Vehicles		1,826	3,522	1,604	3,124
Insurance		63	90	53	65
Commissions		6,970	14,204	6,544	12,456
Freight and custody		7,494	12,974	4,611	11,767
Conferences		353	703	341	889
Advertising		19,088	35,358	15,438	29,867
Training		146	435	224	493
Prizes and rewards		268	306	25	243
Normal research and development		189	237	351	377
	₩	94,977	183,554	101,917	187,527

22. Profit from Operations, Continued

(e) Details of general and administrative expenses for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Salaries	₩	12,365	26,112	14,916	22,364
Retirement and termination benefits		1,300	2,596	4,329	8,082
Employee welfare		1,290	2,457	1,795	1,924
Travel		754	1,271	500	879
Communications		520	1,058	746	1,209
Utilities		428	1,141	298	979
Taxes and dues		233	643	457	807
Supplies		184	498	194	723
Rent		474	631	221	576
Depreciation		2,683	5,205	2,553	5,625
Amortization		8	20	12	34
Repairs and maintenance		632	1,148	544	650
Vehicles		360	718	447	747
Insurance		47	236	19	231
Commissions		9,156	18,371	9,521	16,321
Freight and custody		369	666	429	643
Conferences		366	708	302	699
Advertising		14,663	28,860	18,250	34,038
Training		1,026	1,844	1,027	1,980
Prizes and rewards		226	296	248	435
Normal research and development		2,991	5,544	2,985	4,628
	₩	50,075	100,023	59,793	103,574

(f) Details of other expenses for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Foreign currency transaction loss	₩	5,987	8,011	4,440	7,941
Foreign currency translation loss		7,056	17,980	-	858
Impairment loss on trade and other receivables		1	53	4	13
Donations		169	2,324	493	3,072
Loss on sale of property, plant and equipment		382	483	241	438
Loss on sale of intangible assets		50	174	32	158
Others		1,542	3,157	1,129	2,151
	₩	15,187	32,182	6,339	14,631

June 30, 2011 and 2010

23. Net Finance Costs (Income)

(a) Details of net finance costs (income) for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Financial cost:					
- Interest costs	₩	336	354	46	100
- Impairment loss on available-for-sale financial assets		-	3,988	-	-
		336	4,342	46	100
Financial income:					
- Interest income		(6,329)	(13,924)	(3,203)	(7,096)
- Dividend income		(1,275)	(54,607)	-	(31,855)
- Investment income on long-term deposits in MSA Escrow Fund		(1,770)	(2,072)	(5,197)	(5,549)
- Gain on sale of available-for-sale financial assets		(643)	(643)	(239,748)	(240,104)
		(10,017)	(71,246)	(248,148)	(284,604)
Net finance costs (income)	₩	(9,681)	(66,904)	(248,102)	(284,504)

(b) Details of interest costs for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Related financial liabilities:					
- Trade and other payables		336	354	46	95
- Others		-	-	-	5
	₩	336	354	46	100

(c) Details of interest income for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Related financial assets:					
- Deposits	₩	5,889	13,016	2,429	5,556
- Available-for-sale financial assets		46	58	10	30
- Trade and other receivables		394	850	764	1,510
	₩	6,329	13,924	3,203	7,096

(d) Details of finance income (costs) recognized in other comprehensive income for the six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Before tax	2011 Tax effect	2011 Net of tax	2010 Before tax	2010 Tax effect	2010 Net of tax
Available-for-sale financial assets:							
Net changes in fair value	₩	(17,311)	3,809	(13,502)	78,480	(17,266)	61,214
Less: reclassified to profit or loss		-	-	-	(240,104)	52,823	(187,281)
	₩	(17, 311)	3,809	(13,502)	(161,624)	35,557	(126,067)

24. Income Taxes

(a) The Company was subject to income taxes on taxable income at the following normal tax rates.

Taxable income			Tax rate
2009 and thereafter	2009	2010 & 2011	Thereafter
Up to ₩200 million	12.1%	11.0%	11.0%
Over ₩200 million	24.2%	24.2%	22.0%

In December 2009, the Korean government postponed the reduction of the corporate income tax rate (including resident tax) from 24.2% to 22%, until 2012.

(b) The components of income tax expense (benefit) for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

			2011		2010
In millions of won		Three-month	Six-month	Three-month	Six-month
Current income tax expense	₩	63,884	106,204	128,009	168,160
Adjustments recognized in the period for current tax of prior periods		279	225	(429)	(429)
Changes in temporary difference		(6,253)	(5,050)	(49,970)	(24,805)
Total income tax expense		57,910	101,379	77,610	142,926
Tax expense (benefit) recognized outside profit or loss		(60)	3,791	52,310	34,538
Income tax expense	₩	57,850	105,170	129,920	177,464

(c) Current and deferred tax expense that were recognized outside profit or loss for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

			2011		2010
In millions of won		Three-month	Six-month	Three-month	Six-month
Current:					
- Actuarial gains	₩	(16)	(18)	-	(1,019)
Deferred:					
- Net changes in fair value of available-for-sale financial assets		(44)	3,809	52,310	35,557
Tax expense (benefit) recognized outside profit or loss	₩	(60)	3,791	52,310	34,538

Current and deferred tax expense relating to each component of other comprehensive income is recognized in other comprehensive income.

24. Income Taxes, Continued

(d) The income tax expense calculated by applying statutory tax rates to the Company's profit before tax for the period differs from the actual tax expense in the statements of comprehensive income for the three- and six-month periods ended June 30, 2011 and 2010 for the following reasons:

In millions of won, except tax rate information		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Profit before tax	₩	236,826	483,358	539,630	766,527
Normal tax rate		24.2%	24.2%	24.2%	24.2%
Expense for income taxes at normal tax rate		57,312	116,966	130,584	185,487
Adjustment:					
- Tax effects of permanent differences		543	1,052	544	1,156
- Non-inclusion of proceeds-dividend earned		-	(12,327)	-	(7,394)
- Investment tax credits		(335)	(670)	(678)	(1,254)
- Additional income taxes for prior period		330	149	(530)	(531)
Income tax expense	₩	57,850	105,170	129,920	177,464
Effective tax rate		24.4%	21.8%	24.1%	23.2%

(e) Deferred tax expense (benefit) relating to the origination and reversal of temporary differences for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Deferred tax liabilities at end of period	₩	(88,260)	(88,260)	(97,567)	(97,567)
Deferred tax liabilities at beginning of period		(94,513)	(93,310)	(147,537)	(122,372)
Deferred tax expense (benefit)	₩	(6,253)	(5,050)	(49,970)	(24,805)

(f) Deferred tax assets and liabilities are measured using the tax rate to be applied for the period in which temporary differences are expected to be realized.

(g) The net deferred tax liabilities are reflected in the statements of financial position after offsetting assets and liabilities where there is a legally enforceable right to offset current tax assets and liabilities and where the deferred income taxes relate to the same fiscal authority.

24. Income Taxes, Continued

(h) Changes in deferred tax assets and liabilities for the six-month period ended June 30, 2011 were as follows:

In millions of won		Balance at beginning of period	Credited to profit (charged to loss)	Charged to other comprehensive income	Balance at end of period
Available-for-sale financial assets	₩	9,861	878	-	10,739
Accrued expense		17,863	431	-	18,294
Defined benefit liabilities		179	1,058	-	1,237
Depreciation		3,895	(27)	-	3,868
Investments in subsidiaries		(95,884)	-	-	(95,884)
Foreign currency translations		1,220	(1,220)	-	-
Treasury shares		(8,183)	-	-	(8,183)
Available-for-sale financial assets reserve		(5,087)	-	3,809	(1,278)
Voluntary reserve		(13,200)	-	-	(13,200)
Provision for advanced depreciation		(4,722)	-	-	(4,722)
Others		748	121	-	869
	₩	(93,310)	1,241	3,809	(88,260)

(i) Changes in deferred tax assets and liabilities for the year ended December 31, 2010 were as follows:

In millions of won		Balance at beginning of period	Credited to profit (charged to loss)	Charged to other comprehensive income	Balance at end of period
Available-for-sale financial assets	₩	9,449	412	-	9,861
Accrued expense		20,411	(2,548)	-	17,863
Donations in excess of tax limit		89	(89)	-	-
Defined benefit liabilities		(1,894)	2,073	-	179
Depreciation		4,169	(274)	-	3,895
Investments in subsidiaries		(95,884)	-	-	(95,884)
Foreign currency translations		3,841	(2,621)	-	1,220
Treasury shares		(8,565)	382	-	(8,183)
Available-for-sale financial assets reserve		(36,326)	-	31,239	(5,087)
Voluntary reserve		(13,200)	-	-	(13,200)
Provision for advanced depreciation		(4,722)	-	-	(4,722)
Others		260	488	-	748
	₩	(122,372)	(2,177)	31,239	(93,310)

(j) The income taxes payable and income taxes refund before offsetting as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		June 30 2011	December 31 2010
Income taxes payable	₩	106,204	291,736
Income taxes refund		(2,066)	(100,921)
	₩	104,138	190,815

25. Earnings per Share

Basic and diluted earnings per share for the three- and six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won, except share information		2011 Three-month	2011 Six-month	2010 Three-month	2010 Six-month
Profit for the period	₩	178,976	378,188	409,710	589,063
Weighted-average number of ordinary shares outstanding		127,068,919	127,357,258	127,198,800	127,198,800
Basic and diluted earnings per share in won	₩	1,408	2,970	3,221	4,631

26. Transactions and Balances with Related Companies

(a) Details of parent and subsidiary relationships as of June 30, 2011 and December 31, 2010 were as follows:

			Percentage of ownership					
			June 30 2011			December 31 2010		
Subsidiary	Location	Next most senior parent	Parent	Sub-sidiary	Total	Parent	Sub-sidiary	Total
Korea Ginseng Corporation	Korea	The Company	100.00%	-	100.00%	100.00%	-	100.00%
Yungjin Pharm. Ind. Co., Ltd.	Korea	The Company	53.00%	-	53.00%	53.00%	-	53.00%
Tae-a Industry Co., Ltd. (*1)	Korea	The Company	100.00%	-	100.00%	100.00%	-	100.00%
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Turkey	The Company	99.99%	-	99.99%	99.99%	-	99.99%
Korea Tabacos do Brasil Ltda.	Brazil	The Company	99.90%	-	99.90%	99.90%	-	99.90%
KT&G Pars	Iran	The Company	99.99%	-	99.99%	99.99%	-	99.99%
KT&G Rus L.L.C.	Russia	The Company	100.00%	-	100.00%	100.00%	-	100.00%
KT&G Bio Corp.	Korea	The Company	100.00%	-	100.00%	100.00%	-	100.00%
KGC Life & Gin Co., Ltd.	Korea	The Company	100.00%	-	100.00%	100.00%	-	100.00%
Global Trading, Inc.	USA	The Company	100.00%	-	100.00%	100.00%	-	100.00%
Purpleland Development Co., Ltd.	Korea	The Company	100.00%	-	100.00%	100.00%	-	100.00%
Jilin Hanzheng Ginseng Co., Ltd. (*2)	China	The Company	100.00%	-	100.00%	-	-	-
Korea Ginseng HK, Ltd. (*3)	Hong Kong	Korea Ginseng Corporation	-	-	-	-	99.99%	99.99%
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%

(*1) Tae-a Industry Co., Ltd. increased paid-in capital by way of shareholder allocation and the Company's investments in subsidiaries increased by ₩1,500 million for the six-month period ended June 30, 2011.

(*2) The Company established Jilin Hanzheng Ginseng Co., Ltd. in 2011.

(*3) Korea Ginseng HK, Ltd. was liquidated in 2011.

26. Transactions and Balances with Related Companies, Continued

(b) Significant transactions which occurred in the normal course of business with related companies for the three- and six-month periods ended June 30, 2011 and 2010 are summarized as follows:

In millions of won			2011		2010	
Relationship	Related company		Three-month	Six-month	Three-month	Six-month
Revenue from sales and other income:						
Subsidiary	Korea Ginseng Corporation	₩	1,322	2,396	1,117	2,403
	Yungjin Pharm. Ind. Co., Ltd.		76	148	40	88
	Tae-a Industry Co., Ltd.		2	4	3	6
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.		2,305	3,781	1,643	2,640
	KT&G Pars		1,567	3,940	797	1,864
	KT&G Rus L.L.C.		8,030	12,499	419	462
	KGC Life & Gin Co., Ltd.		177	347	6	13
	Global Trading, Inc.		8,099	16,367	-	-
	Purpleland Development Co., Ltd.		-	7	-	-
		₩	21,578	39,489	4,025	7,476
Purchases and other expenses:						
Subsidiary	Korea Ginseng Corporation	₩	234	647	190	639
	Yungjin Pharm. Ind. Co., Ltd.		6	9	-	-
	Tae-a Industry Co., Ltd.		3,873	7,311	3,078	5,952
	KGC Life & Gin Co., Ltd.		9	9	-	-
		₩	4,122	7,976	3,268	6,591

The Company recognized dividends from Korea Ginseng Corporation amounting to ₩50,000 million and ₩30,000 million as finance income for the six-month periods ended June 30, 2011 and 2010, respectively.

(c) Account balances with related companies as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won				
Relationship	Related Company		June 30 2011	December 31 2010
Receivables:				
Subsidiary	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	₩	20,639	17,642
	KT&G Pars		25,543	22,114
	KT&G Rus L.L.C.		29,867	8,159
	Global Trading, Inc.		12,993	11,248
		₩	89,042	59,163
Payables:				
Subsidiary	Korea Ginseng Corporation	₩	2,429	2,289
	Tae-a Industry Co., Ltd.		1,642	-
		₩	4,071	2,289

26. Transactions and Balances with Related Companies, Continued

(d) Details of guarantees provided for related companies as of June 30, 2011 and December 31, 2010 were as follows:

In thousands of euro				June 30 2011		December 31 2010	
Relationship	Type of guarantee	Guarantee recipient		Limit	Exercise	Limit	Exercise
Subsidiary	Guarantee on foreign currency letter of credit opened	KT&G Rus L.L.C.	€	-	-	2,063	2,063

(e) Details of key management personnel compensation for the three- and six-month periods ended June 30, 2011 and 2010 are summarized as follows:

		2011		2010	
In millions of won		Three-month	Six-month	Three-month	Six-month
Short-term employee benefits	₩	3,293	6,973	3,458	5,415
Post-employment benefits		309	606	108	285
	₩	3,602	7,579	3,566	5,700

27. Risk Management

(a) Overview

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

- credit risk
- liquidity risk
- currency risk
- interest rate risk
- other market price 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 risk and the Company's management of capital including 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 department is to manage the financial risks arising from the Company's underlying operations. The treasury department monitors 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 department provides an internal report analyzing the nature and exposure level on financial risks to the Risk Management Committee of the Company. The Risk Management Committee prepares the overall strategy for financial risk management, and evaluates the effectiveness of the financial risk management strategy. In addition, the internal auditor consistently observes the compliance of the risk management policy and procedures, 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.

27. Risk Management, Continued

(c) Management of Financial Risks

Credit Risk
The Company has exposure to the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. 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 exposure before 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 risk as of June 30, 2011 and December 31, 2010 is as follows:

In millions of won		June 30 2011	December 31 2010
Available-for-sale financial assets	₩	284,411	314,937
Long-term deposits in MSA Escrow Fund		133,961	132,414
Trade and other receivables		679,330	612,422
Cash and cash equivalents		655,093	828,951

Export trade receivables to overseas clients, including Alokozay International Limited are ₩272,292 million, ₩235,636 million, and equal to 54.9% and 56.1% of the aggregate trade receivables, respectively, as of June 30, 2011 and December 31, 2010. The Company's trade receivables mentioned above were insured against non-payment up to USD 39,800 thousand and USD 38,525 thousand by export guarantee insurance with the Korea Export Insurance Corporation, respectively, as of June 30, 2011 and December 31, 2010. The Company has no significant concentration of customer credit risk since trade and other receivables, excluding the above export trade receivables, are widely dispersed amongst a large number of customers.

The Company has made deposits on cash, cash equivalents and long-term deposits in NACF and several financial institutions with high credit ratings, thus the credit risks from these financial institutions are very limited.

Liquidity Risk
The Company has exposure to the risk that an entity will encounter difficulty in meeting obligations 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 Company entered into an overdraft agreement with the NACF to manage the temporary liquidity risk.

27. Risk Management, Continued

(c) Management of Financial Risks, Continued

The maturity analysis with a residual contractual maturity of financial liabilities as of June 30, 2011 and December 31, 2010 is as follows:

In millions of won		Carrying amount	Contractual cash flow	Residual contractual maturity: Within 3 months	Between 3 months and 1 year	Between 1 and 5 years	Beyond 5 years
As of June 30, 2011:							
Derivative financial liabilities	₩	-	-	-	-	-	-
Non-derivative financial liabilities		193,808	194,872	100,533	82,351	9,988	2,000
	₩	193,808	194,872	100,533	82,351	9,988	2,000
As of December 31, 2010:							
Derivative financial liabilities	₩	-	-	-	-	-	-
Non-derivative financial liabilities		152,655	153,199	68,202	75,105	9,892	-
	₩	152,655	153,199	68,202	75,105	9,892	-

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.

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 option contracts to hedge foreign currency risk in case of need.

27. Risk Management, Continued

(c) Management of Financial Risks, Continued

The carrying amounts of monetary assets and liabilities denominated in a currency other than the functional currency as of June 30, 2011 and December 31, 2010 were as follows:

				June 30 2011		December 31 2010
In millions of won		USD	EUR	RUB	USD	EUR
Assets:						
Cash and cash equivalents	₩	31,237	2	-	6,228	1,227
Trade and other receivables		329,631	13,467	9,736	277,055	9,883
Long-term deposits in MSA Escrow Fund		133,961	-	-	132,414	-
	₩	494,829	13,469	9,736	415,697	11,110
Liabilities:						
Trade and other payables	₩	1,266	2,731	-	1,448	2,434

As of June 30, 2011 and December 31, 2010, the effects of a 10% strengthening or weakening of functional currency against foreign currencies other than functional currency on profit before tax were as follows:

			June 30 2011		December 31 2010
In millions of won		10% strengthening	10% weakening	10% strengthening	10% weakening
USD	₩	49,356	(49,356)	41,425	(41,425)
EUR		1,074	(1,074)	868	(868)
RUB		974	(974)	-	-
	₩	51,404	(51,404)	42,293	(42,293)

The above sensitivity analysis was applied to monetary assets and liabilities denominated in foreign currencies other than the functional currency at the end of the reporting period.

Interest Rate 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 market interest rates. The Company's management has monitored the level of interest rates regularly and has maintained the balance of borrowings at variable rates and fixed rates. As of June 30, 2011, 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.

Other Market Price 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 market prices. Other market price risk arises from available-for-sale equity instruments held for investments. The Company's management has monitored the mix of debt and 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.

27. Risk Management, Continued

(c) Management of Financial Risks, Continued

As of June 30, 2011 and December 31, 2010, the effects of a 5% fluctuation of the price index of stocks on other comprehensive income were as follows:

		June 30 2011		December 31 2010	
In millions of won		5% increase	5% decrease	5% increase	5% decrease
Other comprehensive income before tax	₩	9,466	(9,466)	13,338	(13,338)
Tax effect		(2,083)	2,083	(2,934)	2,934
Other comprehensive income, net of tax	₩	7,383	(7,383)	10,404	(10,404)

(d) Management of Capital Risk

The fundamental goal of capital management is the maximization of shareholders' value by means of the stable dividend policy and the retirement of treasury shares. The capital structure of the Company consists of equity and net debt deducting cash and cash equivalents and current financial instruments from borrowings. The Company applied the same capital risk management strategy that was applied in the previous period.

As of June 30, 2011 and December 31, 2010, the Company defines net debt and equity as follows:

In millions of won		June 30 2011	December 31 2010
Net debt:			
Debt (borrowings)	₩	9,349	8,618
Less:			
- Cash and cash equivalents		(655,093)	(828,951)
- Current available-for-sale financial assets		-	(1,000)
	₩	(645,744)	(821,333)
Equity	₩	4,214,487	4,337,686

27. Risk Management, Continued

(e) Fair Value of Financial Instruments

The carrying amount and the fair value of financial instruments as of June 30, 2011 and December 31, 2010 are summarized as follows:

In millions of won		June 30 2011 Carrying amount	June 30 2011 Fair value	December 31 2010 Carrying amount	December 31 2010 Fair value
Assets:					
Financial assets measured at fair value					
- Available-for-sale financial assets	₩	284,411	284,411	314,937	314,937
- Long-term deposits in MSA Escrow Fund		133,961	133,961	132,414	132,414
- Cash and cash equivalents		655,093	655,093	828,951	828,951
	₩	1,073,465	1,073,465	1,276,302	1,276,302
Financial assets measured at amortized cost					
- Trade and other receivables	₩	679,330	679,330	612,422	612,422
	₩	1,752,795	1,752,795	1,888,724	1,888,724
Liabilities:					
Financial liabilities measured at fair value	₩	-	-	-	-
Financial liabilities measured at amortized cost					
- Trade and other payables	₩	(184,459)	(184,459)	(144,037)	(144,037)
- Short-term borrowings		(9,349)	(9,349)	(8,618)	(8,618)
	₩	(193,808)	(193,808)	(152,655)	(152,655)
	₩	(193,808)	(193,808)	(152,655)	(152,655)

27. Risk Management, Continued

(e) Fair Value of Financial Instruments, Continued

The Fair Value Hierarchy
The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The level of fair value hierarchy is as follows:

- Level Ⅰ The quoted prices in active markets for identical assets or liabilities
- Level Ⅱ The inputs that are observable for the asset or liability, either directly or indirectly
- Level Ⅲ The inputs for the asset or liability that are not based on observable market data

The fair value measurements classified by fair value hierarchy as of June 30, 2011 and December 31, 2010 were as follows:

In millions of won		Level Ⅰ	Level Ⅱ	Level Ⅲ	Total
As of June 30, 2011:					
Financial assets					
- Available-for-sale financial assets	₩	234,723	32,129	17,559	284,411
- Long-term deposits in MSA Escrow Fund		133,961	-	-	133,961
- Cash and cash equivalents		655,093	-	-	655,093
	₩	1,023,777	32,129	17,559	1,073,465
As of December 31, 2010:					
Financial assets					
- Available-for-sale financial assets	₩	252,099	40,363	22,475	314,937
- Long-term deposits in MSA Escrow Fund		132,414	-	-	132,414
- Cash and cash equivalents		828,951	-	-	828,951
	₩	1,213,464	40,363	22,475	1,276,302

28. Contingent Liabilities and Financial Commitments

(a) The Company deposited some proportion of sales in accordance with the Tobacco Master Settlement Agreement ("MSA") under the Escrow Statute of the United States government, related to the export of tobacco to the United States. 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 that the fund was established. 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 June 30, 2011, tobacco lawsuits claiming damages of ₩584 million were filed against the Company and the Korean government. The plaintiffs have asserted that the Company and the Korean government did not perform their obligations to notify smokers of the potential health hazards of smoking. Additionally, as of June 30, 2011, the Company is involved in four lawsuits as a defendant for alleged damages totalling ₩3,714 million. The amount of the liability the Company may ultimately be liable for with respect to the litigation cannot be reasonably estimated as of June 30, 2011.

(c) As of June 30, 2011, the Company has entered into letter of credit agreements with Korea Exchange Bank and other banks with limits in aggregate of USD 48,000 thousand.

(d) As of June 30, 2011, the Company's trade receivables from the export of cigarettes were insured against non-payment up to USD 39,800 thousand by an export guarantee insurance with the Korea Export Insurance Corporation.

(e) As of June 30, 2011, the Company has been provided with a foreign currency payment guarantee for local dealers in Russia and other countries up to USD 70,000 thousand by Korea Exchange Bank and others.

(f) As of June 30, 2011, the Company and 28 other companies, which form the Samsung Corporation – National Pension Service Joint Consortium, were guaranteed ₩240,000 million by Seoul Guarantee Insurance Co., Ltd. related to the Yongsan International Commercial Development Project.

(g) The Company resolved to acquire the cosmetic segment of Somang Cosmetics Co., Ltd. at the Board of Directors meeting held on June 24, 2011 and entered into a contract with Somang Cosmetics Co., Ltd. According to the contract, Somang Cosmetics Co., Ltd. shall spin off the non-cosmetic segment into a separate non-cosmetic company and the Company shall acquire 60 percent of common shares issued by the surviving cosmetic company.

29. Non-current Assets Held for Sale

In 2011, the Company entered into a contract to sell the land, buildings and others in Cheongju plant to Cheongju City for the purpose of business rationalization. Also, the Company entered into a contract to sell the land, buildings and others of Jeonbuk headquarters to Inwoo AD Co., Ltd. and other in 2011.

The Company recognized non-current assets held for sale at the lower of its carrying amount and fair value less costs to sell. Non-current assets held for sale as of June 30, 2011 and December 31, 2010 was as follows:

In millions of won		June 30 2011	December 31 2010
Assets in Cheongju plant	₩	5,759	-
Assets of Jeonbuk headquarters		3,196	-
	₩	8,955	-

June 30, 2011 and 2010

30. Cash Flows from Operating Activities

Details of cash generated from operations for the six-month periods ended June 30, 2011 and 2010 were as follows:

In millions of won		2011	2010
Profit for the periods	₩	378,188	589,063
Adjustments for:			
- Income tax expense		105,170	177,464
- Finance costs		4,342	100
- Finance income		(71,246)	(284,604)
- Depreciation		55,697	59,622
- Amortization		20	35
- Retirement benefits		12,827	10,498
- Termination benefits		24	45,526
- Foreign currency translations loss		17,980	858
- Loss on the write-down of inventories		29	125
- Impairment loss on trade and other receivables		53	13
- Loss on sale of property, plant and equipment		483	438
- Loss on sale of intangible assets		174	158
- Other expense		1,912	2,266
- Foreign currency translations gain		(251)	(16,346)
- Gain on sale of property, plant and equipment		(6,625)	(62,596)
- Gain on sale of intangible assets		(605)	(1)
	₩	498,172	522,619
Changes in working capital:			
- Trade and other receivables		(63,173)	(4,435)
- Advance payments		(33,658)	(17,701)
- Prepaid expenses		837	(2,648)
- Prepaid tobacco excise and other taxes		3,709	(92,538)
- Inventories		50,073	25,137
- Trade and other payables		48,825	(5,819)
- Advance receipts		(1,594)	690
- Tobacco excise and other taxes payable		43,911	29,988
- Payment of retirement benefits		(4,034)	(8,191)
Cash generated from operations	₩	543,068	447,102

31. Date of Authorization for Issue

The separate interim financial statements were authorized for issue on July 20, 2011, at the Board of Directors meeting.

32. Event after the Reporting Period

At the Board of Directors meeting held on July 14, 2011, the Company resolved to acquire all of the shares of Renzoluc Pte., Ltd., based in Singapore, which has control over an Indonesian tobacco manufacturing company, PT Trisakti Purworsari Makmur.