KT&G CORPORATION AND SUBSIDIARIES

Consolidated Interim Financial Statements

September 30, 2016 and 2015

(Unaudited)

(With Independent Auditors' Review Report Thereon)

Contents

KPMG SAMJONG

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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 consolidated interim financial statements of KT&G Corporation (the "Parent Company") and its subsidiaries (collectively the "Group"), expressed in Korean won, which comprise the consolidated interim statement of financial position as of September 30, 2016, and the consolidated interim statements of comprehensive income for the three- and nine-month periods ended September 30, 2016 and 2015 and the consolidated interim statements of changes in equity and cash flows for the nine-month periods ended September 30, 2016 and 2015 and notes to the consolidated interim financial statements.

Management's responsibility

Management is responsible for the preparation and fair presentation of these consolidated interim financial statements in accordance with Korean International Financial Reporting Standards ("K-IFRS") 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 consolidated interim financial statements based on our review.

We conducted our review in accordance with the 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 review, nothing has come to our attention that causes us to believe that the accompanying consolidated interim financial statements referred to above are not prepared, in all material respects, in accordance with K-IFRS No.1034.

The accompanying consolidated interim financial statements as of and for the three- and nine-month periods ended September 30, 2016 have been translated into United States dollars solely for the convenience of the reader and such translation does not comply with K-IFRS. We have reviewed the translation and nothing came to our attention that cause us to believe that the consolidated interim financial statements expressed in Korean won have not been translated into dollars on the basis set forth in note 4 to the consolidated interim financial statements.

KPMG Samjong Accounting Corp., a corporation established under
Korean law, is a member firm of KPMG International, a Swiss corporative.

Other matters

The procedures and practices utilized in the Republic of Korea to review such consolidated interim financial statements may differ from those generally accepted and applied in other countries.

The consolidated statement of financial position of the Group as of December 31, 2015, and the related consolidated 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 in accordance with Korean Standards on Auditing and our report thereon, dated February 25, 2016, expressed an unqualified opinion. The accompanying consolidated statement of financial position of the Group as of December 31, 2015 presented for comparative purposes, is not different from that audited by us in all material respects.

KPMG Samjong Accounting Corp.

KPMG Samjong Accounting Corp.
Seoul, Korea
November 14, 2016

This report is effective as of November 14, 2016, 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 consolidated interim financial statements and notes thereto. Accordingly, the readers of the review report should understand that the above review report has not been updated to reflect the impact of such subsequent events or circumstances, if any.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Financial Position
(Unaudited)

As of September 30, 2016 and December 31, 2015

In millions of won and thousands of U.S. dollars	*Note*	September 30 2016 Korean won	September 30 2016 U.S. dollars (note 4)	December 31 2015 Korean won
Assets				
Property, plant and equipment	*6,16*	₩ 1,665,708	$ 1,519,391	₩ 1,789,779
Intangible assets	*7*	107,146	97,734	105,428
Investment property	*8,16*	261,317	238,363	164,489
Investments in associates	*5,9*	38,410	35,036	51,521
Available-for-sale financial assets	*10,31*	381,665	348,139	364,681
Other financial assets	*14,16,31*	11	10	12
Long-term deposits in MSA Escrow Fund	*11,31,33*	444,696	405,634	403,966
Long-term advance payments	*33*	133,336	121,624	107,723
Long-term prepaid expenses		6,488	5,917	7,128
Long-term trade and other receivables	*12,31*	73,939	67,444	75,071
Deferred income tax assets		38,377	35,006	32,696
Total non-current assets		3,151,093	2,874,298	3,102,494
Inventories	*13*	1,942,582	1,771,943	2,119,114
Current available-for-sale financial assets	*10,31*	1,596	1,456	-
Current other financial assets	*14,16,31,32*	1,113,580	1,015,762	1,136,906
Prepaid tobacco excise and other taxes		439,493	400,888	447,771
Trade and other receivables	*12,31*	1,386,542	1,264,747	1,217,938
Advance payments	*33*	93,303	85,107	75,710
Prepaid expenses		21,612	19,713	20,519
Cash and cash equivalents	*14,31,32*	668,249	609,550	546,213
Total current assets		5,666,957	5,169,166	5,564,171
Non-current assets held for sale	*5,15*	26,315	24,004	6,692
Total assets		₩ 8,844,365	$ 8,067,468	₩ 8,673,357

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Financial Position, Continued
(Unaudited)

As of September 30, 2016 and December 31, 2015

In millions of won and thousands of U.S. dollars	*Note*	September 30 2016 Korean won	September 30 2016 U.S. dollars (note 4)	December 31 2015 Korean won
Equity				
Ordinary shares	*1,17*	₩ 954,959	$ 871,075	₩ 954,959
Other capital surplus	*17*	(2,147)	(1,959)	(9,928)
Treasury shares	*18*	(331,772)	(302,629)	(337,062)
Gain on reissuance of treasury shares	*18*	505,191	460,815	494,648
Reserve	*19*	4,274,082	3,898,642	3,704,315
Retained earnings	*20*	1,225,404	1,117,762	1,401,975
Equity attributable to owners of the parent		6,625,717	6,043,706	6,208,907
Non-controlling interests		77,531	70,723	66,592
Total equity		6,703,248	6,114,429	6,275,499
Liabilities				
Long-term borrowings	*16,22,31,32*	113,952	103,942	102,242
Long-term trade and other payables	*16,21,31*	11,287	10,295	13,647
Long-term advance receipts		11,017	10,049	10,390
Net defined benefit liability	*23*	150,621	137,391	120,648
Provision		2,833	2,584	2,765
Deferred income tax liabilities		296,499	270,454	276,472
Total non-current liabilities		586,209	534,715	526,164
Short-term borrowings	*16,22,31,32*	75,010	68,421	206,373
Current portion of long-term borrowings	*16,22,31,32*	9,838	8,974	27,659
Trade and other payables	*16,21,31*	652,607	595,282	606,355
Advance receipts	*24*	7,372	6,724	28,650
Income tax payable		127,647	116,434	224,836
Tobacco excise and other taxes payable		682,434	622,489	777,821
Total current liabilities		1,554,908	1,418,324	1,871,694
Total liabilities		2,141,117	1,953,039	2,397,858
Total equity and liabilities		₩ 8,844,365	$ 8,067,468	₩ 8,673,357

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Comprehensive Income
(Unaudited)

For the nine-month periods ended September 30, 2016 and 2015

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*	2016 Korean won	2016 U.S. dollars (note 4)	2015 Korean won
Sales	*5,24,33*	₩ 3,399,634	$ 3,101,007	₩ 3,303,164
Cost of sales	*24,25*	(1,341,085)	(1,223,283)	(1,336,742)
Gross profit		2,058,549	1,877,724	1,966,422
Selling, general and administrative expenses	*25*	(893,397)	(814,920)	(864,369)
Operating profit	*5*	1,165,152	1,062,804	1,102,053
Other income	*26*	53,236	48,560	124,889
Other expenses	*26*	(130,268)	(118,827)	(77,798)
Net finance income	*27,31*	37,754	34,438	37,852
Share of gain of associates	*9*	1,982	1,808	7,181
Share of loss of associates	*9*	(123)	(112)	-
Profit before income tax		1,127,733	1,028,671	1,194,177
Income tax expense	*28*	(307,521)	(280,507)	(324,129)
Profit for the period		₩ 820,212	$ 748,164	₩ 870,048
Other comprehensive income (loss):				
Items that will never be reclassified to profit or loss				
Remeasurements of net defined benefit liability, net of tax		₩ (150)	$ (137)	₩ (152)
Items that are or may be reclassified subsequently to profit or loss				
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		2,713	2,475	(8,712)
Exchange differences on translating foreign operations, net of tax		(595)	(543)	(7,245)
Other comprehensive income (loss) for the period, net of tax		1,968	1,795	(16,109)
Total comprehensive income for the period		₩ 822,180	$ 749,959	₩ 853,939
Profit attributable to:				
Owners of the Parent Company		₩ 819,461	$ 747,478	₩ 872,824
Non-controlling interests		751	686	(2,776)
		₩ 820,212	$ 748,164	₩ 870,048
Total comprehensive income attributable to:				
Owners of the Parent Company		₩ 821,480	$ 749,320	₩ 857,503
Non-controlling interests		700	639	(3,564)
		₩ 822,180	$ 749,959	₩ 853,939
Earnings per share in won and U.S. dollars:				
Basic and diluted	*29*	₩ 6,497	$ 5.93	₩ 6,929

See accompanying notes to the consolidated interim financial statements

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Comprehensive Income, Continued
(Unaudited)

For the three-month periods ended September 30, 2016 and 2015

In millions of won and thousands of U.S. dollars, except earnings per share	*Note*	2016 Korean won	2016 U.S. dollars (note 4)	2015 Korean won
Sales	*5,24,33*	₩ 1,220,195	$ 1,113,012	₩ 1,134,351
Cost of sales	*24,25*	(477,234)	(435,313)	(476,626)
Gross profit		742,961	677,699	657,725
Selling, general and administrative expenses	*25*	(316,628)	(288,815)	(287,180)
Operating profit	*5*	426,333	388,884	370,545
Other income	*26*	8,266	7,540	64,084
Other expenses	*26*	(91,581)	(83,538)	(25,684)
Net finance income	*27,31*	8,539	7,789	7,066
Share of gain of associates	*9*	576	526	4,391
Share of loss of associates	*9*	(10)	(9)	-
Profit before income tax		352,123	321,192	420,402
Income tax expense	*28*	(102,219)	$ (93,240)	₩ (119,838)
Profit for the period		₩ 249,904	$ 227,952	₩ 300,564
Other comprehensive income (loss):				
Items that will never be reclassified to profit or loss				
Remeasurements of net defined benefit liability, net of tax		₩ 53	$ 48	₩ 31
Items that are or may be reclassified subsequently to profit or loss				
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		8,277	7,550	(1,493)
Exchange differences on translating foreign operations, net of tax		(11,694)	(10,666)	(6,416)
Other comprehensive loss for the period, net of tax		(3,364)	(3,068)	(7,878)
Total comprehensive income for the period		₩ 246,540	$ 224,884	₩ 292,686
Profit attributable to:				
Owners of the Parent Company		₩ 250,127	$ 228,156	₩ 302,699
Non-controlling interests		(223)	(204)	(2,135)
		₩ 249,904	$ 227,952	₩ 300,564
Total comprehensive income attributable to:				
Owners of the Parent Company		₩ 247,180	$ 225,468	₩ 295,117
Non-controlling interests		(640)	(584)	(2,431)
		₩ 246,540	$ 224,884	₩ 292,686
Earnings per share in won and U.S. dollars:				
Basic and diluted	*29*	₩ 1,983	$ 1.81	₩ 2,403

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES

Consolidated Interim Statements of Changes in Equity

(Unaudited)

For the nine-month period ended September 30, 2016

In millions of won	Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Owners of the parent	Non-controlling interests	Total equity
Balance at January 1, 2016	₩ 954,959	(9,928)	(337,062)	494,648	3,704,315	1,401,975	6,208,907	66,592	6,275,499
Total comprehensive income for the period:									
Profit for the period	-	-	-	-	-	819,461	819,461	751	820,212
Other comprehensive income (loss):									
Remeasurements of net defined benefit liability, net of tax	-	-	-	-	-	(146)	(146)	(4)	(150)
Unrealized net changes in fair value of available-for-sale financial assets, net of tax	-	-	-	-	2,713	-	2,713	-	2,713
Exchange differences on translating foreign operations, net of tax	-	-	-	-	(548)	-	(548)	(47)	(595)
Total other comprehensive income (loss)	-	-	-	-	2,165	(146)	2,019	(51)	1,968
Total comprehensive income for the period	-	-	-	-	2,165	819,315	821,480	700	822,180
Transactions with owners, recorded directly in equity:									
Dividends	-	-	-	-	-	(428,284)	(428,284)	-	(428,284)
In-kind donation of treasury shares	-	-	5,290	10,543	-	-	15,833	-	15,833
Transfer from reserve for research and human resource development	-	-	-	-	(10,000)	10,000	-	-	-
Transfer to unconditional reserve	-	-	-	-	577,602	(577,602)	-	-	-
Conversion of redeemable convertible preferred shares of subsidiaries	-	7,781	-	-	-	-	7,781	10,220	18,001
Others	-	-	-	-	-	-	-	19	19
Total transactions with owners	-	7,781	5,290	10,543	567,602	(995,886)	(404,670)	10,239	(394,431)
Balance at September 30, 2016	₩ 954,959	(2,147)	(331,772)	505,191	4,274,082	1,225,404	6,625,717	77,531	6,703,248

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Changes in Equity, Continued
(Unaudited)

For the nine-month period ended September 30, 2016

In thousands of U.S. dollars		Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Owners of the parent	Non-controlling interests	Total equity
Balance at January 1, 2016	$	871,075	(9,056)	(307,454)	451,198	3,378,924	1,278,824	5,663,511	60,743	5,724,254
Total comprehensive income for the period:										
Profit for the period		-	-	-	-	-	747,478	747,478	686	748,164
Other comprehensive income (loss):										
Remeasurements of net defined benefit liability, net of tax		-	-	-	-	-	(133)	(133)	(4)	(137)
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		-	-	-	-	2,475	-	2,475	-	2,475
Exchange differences on translating foreign operations, net of tax		-	-	-	-	(500)	-	(500)	(43)	(543)
Total other comprehensive income (loss)		-	-	-	-	1,975	(133)	1,842	(47)	1,795
Total comprehensive income for the period		-	-	-	-	1,975	747,345	749,320	639	749,959
Transactions with owners, recorded directly in equity:										
Dividends		-	-	-	-	-	(390,664)	(390,664)	-	(390,664)
In-kind donation of treasury shares		-	-	4,825	9,617	-	-	14,442	-	14,442
Transfer from reserve for research and human resource development		-	-	-	-	(9,122)	9,122	-	-	-
Transfer to unconditional reserve		-	-	-	-	526,865	(526,865)	-	-	-
Conversion of redeemable convertible preferred shares of subsidiaries		-	7,097	-	-	-	-	7,097	9,322	16,419
Others		-	-	-	-	-	-	-	19	19
Total transactions with owners		-	7,097	4,825	9,617	517,743	(908,407)	(369,125)	9,341	(359,784)
Balance at September 30, 2016	$	871,075	(1,959)	(302,629)	460,815	3,898,642	1,117,762	6,043,706	70,723	6,114,429

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Changes in Equity, Continued
(Unaudited)

For the nine-month period ended September 30, 2015

In millions of won		Ordinary shares	Other capital surplus	Treasury shares	Gain on reissuance of treasury shares	Reserve	Retained earnings	Owners of the parent	Non-controlling interests	Total equity
Balance at January 1, 2015	₩	954,959	(4,573)	(339,059)	492,032	3,426,367	1,100,876	5,630,602	77,478	5,708,080
Total comprehensive income for the period:										
Profit (loss) for the period		-	-	-	-	-	872,824	872,824	(2,776)	870,048
Other comprehensive loss:										
Remeasurements of net defined benefit liability, net of tax		-	-	-	-	-	(131)	(131)	(21)	(152)
Unrealized net changes in fair value of available-for-sale financial assets, net of tax		-	-	-	-	(8,712)	-	(8,712)	-	(8,712)
Exchange differences on translating foreign operations, net of tax		-	-	-	-	(6,478)	-	(6,478)	(767)	(7,245)
Total other comprehensive loss		-	-	-	-	(15,190)	(131)	(15,321)	(788)	(16,109)
Total comprehensive income (loss) for the period		-	-	-	-	(15,190)	872,693	857,503	(3,564)	853,939
Transactions with owners, recorded directly in equity:										
Dividends		-	-	-	-	-	(428,056)	(428,056)	-	(428,056)
In-kind donation of treasury shares		-	-	1,997	2,616	-	-	4,613	-	4,613
Transfer from reserve for research and human resource development		-	-	-	-	(12,522)	12,522	-	-	-
Transfer to unconditional reserve		-	-	-	-	320,926	(320,926)	-	-	-
Extinguishment of equity conversion option		-	(5,483)	-	-	-	-	(5,483)	(5,390)	(10,873)
Paid-in capital increase of subsidiaries		-	128	-	-	-	-	128	117	245
Others		-	-	-	-	-	-	-	63	63
Total transactions with owners		-	(5,355)	1,997	2,616	308,404	(736,460)	(428,798)	(5,210)	(434,008)
Balance at September 30, 2015	₩	954,959	(9,928)	(337,062)	494,648	3,719,581	1,237,109	6,059,307	68,704	6,128,011

See accompanying notes to the consolidated interim financial statements.

KT&G CORPORATION AND SUBSIDIARIES
Consolidated Interim Statements of Cash Flows
(Unaudited)

For the nine-month periods ended September 30, 2016 and 2015

In millions of won and thousands of U.S. dollars	*Note*	2016 Korean won	2016 U.S. dollars (note 4)	2015 Korean won
Cash flows from operating activities				
Cash generated from operations	*34*	₩ 1,195,864	$ 1,090,818	₩ 1,442,903
Income tax paid		(388,845)	(354,687)	(324,692)
Net cash provided by operating activities		807,019	736,131	1,118,211
Cash flows from investing activities	*34*			
Interest received		29,320	26,745	23,389
Dividends received		13,798	12,586	10,659
Proceeds from sale of property, plant and equipment		7,648	6,976	7,111
Proceeds from sale of intangible assets		1,236	1,128	1,841
Proceeds from sale of non-current assets held for sale		7,945	7,247	4,260
Proceeds from sale of investments in associates		13,095	11,945	-
Collection of loans		11,530	10,517	8,187
Withdrawal of guarantee deposits		16,988	15,495	28,576
Settlement of derivatives, net		-	-	4
Acquisition of property, plant and equipment		(114,561)	(104,498)	(168,735)
Acquisition of intangible assets		(7,862)	(7,171)	(3,997)
Acquisition of investment property		-	-	(64)
Acquisition of available-for-sale financial assets		(15,000)	(13,682)	(28,200)
Increase in loans		(421)	(384)	(13)
Payments of guarantee deposits		(27,135)	(24,752)	(21,994)
Payments of long-term deposits in MSA Escrow Fund		(68,897)	(62,845)	(61,325)
Decrease (increase) in other financial assets, net		23,235	21,194	(395,584)
Net cash used in investing activities		(109,081)	(99,499)	(595,885)
Cash flows from financing activities	*34*			
Paid-in capital increase of subsidiary		-	-	245
Proceeds from borrowings		330,546	301,510	419,187
Increase in deposits received		1,552	1,415	1,541
Dividends paid		(428,284)	(390,663)	(428,056)
Payments of capital share issue cost		(128)	(117)	(249)
Interest paid		(3,337)	(3,044)	(5,359)
Repayment of borrowings		(472,649)	(431,131)	(443,196)
Decrease in deposits received		(2,451)	(2,235)	(3,943)
Net cash used in financing activities		(574,751)	(524,265)	(459,830)
Effect of exchange rate fluctuation on cash held		(1,151)	(1,050)	1,043
Net increase in cash and cash equivalents		122,036	111,317	63,539
Cash and cash equivalents at January 1		546,213	498,233	416,394
Cash and cash equivalents at September 30		₩ 668,249	$ 609,550	₩ 479,933

See accompanying notes to the consolidated interim financial statements.

1. Reporting Entity

(a) Description of the Controlling Company

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

As of September 30, 2016, the Parent Company has three manufacturing plants, including the Shintanjin plant, and 14 local headquarters and 123 branches for the sale of tobacco throughout the country. Also, the Parent Company has the Gimcheon plant for fabrication of leaf tobacco and the Cheonan printing plant for the manufacturing of packaging. The head office of the Parent Company is located in 71, Beotkkot-gil, Daedeok-gu, Daejeon.

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

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

The ownership of the Parent Company's issued ordinary shares as of September 30, 2016 is held as follows:

Shareholder	Number of shares	Percentage of ownership
National Pension Service	11,793,134	8.59%
Industrial Bank of Korea	9,510,485	6.93%
Employee Share Ownership Association	2,818,577	2.05%
Treasury shares	11,148,827	8.12%
Others	102,021,474	74.31%
	137,292,497	100.00%

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries

(i) List of consolidated subsidiaries

Next most senior parent	Subsidiary	Principal operation	Percentage of ownership	Reporting date	Location
KT&G Corporation	Korea Ginseng Corporation	Manufacturing and selling ginseng	100.00%	Sep. 30	Korea
	Yungjin Pharm. Ind. Co., Ltd.	Manufacturing and selling pharmaceuticals	53.00%	Sep. 30	Korea
	Tae-a Industry Co., Ltd.	Manufacturing tobacco materials	100.00%	Sep. 30	Korea
	KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.	Manufacturing and selling tobaccos	99.99%	Sep. 30	Turkey
	Korea Tabacos do Brasil Ltda.	Processing leaf tobaccos	99.99%	Sep. 30	Brazil
	KT&G Pars	Manufacturing and selling tobaccos	99.99%	Sep. 30	Iran
	KT&G Rus L.L.C.	Manufacturing and selling tobaccos	100.00%	Sep. 30	Russia
	KGC Life & Gin Co., Ltd.	Selling ginseng door-to-door	100.00%	Sep. 30	Korea
	Global Trading, Inc.	Selling tobaccos	100.00%	Sep. 30	USA
	Cosmocos Co., Ltd.	Manufacturing and selling cosmetics	98.49%	Sep. 30	Korea
	Renzoluc Pte., Ltd. (*)	Manufacturing and selling tobaccos	100.00%	Sep. 30	Singapore
	KT&G Life Sciences Corporation	Research and development medicine	31.19%	Sep. 30	Korea
	KGC Yebon Corporation	Manufacturing and selling medical herbs	100.00%	Sep. 30	Korea
	K-Q HongKong I, Limited(*)	Manufacturing and selling ginseng	100.00%	Sep. 30	Hongkong
	PT KT&G Indonesia	Manufacturing and selling tobaccos	99.99%	Sep. 30	Indonesia
	K&I HK Co., Ltd.	Selling cosmetics	100.00%	Sep. 30	Hongkong
	K&I China Co., Ltd.	Selling cosmetics	100.00%	Sep. 30	China
	SangSang Stay, Inc.	Hotel	100.00%	Sep. 30	Korea
	KT&G Global Rus L.L.C.	Selling tobaccos	100.00%	Sep. 30	Russia
Renzoluc Pte., Ltd.	PT Trisakti Purwosari Makmur	Manufacturing and selling tobaccos	60.17%	Sep. 30	Indonesia
	PT Mandiri Maha Mulia	Manufacturing and selling tobaccos	66.47%	Sep. 30	Indonesia
PT Trisakti Purwosari Makmur	PT Sentosa Ababi Purwosari	Manufacturing and selling tobaccos	99.24%	Sep. 30	Indonesia
	PT Purindo Ilufa	Manufacturing and selling tobaccos	100.00%	Sep. 30	Indonesia
Korea Ginseng Corporation	Cheong Kwan Jang Taiwan Corporation	Manufacturing and selling ginseng	100.00%	Sep. 30	Taiwan
	Korean Red Ginseng Corp., Inc.	Manufacturing and selling ginseng	100.00%	Sep. 30	USA
	Korea Ginseng (China) Corp.	Manufacturing and selling ginseng	100.00%	Sep. 30	China
	Korea Ginseng Corporation Japan	Manufacturing and selling ginseng	100.00%	Sep. 30	Japan
	PT CKJ INDONESIA	Manufacturing and selling ginseng	99.88%	Sep. 30	Indonesia
	Jilin Hanzheng Ginseng Co., Ltd.	Manufacturing and selling ginseng	100.00%	Sep. 30	China

(*) The Group's percentage of ownership, shown above, excludes preferred shares. As of September 30, 2016, the Group's percentage of ownership would be 68.91% and 50.00% if preferred shares are included.

1. Reporting Entity, Continued

(b) Consolidated Subsidiaries, Continued

For the nine-month period ended September 30, 2016, the Parent Company's ownership interest in Cosmocos Co., Ltd. (former, Somang Cosmetics Co., Ltd.) has increased to 98.49% from 97.73% as a result of the conversion of redeemable convertible preferred shares.

For the nine-month period ended September 30, 2016, the Parent Company's ownership interest in KT&G Life Sciences Corporation has decreased to 31.19% from 73.94% as a result of the conversion of its redeemable convertible preferred shares.

(ii) Financial information of subsidiaries

In millions of won

Subsidiary		Total assets	Total liabilities	Revenue	Net profit (loss)	Total comprehensive income (loss)
Korea Ginseng Corporation	₩	1,879,434	287,473	894,575	129,250	129,596
Yungjin Pharm. Ind. Co., Ltd.		198,660	93,728	141,534	4,516	4,508
Tae-a Industry Co., Ltd.		15,631	4,053	10,630	809	815
KT&G Tutun Mamulleri Sanayi ve Ticaret A.S.		45,547	33,793	9,964	2,977	1,877
Korea Tabacos do Brasil Ltda.		2,615	6	-	-	-
KT&G Pars		30,533	50,491	883	(2,016)	(2,016)
KT&G Rus L.L.C.		130,020	67,698	19,384	5,438	10,173
KGC Life & Gin Co., Ltd.		26,486	9,017	39,757	(1,658)	(1,659)
Global Trading, Inc.		45,883	28,517	101,426	(96)	(1,296)
Cosmocos Co., Ltd.		75,146	14,490	60,868	(2,037)	(2,048)
Renzoluc Pte., Ltd.		46,278	76,163	-	(1,003)	(801)
KT&G Life Sciences Corporation		16,197	450	120	(3,174)	(3,174)
KGC Yebon Corporation		54,331	7,056	5,970	268	213
K-Q HongKong I, Limited		38,240	-	-	(903)	(3,552)
PT KT&G Indonesia		15,787	36,701	12,974	(546)	(404)
K&I HK Co., Ltd.		694	208	1,493	343	313
K&I China Co., Ltd.		4,314	837	547	(985)	(1,305)
SangSang Stay, Inc.		14,368	1,524	5,217	(6,730)	(6,730)
KT&G Global Rus L.L.C.		1,449	-	-	(19)	(48)
PT Trisakti Purwosari Makmur, etc.		81,686	64,372	26,825	(1,762)	(1,820)
PT Mandiri Maha Mulia		19,621	14,354	8,911	1,584	1,513
Cheong Kwan Jang Taiwan Corporation		11,984	10,558	11,316	43	18
Korean Red Ginseng Corp., Inc.		10,619	6,638	12,115	673	404
Korea Ginseng (China) Corp.		35,634	20,433	14,778	(6,504)	(7,722)
Korea Ginseng Corporation Japan		5,185	3,688	8,834	435	549
PT CKJ INDONESIA		981	1,060	-	-	-
Jilin Hanzheng Ginseng Co., Ltd.		70,621	6,944	1,905	(5,041)	(9,890)

(c) Change in Consolidated Group

For the nine-month period ended September 30, 2016, the Parent Company established KT&G Global Rus L.L.C.

2. Basis of Preparation

(a) Statement of Compliance

The consolidated interim financial statements have been prepared in accordance with Korean International Financial Reporting Standards ("K-IFRS"). These consolidated interim financial statements were prepared in accordance with K-IFRS No. 1034 *Interim Financial Reporting* as part of the period covered by the Group's K-IFRS annual consolidated financial statements.

The consolidated interim financial statements were authorized for issue by the Board of Directors on October 27, 2016.

(b) Basis of Measurement

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

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

(c) Functional and Presentation Currency

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

(d) Use of Estimates and Judgments

The preparation of the consolidated interim 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.

In preparing these consolidated interim financial statements, the significant judgments made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the financial statements as of and for the year ended December 31, 2015.

3. Significant Accounting Policies

The significant accounting policies applied by the Group in preparation of its consolidated interim financial statements are included below. The accounting policies set out below have been applied consistently to all periods presented in these consolidated interim financial statements.

(a) Basis of Consolidation

(i) Non-controlling interests

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

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

(ii) Subsidiaries

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

(iii) Loss of control

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

(iv) Interests in equity-accounted investees

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

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

(v) Transactions eliminated on consolidation

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

3. Significant Accounting Policies, Continued

(b) Property, Plant and Equipment

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

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

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

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

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

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

(c) Borrowing Costs

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

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

3. Significant Accounting Policies, Continued

(d) Government Grants

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

(e) Intangible Assets except for Goodwill

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

The estimated useful lives were as follows:

	Useful lives (years)
Industrial property rights	5 ~ 20 or indefinite
Facility usage rights	indefinite
Other intangible assets	3 ~ 5 or indefinite

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

(f) Investment Property

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

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

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

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

3. Significant Accounting Policies, Continued

(g) Non-current Assets Held for Sale

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

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

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

(h) Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories comprises all costs of purchase, costs of 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 merchandise, finished goods, by-products, work-in-progress and tobacco leaf in raw materials, by the moving-average method for raw materials and supplies; and by 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 ₩266,683 million and ₩310,043 million, respectively, as of September 30, 2016 and December 31, 2015.

(i) Impairment of Non-financial Assets

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

3. Significant Accounting Policies, Continued

(i) Impairment of Non-financial Assets, Continued

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

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

(j) Non-derivative Financial Assets

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

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

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

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

(ii) Held-to-maturity investments

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

(iii) Loans and receivables

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

3. Significant Accounting Policies, Continued

(j) Non-derivative Financial Assets, Continued

(iv) Available-for-sale financial assets

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

(v) De-recognition of financial assets

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

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

(vi) Offsetting between financial assets and financial liabilities

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

(k) Derivative financial instruments

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

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

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

3. Significant Accounting Policies, Continued

(l) Impairment of Financial Assets

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

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

(i) Financial assets measured at amortized cost

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

(ii) Financial assets carried at cost

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

(iii) Available-for-sale financial assets

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

3. Significant Accounting Policies, Continued

(m) Cash and Cash Equivalents

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

(n) Non-derivative Financial Liabilities

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

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

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

(ii) Financial guarantee liabilities

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

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

(iii) Other financial liabilities

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

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

3. Significant Accounting Policies, Continued

(o) Employee Benefits

(i) Short-term employee benefits

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

(ii) Retirement benefits: defined contribution plans

When an employee has rendered service to the Group during a period, the Group 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 Group recognizes that excess as an asset (prepaid expense) to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(iii) Retirement benefits: defined benefit plans

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

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

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

(iv) Termination benefits

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

3. Significant Accounting Policies, Continued

(p) Provisions

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

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

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

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

(q) Equity Capital

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

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

(r) Revenue Recognition

The Group's revenue categories consist of goods sold, services and other income.

Revenue from sale of goods is measured at the fair value of the consideration received or receivable, net of tobacco excise and other taxes, trade discounts and volume rebates. Revenue from the sale of goods is recognized when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods, the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Tobacco excise and other taxes deducted from revenue for the nine-month periods ended September 30, 2016 and 2015 were ₩4,895,749 million and ₩3,828,667 million, respectively.

3. Significant Accounting Policies, Continued

(r) Revenue Recognition, Continued

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

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

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

(s) Finance Income and Finance Costs

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

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

(t) Income Taxes

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

(i) Current tax

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

3. Significant Accounting Policies, Continued

(t) Income Taxes, Continued

(ii) Deferred tax

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

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

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

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

(u) Foreign Currencies

(i) Foreign currency transactions

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

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

(ii) Foreign operations

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

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

3. Significant Accounting Policies, Continued

(u) Foreign Currencies, Continued

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

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

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

(v) Earnings per Share

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

4. Basis of Translating Financial Statements

The consolidated interim financial statements are expressed in Korean won and have been translated into U.S. dollars at the rate of ₩1,096.30 to $1, the basic exchange rate on September 30, 2016 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. Operating Segments

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

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

5. Operating Segments, Continued

(b) Segment information on sales and operating profit for the nine-month period ended September 30, 2016 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:								
Total segment sales	₩	2,200,303	941,299	107,327	341,657	3,590,586	(190,952)	3,399,634
Less: Inter-segment sales		112,505	37,181	6,875	34,390	190,951	(190,952)	-
External sales	₩	2,087,798	904,118	100,452	307,267	3,399,635	-	3,399,634
Segment profit:								
Operating profit	₩	946,005	163,833	25,554	26,328	1,161,720	3,432	1,165,152

(c) Segment information on sales and operating profit for the nine-month period ended September 30, 2015 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Sales:								
Total segment sales	₩	2,317,041	801,170	99,798	280,513	3,498,522	(195,358)	3,303,164
Less: Inter-segment sales		96,684	52,274	5,193	41,207	195,358	(195,358)	-
External sales	₩	2,220,357	748,896	94,605	239,306	3,303,164	-	3,303,164
Segment profit:								
Operating profit	₩	960,420	121,582	12,667	17,793	1,112,462	(10,409)	1,102,053

(d) Segment information on assets and liabilities as of September 30, 2016 was as follows:

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	3,923,444	1,780,448	228,999	282,264	6,215,155	(204,530)	6,010,625
Investments in associates		-	-	35,323	3,087	38,410	-	38,410
Non-current assets held for sale		-	5,150	21,165	-	26,315	-	26,315
		3,923,444	1,785,598	285,487	285,351	6,279,880	(204,530)	6,075,350
Unallocated assets								2,769,015
Total assets	₩							8,844,365
Liabilities:								
Segment liabilities	₩	1,358,539	214,858	-	84,001	1,657,398	(165,950)	1,491,448
Unallocated liabilities								649,669
Total liabilities	₩							2,141,117

5. Operating Segments, Continued

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

In millions of won		Tobacco	Ginseng	Real estate	Others	Segment total	Elimination	Consolidated
Assets:								
Segment assets	₩	3,990,313	1,831,157	149,522	365,152	6,336,144	(319,032)	6,017,112
Investments in associates		-	-	48,800	2,721	51,521	-	51,521
Non-current assets held for sale		1,542	5,150	-	-	6,692	-	6,692
		3,991,855	1,836,307	198,322	367,873	6,394,357	(319,032)	6,075,325
Unallocated assets								2,598,032
Total assets	₩							8,673,357
Liabilities:								
Segment liabilities	₩	1,443,132	161,563	-	84,536	1,689,231	(155,384)	1,533,847
Unallocated liabilities								864,011
Total liabilities	₩							2,397,858

(f) Revenues from major customers which amount to more than 10 percent of the details of the Group's consolidated total revenues for the nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016	2015
Alokozay International Limited	₩	373,394	335,234

6. Property, Plant and Equipment

(a) Details of property, plant and equipment as of September 30, 2016 and December 31, 2015 are summarized as follows:

				September 30 2016			December 31 2015
In millions of won		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	586,939	-	586,939	583,481	-	583,481
Buildings		967,374	(414,997)	552,377	963,700	(389,526)	574,174
Structures		71,729	(41,192)	30,537	72,949	(39,770)	33,179
Machinery		1,318,413	(984,800)	333,613	1,278,124	(933,159)	344,965
Vehicles		11,637	(9,189)	2,448	12,907	(10,572)	2,335
Tools		63,985	(55,099)	8,886	63,467	(52,664)	10,803
Furniture and fixtures		252,649	(203,686)	48,963	245,349	(195,912)	49,437
Others		1,798	-	1,798	1,508	-	1,508
Construction-in-progress		100,147	-	100,147	189,897	-	189,897
	₩	3,374,671	(1,708,963)	1,665,708	3,411,382	(1,621,603)	1,789,779

(b) Changes in property, plant and equipment for the nine-month period ended September 30, 2016 were as follows:

In millions of won		January 1 2016	Acquisition	Disposal	Depreciation	Transfer of construction -in-progress	Net exchange difference and others	September 30 2016
Land	₩	583,481	114	(1,923)	-	52,028	(46,761)	586,939
Buildings		574,174	5,267	(1,232)	(27,877)	80,136	(78,091)	552,377
Structures		33,179	304	(804)	(2,576)	594	(160)	30,537
Machinery		344,965	7,897	(236)	(54,975)	36,854	(892)	333,613
Vehicles		2,335	490	(253)	(645)	531	(10)	2,448
Tools		10,803	1,719	(13)	(3,585)	-	(38)	8,886
Furniture and fixtures		49,437	12,339	(529)	(18,133)	5,922	(73)	48,963
Others		1,508	-	-	-	290	-	1,798
Construction-in-progress		189,897	86,728	-	-	(176,355)	(123)	100,147
	₩	1,789,779	114,858	(4,990)	(107,791)	-	(126,148)	1,665,708

For the nine-month period ended September 30, 2016, the Group received ₩289 million of government grant related with acquisition of buildings and furniture and fixtures.

For the nine-month period ended September 30, 2016, land, buildings and structures with a carrying amount of ₩124,347 million were transferred to investment property and construction-in-progress with a carrying amount of ₩107 million were transferred to intangible assets.

6. Property, Plant and Equipment, Continued

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

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

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

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

7. Intangible Assets

(a) Details of intangible assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

		September 30 2016			December 31 2015		
In millions of won		Cost	Accumulated amortization and impairment	Carrying amount	Cost	Accumulated amortization and impairment	Carrying amount
Goodwill	₩	87,902	(72,841)	15,061	87,902	(72,841)	15,061
Industrial property rights		47,477	(32,038)	15,439	46,806	(32,015)	14,791
Facility usage rights		32,087	(1,709)	30,378	28,282	(2,731)	25,551
Other intangible assets		114,585	(72,302)	42,283	116,349	(70,150)	46,199
Intangible assets under development		6,347	(2,362)	3,985	6,180	(2,354)	3,826
	₩	288,398	(181,252)	107,146	285,519	(180,091)	105,428

7. Intangible Assets, Continued

(b) Changes in intangible assets for the nine-month period ended September 30, 2016 were as follows:

In millions of won		January 1 2016	Acquisition	Disposal	Transfer from property, plant and equipment, etc.	Amortization	Impairment	Net exchange difference and others	September 30 2016
Goodwill	₩	15,061	-	-	-	-	-	-	15,061
Industrial property rights		14,791	1,527	-	6	(885)	-	-	15,439
Facility usage rights		25,551	5,985	(1,194)	36	-	-	-	30,378
Other intangible assets		46,199	178	-	70	(3,582)	-	(582)	42,283
Intangible assets under development		3,826	172	-	(5)	-	(8)	-	3,985
	₩	105,428	7,862	(1,194)	107	(4,467)	(8)	(582)	107,146

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

In millions of won		January 1 2015	Acquisition	Disposal	Transfer of Intangible assets under development	Amortization	Impairment	Net exchange difference and others	December 31 2015
Goodwill	₩	32,161	-	-	-	-	(17,941)	841	15,061
Industrial property rights		17,000	1,030	(104)	82	(1,330)	(1,575)	(312)	14,791
Facility usage rights		23,550	4,042	(2,041)	-	-	-	-	25,551
Other intangible assets		79,086	221	-	-	(9,429)	(23,694)	15	46,199
Intangible assets under development		3,140	783	-	(82)	-	(14)	(1)	3,826
	₩	154,937	6,076	(2,145)	-	(10,759)	(43,224)	543	105,428

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

(d) Expenditures not capitalized for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

		2016		2015	
In millions of won		Three-month	Nine-month	Three-month	Nine-month
Cost of sales	₩	147	700	485	2,192
Selling, general and administrative expenses		7,839	22,463	8,327	24,141
	₩	7,986	23,163	8,812	26,333

8. Investment Property

(a) Details of investment property as of September 30, 2016 and December 31, 2015 are summarized as follows:

				September 30 2016			December 31 2015
In millions of won		Cost	Accumulated depreciation and impairment	Carrying amount	Cost	Accumulated depreciation and impairment	Carrying amount
Land	₩	74,784	-	74,784	49,123	-	49,123
Buildings		253,838	(67,305)	186,533	179,949	(64,583)	115,366
	₩	328,622	(67,305)	261,317	229,072	(64,583)	164,489

(b) Changes in investment property for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

				2016			2015
In millions of won		Land	Buildings	Total	Land	Buildings	Total
Beginning balance	₩	49,123	115,366	164,489	48,293	119,675	167,968
Acquisition		-	-	-	-	64	64
Depreciation		-	(6,354)	(6,354)	-	(6,275)	(6,275)
Transfer from property, plant and equipment		46,826	77,521	124,347	830	1,902	2,732
Transfer to non-current assets held for sale		(21,165)	-	(21,165)	-	-	-
Ending balance	₩	74,784	186,533	261,317	49,123	115,366	164,489

(c) The amounts recognized in profit or loss from investment property for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

			2016		2015
In millions of won		Three-month	Nine-month	Three-month	Nine-month
Rental income	₩	10,218	28,542	8,588	26,181
Direct operating expense		(2,572)	(6,411)	(1,653)	(4,958)
	₩	7,646	22,131	6,935	21,223

(d) The carrying amount and the fair value of investment property as of September 30, 2016 and December 31, 2015 were as follows:

			September 30 2016		December 31 2015
In millions of won		Fair value	Carrying amount	Fair value	Carrying amount
Land	₩	539,689	74,784	435,034	49,123
Buildings		232,807	186,533	177,756	115,366
	₩	772,496	261,317	612,790	164,489

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

9. Investments in Associates

(a) Investments in associates as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won, except percentage of ownership

Associate	Location	Principal operation	September 30 2016 Percentage of ownership	September 30 2016 Carrying amount	December 31 2015 Percentage of ownership	December 31 2015 Carrying amount
Lite Pharm Tech, Inc.	Korea	Manufacturing medical supplies	20.24%	₩ 3,087	20.24%	₩ 2,720
KVG REIT 1 Co., Ltd.	Korea	Renting of real estate	29.67%	6,300	29.67%	6,635
KOCREF REIT 17 Co., Ltd.	Korea	Renting of real estate	-	-	22.06%	13,208
JR REIT V Co., Ltd.	Korea	Renting of real estate	34.63%	5,584	34.63%	5,470
JR REIT VIII Co., Ltd.	Korea	Renting of real estate	21.74%	9,828	21.74%	9,693
LSK Global Pharma Services Co., Ltd.	Korea	Research and development medicine	23.15%	-	23.15%	-
JR REIT X Co., Ltd.	Korea	Renting of real estate	28.79%	8,878	28.79%	8,907
JR REIT XIII Co., Ltd.	Korea	Renting of real estate	27.03%	4,733	27.03%	4,888
				₩ 38,410		₩ 51,521

(b) Financial information of associates, which represents 100% of the entities' balances as of and for the nine-month period ended September 30, 2016 are summarized as follows:

In millions of won

Associate		Total assets	Total liabilities	Revenue	Total comprehensive income (loss)
Lite Pharm Tech, Inc.	₩	16,313	1,060	7,998	1,687
KVG REIT 1 Co., Ltd.		49,289	28,054	4,494	1,277
JR REIT V Co., Ltd.		31,306	15,181	1,937	999
JR REIT VIII Co., Ltd.		108,288	63,083	6,983	3,108
LSK Global Pharma Services Co., Ltd.		5,247	8,377	12,662	(1,639)
JR REIT X Co., Ltd.		86,722	55,886	3,245	597
JR REIT XIII Co., Ltd.		46,806	29,298	1,008	(179)

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

In millions of won

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

9. Investments in Associates, Continued

(d) Changes in investments in associates for the nine-month period ended September 30, 2016 were as follows:

In millions of won

Associate		January 1 2016	Disposal	Share of gain (loss)	Dividends	September 30 2016
Lite Pharm Tech, Inc.	₩	2,720	-	367	-	3,087
KVG REIT 1 Co., Ltd.		6,635	-	400	(735)	6,300
KOCREF REIT 17 Co., Ltd.		13,208	(13,095)	(113)	-	-
JR REIT V Co., Ltd.		5,470	-	458	(344)	5,584
JR REIT VIII Co., Ltd.		9,693	-	549	(414)	9,828
LSK Global Pharma Services Co., Ltd.		-	-	-	-	-
JR REIT X Co., Ltd.		8,907	-	208	(237)	8,878
JR REIT XIII Co., Ltd.		4,888	-	(10)	(145)	4,733
	₩	51,521	(13,095)	1,859	(1,875)	38,410

For the nine-month period ended September 30, 2016, the Group received ₩13,095 million of dividend related with liquidation of KOCREF REIT 17 Co., Ltd.

(e) Changes in investments in associates for the year ended December 31, 2015 were as follows:

In millions of won

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

(f) Reconciliation of the summarized financial information presented to the carrying amount of the Group's interest in associates as of September 30, 2016 are summarized as follows:

In millions of won, except percent of ownership

Associate	Percentage of ownership		Equity attributable to owners of the parent	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	20.24%	₩	15,253	3,087	-	3,087
KVG REIT 1 Co., Ltd.	29.67%		21,235	6,300	-	6,300
JR REIT V Co., Ltd.	34.63%		16,125	5,584	-	5,584
JR REIT VIII Co., Ltd.	21.74%		45,205	9,828	-	9,828
LSK Global Pharma Services Co., Ltd.	23.15%		(3,130)	(725)	725	-
JR REIT X Co., Ltd.	28.79%		30,836	8,878	-	8,878
JR REIT XIII Co., Ltd.	27.03%		17,508	4,733	-	4,733
		₩				38,410

9. Investments in Associates, Continued

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

In millions of won, except percent of ownership

Associate	Percentage of ownership		Equity attributable to owners of the parent	Share of net assets	Share of loss not recognized	Carrying amount
Lite Pharm Tech, Inc.	20.24%	₩	13,439	2,720	-	2,720
KVG REIT 1 Co., Ltd.	29.67%		22,363	6,635	-	6,635
KOCREF REIT 17 Co., Ltd.	22.06%		59,872	13,208	-	13,208
JR REIT V Co., Ltd.	34.63%		15,797	5,470	-	5,470
JR REIT VIII Co., Ltd.	21.74%		44,586	9,693	-	9,693
LSK Global Pharma Services Co., Ltd.	23.15%		(2,484)	(575)	575	-
JR REIT X Co., Ltd.	28.79%		30,939	8,907	-	8,907
JR REIT XIII Co., Ltd.	27.03%		18,081	4,888	-	4,888
		₩				51,521

10. Available-for-sale Financial Assets

(a) Changes in available-for-sale financial assets for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	364,681	326,833
Acquisitions		15,000	63,190
Net changes in fair value		3,580	3,881
Disposals and exercise of convertible right		-	(29,223)
Ending balance	₩	383,261	364,681
Statements of financial position:			
Current	₩	1,596	-
Non-current		381,665	364,681
	₩	383,261	364,681

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

10. Available-for-sale Financial Assets, Continued

(b) Available-for-sale financial assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016	December 31 2015
Available-for-sale debt instruments:			
Government and municipal bonds	₩	96	96
Corporate bonds		1,500	1,500
Total available-for-sale debt instruments		1,596	1,596
Available-for-sale equity instruments:			
Listed			
– YTN Co., Ltd.		24,972	24,428
– Oscotech, Inc.		5,053	3,696
– Shinhan Financial Group Co., Ltd.		160,935	158,530
– Rexahn Pharmaceuticals, Inc.		1,471	2,696
– U&I Corporation		22,081	22,564
		214,512	211,914
Unlisted		167,153	151,171
Total available-for-sale equity instruments		381,665	363,085
Total available-for-sale financial assets	₩	383,261	364,681

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

As of September 30, 2016 and December 31, 2015, ₩52,660 million and ₩37,659 million of available-for-sale financial assets, respectively, that do not have a market price in an active market and whose fair value cannot be reliably measured or is similar to their carrying amount are measured at cost.

11. Long-term Deposits in MSA Escrow Fund

Long-term deposits in MSA Escrow Fund as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016	December 31 2015
MMF	₩	260,925	43,309
Treasury note		183,771	360,657
	₩	444,696	403,966

As discussed in note 33 to the consolidated interim 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 nine-month periods ended September 30, 2016 and 2015 are ₩68,897 million and ₩61,325 million, respectively.

Interest income on long-term deposits in MSA Escrow Fund for the nine-month periods ended September 30, 2016 and 2015 are ₩3,554 million and ₩1,796 million, respectively.

12. Trade and Other Receivables

(a) Trade and other receivables as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016 Current	Non-current	December 31 2015 Current	Non-current
Loans to employees	₩	14,466	43,903	15,774	52,275
Loans		1,427	712	2,504	315
Other receivables		106,228	226	127,369	323
Guarantee deposits		38,046	29,098	34,730	22,158
Accrued income		3,515	-	5,943	-
Trade receivables		1,222,860	-	1,031,618	-
	₩	1,386,542	73,939	1,217,938	75,071

(b) Trade and other receivables as of September 30, 2016 and December 31, 2015 have been reported in the consolidated statements of financial position net of allowances as follows:

In millions of won		September 30 2016 Current	Non-current	December 31 2015 Current	Non-current
Gross trade and other receivables	₩	1,416,330	73,939	1,251,180	75,071
Allowance:					
Loans		(197)	-	(197)	-
Other receivables		(2,293)	-	(2,296)	-
Trade receivables		(27,298)	-	(30,749)	-
		(29,788)	-	(33,242)	-
Net trade and other receivables	₩	1,386,542	73,939	1,217,938	75,071

(c) Changes in the allowance account for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	33,242	39,659
Impairment loss		-	12
Reversal of impairment loss		(8)	(5,465)
Net exchange difference and others		(3,446)	(964)
Ending balance	₩	29,788	33,242

Impairment loss (reversal of impairment loss) on trade receivables is included as part of selling, general and administrative expenses and impairment loss (reversal of impairment loss) on other receivables are included as part of other expense (income) in the consolidated 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 September 30, 2016 and December 31, 2015 is as follows:

In millions of won		September 30 2016	December 31 2015
Within 1 month	₩	84,107	67,309
Between 1 and 2 months		41,932	64,851
Beyond 2 months		183,184	198,982
	₩	309,223	331,142

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 Group holds pledged assets and guarantees in respect of some of the past due debtor balances.

(e) Details of trade and other receivables that are measured at amortized cost as of September 30, 2016 and December 31, 2015 were as follows:

In millions of won, except percentage of interest rate	September 30 2016				December 31 2015			
	Effective interest rate		Current	Non-current	Effective interest rate		Current	Non-current
Loans to employees	1.83~5.68%	₩	14,466	43,903	1.89~5.68%	₩	15,774	52,275
Loans	1.93~2.71%		810	712	2.71%		1,863	315
Guarantee deposits	1.40~5.68%		36,710	27,664	1.52~5.68%		33,787	20,260
		₩	51,986	72,279		₩	51,424	72,850

13. Inventories

(a) Inventories as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016	December 31 2015
Merchandise, net of loss on the write-down of inventories	₩	3,538	7,677
Finished goods, net of loss on the write-down of inventories		661,381	610,309
Work-in-progress, net of loss on the write-down of inventories		430,267	608,280
Raw materials, net of loss on the write-down of inventories		750,922	770,561
Supplies		29,811	27,367
By-products		6,414	7,051
Buildings under construction		7,204	3,618
Sites for lotting-out construction		19,044	25,815
Goods-in-transit		34,001	58,436
	₩	1,942,582	2,119,114

13. Inventories, Continued

(b) The amount of inventories recognized as an expense for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Cost of sales:					
Write-down (reversal of write-down) of inventories	₩	(597)	(791)	152	(739)
Loss on retirement of inventories		1,858	6,432	1,306	3,270
Other expense:					
Loss on retirement of inventories		68	1,045	479	2,624
	₩	1,329	6,686	1,937	5,155

14. Cash and Cash Equivalents and Other Financial Assets

(a) Cash and cash equivalents as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016	December 31 2015
Cash on hand	₩	1,921	2,788
Demand deposits		236,112	161,627
Short-term investment assets		430,216	381,798
	₩	668,249	546,213

(b) Other financial assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016 Current	September 30 2016 Non-current	December 31 2015 Current	December 31 2015 Non-current
Time deposits	₩	115,346	-	120,141	-
Certificates of deposit		31,316	-	31,406	-
Money trust		966,918	-	985,359	-
Security deposits for checking accounts		-	11	-	12
	₩	1,113,580	11	1,136,906	12

(c) Financial assets restricted in use as of September 30, 2016 and December 31, 2015 were as follows:

In millions of won			September 30 2016	December 31 2015
Other financial assets	Security deposits for checking accounts	₩	11	12
Current other financial assets	Pledge for borrowings		1,316	1,406
		₩	1,327	1,418

15. Non-current Assets Held for Sale

Changes in non-current assets held for sale for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	6,692	426
Transfer from property, plant and equipment		-	6,692
Transfer from investment property		21,165	-
Disposal		(1,542)	(426)
Ending balance	₩	26,315	6,692

16. Pledged Assets

(a) The followings assets were pledged as collateral for borrowings as of September 30, 2016.

In millions of won

Asset		Carrying amount	Type		Received amount	Collateralized amount	Holder
Investment property	₩	66,361	Leasehold deposits received	₩	8,975	9,225	Metlife Insurance Korea Co., Ltd., etc.
Property, plant and equipment, etc.		57,788	Short-term borrowings		13,000	49,243	KEB Hana Bank, etc.
			Long-term borrowings		13,131	15,757	KEB Hana Bank, etc.
Property, plant and equipment		32,576	Investment subsidy		-	660	Chungju-si
			Short- and long-term borrowings		4,730	14,500	The Korea Development Bank
Other financial assets		1,316	ACH pledged		-	1,316	Bank of Oklahoma
	₩	158,041		₩	39,836	90,701	

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

In millions of won

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

17. Share Capital and Other Capital Surplus

(a) Details of share capital as of September 30, 2016 and December 31, 2015 were as follows:

In won, except number of shares		September 30 2016	December 31 2015
Number of ordinary shares:			
Authorized		800,000,000	800,000,000
Issued		137,292,497	137,292,497
Outstanding		126,143,670	125,965,892
Par value	₩	5,000	5,000

The Parent Company has, thus far, reacquired and retired 53,699,400 shares of treasury share. Accordingly, as of September 30, 2016, the Parent Company's ordinary share differs from the aggregate par value of issued shares by ₩268,497 million.

(b) Changes in the number of shares for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

	2016			2015		
Number of share	Ordinary shares	Treasury shares	Total	Ordinary shares	Treasury shares	Total
Beginning balance	137,292,497	(11,326,605)	125,965,892	137,292,497	(11,393,697)	125,898,800
In-kind donation of treasury shares	-	177,778	177,778	-	67,092	67,092
Ending balance	137,292,497	(11,148,827)	126,143,670	137,292,497	(11,326,605)	125,965,892

(c) Changes in other capital surplus for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	(9,928)	(4,573)
Extinguishment of equity conversion options		-	(5,483)
Paid-in capital increase of subsidiary		-	128
Conversion of redeemable convertible preferred shares of subsidiaries		7,781	-
Ending balance	₩	(2,147)	(9,928)

For the nine-month period ended September 30, 2016, changes in the ownership interest in Cosmocos Co., Ltd. and KT&G Life Sciences Corporation resulting from the conversion of redeemable convertible preferred shares were recognized in other capital surplus.

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

For the year ended December 31, 2015, changes in the ownership interest in Cosmocos Co., Ltd. resulting from its paid-in capital increase were recognized in other capital surplus.

18. Treasury Shares and Gain on Reissuance of Treasury Shares

(a) Changes in the treasury shares for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

	2016		2015	
In millions of won, except number of shares	Number of shares	Carrying amount	Number of shares	Carrying amount
Beginning balance	11,326,605	₩ 337,062	11,393,697	₩ 339,059
In-kind donation of treasury shares	(177,778)	(5,290)	(67,092)	(1,997)
Ending balance	11,148,827	₩ 331,772	11,326,605	₩ 337,062

(b) Changes in gain on reissuance of treasury shares for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	494,648	492,032
In-kind donation of treasury shares, net of tax		10,543	2,616
Ending balance	₩	505,191	494,648

19. Reserves

(a) Details of reserves as of September 30, 2016 and December 31, 2015 were as follows:

In millions of won		September 30 2016	December 31 2015
Available-for-sale financial assets - net change in fair value	₩	(27,665)	(30,378)
Foreign operations - foreign currency translation differences		(95,658)	(95,110)
Legal reserve		603,145	603,145
Voluntary reserve		3,794,260	3,226,658
	₩	4,274,082	3,704,315

(b) Available-for-sale financial assets - net change in fair value as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016	December 31 2015
Available-for-sale financial assets - net change in fair value before tax	₩	(36,497)	(40,077)
Tax effect		8,832	9,699
	₩	(27,665)	(30,378)

(c) Legal Reserve

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

19. Reserves, Continued

(d) Details of voluntary reserve as of September 30, 2016 and December 31, 2015 were as follows:

In millions of won		September 30 2016	December 31 2015
Reserve for business rationalization	₩	12,851	12,851
Reserve for research and human resource development		20,000	30,000
Reserve for business expansion		698,881	698,881
Unconditional reserve		3,062,528	2,484,926
	₩	3,794,260	3,226,658

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

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

Reserve for research and human resource development
According to *the Restriction of Special Taxation Act*, certain taxable deductions are required to be transferred from retained earnings to reserve for research and human resource development. This reserve may be used for each purpose and their remaining amounts could be reclassified as a voluntary reserve.

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

20. Retained Earnings

Changes in retained earnings for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	1,401,975	1,100,876
Dividends		(428,284)	(428,056)
Transfer from reserve for research and human resource development		10,000	12,522
Transfer to unconditional reserve		(577,602)	(320,926)
Profit for the periods		820,212	1,032,220
- Less: non-controlling interests		(751)	3,497
Remeasurements of net defined benefit liability, net of tax		(150)	37
- Less: non-controlling interests		4	1,805
Ending balance	₩	1,225,404	1,401,975

21. Trade and Other Payables

Trade and other payables as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won		September 30 2016 Current	Non-current	December 31 2015 Current	Non-current
Leasehold deposits received	₩	23,123	3,605	19,404	7,030
Trade payables		74,377	-	103,591	-
Withholdings		258,519	107	212,891	171
Accrued expenses		169,445	-	180,172	-
Other payables		127,143	7,575	90,297	6,446
	₩	652,607	11,287	606,355	13,647

22. Borrowings

(a) Short-term borrowings as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won	Lender	Annual interest rate		September 30 2016	December 31 2015
Borrowings	Kookmin Bank, etc.	2.82%	₩	2,000	23,469
	KEB Hana Bank	2.72 ~ 3.00%		11,000	13,500
	KEB Hana Bank	3M LIBOR+1.3%,etc.		11,128	44,252
	The Korea Development Bank	2.51% ~ 2.62%		1,530	100,000
	PT Bank Woori Saudara	10.66%		2,535	2,550
Customer credit contracts(*)	Nonghyup Bank, etc.	6.09%, etc.		46,817	22,602
			₩	75,010	206,373

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

22. Borrowings, Continued

(b) Long-term borrowings as of September 30, 2016 and December 31, 2015 are summarized as follows:

In millions of won	Lender	Maturity	Annual interest rate		September 30 2016	December 31 2015
Borrowings	Nonghyup Bank	Mar.2021	0.00%	₩	45,908	34,514
	KEB Hana Bank	Mar.2017	1.54%		131	1,936
	Kookmin Bank	Sep.2023	2.35% ~ 2.90%		13,000	13,000
	The Korea Development Bank	Sep.2021	2.33% ~ 2.45%		3,200	-
Convertible bond					8,450	8,500
Redeemable convertible preferred shares					35,340	53,340
Redeemable preferred shares					17,761	18,611
				₩	123,790	129,901
Statement of financial position:						
Current				₩	9,838	27,659
Non-current					113,952	102,242
				₩	123,790	129,901

Details of convertible bond and preferred shares as of September 30, 2016 are summarized as follows:

Description	*Issuing company*	*Details*
Convertible bond(*)	PT Trisakti Purwosari Makmur	Issue date: Dec.2011 Par value: IDR 100,000 million Issued value: IDR 100,000 million Carrying amount: ₩8,450 million (IDR 100,000 million) Interest rate: 9.5% The bonds will mature four years from the issue date and become convertible into shares at the rate of IDR 9,659 per share.
Redeemable convertible preferred shares	Renzoluc Pte, Ltd.	Issue date: Sep.2012 Issued value: ₩35,340 million Carrying amount: ₩35,340 million The convertible instrument will mature ten years from the date of establishment of QCP 2011 Corporate Partnership Private Equity Fund (the "PEF"). The instrument can be converted into 6,978,948 ordinary shares at any time after five years from the issue date. Payable on demand from 270 days prior to the expiration of the PEF
Redeemable preferred shares	K-Q HongKong I, Limited	Issue date: Aug.2012, Sep.2012, Dec.2012 Issued value: ₩17,761 million Carrying amount: ₩17,761 million The convertible instrument will mature ten years from the date of establishment of the PEF. Payable on demand from 270 days prior to the expiration of the PEF

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

22. Borrowings, Continued

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

(c) As discussed in note 16 to the consolidated financial statements, the Group provided collateral for the above borrowings as of September 30, 2016.

23. Retirement Benefits Plan

(a) The components of retirement benefits for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Defined benefit plans:					
Current service cost	₩	12,096	32,952	11,030	33,079
Net interest cost		732	2,257	837	2,512
		12,828	35,209	11,867	35,591
Defined contribution plans:					
Contributions recognized as expense		2,151	5,040	1,024	3,130
	₩	14,979	40,249	12,891	38,721

The Group recognized termination benefits amounting to ₩273 million and ₩8,012 million as an expense for the nine-month periods ended September 30, 2016 and 2015, respectively.

(b) Net defined benefit liability as of September 30, 2016 and December 31, 2015 were summarized as follows:

In millions of won		September 30 2016	December 31 2015
Present value of defined benefit obligations	₩	388,323	373,590
Fair value of plan assets		(237,702)	(252,942)
	₩	150,621	120,648

24. Revenue from Real Estate Sales

(a) Details of agreements for real estate sales under construction as of September 30, 2016 was as follows:

In millions of won	Construction period		Total revenue estimated	Total revenue contracted
Daegu Station Central-Xi	Dec. 2014 ~ Oct. 2017	₩	342,666	318,525

(b) Changes in the balance of contract amounts for the nine-month period ended September 30, 2016 was as follows:

In millions of won		2016
Beginning Balance	₩	246,340
Revenue recognition		(71,517)
Ending Balance	₩	174,823

(c) Recognized profits and related balance for agreements under construction as of September 30, 2016 is summarized as follows:

In millions of won	Stage of completion		Aggregate revenue recognized	Aggregate expenses recognized	Due from customers for contract work
Daegu Station Central-Xi	45.11%	₩	143,702	112,297	16,294

(d) There was no change in the estimates of total revenue and total costs during the nine-month period ended September 30, 2016. The total revenue and the total costs are estimated based on the information and circumstances available at the end of the reporting period and actual results may differ from these estimates.

25. Result from Operating Activities

(a) Details of expenses classified by nature for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

		2016		2015	
In millions of won		Three-month	Nine-month	Three-month	Nine-month
Changes in inventories	₩	28,065	176,532	45,391	186,607
Raw materials and consumables purchased		300,498	768,265	292,250	781,987
Salaries		132,085	390,750	121,649	388,844
Retirement and termination benefits		15,057	40,522	14,069	46,733
Depreciation		38,446	114,145	38,576	113,202
Amortization		1,474	4,467	2,678	8,128
Employee welfare		27,859	70,430	20,928	74,604
Advertising		70,960	179,403	66,032	173,662
Commissions		86,238	242,546	79,644	208,790
Other expenses		93,180	247,422	82,589	218,554
	₩	793,862	2,234,482	763,806	2,201,111

25. Result from Operating Activities, Continued

(b) Details of selling, general and administrative expenses for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Salaries	₩	87,689	259,609	80,185	257,944
Retirement and termination benefits		8,859	25,696	8,534	30,896
Employee welfare		22,558	54,323	14,481	53,648
Travel		3,670	9,787	3,075	8,401
Communications		1,317	3,949	1,259	3,907
Utilities		2,520	7,032	2,325	7,223
Taxes and dues		2,714	17,928	1,001	16,026
Supplies		845	4,952	690	2,471
Rent		6,203	17,664	5,604	17,659
Depreciation		10,042	30,171	11,175	33,117
Amortization		1,427	4,321	2,628	7,979
Repairs and maintenance		1,161	3,325	1,157	3,389
Vehicles		1,448	4,227	1,707	5,024
Insurance		465	1,518	509	1,478
Commissions		72,706	202,155	60,317	168,493
Freight and custody		12,418	36,864	14,940	39,630
Conferences		495	1,864	789	2,537
Advertising		70,930	179,293	66,011	173,559
Training		1,429	4,314	1,607	4,484
Prizes and rewards		494	1,339	489	1,684
Cooperation		226	609	220	533
Normal research and development		7,839	22,463	8,327	24,141
Impairment loss (reversal of impairment loss) on trade receivables		(827)	(6)	150	146
	₩	316,628	893,397	287,180	864,369

26. Other Income and Expenses

(a) Details of other income for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

		2016		2015	
In millions of won		Three-month	Nine-month	Three-month	Nine-month
Foreign currency transaction gain	₩	2,835	16,684	14,202	22,838
Foreign currency translation gain		-	12,137	44,747	76,412
Reversal of impairment loss on other receivables		-	2	1,947	9,069
Gain on sale of property, plant and equipment		847	9,439	36	789
Gain on sale of intangible assets		-	50	-	3
Others		4,584	14,924	3,152	15,778
	₩	8,266	53,236	64,084	124,889

(b) Details of other expenses for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

		2016		2015	
In millions of won		Three-month	Nine-month	Three-month	Nine-month
Foreign currency transaction loss	₩	13,505	25,259	2,541	9,632
Foreign currency translation loss		54,136	69,848	15,803	30,587
Impairment loss on other receivables		-	-	-	13
Donations		20,863	24,844	2,638	24,399
Loss on sale of property, plant and equipment		248	2,090	166	812
Loss on sale of intangible assets		3	8	-	4
Impairment loss on intangible assets		8	8	4	161
Others		2,818	8,211	4,532	12,190
	₩	91,581	130,268	25,684	77,798

27. Net Finance Income

(a) Details of net finance income for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Finance cost:					
Interest expense	₩	(1,311)	(4,861)	(2,573)	(8,202)
Impairment loss on available-for-sale financial assets		-	-	(95)	(95)
Loss on transactions of derivative instruments		-	-	(2)	(2)
		(1,311)	(4,861)	(2,670)	(8,299)
Finance income:					
Interest income		8,859	27,615	8,467	23,999
Dividend income		1,526	11,446	540	8,387
Interest income on long-term deposits in MSA Escrow Fund		(535)	3,554	729	1,796
Gain on transactions of derivative instruments		-	-	-	7
Gain on debt redemption		-	-	-	11,962
		9,850	42,615	9,736	46,151
Net finance income	₩	8,539	37,754	7,066	37,852

(b) Details of interest expense for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Borrowings	₩	634	2,692	1,261	3,768
Trade and other payables		677	2,167	669	1,556
Others		-	2	643	2,878
	₩	1,311	4,861	2,573	8,202

(c) Details of interest income for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Deposits	₩	8,103	24,872	8,284	21,949
Available-for-sale financial assets		7	22	7	32
Trade and other receivables		749	2,721	176	2,018
	₩	8,859	27,615	8,467	23,999

28. Income Tax

(a) Income tax expense was recognized as current tax expense adjusted to current adjustments for prior periods, deferred tax expense (income) by origination and reversal of deferred tax assets (liabilities) and temporary differences, and income tax recognized in other comprehensive income. The average effective tax rate was 27.27% and 27.14% for the nine-month periods ended September 30, 2016 and 2015, respectively.

(b) Deferred tax assets have been recognized to the extent the Group has determined it is probable that future profits will be available against which the Group can utilize the related benefit.

29. Earnings per Share

Basic and diluted earnings per share for the three- and nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won, except share information		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Profit for the period attributable to owners of the parent in millions of won	₩	250,127	819,461	302,699	872,824
Weighted-average number of ordinary shares outstanding		126,143,670	126,133,902	125,965,892	125,960,485
Basic and diluted earnings per share in won	₩	1,983	6,497	2,403	6,929

30. Transactions and Balances with Related Companies

(a) The Group has no significant transactions, receivables and liabilities with related parties, as of and for the nine-month period ended September 30, 2016.

(b) There is no guarantee being provided by related parties as of September 30, 2016.

(c) Details of key management personnel compensation for the three- and nine-month periods ended September 30, 2016 and 2015 are summarized as follows:

In millions of won		2016 Three-month	2016 Nine-month	2015 Three-month	2015 Nine-month
Short-term employee benefits	₩	5,932	17,093	3,810	16,677
Retirement benefits		618	1,954	440	1,896
	₩	6,550	19,047	4,250	18,573

31. Risk Management and Fair Value of Financial Instruments

(a) Overview

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

- Market risk
- Credit risk
- Liquidity risk

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

(b) Risk Management Framework

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

(c) Management of Financial Risks

(i) Market risk

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

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

31. Risk Management and Fair Value of Financial Instruments, 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 September 30, 2016 and December 31, 2015 were as follows:

In millions of won		September 30 2016 Assets	September 30 2016 Liabilities	December 31 2015 Assets	December 31 2015 Liabilities
USD	₩	860,252	32,409	797,656	46,905
EUR		208	2,657	541	1,695
Others		9,746	3,350	7,645	21,151
	₩	870,206	38,416	805,842	69,751

As of September 30, 2016 and December 31, 2015, the effects of a 10% weakening or strengthening of functional currency against foreign currencies on profit before tax were as follows:

In millions of won		September 30 2016 10% weakening	September 30 2016 10% strengthening	December 31 2015 10% weakening	December 31 2015 10% strengthening
Increase (decrease) in profit before tax	₩	83,179	(83,179)	73,609	(73,609)

Equity price risk
The Group 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 Group'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 Group's management.

As of September 30, 2016 and December 31, 2015, the effects of a 5% fluctuation of the price index of stocks on other comprehensive income were as follows:

In millions of won		September 30 2016 5% increase	September 30 2016 5% decrease	December 31 2015 5% increase	December 31 2015 5% decrease
Comprehensive income before tax	₩	4,710	(4,710)	1,780	(1,780)

Interest rate risk
The Group 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 Group'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 September 30, 2016, 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.

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

(c) Management of Financial Risks, Continued

(ii) Credit risk

The Group 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 Group has transacted with customers with high credit ratings to manage credit risk, and has implemented and operated policies and procedures for credit enhancements of the financial assets. Counterparty credit risk is managed by evaluating its credit rating and limiting the aggregate amount and duration of exposure before sales commence, and the Group 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 Group's assets.

The carrying amount of financial assets is maximum exposure to credit risk. The maximum exposure to credit risk as of September 30, 2016 and December 31, 2015 is as follows:

In millions of won		September 30 2016	December 31 2015
Available-for-sale debt instruments	₩	1,596	1,596
Long-term deposits in MSA Escrow Fund		444,696	403,966
Trade and other receivables		1,460,481	1,293,009
Other financial assets		1,113,591	1,136,918
Cash and cash equivalents (excluding cash on hand)		666,328	543,425
Financial guarantee contract		114,855	76,566
	₩	3,801,547	3,455,480

(iii) Liquidity risk

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

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

(c) Management of Financial Risks, Continued

The maturity analysis with a residual contractual maturity of financial liabilities as of September 30, 2016 and December 31, 2015 is as follows:

				Residual contractual maturity			
In millions of won		Carrying amount	Contractual cash flow	Within 3 months	Between 3 months and 1 year	Between 1 and 5 years	Beyond 5 years
As of September 30, 2016:							
Trade and other payables	₩	405,268	405,841	368,160	27,547	7,217	2,917
Long-term borrowings		113,952	115,511	85	256	57,565	57,605
Current portion of long-term borrowings		9,838	9,839	56	9,783	-	-
Short-term borrowings		75,010	75,319	54,147	21,172	-	-
Financial guarantee contract		-	114,855	-	-	114,855	-
	₩	604,068	721,365	422,448	58,758	179,637	60,522
As of December 31, 2015:							
Trade and other payables	₩	406,940	408,593	368,074	27,043	11,042	2,434
Long-term borrowings		102,242	104,044	98	293	43,557	60,096
Current portion of long-term borrowings		27,659	27,676	296	27,380	-	-
Short-term borrowings		206,373	208,593	122,917	85,676	-	-
Financial guarantee contract		-	76,566	-	-	76,566	-
	₩	743,214	825,472	491,385	140,392	131,165	62,530

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

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

(d) Fair value of Financial Instruments

The carrying amount of each category of financial assets and liabilities as of September 30, 2016 and December 31, 2015 are as follows:

In millions of won		September 30 2016	December 31 2015
Financial assets:			
Available-for-sale financial assets	₩	383,261	364,681
Loans and receivables			
- Long-term deposits in MSA Escrow Fund		444,696	403,966
- Trade and other receivables		1,460,481	1,293,009
- Other financial assets		1,113,591	1,136,918
- Cash and cash equivalents		668,249	546,213
		3,687,017	3,380,106
	₩	4,070,278	3,744,787
Financial liabilities:			
Financial liabilities measured at amortized cost			
- Trade and other payables	₩	405,268	406,940
- Long-term borrowings		113,952	102,242
- Current portion of long-term borrowings		9,838	27,659
- Short-term borrowings		75,010	206,373
	₩	604,068	743,214

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

(d) Fair value of Financial Instruments, Continued

The fair value measurements classified by fair value hierarchy as of September 30, 2016 and December 31, 2015 were as follows:

In millions of won		Carrying amount	Fair value Level I	Level II	Level III
As of September 30, 2016:					
Financial assets					
Available-for-sale financial assets	₩	330,601	214,512	-	116,089
As of December 31, 2015:					
Financial assets					
Available-for-sale financial assets	₩	327,022	211,914	-	115,108

There is no transfer between fair value hierarchy levels of recurring fair value measurements for the nine-month period ended September 30, 2016 and the year ended December 31, 2015.

The fair value measurements for available-for-sale equity instruments in real estate trust fund have been measured using the adjusted net asset method and categorized as a level 3 fair value based on the inputs to the valuation techniques used. Changes in fair value classified as level 3 for the nine-month period ended September 30, 2016 and the year ended December 31, 2015 were as follows:

In millions of won		2016	2015
Beginning balance	₩	115,108	90,726
Acquisition		-	22,200
Changes in fair value		981	2,182
Ending balance	₩	116,089	115,108

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

(e) Finance income (costs)

(i) Details of finance income (costs) by categories for the nine-month period ended September 30, 2016 were as follows:

In millions of won		Financial assets at fair value through profit or loss	Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	₩	-	22	27,593	-	27,615
Dividend income		-	11,446	-	-	11,446
Interest income on long-term deposits in MSA Escrow Fund		-	-	3,554	-	3,554
Interest expense		-	-	-	(4,861)	(4,861)
	₩	-	11,468	31,147	(4,861)	37,754
Comprehensive income before tax						
Net change in fair value	₩	-	3,580	-	-	3,580

(ii) Details of finance income (costs) by categories for the nine-month period ended September 30, 2015 were as follows:

In millions of won		Financial assets at fair value through profit or loss	Available -for-sale financial assets	Loans and receivables	Financial liabilities measured at amortized cost	Total
Profit or loss:						
Interest income	₩	-	32	23,967	-	23,999
Dividend income		-	8,387	-	-	8,387
Interest income on long-term deposits in MSA Escrow Fund		-	-	1,796	-	1,796
Gain on transactions of derivative instruments		7	-	-	-	7
Gain on debt redemption		-	-	-	11,962	11,962
Interest expense		-	-	-	(8,202)	(8,202)
Impairment loss		-	(95)	-	-	(95)
Loss on transactions of derivative instruments		(2)	-	-	-	(2)
	₩	5	8,324	25,763	3,760	37,852
Comprehensive loss before tax						
Net change in fair value	₩	-	(11,589)	-	-	(11,589)
Reclassification adjustments upon impairment		-	95	-	-	95
	₩	-	(11,494)	-	-	(11,494)

32. Capital Management

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

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

As of September 30, 2016 and December 31, 2015, the Group's capital structure was as follows:

In millions of won		September 30 2016	December 31 2015
Net debt:			
Debt (borrowings)	₩	198,800	336,274
Less:			
Cash and cash equivalents		(668,249)	(546,213)
Current other financial assets		(1,113,580)	(1,136,906)
		(1,583,029)	(1,346,845)
Equity	₩	6,703,248	6,275,499

33. Contingent Liabilities and Commitments

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

(b) As of September 30, 2016, a lawsuit by National Health Insurance Service claiming damages of ₩53,742 million is filed against the Group. Additionally, as of September 30, 2016, the Group is involved in eleven lawsuits as a plaintiff for alleged damages totalling ₩16,227 million and ten lawsuits as a defendant for alleged damages totalling ₩2,265 million. The amount of the liability the Group may ultimately be liable for with respect to the litigation cannot be reasonably estimated as of September 30, 2016.

(c) As of September 30, 2016, the Group has entered into letter of credit agreements with KEB Hana Bank and other banks with limits in the aggregate of USD 66,100 thousand.

(d) As of September 30, 2016, the Group's trade receivables from the export of cigarettes are insured against non-payment up to USD 20,627 thousand by an export guarantee insurance with the Korea Export Insurance Corporation.

33. Contingent Liabilities and Commitments, Continued

(e) The Group has been provided with a foreign currency payment guarantee by KEB Hana Bank up to USD 40,000 thousand for L/C or guarantees related with its foreign exports. Details of guarantees exercised as of September 30, 2016, are summarized as follows:

In thousands of USD, THB and millions of IDR		Exercised amount
Customs bond and L/C opening of Global Trading, Inc.	USD	14,222
Bidding guarantee for export of tobacco sheet to Taiwan Tobacco and Liquor Corporation	USD	85
Performance guarantee for export of tobacco sheet to Thailand Tobacco Monopoly	THB	11,980
Payment guarantee for purchase of certificate stamp of PT Mandiri Maha Mulia	IDR	175,166

(f) The Group has maintained a contract with the farmers who grow six-year old green ginseng for purchase volume guarantees and recorded contractual amounts paid to the farmers as advance payments in the amount of ₩175,696 million and ₩151,783 million as of September 30, 2016 and December 31, 2015, respectively.

(g) As of September 30, 2016, the Group has an accounts receivable loan agreement with a limit of ₩107,000 million with KEB Hana Bank and other financial institutions.

(h) As of September 30, 2016, the Group has a trade bill loan agreement with a limit of ₩10,000 million with KEB Hana Bank.

(i) As of September 30, 2016, the Group has a loan agreement with a limit of ₩146,600 million with Shinhan Bank and other financial institutions.

(j) As of September 30, 2016, the Group has provided one blank note, five notes amounting to ₩4,000 million and two blank checks to Nara Credit and other financial institutions. Besides, As of September 30, 2016, the Group lost seven blank notes and one blank check and expects to proceed a judgment of nullification.

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

33. Contingent Liabilities and Commitments, Continued

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

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

(m) As of September 30, 2016, the Group has provided guarantees up to ₩225,600 million with an exercised amount of ₩114,855 million for the buyers of apartments in respect of their borrowings from Shinhan Bank.

(n) As of September 30, 2016, the Group is insured by performance bond insurance up to ₩2,055 million with the Seoul Guarantee Insurance.

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

34. Cash Flows from Operating Activities

(a) Details of cash generated from operations for the nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016	2015
Profit for the period	₩	820,212	870,048
Adjustments for:			
Income tax expense		307,521	324,129
Finance costs		4,861	8,299
Finance income		(42,615)	(46,151)
Depreciation		114,145	113,202
Amortization		4,467	8,128
Retirement and termination benefits		40,522	46,733
Foreign currency translations loss		69,848	30,587
Impairment loss on trade and other receivables		-	159
Reversal of write-down of inventories		(791)	(739)
Loss on sale of property, plant and equipment		2,090	812
Loss on sale of intangible assets		8	4
Impairment loss on intangible assets		8	161
Other expense, etc.		4,276	11,030
Share of loss of associates		123	-
Share of gain of associates		(1,982)	(7,181)
Foreign currency translations gain		(12,137)	(76,412)
Reversal of impairment loss on trade and other receivables		(8)	(3)
Gain on sale of property, plant and equipment		(9,439)	(9,069)
Gain on sale of intangible assets		(50)	(789)
		1,301,059	1,272,948
Changes in working capital:			
Trade and other receivables		(172,818)	(255,614)
Advance payments		(43,322)	(67,681)
Prepaid expenses		(517)	(1,321)
Prepaid tobacco excise and other taxes		8,312	(145,374)
Inventories		163,673	182,620
Trade and other payables		69,833	82,700
Advance receipts		(22,908)	(6,011)
Tobacco excise and other taxes payable		(95,887)	395,129
Payment of retirement and termination benefits		(11,561)	(14,493)
Cash generated from operations	₩	1,195,864	1,442,903

34. Cash Flows from Operating Activities, Continued

(b) Details of material transactions without cash inflow and outflow for the nine-month periods ended September 30, 2016 and 2015 were as follows:

In millions of won		2016	2015
In-kind donation of treasury shares	₩	19,200	5,448
Increase(decrease) in accrued expenses related to payment of retirement and termination benefits		(896)	22
Increase(decrease) in other payables related with acquisition of property, plant and equipment		297	(9,524)
Increase(decrease) in advance receipts related with disposal of property, plant and equipment and non-current assets held for sale		(422)	758
Increase in other receivables related with disposal of property, plant and equipment		10	181

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