

In this section we outline the risks we face across our business and our approach to managing them.

### Our Approach

Our ability to achieve our strategic objectives and capitalise on growth opportunities requires effective management of the risks we face.

Our risk management system is designed to identify risks that could prevent the achievement of strategic objectives as early as possible, and to ensure that appropriate and agreed mitigation is in place. The approach seeks to manage, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. Where risks do crystallise, we respond immediately to reduce the impact of that risk and to ensure that the causes and consequences have been evaluated and any wider implications assessed.

Our risk management approach provides a framework which allows for the identification and management of both Group risks and those risks specific to a location. In a business with a global market footprint as diverse as ours it is imperative to ensure that resource is directed at the most relevant risks and that our management is sufficiently supported to achieve positive outcomes.

A year end certification process is completed, under which management confirms that risk mitigation controls have operated effectively throughout the year and that entities have complied with our policies, including the Code of Conduct and anti-bribery requirements, as well as fraud prevention processes. As a separate exercise, all our senior managers are also required to certify that there have been no related party transactions within their areas of control.

Our people have the opportunity to make confidential disclosures about suspected impropriety or wrongdoing via an independent external service (Speaking Up), details of which have been translated into 36 languages and can be found in the Investors section of our website.

In accordance with the recommendations of the FRC's Guidance for Directors on Internal Control (formerly known as the Turnbull guidance), the Group's systems of internal control are designed and operated to support the identification, evaluation and management of risks affecting the Group. They facilitate the effective and efficient operation of our business, provide assurance regarding the integrity of our internal reporting and are designed to comply with relevant laws and regulations, across all areas of operations. These systems are subject to continuous review as circumstances change and new risks emerge.

Our risk management approach continues to develop, ensuring we continue to identify, manage and monitor the risks we face.

### Risk Management

#### The Board and Audit Committee

The Board has ultimate responsibility for the Group's strategy and related risk appetite. In addition, the Board is accountable for reviewing the effectiveness of the systems and processes of risk management and internal control, with the Audit Committee assisting in the discharge of this responsibility.

The Audit Committee oversees the effectiveness of the Group's risk management system and internal controls and is assisted by the Group's Corporate Assurance department (which oversees the completion of the annual assessment of risk management and internal control). The Audit Committee reports to the Board on its activities and makes recommendations and escalates significant risks or issues to the Board as appropriate.

Ensuring that the Board has the right balance of skills and experience to develop our strategy and support its successful implementation, including support of, and insight into, the risk management approach, is the responsibility of the Nominations Committee. This committee provides the Board with the required support to identify and recruit the necessary talent to achieve the Group's objectives.

Achieving the Group's objectives in accordance with our Code of Conduct and business principles is supported by the Remuneration Committee which aligns appropriate senior management objectives and remuneration packages.

In order to assist the Board in its requirement to provide a fair and balanced view of business performance, and to assist with legal and regulatory compliance, oversight of the integrity of the communication of the Group's financial disclosures is provided by the Disclosure Committee. This is chaired by the Company Secretary and comprises senior management from across our business. It meets as required to consider major financial disclosures including the Group's key periodic external reports, including the consolidated and parent company financial statements.

While risk management and the identification of existing and emerging risks are the responsibility of all our people, the Board is supported in the assessment of key risks through work facilitated by the Group's Corporate Assurance department. The approach ensures a consistent top-down method in how we identify, assess and prioritise risks, as well as assessing our existing measures to manage and mitigate those risks.

The top-down approach that supports the Board is complemented by an annual bottom-up review by local management across the organisation which assesses our principal areas of risk and uncertainty across each part of the business. This assessment includes a review of both Group and local risks, along with an assessment of the mitigating controls in place to manage the risks. The separation of risks into Group and Local classifications enables appropriate focus at both senior and local management level, and assists us in the identification of emerging risks. The Group risks are individually owned by a member of the Operating Executive, and ongoing development of the risk management approach continues to improve consistent management of these risks across our global footprint.

### The Operating Executive (OPEX)

The OPEX is ultimately responsible for the effective operational management and mitigation of the Group's key risks. The successful and effective implementation of Group strategies into our operational activities is the responsibility of the Operating Executive and its functional and divisional management teams. These management teams are responsible for ensuring that the Group's strategic goals are achieved in line with Group policies and standards, and that we conduct business in compliance with our Code of Conduct. This tone from the top extends to responsibility for the monitoring of operational and financial performance, the assessment and control of financial, business and operational risks and the maintenance and ongoing development of a robust control framework and environment in their areas of responsibility.

### Operational Management

Across the business, operational management is responsible for the implementation and monitoring of the Group's processes and systems of control. This includes ensuring that our people have appropriate training and knowledge to perform their roles in accordance with the Group's policies and standards and defined lines of accountability and delegation of authority.

The Group's functional and divisional management structures enable a continuing process for the identification, evaluation and management of significant risks to the achievement of business objectives and support the controls in place.

### Oversight

In addition to the oversight provided by our management structures the Group also benefits from the work carried out by subject matter experts it employs to manage specific technical or legal and regulatory risks. These teams form a key part of our "second line of defence" and are referred to as part of our "other assurance provider" network.

These departments design and implement appropriate control structures and monitoring in order to manage the relevant risks. They also act as centres of excellence, providing advice and assistance to the business to help facilitate local solutions where necessary. These "other assurance providers" liaise with our Director of Corporate Assurance to promote a consistent approach and knowledge sharing within the Group's developing "Total Assurance" model.

Our Group Finance department is responsible for the financial policies and standards adopted within the Group. It also manages our financial reporting processes to ensure the timely and accurate provision of information, which enables the Board to discharge its responsibilities, including the production of our half yearly and annual accounts.

Group Finance is supported by a network of finance managers throughout the Group who have the responsibility and accountability to provide information in keeping with our policies, procedures and internal best practices as documented in our Group Finance Manual.

### Governance Framework

The Group's Corporate Assurance department oversees the Group's risk management process and includes our Group Internal Audit team.

Risk management and assurance activities are key elements of our overall governance framework which is based upon a three lines of defence model.

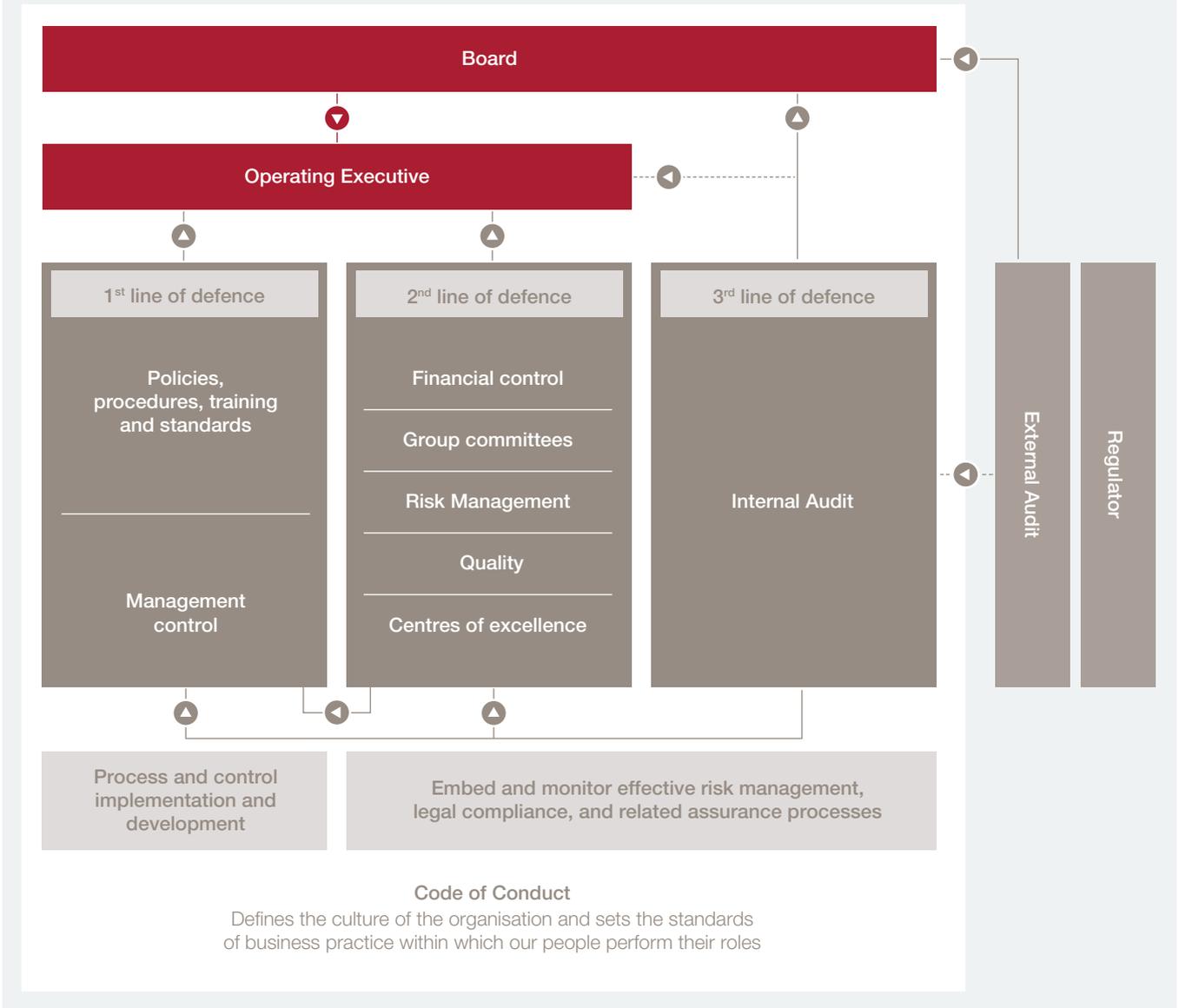
We operate an integrated approach, aligned to ensure that our operational management has the tools, knowledge, and support in order to manage risks as part of its business as usual business processes.

Key elements of our framework:

- our Company Secretary is responsible for maintaining and developing the Group's framework of governance, including our Code of Conduct, Group policies and Speaking Up (whistleblowing) process;
- operational management is provided with training and guidance that enables it to implement effective controls and to manage their business risks;
- centres of excellence and Group committees exist in order to provide expert technical advice and guidance in the development of policy and control relating to our legal and regulatory requirements. These centres of excellence provide assurance activities that ensure effective risk management is implemented through our business processes; and
- our Director of Corporate Assurance provides assurance that the controls to mitigate risks to an acceptable level are operating as they should, through both the risk management processes and internal audit work.

This includes co-ordination of the work of other assurance providers within the Group who are technical experts in their field of risk management such as OHSE and product quality.

# ITG Governance Framework



## Assurance

The Internal Audit department provides independent assessment on the robustness and effectiveness of the systems and processes of risk management and control across the Group. It achieves this through the completion of reviews which are approved by, and reported to, the Audit Committee.

This approach is aligned to the “three lines of defence” model, adopted as an effective structure for risk management.

## PRINCIPAL RISKS AND UNCERTAINTIES

### Risk Management Overview

In the following section we highlight the principal risks we face and identify the mitigations that we have in place to manage the impact of these risks upon the business. Not all of these factors are within our direct control, and the list cannot be considered to be exhaustive, as other risks and uncertainties may emerge in a changing business environment.

As is common with most large organisations the Group is subject to general commercial risks; for example, cyber-security breaches, failure of our IT infrastructure, the cost of our raw materials, and the impact of competition.

#### Risk – Reduction in the size of the legitimate tobacco market

##### What affects us

##### Changes in regulation

Regulatory restrictions exist in many of our markets which impact our consumers by influencing availability, demand and freedom to use our products. The introduction of excessive and disproportionate regulation, both present and future, could have an adverse effect on consumer choice, potentially impacting the demand for our products, as well as the cost of continuing to comply with such increasing regulation.

##### What we do

The Group's "rational regulator" strategy is designed to engage with key internal and external stakeholders to ensure that proposed regulatory change is proportionate and does not lead to excessive regulation. This engagement includes:

- consulting with external experts to provide advice and guidance;
- engagement, where possible, with regulators;
- providing industry specific information to ensure that regulators have a more balanced fact base;
- highlighting the unintended consequences of proposed regulatory change; and
- making legal challenges against excessive regulation.

We prioritise the Group's expertise and resources according to the relevant key regulatory issues. Cross-market liaison is promoted within the Group to ensure best practice and opportunities from markets already impacted are identified, understood, and applied.

##### Increases in excise duty

Governments across the world perceive the use of tobacco excise rates to be a means of raising additional public funding and/or the satisfying of public/private tobacco control agendas.

We engage with local tax and customs authorities as well as politicians/legislators and media where appropriate to provide informed input to the unintended consequences of excise increases. The widening price differential between tobacco products in neighbouring countries increases both the availability and attractiveness to the consumer of purchasing non-domestic duty paid product.

We take commercial steps to mitigate the impact of this issue through the monitoring and compilation of ongoing analysis to ensure strategic price and product offerings exist in the context of the excise duty structures in each market. Through our portfolio of products we are able to meet consumer preferences across different price points.

##### Illicit trade

The consequence of excise and regulatory regimes is a widening gap between price of legitimate and illegitimate product. As a result the legitimate tobacco industry continues to be subject to the significant impact and increasing threat of illicit trade. The sale of counterfeit product and smuggled "illicit whites" in our markets act as a direct competitor to legitimate domestic duty paid, travel retail and duty free products, eroding our volumes and market shares.

We seek to work with governments and law enforcement agencies around the world on anti-illicit trade initiatives, and work alongside the European Commission's Anti-Fraud Office (OLAF) and law enforcement agencies both in the EU and elsewhere.

In order to achieve this we employ specialist teams to provide effective support to the business and governments/law enforcement agencies, performing market analysis and intelligence to provide appropriate and targeted solutions to the combating of illicit trade. We maintain strong business conduct standards and controls, both for our business and our first-line customers in order to prevent our products being diverted.

##### Macro-economic conditions

A material decline in the economic conditions affecting consumers, notably an impact upon disposable income, may change their consumption patterns, including an increased propensity to purchase illicit products.

We monitor and analyse consumption patterns and economic indicators in order to ensure that our current and future portfolio provides the consumer with a range of products across different price points. This analysis is a key input to our product development and pricing strategies.

## Risk – Marketplace

What affects us	What we do
<p><b>Marketplace</b></p> <p>The Group has a significant presence in mature European markets and thus any material decline in the economic circumstances of, and/or our performance in, our key European markets may affect our future profit development and have an adverse impact on the Group's revenue or profits.</p> <p>Should concerns regarding the future of the euro, or the exit of one or more Eurozone countries re-emerge, consumer spending patterns could be impacted. Such an event could also cause disruption to the business as a whole, including impact upon financing arrangements (both Group and Local), and could also have a short-term impact upon our Manufacturing and Supply Chain operations.</p> <p>As with all businesses our route to market could be affected by political instability, civil unrest, and sanctions, and could also have a detrimental effect on our Manufacturing and Supply Chain operations.</p>	<p>We continuously monitor our exposure and review our portfolio and our existing processes and policies to minimise our economic exposure and to preserve our ability to operate in a range of potential conditions that may exist should one or more of these future events occur.</p> <p>Our international footprint and comprehensive portfolio provides an increasingly balanced exposure to both EU and non-EU markets, with the core of our market concentration being in countries with a lower risk of political instability and civil unrest.</p> <p>The alignment of our market management structures to key strategic drivers enables a more consistent approach to the evaluation of risks and opportunities.</p> <p>Our global manufacturing and supply chain operations have crisis management and contingency plans in place which are regularly reviewed in line with the risks to their ongoing requirements.</p>

## Financing

What affects us	What we do
<p><b>Funding and liquidity management</b></p> <p>We have a significant level of committed debt, financed in the debt capital markets and bank loan markets. We expect any future required refinancing of this debt upon maturity to be obtained from these markets and for us to be able to rely on funds being available from our bank counterparties when requested to be drawn.</p> <p>Approximately half of the Group's debt is currently at fixed levels of interest, and therefore the Group is exposed to movements in interest rates which could result in higher funding costs and cash outflows on the remainder.</p> <p>A fall in certain of our credit ratings could raise our cost of funding and affect our ability to raise debt with the breadth of funders we currently enjoy.</p>	<p>Our Group Treasury Committee (GTC) oversees the operation of Group Treasury in accordance with the terms of reference set out by the Board.</p> <p>The GTC sets out a framework for the treasury function to operate within. The framework covers, amongst other things, financing, liquidity and counterparty risk and is fully reviewed periodically. The GTC receives regular reporting on all matters covered by the framework.</p> <p>Cash flows, financing requirements and key rating agency metrics are regularly forecast and updated in line with business performance. This information is considered alongside conditions in debt capital and bank loan markets to ensure we are well placed to meet the future financing needs of the Group, and optimise its cost and availability.</p>

## Legal and regulatory compliance

What affects us	What we do
<p><b>Failure to comply with legislation</b></p> <p>Failure to comply with local and international laws (including sanctions) may result in investigations. This may cause damage to our reputation and has the potential for financial and criminal penalties for both the Group and individuals.</p>	<p>We monitor closely developments in international sanctions and actively seek external advice to ensure that we remain compliant with them.</p> <p>The Group's policies and standards, including our Code of Conduct, mandate that all employees must comply with legislation relevant to a UK listed company and in the countries in which we operate. E-learning courses are provided to management and relevant employees to ensure understanding of key regulatory and compliance requirements.</p> <p>Additionally, senior management certify the compliance of their area of the business with the Code of Conduct as part of an annual certification process. Exceptions are reported and mitigating actions taken.</p> <p>Steering groups exist for key areas of legal compliance to provide expert advice in the development of policy, process, training and monitoring of compliance.</p>

## PRINCIPAL RISKS AND UNCERTAINTIES continued

What affects us	What we do
<p><b>Tobacco litigation</b></p> <p>Tobacco litigation claims are pending against the Group in a number of countries. More claims may be brought in the future, including claims for personal injury and the recovery of medical costs allegedly incurred in treating smokers. If any claim were to be successful, it might result in a significant liability for damages and might lead to further claims against us. Regardless of the outcome, the costs of defending such claims can be substantial and may not be fully recoverable.</p>	<p>To date, no tobacco litigation claim brought against the Group has been successful and/or resulted in the recovery of damages. We employ internal and external lawyers specialising in the defence of product liability litigation to provide advice and guidance on defence strategies and to direct and manage litigation risk and monitor potential claims around the Group.</p>
<p><b>Significant market positions</b></p> <p>Our significant market position in certain countries could result in investigations and adverse regulatory action by relevant competition authorities, including the potential for monetary fines and negative publicity.</p>	<p>The Group's policies and standards, including our Code of Conduct, mandate that all employees must comply with competition laws in the countries in which we operate. We provide training and guidance to relevant employees detailing the obligations and requirements of competition laws. We employ experienced internal and external lawyers specialising in competition laws to provide advice and guidance regarding interpretation and compliance with competition laws. In the event of any investigation (which may or may not result in actions being brought against us), we cooperate fully with the relevant authority making the investigation and will continue to do so.</p>
<p><b>Material strategic initiatives</b></p> <p><b>What affects us</b></p> <p>In order to achieve our strategic objectives, the Group may be required to undertake material initiatives, including acquisitions and change programmes. The Group operates within a regulatory environment that can require the implementation of material initiatives to address changing legal requirements.</p>	<p><b>What we do</b></p> <p>The Group operates a formal project sign-off approach, ensuring an appropriate and transparent review and selection of project proposals aligned to the Group's strategic and operational objectives. To support the successful delivery of material initiatives within the organisation the Group has developed and implemented a standardised project management process that provides a robust framework to enable effective change management. This approach is adopted across the Group and provides a consistent and disciplined approach to the management of material initiatives, supported by the employment of project managers across the Group to ensure the right skills are available to successfully deliver such initiatives. The majority of the Group's material change programmes are coordinated under a single umbrella programme, ensuring alignment of deliverables, management of interdependencies, and limiting the impact of change upon our operational activities. The Operating Executive receives regular reporting on the progress of key projects. This provides a continuing assessment of deliverables in changing markets, and the evaluation of interdependencies across the business. Benefits achieved on key projects are appropriately certified before being reported externally. We also carry out post-implementation reviews to ensure appropriate feedback is captured to constantly improve our change management approach.</p>