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## [Cover]

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## A. Company Information

### I. Overview of the Group

#### 1. Trends in Principal Management Benchmarks

##### (1) Management Benchmarks (Consolidated)

Term	International Financial Reporting Standards				
	32nd term	33rd term	34th term	35th term	36th term
Accounting period	From January 1, 2016 to December 31, 2016	From January 1, 2017 to December 31, 2017	From January 1, 2018 to December 31, 2018	From January 1, 2019 to December 31, 2019	From January 1, 2020 to December 31, 2020
Revenue (Millions of yen)	2,143,287	2,139,653	2,215,962	2,175,626	2,092,561
Profit before income taxes (Millions of yen)	578,237	538,532	531,486	465,232	420,063
Profit for the year (Millions of yen)	425,773	396,749	387,431	361,622	312,029
Profit attributable to owners of the parent company (Millions of yen)	421,695	392,409	385,677	348,190	310,253
Comprehensive income (loss) for the year (Millions of yen)	235,250	554,198	129,302	365,816	132,883
Total equity (Millions of yen)	2,528,041	2,842,027	2,700,445	2,743,611	2,599,495
Total assets (Millions of yen)	4,744,374	5,221,484	5,461,400	5,553,071	5,381,382
Equity attributable to owners of the parent company per share (Yen)	1,371.39	1,541.94	1,468.44	1,501.12	1,421.92
Basic earnings per share (Yen)	235.47	219.10	215.31	195.97	174.88
Diluted earnings per share (Yen)	235.33	218.97	215.20	195.87	174.80
Ratio of equity attributable to owners of the parent company to total assets (%)	51.77	52.89	48.17	47.95	46.88
Ratio of profit to equity attributable to owners of the parent company (%)	17.19	15.04	14.30	13.16	11.97
Price earnings ratio (PER) (Times)	16.32	16.57	12.15	12.41	12.02
Net cash flows from operating activities (Millions of yen)	376,549	419,212	461,389	540,410	519,833
Net cash flows from investing activities (Millions of yen)	(687,509)	(352,632)	(383,307)	(123,571)	5,354
Net cash flows from financing activities (Millions of yen)	91,318	(77,032)	(62,360)	(333,832)	(297,404)
Cash and cash equivalents at the end of the year (Millions of yen)	294,157	285,486	282,063	357,158	538,844
Number of employees [Separately, average number of temporary employees] (Person)	44,667 [7,904]	57,963 [6,744]	63,968 [6,618]	61,975 [7,116]	58,300 [6,681]

Notes: 1. The Group prepares the consolidated financial statements in accordance with International Financial Reporting Standards (hereinafter, "IFRS").

2. The yen amounts are rounded to the nearest million.

3. Revenue does not include consumption taxes.

## (2) Filing Company's Management Benchmarks (Non-consolidated)

Term	32nd term	33rd term	34th term	35th term	36th term
Accounting period	From January 1, 2016 to December 31, 2016	From January 1, 2017 to December 31, 2017	From January 1, 2018 to December 31, 2018	From January 1, 2019 to December 31, 2019	From January 1, 2020 to December 31, 2020
Net sales (Millions of yen)	729,286	681,840	696,250	660,805	596,887
Ordinary income (Millions of yen)	203,242	199,336	190,343	278,968	240,491
Net income (Millions of yen)	173,607	160,120	164,595	262,469	241,752
Share capital (Millions of yen)	100,000	100,000	100,000	100,000	100,000
Total number of shares issued (Thousands of shares)	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000
Net assets (Millions of yen)	1,663,675	1,592,966	1,493,562	1,417,365	1,390,011
Total assets (Millions of yen)	2,849,913	2,885,760	2,670,883	2,614,357	2,597,930
Net assets per share (Yen)	927.93	888.31	832.87	798.18	782.73
Cash dividends per share (Yen)	130	140	150	154	154
[Interim dividends per share] (Yen)	[64]	[70]	[75]	[77]	[77]
Net income per share (Yen)	96.94	89.40	91.89	147.72	136.27
Diluted net income per share (Yen)	96.88	89.35	91.84	147.65	136.21
Equity ratio (%)	58.3	55.1	55.9	54.2	53.5
Return on equity (ROE) (%)	10.29	9.84	10.68	18.05	17.24
Price earnings ratio (PER) (Times)	39.65	43.00	28.48	16.47	15.43
Dividend payout ratio (%)	134.1	156.6	163.2	104.3	113.0
Number of employees [Separately, average number of temporary employees] (Person)	7,298 [1,117]	7,336 [1,222]	7,457 [1,225]	7,464 [1,221]	7,366 [1,183]
Total shareholder return (%) [Comparative indicator: Dividend-included TOPIX] (%)	88.9 [100.3]	87.3 [122.6]	67.9 [103.0]	67.2 [121.7]	63.3 [130.7]
Highest share price (Yen)	4,850.0	4,243.0	3,708.0	2,899.0	2,437.5
Lowest share price (Yen)	3,627.0	3,607.0	2,481.0	2,179.0	1,796.5

Notes: 1. The financial statements of the filing company are prepared in accordance with Japanese GAAP.

2. The yen amounts are rounded to the nearest million.

3. Net sales do not include consumption taxes.

4. The yearly highest and lowest share prices were those recorded on the first section of the Tokyo Stock Exchange.

5. The Company has applied the "Partial Amendments to Accounting Standard for Tax Effect Accounting" (ASBJ Statement No. 28, February 16, 2018) and relevant Guidances effective from the beginning of the 35th term, and the principal management benchmarks for the 34th term represent those after this accounting standard, etc. was applied retrospectively.

## **2. History**

### **(1) Background of the Company's Transition to Stock Company**

Before it became a stock company, Japan Tobacco Inc. (hereinafter, “the Company”) was formerly Japan Tobacco and Salt Public Corporation, or JTS. JTS was established on June 1, 1949 with the “Aim to bring soundness and efficiency to the operation of the national government monopolies.” JTS, serving as the main body for conducting operations of the tobacco monopoly system and other government monopolies, contributed to establishing stable supply of tobacco and securing tobacco-derived financial revenues.

However, the growth in demand for cigarettes in Japan began to slow in the mid-1970s as the result of demographic trends and growing concern about health risks associated with smoking. This trend continued, such that growth in industry sales essentially stopped. In addition to the structural change, the Japanese domestic tobacco market was virtually opened to foreign tobacco suppliers, triggering competition between domestic and foreign tobacco products in Japan, and foreign countries stepped up pressure on Japan to take further market-opening measures, which were difficult to implement within the framework of the monopoly tobacco sales system. Amid such pressure as well as moves toward the reform of government-run public corporations, Ad Hoc Commission on Administrative Reform was established in March 1981 to conduct research on the public corporation system. In its third report (July 30, 1982), the commission proposed drastic reform of the monopoly system and the public corporation system.

In response to this proposal, the government conducted a comprehensive review of these systems and drafted bills to:

- Abolish the tobacco monopoly law in order to liberalize tobacco imports and establish a tobacco business law in order to make necessary adjustments related to the tobacco business.
- Abolish the JTS law, reorganize JTS as stock company so as to enable it to pursue rational corporate management as much as possible and establish the Act on Japan Tobacco Inc., which provides for a necessary minimum level of regulation in light of the corporation's need to compete with foreign tobacco companies on an equal footing in the domestic market following the liberalization of tobacco imports.

These bills were enacted on August 3, 1984 in the 101st session of the Diet and promulgated on August 10 of the same year.

### **(2) Status of the Company After Its Incorporation**

The Company was incorporated on April 1, 1985, pursuant to the Act on Japan Tobacco Inc. (Act No. 69 of August 10, 1984; hereinafter, the “JT Act”), and all of the start-up capital was provided by the Japan Tobacco and Salt Public Corporation, or JTS. When incorporated, the Company succeeded all the rights and obligations of JTS.

The main changes since the incorporation of the Company are as follows:

Date		Details of change
April	1985	Japan Tobacco Inc. was incorporated.
April	1985	The Business Development Division was established to promote active development of new businesses. Subsequently until July 1990, in order to reinforce the promotion system for each business, this division was transformed into business departments such as pharmaceutical, food, etc.
March	1986	Fukuoka and Tosu Factories closed and Kitakyushu Factory built to modernize and streamline tobacco production. By June 1996, nine more tobacco factories were closed down to further streamline the tobacco production system.
October	1988	The communication name “JT” was introduced.
July	1991	The Head Office was relocated from 2-1, Toranomon 2-chome, Minato-ku, Tokyo, to 12-62, Higashi-Shinagawa 4-chome, Shinagawa-ku, Tokyo to make way for the construction of the new Head Office building (now the former JT head office building)
September	1993	The Central Pharmaceutical Research Institute was established to reinforce the internal pharmaceutical research and development capabilities.
October	1994	The initial public offering of the Company shares held by the Japanese government. (394,276 shares) The Company shares were listed on the First Section of the Tokyo, Osaka and Nagoya Stock Exchanges.
November	1994	The Company shares were listed on the Kyoto, Hiroshima, Fukuoka, Niigata and Sapporo Stock Exchanges.
May	1995	The Head Office was relocated from 12-62, Higashi-Shinagawa 4-chome, Shinagawa-ku, Tokyo to 2-1, Toranomon 2-chome, Minato-ku, Tokyo
June	1996	The second public offering of the Company shares held by the Japanese government. (272,390 shares)
April	1997	In accordance with the abolition of the salt monopoly, the Company ended its salt monopoly business. The Tobacco Mutual Aid Pension scheme was united with the Employees’ Pension scheme.
April	1998	The Company signed an agreement with Unimat Corporation to form a business alliance in the soft drinks business and acquired a majority stake in the company.
December	1998	The Company acquired a majority stake in Torii Pharmaceutical Co., Ltd. through a tender offer.
May	1999	The Company acquired the non-US tobacco operations of RJR Nabisco Inc.
July	1999	The Company acquired the food business of Asahi Kasei Corporation, including eight subsidiaries such as Asahi Foods Corporation.
October	1999	Through the business alliance with Torii Pharmaceutical Co., Ltd., research and development functions in the prescription drug business were concentrated in the Company while promotion functions were united within Torii Pharmaceutical.
March	2003	In order to establish a basis for future profit growth in the Domestic Tobacco Business, Sendai, Nagoya and Hashimoto Factories were closed down.
March	2004	In order to establish a basis for future profit growth in the Domestic Tobacco Business, Hiroshima, Fuchu, Matsuyama and Naha Factories were closed down.
June	2004	The third public offering of the Company shares held by the Japanese government. (289,334 shares)
March	2005	In order to establish a basis for future profit growth in the Domestic Tobacco Business, Ueda, Hakodate, Takasaki, Takamatsu, Tokushima, Usuki, Kagoshima and Miyakonojo Factories were closed down.
April	2005	The Company ceased to produce, sell and use Marlboro brand cigarette exclusively in Japan upon the expiration of the exclusive license agreement.
April	2007	The Company acquired shares issued of the Gallaher Group Plc of the United Kingdom through an acquisition method under English act known as a scheme of arrangement.
January	2008	The Company acquired the shares of Katokichi Co., Ltd. through a tender offer
March	2009	In order to restructure the Domestic Tobacco Business in ways to make it more competitive, Kanazawa Factory was closed down.
March	2010	In order to restructure the Domestic Tobacco Business in ways to make it more competitive, Morioka and Yonago Factories were closed down.
March	2011	In order to restructure the Domestic Tobacco Business in ways to make it more competitive, Odawara Factory was closed down.
March	2012	In order to restructure the Domestic Tobacco Business in ways to make it more competitive, Hofu Factory was closed down.
February	2013	The Mild Seven brand was renewed as “Mevious” in Japan.
March	2013	The fourth public offering of the Company shares held by the Japanese government. (253,261,800 shares)
March	2015	In order to further strengthen the competitiveness of Domestic Tobacco Business, Koriyama, Hamamatsu and Okayama Printing Factories were closed down.

Date		Details of change
July	2015	The Company transferred shares the Company held in Japan Beverage Holdings Inc., JT A-Star Co., Ltd. and others, and JT beverage brands “Roots” and “Momono Tennensui.” Subsequently, the Company withdrew from manufacture and sale of JT beverage products in September 2015 and the Beverage Business Division was closed down in December 2015.
March	2016	In order to further strengthen the competitiveness of Domestic Tobacco Business, Hiratsuka factory was closed down.
June	2018	The Company began selling T-Vapor products nationwide.
October	2020	The Head Office was relocated from 2-1, Toranomom 2-chome, Minato-ku, Tokyo to 1-1, Toranomom 4-chome, Minato-ku, Tokyo

Note: The stock split of at a ratio of five to one was conducted as of April 1, 2006 and the stock split at a ratio of 200 to one was conducted as of July 1, 2012.

### 3. Business Description

The Group's management principles are based on the pursuit of the 4S model. The model requires the Group to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can.

The Group created our vision and mission based on the 4S model. The vision is to continue to be a growing global company by providing diversified value that is uniquely available from the JT Group. The mission is to create, develop and nurture the Group's unique brands to win consumer trust, while understanding and respecting the environment and the diversity of societies and individuals.

The Group has also adopted The JT Group WAY as a code of conduct which all members of the Group should follow. The JT Group WAY requires that the Group fulfills the expectations of the Group's consumers and behaves responsibly, strives for quality in everything we do through continuous improvement, and leverages diversity across the Group.

The Group, consisting of the Company, its 235 consolidated subsidiaries and 13 companies accounted for by the equity method, is a global company operating the Domestic and International Tobacco Businesses, Pharmaceutical Business and Processed Food Business. The main business activities operated by the Group and the relationship of each affiliates to the Group's business activities are stated below.

The following four segments are the same as the segmentation of reportable segments in "V. Accounting, 1. Consolidated Financial Statements, (1) Consolidated Financial Statements, Notes to Consolidated Financial Statements, 6. Operating Segments, (1) Outline of Reportable Segments."

#### Domestic Tobacco Business

The Domestic Tobacco Business consists of the manufacture and sale of tobacco products. The Company manufactures and sells tobacco products, and TS Network Co., Ltd. conducts distribution-related operations such as distribution of the Company's tobacco products and wholesale of foreign tobacco products (imported tobacco products). Japan Filter Technology Co., Ltd. and other subsidiaries manufacture materials. Moreover, some of the operations related to Natural American Spirit products are carried out by TRUE SPIRIT TOBACCO COMPANY.

##### *Major subsidiaries and affiliates*

TS Network Co., Ltd., JT Logistics Co., Ltd., Japan Filter Technology Co., Ltd., Fuji Flavor Co., Ltd., JT Engineering Inc., TRUE SPIRIT TOBACCO COMPANY

Besides the companies named above, there are 7 consolidated subsidiaries and 1 company accounted for by the equity method.

#### International Tobacco Business

The International Tobacco Business consists of the manufacture and sale of tobacco products with JT International S.A. as the core company.

##### *Major subsidiaries and affiliates*

JT International S.A., LLC JTI Russia, Gallaher Ltd., LLC Petro, JT International Germany GmbH, JTI Polska Sp. z o. o., JTI Tütün Ürünleri Sanayi A.Ş.

Besides the companies named above, there are 166 consolidated subsidiaries and 8 companies accounted for by the equity method.

## **Pharmaceutical Business**

The Pharmaceutical Business consists of research and development, manufacture, sale and promotion of prescription drugs. The Company concentrates on research and development while Torii Pharmaceutical Co., Ltd. manufactures, sells and promotes drugs (including the Company's products).

### *Major subsidiaries and affiliates*

Torii Pharmaceutical Co., Ltd., Akros Pharma Inc.

## **Processed Food Business**

In the Processed Food Business, TableMark Co., Ltd. and certain other subsidiaries are engaged in manufacture and sale of frozen and ambient foods, seasonings and bakery products.

### *Major subsidiaries and affiliates*

TableMark Co., Ltd.

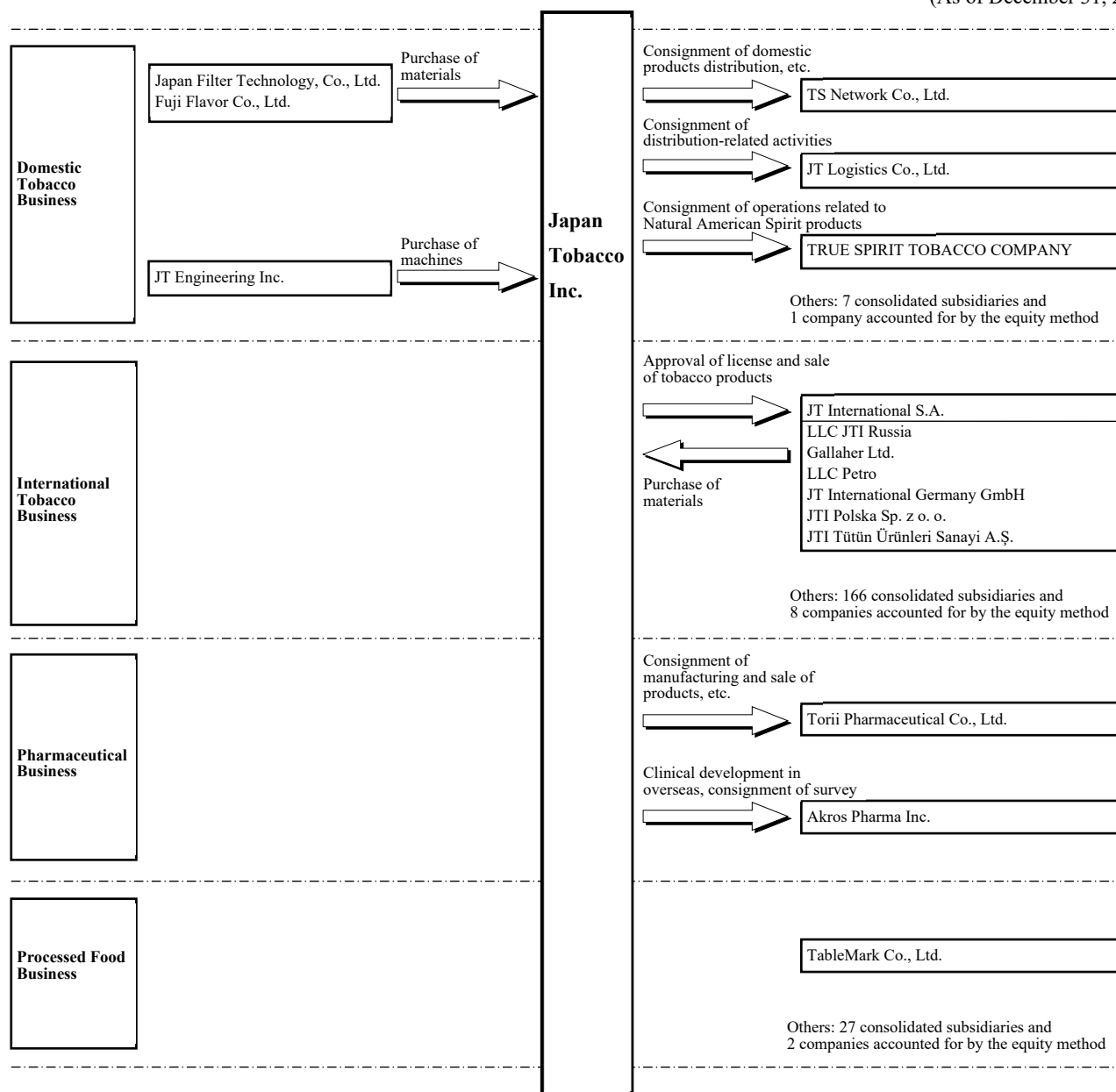
Besides the companies named above, there are 27 consolidated subsidiaries and 2 companies accounted for by the equity method.

In addition to the reportable segments mentioned above, the Group runs businesses, including business relating to the rent of real estate. There are 19 consolidated subsidiaries and 2 companies accounted for by equity method deemed as subsidiaries and affiliates not affiliated to any reportable segment.



The following business activities diagram shows the matters described above.

(As of December 31, 2020)



\* In addition to the reportable segments mentioned above, the Group runs businesses including business relating to the rent of real estate. There are 19 consolidated subsidiaries and 2 companies accounted for by equity method deemed as subsidiaries and affiliates not affiliated to any reportable segment.

An overview of each of the fields of research and development, procurement, manufacturing and sales in each business is as follows.

## **Tobacco Business**

The Group's tobacco business (the Group's tobacco business is managed separately for domestic and overseas markets. The tobacco business' reportable segments are accordingly divided into "Domestic Tobacco Business" and "International Tobacco Business") has the third largest sales volume in the world (excluding China National Tobacco Corporation), operates in at least 70 countries and territories, and sells products in at least 130 countries and territories. The Group's portfolio includes 3 of the top 10 selling global brands.

### **<Research and development>**

The Group is committed to strengthening its R&D capabilities to ensure a long-term competitive advantage. The focus areas in the R&D activities are the development of new leaf tobacco varieties, improvement of tobacco leaves and their processing, enhancement of aroma and taste, upgrading manufacturing technology, and continuous progress on RRP<sup>(Note)</sup>-related technologies. The Group has been striving to add value to the products in these focus areas in a cost efficient manner. It has established a global research platform in Japan, which focuses on the fundamental research and product technology development. To best meet consumers' needs and preferences, the market teams are continuously engaged in the product development.

Note: Reduced-Risk Products (RRP) are products with potential to reduce the risks associated with smoking such as E-Vapor products and T-Vapor products.

### **<Procurement of tobacco leaves>**

The supply of tobacco leaves, raw materials used in manufacturing tobacco products is affected by a variety of factors, such as climate conditions, agricultural product prices, and energy costs. As a result of an increase in costs, the supply of tobacco leaves has been unstable, leading to the fluctuations in tobacco leaf prices. Given these circumstances, the Group has been striving to secure a stable supply and ensure competitive leaf purchase prices. This will be achieved through further vertical integration and strengthening of the relationships with the leaf suppliers.

- Procurement of non-Japan origin tobacco leaf

The Group sources leaves both directly, from major tobacco leaf producing countries (the United States, Brazil, Malawi, etc.), and indirectly, mainly from the three leading international suppliers.

The internal source was established in 2009, when the Group acquired the tobacco leaf suppliers (in Brazil and in Africa), and set up a U.S. joint venture operation. Since then, the efforts have been focused on ensuring the stable procurement through vertical integration, strengthening quality control by supporting farmers, and reinforcing the leaf procurement organization by developing expertise in this area.

- Procurement of Japan origin tobacco leaves

In Japan, the Tobacco Business Act requires the Company to enter into purchase contracts with tobacco farmers every year and purchase the entire usable tobacco harvest. The aggregate cultivation area size and leaf prices for the subsequent year are determined respecting the recommendations from the Leaf Tobacco Council<sup>(Note)</sup>.

Note: The Leaf Tobacco Council is a council which confers on important matters concerning the cultivation and purchase of domestically grown leaf tobacco in response to inquiries by the Company's representatives. The council consists of no more than 11 members, who represent domestic leaf tobacco growers as well as appointees from the academia appointed by the Company with the approval of the Minister of Finance (MOF).

### **<Manufacturing>**

The Group has a global manufacturing footprint in order to manufacture quality tobacco products that secure consumers' reliability trust. The Group operates 6 factories in Japan (4 tobacco manufacturing and 2 tobacco-related factories), and 35 factories in 28 other countries (including tobacco-related factories). In a limited number of cases, the Group also partners with competing manufacturers under contracts and/or license agreements to manufacture the Group's products.

### <Marketing>

To enhance brand loyalty, the Group is conducting extensive and effective marketing activities in accordance to the various regulations and standards.

Globally, the marketing activities are focused on Global Flagship Brands (hereinafter, “GFB”)<sup>(Note)</sup>, while complementing the brand portfolio by promoting local brands as well.

Note: GFB consists of four brands, which serve as flagships of the Group’s brand portfolio - Winston, Camel, MEVIUS and LD.

### <Retail prices>

In setting a retail price for a product, the Group considers various factors, including positioning of the brand, perceived value of the product, retail price of competing products, and the margin. In addition, there are regulations that influence the price-setting decisions. For example, some countries adopt a fixed retail price requirement, and forms of excise taxation on tobacco products (specific and/or ad valorem) differ among the countries. Retail price changes most often occur in case of tax increase. Globally, governments increase taxes to secure tax revenues and promote public health.

### <Sales (distribution)>

To ensure that the products are delivered to consumers, the Group makes sure to use optimal distribution networks for each market complying with the restrictions and in accordance with established local business practices, and other factors. The distribution networks of the Group can be independent distribution networks or local agencies and distributors.

There are various sales channels for tobacco products; chain stores such as convenience stores, gas stations and supermarkets, small independent retailers and vending machines. The contribution of each channel to the total industry sales varies from market to market. Accordingly, the Group develops different trade marketing initiatives for each market, depending on the focus channels as well as consumer trend and competitors’ strategies.

## **Pharmaceutical Business**

The Group commenced the Pharmaceutical Business in 1987. The Group’s mission is to build world-class, unique R&D capabilities and reinforce its market presence through innovative drugs. The Pharmaceutical Business is currently focusing on the development, manufacture, and sales and promotion of prescription drugs.

In December 1998, the Company acquired a majority of the outstanding shares in Torii Pharmaceutical Co., Ltd. (hereinafter, “Torii Pharmaceutical”). After the acquisition, all manufacture, sales and promotion functions were integrated under Torii Pharmaceutical, while all R&D functions were grouped under the Company.

In April 2000, the Company established an R&D base outside Japan by adding a clinical development function to Akros Pharma Inc., a Group company based in the state of New Jersey, United States.

In order to make stable profit contribution, the Group is maximizing the value of each product, enhancing the R&D pipeline, exploring opportunities for strategic in- or out-licensing and strengthening collaboration with license partners.

### <Research and development>

R&D activities are the foundation of the Group’s Pharmaceutical Business and are critical for its long-term growth and profitability. The R&D activities focus mainly on the fields of glucose and lipid metabolism, immune disorders and inflammation, and virus research. In the fiscal year ended December 31, 2020, the Group invested ¥25.2 billion in these activities.

- R&D process

The Central Pharmaceutical Research Institute is responsible for discovery research, drug development, and pre-clinical trial research. The Company’s pharmaceutical development division and the Group company Akros Pharma Inc. undertake clinical trials and handle the application process to receive certification for any new drugs. Concerning compounds out-licensed for development and commercialization outside Japan, the licensees implement the subsequent processes.

### <Manufacturing>

Because the manufacture of the Group's pharmaceutical products at Group factories was discontinued in 2020, all pharmaceutical product manufacturing processes are now outsourced.

### <Sales and promotion>

- Sales and promotion outside Japan

At present, the Group does not have its own sales organization for pharmaceutical products outside Japan. The Group out-licenses the right to develop and commercialize outside Japan for certain compounds in the development stage and receives royalties from the partners linked to their sales performance.

- Sales and promotion in Japan

Torii Pharmaceutical is mainly responsible for sales of the Group's pharmaceutical products to pharmaceutical wholesalers and promotion to medical facilities. Promotional activities are conducted by 335 medical representatives (MRs) stationed at Torii Pharmaceutical's 7 regional sales headquarters across Japan.

CORECTIM® Ointment for treatment of atopic dermatitis, Riona® Tablets, a hyperphosphatemia treatment, and REMITCH®, a drug for treating pruritus in dialysis patients, are the main products.

### **Processed Food Business**

The Group started its Processed Food Business in 1998. Since then, the Group has been expanding the business through organic growth as well as business investments in the form of M&As and strategic partnerships.

In 2008, the Group acquired Katokichi Co., Ltd., a major frozen food manufacturing company in Japan, through a tender offer. The Group's processed food operations were transferred over to Katokichi Co., Ltd. as part of the integration. In 2010, Katokichi Co., Ltd. changed its corporate name to TableMark Co., Ltd. to pursue synergies and foster a sense of unity within the group.

At the end of the current fiscal year, this business is operated by TableMark Co., Ltd., Fuji Foods Corporation, Saint-Germain Co., Ltd., and other Group companies. TableMark Co., Ltd., which operates mainly in Japan, handles the frozen and ambient foods business, mainly frozen udon noodles, packaged cooked rice and frozen okonomiyaki (Japanese savory pancakes). Fuji Foods Corporation handles the seasonings business, which focuses on seasonings including yeast, kelp and bonito extracts, combination seasonings and processed seasonings for direct consumer consumption such as oyster sauce, and Saint-Germain Co., Ltd. operates the bakery business through bakery chain outlets in the Tokyo metropolitan area.

Major Group products include "Reito-Sanuki-Udon" (frozen noodles), "Takitate-Gohan" (packaged cooked rice), and the "Vertex" (yeast extract seasonings) in particular.

### <Research and development>

The Group devotes its efforts to the development of innovative products that meet consumers' needs and preferences. In order to meet the diversifying needs of consumers, the Group works to develop value-added products using its original techniques.

Specifically, the Group has used its original techniques for fermentation, baking, and freezing to recreate and preserve the taste and texture of fresh bread, and developed frozen bread products which allow consumers to simply enjoy the taste of freshly baked bread at home. In addition, in the area of frozen noodles the Group developed a new production method, the "Tannen-jikomi" weaving and maturing process. This enabled the Group to realize udon noodle products with higher quality and higher added value.

### <Procurement>

The first step to produce safe foods is to procure safe and high-quality raw materials. For the procurement, the Group reviews quality assurance certificates submitted by its suppliers. The Group also carries out monitoring inspections to check agrochemical residues as well as conducts regular inspections at processing factories to ensure compliance with the Group's internal standards, in addition to the Food Sanitation Act and other relevant laws.

Furthermore, the Group examines the safety of production sites for raw materials which are procured from overseas. Concerning agricultural farms, the Group checks not only soil and water, but also how products are cultivated and how agrochemicals are handled. Breeding farms and fish farms are also inspected.

### <Manufacturing>

The Group operates 23 factories in Japan and 9 outside Japan. The Group outsources manufacturing of some processed foods to domestic and international contract manufacturers. Excluding one factory<sup>(Note)</sup> that began operations in fiscal 2020, all of the Group factories inside and outside Japan, as well as the factories of the Group's business partners, that produce frozen foods, have achieved ISO 22000 or FSSC 22000 certification. Under the ISO 22000 and FSSC 22000 standards, continuous improvements are made following effective rules to control sanitation and other key issues. These rules are set based on the HACCP concept and their effectiveness is tested using scientific evidence.

Note: This factory is currently progressing toward ISO 22000 and FSSC 22000 certification.

### <Marketing>

The Group analyzes the market from consumers' point of view and, by its technology, it has been striving to provide products with new values to expand the market and increase its place there. The Group has been striving for effective marketing in order to improve consumer awareness of its products.

### <Sales and distribution>

The Group has been striving to enhance profitability through sales division structure optimization and its initiatives to increase its presence in supermarkets and convenience stores, by offering a wider range of products while also seeking better shelf space.

### <Food safety>

To ensure that consumers can continue to enjoy the products safely, the Group has established Quality Control Centers in Tokyo and Qingdao (China), and it not only inspects and monitors the raw materials it uses from the product planning and development stages, but also makes inspections at factories at the time of production and before shipment, and carries out safety management throughout the product manufacturing process. The Group seeks assessment and advice on its initiatives from external food safety experts. The Group reflects the experts' knowledge and viewpoints in its business by actively incorporating them into food safety controls. Details of the food safety activities, including the discussions described in the above "Procurement" and "Manufacturing" sections, are disclosed on the website.

## 4. Status of Subsidiaries and Affiliates

(As of December 31, 2020)

Name	Location	Capital (Millions of yen)	Principal business	Holding rate of voting rights (%)	Relationship				
					Interlocking of officers		Financial assistance	Business relationship	Facility leasing
					Officer of the Company	Employee of the Company			
(Consolidated subsidiaries) 235 companies									
TS Network Co., Ltd. *1	Taito-ku, Tokyo	460	Domestic tobacco	85.3	No	Yes	No	Consignment of tobacco products distribution	Yes
JT Logistics Co., Ltd.	Chuo-ku, Tokyo	207	Domestic tobacco	100.0	No	Yes	No	Consignment of tobacco products and raw materials distribution	Yes
Japan Filter Technology, Co., Ltd. *1	Sumida-ku, Tokyo	461	Domestic tobacco	100.0	No	Yes	No	Purchase of filter for tobacco products	Yes
Fuji Flavor Co., Ltd.	Hamura-shi, Tokyo	196	Domestic tobacco	100.0	No	Yes	No	Purchase of flavors for tobacco products	No
JT Engineering Inc.	Sumida-ku, Tokyo	200	Domestic tobacco	100.0	No	Yes	No	Purchase of machines	Yes
TRUE SPIRIT TOBACCO COMPANY	Minato-ku, Tokyo	45	Domestic tobacco	100.0	No	Yes	No	Consignment of operations related to Natural American Spirit products	No
JT International Group Holding B.V. *1	Netherlands	Thousands of USD 1,800,372	International tobacco	100.0	Yes	Yes	No	No	No
JT International Holding B.V. *1	Netherlands	Thousands of USD 1,800,372	International tobacco	100.0 (100.0)	Yes	No	No	No	No
JT International S.A. *1	Switzerland	Thousands of CHF 923,723	International tobacco	100.0 (100.0)	No	No	No	Approval of license and sale of tobacco products	No
LLC JTI Russia	Russia	Thousands of RUB 108,700	International tobacco	100.0 (100.0)	No	No	No	No	No
Gallaher Ltd. *1	U.K.	Thousands of GBP 172,495	International tobacco	100.0 (100.0)	No	No	No	No	No
JTI Polska Sp. z o. o.	Poland	Thousands of PLN 200,000	International tobacco	100.0 (100.0)	No	No	No	No	No
LLC Petro	Russia	Thousands of RUB 328,439	International tobacco	100.0 (100.0)	No	No	No	No	No
JT International Germany GmbH	Germany	Thousands of EUR 37,394	International tobacco	100.0 (100.0)	No	No	No	No	No
JTI Tütün Ürünleri Sanayi A.Ş.	Turkey	Thousands of TRY 148,825	International tobacco	100.0 (100.0)	No	No	No	No	No
Torii Pharmaceutical Co., Ltd. *2	Chuo-ku, Tokyo	5,190	Pharmaceutical	54.9	No	No	No	Consignment of manufacturing and sale of products	Yes
Akros Pharma Inc.	U.S.A.	Thousands of USD 1	Pharmaceutical	100.0 (100.0)	No	Yes	No	Clinical development in overseas, consignment of survey	No
TableMark Co., Ltd. *1	Chuo-ku, Tokyo	22,500	Processed Food	100.0	No	Yes	Yes	No	Yes
Other 217 companies *1									
(Companies accounted for by the equity method) 13 companies									
Megapolis Distribution B.V.	Netherlands	EUR 15	International tobacco	23.0 (23.0)	No	No	No	No	No
Other 12 companies									

- Notes: 1. Descriptions in the “Principal business” column are names of segments.
2. The figures in parentheses in the “Holding rate of voting rights” column are indirect holding rates included in the figures outside the parentheses.
3. “Interlocking of officers” includes interlocking of officers of associated companies and secondment of officers of the Company.
4. \*1: These companies are classified as specified subsidiaries. Companies that fall under the category of specified subsidiaries included in “Other 217 companies” are as follows.  
JTI-Macdonald Corp., JTI Tütün Ürünleri Pazarlama A.Ş., JT Canada LLC Inc., JT International (Philippines) Inc., JTI Processadora de Tabaco do Brasil Ltda., Japan Tobacco International Manufacturing Co., Ltd., JT International Distribuidora de Cigarros Ltda., PT Karyadibya Mahardhika, Japan Tobacco (Bangladesh) Limited, JT International Asia Manufacturing Corp., JTI (UK) Management Ltd., Gallaher Group Ltd., Benson & Hedges Ltd., Gallaher Overseas (Holdings) Ltd., Al Nakhla Tobacco Company S.A.E.
5. \*2: This company files Annual Securities Report.
6. Consolidated subsidiary Green Foods Co., Ltd. is insolvent, with liabilities exceeding assets by ¥10,815 million. Green Foods Co., Ltd. suspended business operations in December 2012.

## 5. Status of Employees

### (1) Consolidated Companies

(As of December 31, 2020)

Segment	Number of employees (Person)
Domestic Tobacco Business	10,354 [2,931]
International Tobacco Business	40,576 [2,054]
Pharmaceutical Business	1,379 [62]
Processed Food Business	5,021 [1,506]
Common company-wide services within the filing company	970 [128]
Total	58,300 [6,681]

- Notes: 1. The number of employees indicates the number of working employees, and the average number of temporary employees during this fiscal year ended December 31, 2020 is given in parentheses separately.  
 2. The number of employees in the “Common company-wide services within the filing company” row is the number of those working for departments unclassifiable to specific segments, such as the administrative department.

### (2) Filing Company (the Company)

(As of December 31, 2020)

Number of employees (Person)	Average age (Year old)	Average years of service (Year)	Average annual salary (Yen)
7,366 [1,183]	43.2	18.1	8,295,884

The numbers of employees by segment are as follows.

Segment	Number of employees (Person)
Domestic Tobacco Business	6,062 [1,169]
Pharmaceutical Business	773 [11]
Processed Food Business	20 [0]
Common company-wide services within the filing company	511 [3]
Total	7,366 [1,183]

- Notes: 1. The number of employees indicates the number of working employees, and the average number of temporary employees during this fiscal year ended December 31, 2020 is given in parentheses separately.  
 2. The number of employees in the “Common company-wide services within the filing company” row is the number of those working for departments unclassifiable to specific segments, such as the administrative department.  
 3. The number of employees includes contract employees (144), employees on leave (159) and employees transferred to the Company (80), but excludes employees transferred from the Company (634).  
 4. Average years of service include years of service at Japan Tobacco and Salt Public Corporation.  
 5. Average annual salary (including taxes) includes bonuses and surplus wages.

### (3) Status of Labor Union

In the Group, the labor-management relations are stable and there are no matters that should be reported.



## II. Review of Operations

### 1. Management Policy, Business Environment, Issues to Be Addressed, Etc.

The following includes forward-looking statements determined, unless otherwise indicated, as of the filing date.

#### (1) Management Principles

The Group's management principles are based on the pursuit of the 4S model. The model requires the Group to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can.

The Group created its vision and mission based on the 4S model. The vision is to continue to be a growing global company by providing diversified value that is uniquely available from the JT Group. The mission is to create, develop and nurture the Group's unique brands to win consumer trust, while understanding and respecting the environment and the diversity of societies and individuals.

The Group has also adopted The JT Group WAY as a code of conduct which all members of the Group should follow. The JT Group WAY requires that the Group fulfills the expectations of the Group's consumers and behaves responsibly, strives for quality in everything we do through continuous improvement, and leverages diversity across the Group.

The Group has attained sustainable profit growth and will continue to do so through the pursuit of the 4S model. Since attaining sustainable profit growth requires the Group to continue to provide new value and satisfaction to consumers, the Group believes it is essential to steadily make business investments for future mid- to long-term profit growth.

The Group believes that the pursuit of the 4S model will lead to a consistent increase in corporate value in the mid- to long-term and therefore that it is the best approach to serve the interests of all stakeholders.

#### (2) Allocation of Management Resource

Concerning the mid- to long-term resource allocation of the Group, it will place top priority on business investments that will lead to sustainable profit growth in the mid- to long-term based on the management principles.

Of the Group's core businesses, the Group regards the tobacco business as the core business and profit growth engine, so it places top priority on business investments that will lead to the sustainable profit growth of the tobacco business. On the other hand, with the aim of positioning the Pharmaceutical Business and the Processed Food Business as complementary drivers of profit growth for the Group as a whole, the focus will be on rebuilding their business foundations, and making the investments required to implement that.

From 2021 onward, there is no change in the Group's management resources allocation policy, under which the Group will continue to place a high priority on making business investments<sup>(Note)</sup> that contribute to sustainable mid- to long-term profit growth as well as on valuing the balance between profit growth through business investments and shareholder returns.

Note: Investment towards the growth of the tobacco business is our highest priority. Pursue growth of adjusted operating profit at constant FX through quality top-line growth

#### (3) Group-Wide Profit Targets and Policy on Shareholder Return

The Group has set group-wide profit targets and a mid- to long-term guidance on shareholder return in the Business Plan 2021 in accordance with the management principles and the resource allocation policy.

In the Business Plan 2021, the Group will continue to pursue mid to high single digit annual average growth rate over the mid- to long-term in adjusted operating profit at constant FX.

The Company approaches its shareholder return policy from the twin perspectives of prioritizing business investments for sustainable profit growth in the mid to long term, and strike a balance between profit growth through business investments and shareholder returns which are mentioned in the resource allocation policy and based on the 4S model, as follows.

- Aim to enhance shareholder returns by realizing the Company's mid- to long-term profit growth, while maintaining a solid financial base<sup>(Note 1)</sup>
- Target a dividend payout ratio of about 75%<sup>(Note 2)</sup>, a competitive level<sup>(Note 3)</sup> in the capital markets

- Consider implementing a share buy-back program, mainly taking into account the Company's financial outlook of the respective year and mid-term capital needs.

Notes: 1. The Company will maintain a solid financial base that secures stability in case of changes in business environment such as economic crises and flexibility enabling expeditious responses to business investment opportunities.  
 2. To be in the range of approximately  $\pm 5\%$   
 3. Monitor the shareholder return trends of global Fast-Moving Consumer Goods (FMCG) companies which have a stakeholder model similar to our 4S model and have realized strong business growth.

#### **(4) Business Environment and Basic Strategies for Attaining Group-Wide Profit Targets**

##### **i. Business environment**

The business environment in which the Group operates is characterized by an increasing degree of uncertainty, such as changes in the international political situation, and foreign exchange risks associated with declines in value for the currencies of emerging countries. In particular, global economic conditions have deteriorated as a result of the lockdowns and restrictions on cross-border travel caused by spread of the novel coronavirus disease (COVID-19), which have given rise to significant changes in consumer behavior and corporate activity, and we recognize that the outlook going forward is even more unclear. Enhancing adaptability to such a changing environment is critical to achieve sustainable profit growth by overcoming the uncertain business environment and adequately executing business on a global scale. "Adaptability" refers to the ability to assume a wider range of contingencies than in the past, during the planning phase, and to quickly and flexibly respond to changes and events that surpass the assumptions so that the Group can deal with uncertainty over the future. The Group believes that how well and how quickly companies can overcome uncertainties will be the key to determine their competitiveness.

Moreover, in view of the forward march of digital technology, changes in the consciousness and behavior of consumers, and the shift towards greater awareness of sustainability, etc., the Group believes that, rather than merely responding passively while enhancing its adaptability to such a changing environment, the Group should initiate transformation itself, while accelerating evolution to an organization that will lead this revolution.

The Group formulates its business plan, a three-year plan that is renewed each year on a rolling basis in order to speed up responsiveness and strengthen competitiveness while keenly identifying challenges in our operating environment, which presents increasing uncertainties.

##### **ii. Basic strategies**

As basic strategies for attaining the targets, the Group will strive for "achieving quality top-line growth," "strengthening cost competitiveness," and "strengthening business foundations," implementing the strategies based on the concept of selection and focus.

Mainly, the Group places emphasis on "achieving quality top-line growth," concentrating resources in key brands and product categories, in order to increase value added to products and services, as described in the following explanations of business strategies.

Concerning "strengthening cost competitiveness," the Group aims at improving profitability and enhancing cash generation capability by optimizing business and corporate costs and establishing quick and efficient business operation systems, while leveraging the efforts of maintaining and enhancing quality. Additionally, the Group will reinforce its business continuity capabilities, while seeking to improve cost competitiveness.

When "strengthening business foundations," it is critical to accurately identify changes in the business environment and to keep ourselves ready to readjust in order to meet challenges without being constrained by precedents. The Group will make continuous improvement efforts from that perspective. In addition, the Group will maximize synergies by leveraging the global footprint as represented by the Group's worldwide business operations, which are spread across at least 70 countries and territories, and the diversity of the Group's global workforce, which represents at least 100 nationalities, and by promoting collaboration on a global scale. As the Group strongly believes that the quality of human resources is the key to business activity and performance, it will strengthen human resource development.

The Group also recognizes that in order for it to achieve sustainable growth, it is essential for the business to contribute to the sustainable development of our society, based on which perception the Group has put sustainability initiatives at the heart of managing the business. Having identified key challenges that must be addressed to allow the Group to grow sustainably along with society as part of its materiality initiative, the Group has formulated a sustainability strategy. We have set out three absolute requirements for sustainability (Respect for Human Rights, An Improved Social and Environmental Impact, and Good Governance and Business Standards) that apply across the Group and take into account the characteristics of each business, and have set areas of focus to be prioritized as well as associated targets.

Business environment and basic strategies by segment are as follows.

## **Tobacco Business**

The tobacco business is the Group's core business and profit growth engine and aims for mid to high single digit annual average growth rate over the mid- to long-term in adjusted operating profit growth rate at constant FX. The Domestic Tobacco Business acts as highly competitive platform of profitability, while the International Tobacco Business serves as the profit growth engine of the Group.

### **i. Business environment**

The Tobacco Industry is evolving and there are many types of tobacco products available in this marketplace today. Cigarettes remain the most popular choice for consumers, while fine cut tobacco, cigars, pipe tobacco, smokeless tobacco, waterpipe tobacco and kretek continue to draw consumers' interest. In addition, the RRP category including E-Vapor products and T-Vapor products has become increasingly popular. In the market for E-Vapor products, which instead of using tobacco leaf vaporize liquids containing nicotine so that the generated vapor can then be enjoyed by the user, the Group has achieved a certain presence, notably in the U.S. and across Europe. As E-Vapor products do not use tobacco leaf, they have not usually been regulated or taxed as tobacco containing products. However, regulation and taxation of the products have changed in some countries in accordance with the expansion of this category. T-Vapor products do use tobacco leaf, but instead of burning the leaf, they use methods such as heating the leaf to generate tobacco vapor (which includes compounds derived from the tobacco leaf) for the user to enjoy, and have been growing steadily, particularly in Japan. The products are taxed and regulated as tobacco products in principle because they use tobacco leaves. Development of T-Vapor products (including heated tobacco sticks that use high-temperature heating) is an area of keen interest for all market players, and the Group expects innovation to drive further growth. In addition to these two types, the growth of smokeless tobacco has accelerated in markets with a long history of these products, particularly in Europe and the U.S. With smokeless tobacco, users can enjoy the characteristic tobacco taste and flavor directly through their nose or mouth.

Approximately 5.4 trillion cigarettes<sup>(Note 1)</sup> are consumed annually around the world, reaching global sales of approximately USD700 billion<sup>(Note 1)</sup>. China is by far the largest market, accounting for over 40% of global consumption, but is almost exclusively operated by a state monopoly, China National Tobacco Corporation. Indonesia, the U.S., Russia and Japan are the following four largest markets<sup>(Note 1)</sup>. Excluding China National Tobacco Corporation, there are four major global tobacco players: Philip Morris International Inc., British American Tobacco Plc., the JT Group and Imperial Brands Plc. In terms of RRP, besides these four companies, JUUL Labs, Inc. (E-Vapor products) and Swedish Match AB (smokeless tobacco) also have a meaningful presence.

In general, the market dynamics of cigarettes<sup>(Note 2)</sup> are distinctively different between mature and emerging markets. In mature markets, cigarette industry volume tends to decline and these movements can reflect various factors, such as limited economic growth, tax increases, tightening regulations and demographic changes among others. In addition, down-trading is prevalent in these markets, as limited growth of income inclines consumers to seek more value in comparatively affordable tobacco products. In emerging markets, on the other hand, cigarette industry volume tends to be more resilient, driven by population growth and economic development, particularly across the Middle East and Africa. As personal income generally increases year on year, consumers look for quality and trade up to products in a higher price range.

Overall, the global industry volume<sup>(Note 1)</sup> of cigarettes has been decreasing in recent years, although at a sustainable pace. However, more importantly, the profit-generating structure of the tobacco industry remains solid, and despite environmental difficulties, the Group expects industry value to continue growing during Business Plan 2021's term, with price increases more than compensating for the volume contraction, particularly in cigarettes. These trends – decline in volume and increase in value – are expected to continue. In addition, due to consumer demand and other factors, the market mix for E-Vapor products, heated tobacco sticks and related products varies from country to country, but the main markets for RRP include the U.S., Japan, Italy, South Korea, United Kingdom, Germany, and Russia. Compared to that of cigarettes<sup>(Note 2)</sup> the size of the market is still small, but it is growing year after year and the RRP market is forecast to expand going forward, driven by growth in heated tobacco sticks.

In addition, due the impact of COVID-19 that appeared in 2020 the outlook for the tobacco industry as a whole going forward has become even more unclear. The Group recognizes that the effects on consumer purchasing power, consumption and purchasing behavior may persist to some extent in the future, but it is assumed that there will be no significant impact over the mid-term. On the other hand, given that the situation varies according to the country and region, and given the possibility of tax increases in various countries driven by the

need for fiscal stimulus to offset the negative economic impact, the Group is on the alert for changes in the business environment going forward.

- Notes: 1. According to fiscal 2019 data Including fine cut tobacco  
2. Including fine cut tobacco

## ii. Basic strategies

### <Quality top-line growth>

- Strengthening RRP initiatives

The Group believes that RRP are beneficial to the consumer, to society, and to the business of the Group, and has positioned RRP as the pillar of sustainable growth for the Tobacco Business, with resources to this area being given priority allocation going forward. The Group will focus on developing RRP that will be chosen by more consumers, and leverage innovation to broaden its portfolio of high-quality products, thus satisfying the changing needs of consumers. With regard to existing tobacco products, there has been no change to their importance as the foundation of our profits, and the Group will continue to make business investments with the aim of achieving sustainable growth.

- Maintaining and increasing shares in the key markets through brand equity enhancement

Over the past years, the JT Group's tobacco business has grown its share in most of the key markets through superior brand equity.

In order to further grow market share, the Group will continue strengthening its brands, especially through consistent investments in the GFB. At the same time, the Group will also strengthen its local brands. These diverse local brands allow the Group to meet the unique preferences of the consumers and complement the brand portfolios in the diverse markets and regions where the Group is active. The Group will continue to focus the investments in innovation, as it is one of the most effective methods to enhance brand equity.

The Group's innovation efforts target five key elements which add value to its tobacco products: 1) tobacco blends, 2) flavors, 3) filters and other non-tobacco materials—these three are important elements to determine quality of taste—4) capability to process these innovations into products and 5) package design, which is critical to visual quality.

The Group recognizes the growing importance of connection especially at point-of-sale for “brand communications” with consumers, which support share gains, since the use of mass media (TV, radio, newspapers and magazines) to promote tobacco products is severely restricted by regulations on advertisement and promotion. With this in mind, the Group believes that the enhancement of its trade marketing activities is critical to improve point-of-sale visibility. The Group's approach will be tailored to each market, where local regulations, the key sales channels, consumers' purchasing patterns and competitors' trade marketing tactics vary greatly among one another.

- Geographic expansion

Over the years, the Group has increased its presence as a leading global tobacco manufacturer through large-scale M&As, most notably RJR Nabisco's non-US tobacco operations in 1999 and Gallaher Group Plc in 2007.

The geographical expansion achieved with these two acquisitions has been the main driver of the growth for over a decade. The success of these acquisitions, owing in part to the prompt postmerger integration within the Group's business, has reinforced its global business base.

Since that time, with the aim of both entering new markets and expanding its presence in existing markets, the Group has continued to build a geographically balanced portfolio primarily in high-margin markets in developed countries and primarily in high-growth markets in emerging countries, through such measures as strengthening investment in existing businesses and acquiring external resources through acquisition and by taking equity stakes. Moving forward, the Group will continue to seek out growth opportunities. The strengthening of the tobacco business base as well as expansion into emerging markets will help promote organic growth. In addition, growth opportunities will be pursued by other strategic alternatives that may arise.

### <Strengthening cost competitiveness>

The tobacco business will persistently pursue continuous cost efficiency improvement of the operations, in particular with respect to the global supply chain, with an emphasis on agility and efficiency without compromising quality. The Group will enhance its cost competitiveness by optimizing the global supply chain through various initiatives, including: further vertical integration in global leaf procurement; extended use of common non-tobacco materials; increased collaboration among suppliers; flexible procurement to benefit from attractive market prices; and improved inventory management for both tobacco and non-tobacco materials.

Furthermore, enhanced productivity through realignment of manufacturing process and optimal level of capital expenditures will ensure conversion cost containment. The Group is also determined to improve its business continuity capability by securing options for sourcing and geographically spreading critical functions. Specifically, the Group has been striving to ensure a framework of multiple supply sources, optimal manufacturing capacity allocation on a global basis and diversification of production capability for priority SKUs (Stock Keeping Units).

The Group will improve the margin through increased cost efficiency while maintaining quality, and enhance cash flow generation by optimizing working capital and capital expenditures.

### <Strengthening business foundations>

The Group believes that human resource development is the key driver of sustainable profit growth in the tobacco business.

The Group has business operations in at least 70 countries and territories, and the global workforce of employees representing at least 100 nationalities works regardless of nationality, gender, and age. The Group maximizes synergies by leveraging this diversity and promoting collaboration on a global scale. As the Group believes that the quality of human resources is the key to business activity and performance, it will strengthen human resource development and enhance its ability to recruit, develop, and retain employees on a global basis.

The tobacco business remains committed to increasing its presence as a leading global tobacco manufacturer and further strengthening its role as the core business and profit growth engine of the Group, by steadily implementing the above business strategies.

## **Pharmaceutical Business**

The Group's Pharmaceutical Business will strive to make stable profit contribution to the Group through the promotion of R&D on next-generation strategic products and by maximizing the value of each product.

### i. Business environment

The global pharmaceutical market continued to grow, with an average annual increase of about 3.4% over the past five years, to USD1,262.4 billion in 2019, up 3.3% year on year<sup>(Note)</sup>. While these factors result in a higher demand for more advanced drugs, governments are strengthening their control on drug prices by holding back medical costs, due mainly to the rapidly aging society and fiscal deficits.

In order to control medical care expenses, the Japanese government has been promoting the use of generic drugs, leading the generic drugs market to expand in the Japanese pharmaceutical market. Additionally, a drastic reform of the drug pricing system will lead to a gradual price reduction each year from 2021, creating challenges for the industry. The drug price reduction rate in April 2020 was 4.4% on average.

It is not easy to discover promising drug development targets and, amid stricter approval standards for new drugs, the global competitiveness in development is intensifying. The Company possesses R&D capabilities for creating world-class, original drugs, and competes with numerous companies, not only those in Japan, but also foreign companies, including large pharmaceutical companies and start-up companies.

Note: Created based on IQVIA World Review Executive 2015-2019

## ii. Basic strategies

### <Stable profit contribution>

To make stable profit contribution, the Group will step up efforts to promote R&D on next-generation strategic products and seek optimum timing for out-licensing, and maximize the value of each product, as key tasks to strengthen the earnings base further.

- Promoting R&D on next-generation strategic products and seeking optimum timing for out-licensing

Promoting R&D on next-generation strategic products is a key task from the perspective of the sustainable development of the Group's Pharmaceutical Business. Market launch of new drugs is becoming increasingly difficult every year. However, the Group will explore appropriate drug development opportunities by collecting information concerning unmet needs of medical facilities around the world. The Group will also conduct flexible research management, carefully tailored to each drug candidate.

With the intensification of worldwide R&D competition in recent years, it is essential to define a sophisticated development strategy that takes into account of the requirements of medical facilities and implementation of clinical tests quickly. In order to accelerate the speed of the R&D and swiftly provide the new drugs the Group has created to patients around the world, the Group not only promotes in-house development but also continues to out-license compounds to other companies, particularly global pharmaceutical companies, and aggressively explore alliance opportunities.

- Maximizing the value of each product

Since 2014 the Group has launched Riona® Tablets (hyperphosphatemia treatment), CEDARTOLEN® SUBLINGUAL DROP - Japanese Cedar Pollen, MITICURE® House Dust Mite Sublingual Tablets and CEDARCURE® Japanese Cedar Pollen Sublingual Tablets (three hyposensitization therapy (allergen immunotherapy) drugs), CORECTIM® Ointment for treatment of atopic dermatitis, and ENAROY® Tablets for treatment of anemia associated with chronic kidney disease, all in Japan. Outside Japan, the licensing partners are currently selling Stribild® Combination Tablets (anti-HIV drug), Genvoya® (anti-HIV drug) and Mekinist® (melanoma and NSCLC treatment). In order to maximize the contribution to medical facilities through these products, the Company will work to steadily spread the products in the market in close partnership with the Group company Torii Pharmaceutical and the Company's licensing partners.

The Group recognizes, in order to conduct these various activities in an effective manner, the urgent requirement of training personnel who can collect accurate information regarding unmet needs at medical facilities and the latest pharmaceutical research, and use the information to formulate a sophisticated development strategy and a strategy to maximize product value, and global personnel capable of competing with academia and pharmaceutical companies around the world. The Group will concentrate efforts on its initiatives for these purposes.

## Processed Food Business

The Group's Processed Food Business aims to contribute to the earnings of the Group through mid- to long-term profit growth driven by high-quality expansion in the top line.

### i. Business environment

In 2019, annual consumption of frozen food in Japan<sup>(Note)</sup> increased 2.0% to 2.95 million tons from the previous fiscal year, a record high. Domestic market size on a consumption basis including imports<sup>(Note)</sup> grew 0.1% from the previous fiscal year to ¥1,076.9 billion, exceeding ¥1 trillion for the third consecutive year. Additionally, in 2020 the pandemic encouraged people to stay home and work from home, resulting in more opportunities to eat at home. This led to demand growth in frozen food, as consumers value its preservation and convenience.

We expect the Japanese processed food industry to continue to grow as lifestyles change including an increase of double-income households. This change leads to a growing consumer need for simpler and shorter cooking times. Frozen foods can help meet the diverse needs of consumers with its abundant variety and convenience in recreating freshly served taste.

The Company's subsidiary, TableMark Co., Ltd., is competing against major players like Maruha Nichiro, Nichirei Foods, Ajinomoto Frozen Foods and Nippon Suisan Kaisha as well as a multitude of mid- or small-scale producers, although the Group is starting to see segregation of competition within the industry according to the product categories these competitors respectively own. These competitors are not the only ones the Group needs to keep an eye out on. The Group believes it is necessary to monitor trends in sales channels amid the expansion of private brand products by various distribution companies; and the reorganization of wholesale entities. The Group also needs to be aware of the continuing risk of price fluctuations in raw materials due to global food shortages.

Note: Source: Japan Frozen Food Association (2019 data)

## ii. Basic strategies

### <Quality top-line growth>

The Processed Food Business focuses primarily on frozen and ambient foods, including staple food products such as frozen Udon noodles, packed cooked rice, and frozen Okonomiyaki, as well as seasonings and bakery products. In the area of product line-up, the Group plans to create products that offer good value for the price from consumers' perspective while using its unique technology. This will be achieved by improving the ability to identify consumers' needs, generate ideas based on the identified needs, and transform the generated ideas into products. Concerning marketing, the Group will develop effective and efficient advertising and promotional activities in line with this product strategy and reinforce the trade marketing capabilities. By adopting these measures, the Group aims to further expand its market share.

### <Strengthening cost competitiveness>

In the Processed Food Business, the Group has a variety of cost containment programs, including strengthening the raw materials procurement capabilities, efficiently managing the distribution network, and improving the productivity of the Group factories. In addition, consistent group-wide efforts will be made to lower fixed costs, including more efficient use of sales activity expenditures, through better selection and focus of promotional activities. By these means, the Group will work to improve cost competitiveness.

### <Strengthening business foundations>

- Food safety control

Looking ahead, the Group will continue to manage the businesses while taking all possible measures to ensure food safety control from the four perspectives of food safety, food defense, food quality, and food communication in order to deliver safe and high-quality food products to consumers.

Regarding food safety, the Group will seek to minimize risks by utilizing food safety management systems already introduced.

Regarding food defense, the Group will further promote the already implemented Food Defense Program in order to prevent purposeful attacks.

Regarding food quality, the Group will pursue "deliciousness," which should be the fundamental quality of foods. The Group will also seek to enhance product added value and consumer satisfaction through continued improvement in accordance with inquiries and information from consumers.

Regarding food communication, the Group will conscientiously listen to the voices of consumers and actively provide information so as to make the Group's activities more visible to the outside.

- Human resource development

Development of human resources that support the business activities is critically important. Competence development programs as well as appropriate career paths of the employees will be created and implemented in order to develop personnel with various skills including marketing expertise and product development knowhow.

In summary, the Group will pursue the 4S model as the basis of the Group's management principles, enhance its ability to adapt to changes, implement bold and expeditious reforms of mindset and behavior, and consistently execute its growth strategy. Through these initiatives, the Group will achieve sustainable profit growth and continuously increase corporate value in the mid- to long-term.



## 2. Business and Other Risks

Listed below are major items that, among those relating to the review of operations and accounting revealed in the Annual Securities Report, are recognized by management as items that may significantly influence financial position, operating results and cash flows of consolidated companies. These items include items that may significantly affect the achievement of the Group's management targets and business strategy as well as items that may significantly influence investor decisions from the viewpoint of proactive information disclosure.

However, the risks described below do not constitute an exhaustive list of all the risks related to the Group, and risks not described below also exist. All of the risk factors may potentially have an effect on investment decisions.

The following includes forward-looking statements determined, unless otherwise indicated, as of the filing date.

### <Risk Management System>

The Group defines risks that may affect the Group, and closely observing these trends, takes measures to prevent these risks from actualizing and to minimize the impact in the event that they are actualized. Furthermore, the Group has established a system that can comprehensively understand and manage all of these risks, and the risk management process consists of the following four steps.

(Risk identification)

The person in charge of risk management promotion (currently Member of the Board, Chief Sustainability Officer), who is designated by the President, will understand all risks that may affect the Group.

(Risk evaluation)

Each Executive Officer will evaluate the risks for their own departments from the viewpoint of the possibility of actualization and the amount of impact in the event of actualization, select significant risks to observe closely, and report to the person in charge of risk management promotion.

Based on this, the person in charge of risk management promotion will determine significant risks to the Group that may cause significant loss regarding the achievement of the Group's management targets and business strategy, and report to the President.

(Formulation of plans to address risks)

Significant risks to the Group are reported to the person in charge of risk management promotion and the President after plans to address risks are designed by each Executive Officer.

(Monitoring of plans to address risks)

The progress of plans to address the Group's significant risks is regularly reported to the person in charge of risk management promotion and the President by each Executive Officer.

### (1) Risks Relating to the Business, Profit Structure and Management Policy of the Group

#### a. Significance of tobacco revenue from the Japanese market in consolidated revenue

The Group operates in at least 70 countries and regions around the world and sells products in at least 130 countries and regions, mainly in the tobacco business. Among these, tobacco revenue in the Japanese market makes a considerable contribution to the Group's revenue. Accordingly, in the event that the Japanese market is negatively affected in some way due to the manifestation of various risks that exist in the environment for the tobacco business, such as a decrease in tobacco demand, tax increases, regulations and other factors (for details of risks relating to the tobacco business, see "(2) Risks Relating to the Group Businesses, Risks Relating to the Tobacco Business" below), the Group's business performance may be negatively affected, such as revenue from the Domestic Tobacco Business deteriorating.

The Group is working to maintain and grow tobacco revenue from the Japanese market by optimizing its product portfolio, reinforcing trade marketing capabilities and implementing measures for effective promotions. Furthermore, the Group has continued to build a geographically balanced portfolio primarily in high-margin markets in developed countries and primarily in high-growth markets in emerging countries, through such measures as increasing its presence as a global tobacco manufacturer, strengthening investment in existing businesses and acquiring external resources by using measures to expand geographically through M&As. By further strengthening and expanding the business base not only in the Japanese market, but globally as well, the Group will work to secure various markets in which it is possible to continuously generate profits without depending only on specific markets.

## b. Business expansion

The Group views the role of Pharmaceutical Business and the Processed Food Business as that of supplementing sustainable profit growth over the mid- to long-term, and believes that also in the future these businesses will make a stable and even larger profit contribution. However, although the Group plans to continue to invest in these businesses, this investment is not guaranteed to generate the returns that the Group anticipates.

The Group worked proactively to obtain external resources for the business expansion, such as the acquisition of the RJR Nabisco Inc.'s non-U.S. tobacco business (acquired in 1999 for approximately USD7.8 billion, or ¥944.0 billion as calculated by the exchange rate at the time of the acquisition; the same applies hereinafter), as well as the acquisition of Gallaher Group Plc (acquired in 2007 for approximately GBP 7.5 billion, or ¥1,720.0 billion), the acquisition of Katokichi Co., Ltd. (now TableMark Co., Ltd.) (acquired in 2008 for approximately ¥109.0 billion), and the acquisition of the non-U.S. tobacco business of Natural American Spirit (acquired in 2016 for approximately USD5.0 billion, or ¥591.4 billion). In an effort to expand its business, the Group will consider acquisitions, capital movements, business tie-ups and cooperative arrangements with other companies and may execute when the Group judges such transactions would contribute to the future earnings of the Group. However, should such transactions not generate the expected outcome, or should a significant, unforeseen problem be discovered after the acquisition, same may negatively affect the Group's business performance. Examples that may have such an impact include a failure to carry out operational, personnel, technological or organizational integration due to geographical or cultural differences; a failure to maintain sustained demand for the products of a business subject to acquisition or tie-up, or manufacture and sell said products; a failure to continue the Group's present operations; a failure to retain personnel with superior capabilities at an acquired business or maintain the motivation of its employees; a failure to apply the Group's internal control system to an acquired business; a failure to build an effective brand and product portfolio; a failure to link sales and market strategies of different product lines; or a dispersal of management's attention from the Group's present operations.

Also, as a result of the acquisitions, the Group has recorded a substantial amount of goodwill and intangible assets in the consolidated statements of financial position, and the amounts of goodwill and intangible assets account for 35.5% (¥1,909.4 billion) and 6.8% (¥363.6 billion) of the consolidated total assets, respectively, as of the end of the fiscal year. The Group believes that the abovementioned goodwill and intangible assets appropriately reflect the future profitability that will result from the unleashing of synergy effects of each business value and integration; however, if it is determined that this expected outcome does not materialize as a result of factors such as changes in the business environment or competitive forces, or if the discount rate applied becomes higher, the Group may incur an impairment loss that negatively impacts the Group's performance.

When carrying out acquisitions, capital movements, business tie-ups and cooperative arrangements with other companies to expand its business, the Group utilizes timely and appropriate external knowledge and evaluations, and makes decisions using the Board of Directors, etc. upon deliberations with related top management regarding the appropriateness of acquisition costs, contract conditions, etc. In addition, after acquisition, the Group incorporates the status of the acquired company's business operations into each business's Business Plan and regularly monitors such status, and takes actions, such as following up and understanding signs of impairment, to maximally realize synergy.

## c. Effects of foreign exchange and interest rate fluctuations

The Company reports its consolidated financial statements indicating all figures in yen; however, overseas Group companies report their financial statements in other currencies such as Russian ruble, euro, British pound, Taiwanese dollar, US dollar, and Swiss franc. Accordingly, the results, assets, and liabilities of overseas Group companies are converted into yen when the consolidated financial statements of the Company are prepared and indicated in yen therein. As a result, those figures are affected by fluctuations from the currency used by overseas Group companies in their accounts settlement against the yen. The respective ratios of the Group's revenue and adjusted operating profit attributable to the International Tobacco Business were 62.4% and 70.0% in the fiscal year ended December 31, 2020. Therefore, foreign exchange fluctuation may greatly impact consolidated financial statements along with the expansion of the International Tobacco Business and its contribution to the results.

JT International Holding B.V. (hereinafter referred to as "JTIH"), which is responsible for consolidating the financial results of the Group's International Tobacco Business, uses the US dollar for its financial reporting. However, JTIH does business through consolidated subsidiaries and affiliates around the world, some of which

use foreign currencies other than the US dollar. This means that the Group's consolidated results are affected not only by exchange rate fluctuations between the Japanese yen and the US dollar but also by those between the US dollar and other foreign currencies used by the consolidated subsidiaries and affiliates for their financial reporting.

In addition, any liquidation, sale or significant drop in the value of a foreign Group company whose foreign currency denominated stock was acquired by the Company will result in the recording of an investment loss with respect to said company in the consolidated financial statements of the Company and this loss will be affected by the exchange rate fluctuation between the yen and the foreign currency that was used to acquire said stock.

Furthermore, most of the Group's international transactions are subject to the effects of foreign currency exchange rates. As an example of this risk, in the Domestic Tobacco Business or the International Tobacco Business, the Group uses foreign-grown leaf tobacco. While this leaf tobacco is procured to some degree in US dollars, the tobacco products that contain it are sold in the local currencies of various countries. Therefore, should the US dollar appreciated against these various local currencies, this may have a negative effect on profitability at the Group.

Furthermore, the Group holds financial assets, such as bank deposits and government bonds, and financial liabilities, such as bank loans and bonds. The fluctuation of interest rates pertaining to these assets and liabilities may affect the performance and financial position of the Group as these fluctuations affect the variance of interest income and interest expenses and the price of financial assets and financial liabilities.

In addition, the Group's business performance and financial position may be affected in the event that the amount of plan assets, amount of retirement benefit obligations, etc. of the Group fluctuate due to the fluctuation of foreign exchange markets or interest rate levels.

The Group formulates and implements a foreign exchange hedge policy and an interest rate hedging policy, taking into consideration the current condition of the foreign exchange market and interest rates in a comprehensive manner, and the results are regularly reported by the Treasury Division to the president and the Board of Directors of the Company.

#### d. Natural disasters and other contingency situations

The Group has expanded its business in various countries and regions in the world, and is working to further strengthen and expand its global business base in the tobacco business in particular. Recently, natural disasters have occurred in Japan and overseas such as earthquakes, tsunamis, typhoons or floods. Future large-scale natural disasters or human-made disasters such as suspension of infrastructure, political instability or bombings, or other such unforeseen emergencies, may negatively affect the Group's business performance. Such effects may be caused by supply shortages from damage to suppliers; disruptions to traffic, logistics services or sales channels; suspension of utilities such as electric or water; declines in demand; or employees suffering damage in a disaster.

The Group prepares against the occurrence of natural disasters and unforeseen circumstances, and carries out initiatives to increase employee's disaster prevention awareness, such as continuously gathering and sharing crisis management-related information during the quiet period in addition to the introduction of a safety confirmation system that confirms the safety of employees and their families, and disaster prevention training. The Group makes preparations to minimize the damage on business activities by carrying out seismic retrofitting at multiple bases, which includes factories in Japan, in order to stably provide products, and establishing a backup system, such as by establishing a manufacturing system and installing standby power at multiple bases. Furthermore, in order to keep losses from damage to a minimum, the Group insures key assets, such as buildings, machinery, equipment and inventory, with casualty insurance as appropriate. In addition, in the event of natural disasters or other contingency situations occurring, the Group will review the Business Continuity Plan and revise it if necessary, and swiftly and flexibly respond so that it can carry out its Business Continuity Plan based on appropriate information gathering and the assessment of the situation.

#### e. Infectious disease

As the Group has expanded its business in various countries and regions in the world, the global spread of infectious diseases may significantly affect the Group's business operations. Recently, the global spread of COVID-19 has brought about unprecedented situations, such as slowdown and regression of the global economy and lifestyle changes, and as it is difficult to predict when COVID-19 will be brought under control, the overall outlook for the economy going forward is unclear.

The spread of COVID-19 has affected the Group businesses, including a decrease in duty-free sales in the tobacco business and a change in consumer trends in the Domestic Tobacco Business and the Processed Food Business, and the impact is expected to lower revenue group-wide by approximately ¥61.0 billion for the fiscal year ended December 31, 2020. At present, the impact of COVID-19 is not obstructing business continuity, but as it is difficult at this time to predict when COVID-19 will be brought under control and its future impact, it is unclear what impact there will be on mid- to long-term consumer trends and demand trends in each business, and regarding the business and financial impacts, it is also necessary to carefully monitor and examine foreign exchange rate trends and the responses of the governments and relevant authorities of each country. In the event of the spread of an infectious disease, such as COVID-19, going forward, the Group's business performance may be negatively affected.

Concerning the spread of COVID-19, the Group is conducting business operations of the tobacco business, the Pharmaceutical Business and the Processed Food Business fully in compliance with the policies and directives of the governments and relevant authorities of each country. In January 2020 the Group established a task force, which is led by senior management, has prepared measures in response to COVID-19, and implemented day-to-day management of the situation. Specifically, from the perspective of preventing the spread of COVID-19 inside and outside the Group and ensuring the safety of employees and their families, etc., the Group has actively used teleworking, enhanced workplace hygiene management, restricted business trips and implemented various other infection-prevention measures. Furthermore, the Group has developed a stable product distribution system by continuing the manufacturing system that ensures safety through thorough sanitation control of processes, etc., and having multiple suppliers.

#### f. Climate change

The Group recognizes that in order for it to achieve sustainable growth, it is essential for our business to contribute to the sustainable development of our society. The Group believes that working on sustainability is at the heart of managing our business. Our sustainability strategy is formulated based on the 4S model, our management principles, and encompasses our materiality analyses. In particular, social concern regarding environmental issues is increasing yearly, and “reducing the impact on the environment” has been established as the Group's shared base. We recognize that climate change remains a key environmental challenge for us, as it can have a direct impact on our value chain and the society at large. Based on this, the Group has expressed its approval of the recommendations of the “Task Force on Climate-related Financial Disclosures (TCFD),” and is analyzing climate change scenarios. According to this analysis, factors such as an increase of the carbon tax burden, etc. associated with the transition to a carbon-free society and changes to the habitat of tobacco leaves due to the intensification of climate change may negatively affect the Group's business performance.

The Group formulated the “JT Group Environment Plan 2030” in 2019 in order to reduce its environmental burden. Within this, “Energy and Emissions” has been selected as an area for significant initiatives, and the plan specifies the target for reducing greenhouse gas emissions in compliance with the Paris Agreement. This target covers not only the Group, but also the Group's value chain, and is certified as the reduction target (Science Based Target) based on scientific reasoning. Furthermore, the Group is working to minimize the negative effects of climate change by promoting initiatives to diversify the procurement of tobacco leaves. The Group will put in place a system in order to enable it to more accurately grasp, and create appropriate responses to the way that climate change affects its business, reflect it in the business strategy and further promote appropriate information disclosure.

#### g. Country risk

The Group operates in various countries and regions around the world. As a consequence, the International Tobacco Business in particular is growing in importance. In order to achieve long-term growth, the Group will continue to expand the business base. Geographical expansion increases exposure to country risks, such as a change in the political environment, a change in the economic conditions, a change in the social environment, a change in the legal system, or the occurrence of riots, terrorism or war. If materialized, these risks could negatively affect the Group's business performances due to blockage to supply chains or distribution networks, damage to assets or facilities, or difficulties in allocation of personnel or sales management.

Furthermore, the Group conducts business in countries that are subject to economic sanctions. Although the Group manages its business operations appropriately and lawfully in accordance with these various economic sanctions, if it is acknowledged that the Group has violated the sanctions, the Group would be at risk of being subject to large monetary penalties or other such consequences. Also, if there is a development such as a change in the details of the sanctions, this may negatively affect the Group's business performances by, for example,

making the Group unable to continue operating in the countries subject to the sanctions. Even if the Group obeys the sanctions, simply operating in the countries subject to the sanctions may have a detrimental effect on the public image of the Group.

The Group gathers and monitors information pertaining to country risk in each country and region in which it has expanded its business, and works for stable business operations while ascertaining geopolitical factors. Furthermore, by strengthening and expanding its global business base and securing multiple markets that can continuously generate profits, the Group is working to minimize the negative effects on the Group's business performance in the event that country risks are realized in specific markets.

#### h. Changes in consumer preferences and behaviors

Uncertainties in the business environment in which the Group operates, such as the contraction of the global economy and a slowdown in economic growth, continue to increase. Within this, the Group recognizes that continuing to provide new value and satisfaction to consumers for continuous profit growth is important, and is working to enhance product and service added value based on changes in consumer preferences and behaviors. However, in the event that consumer preferences and behaviors change due to a deterioration of the economy, etc. and the Group is unable to appropriately respond, the Group's business performance could be negatively affected due to factors such as consumers in existing businesses leaving and the loss of opportunities for growth.

In order to continue to provide new value and satisfaction to consumers, the Group identifies consumer preferences by analyzing market trends and carrying out qualitative and quantitative consumer surveys, and works to realize high value-added products that conform to consumers' preferences such as by improving existing products and developing new products. For example, in the tobacco business, the Group has improved existing RRP products by increasing the convenience sought by consumers and developed new products, and has secured high-quality products, such as cigarettes, and set appropriate prices.

In the Processed Food Business, the Group is developing products that take health into consideration due to increasing health consciousness recently.

#### i. Competition with rival companies

The Group is a global company operating the Domestic and International Tobacco Businesses, Pharmaceutical Business and Processed Food Business. It rigorously competes with rival companies engaged in any of these businesses, and going forward, competition may further intensify.

In the Japanese domestic tobacco market, competition has intensified partly due to the diversification of smoker preferences and aggressive marketing activities by rival companies ever since the easing of regulations relating to imported tobacco products in 1985 and the abolishment of tariffs on imported cigarettes in 1987. In addition, in accordance with the diversifying needs of consumers, the RRP market has been expanding rapidly in recent years, and the Group perceives that continuing to provide products that precisely capture consumer needs is even more important than it has been hitherto.

In overseas tobacco markets, the Group expanded its business by building on its self-sustaining growth and by acquiring the RJR Nabisco Inc.'s non-U.S. tobacco business and Gallaher Group Plc. As a result, its competitive relationships with global players in the International Tobacco Business such as Phillip Morris International and British American Tobacco as well as strong firms operating in localized markets are observed.

In the Pharmaceutical Business, the Group competes with numerous companies, not only those in Japan, but also foreign companies, including large pharmaceutical companies and start-up companies. In the Processed Food Business, the Group is starting to see segregation of competition within the industry according to the product categories these competitors respectively own. The Company's subsidiary, TableMark Co., Ltd., is competing against major players like Maruha Nichiro, Nichirei Foods, Ajinomoto Frozen Foods and Nippon Suisan Kaisha as well as a multitude of mid- or small-scale producers.

Each business and market share fluctuates under multiple factors including competition, regulations, pricing strategies, changing consumer preferences and behaviors, heightened societal interest in health issues, brand strengths and economic conditions occurring in different markets not to mention short-term fluctuations caused by temporary factors such as the introduction of new products by the Group and other companies and the special promotional activities effected for them. A lower market share or decreased competitiveness due to these factors may negatively affect the Group's business performance.

In this competition with rival companies, the Group assumes that it will continue to provide new value and satisfaction to consumers in order to realize continuous profit growth. To that end, the Group provides products that match the changes in consumer preferences and behaviors, optimizes its product portfolio, reinforces the trade marketing capabilities and carries out effective promotional activities, and constantly considers and implements measures such as further increasing cost efficiency and securing multiple markets that can continuously generate profits.

j. Instability in supplies of key materials and transport costs

The Group has a global manufacturing footprint, and procures various types of raw materials from Japan and various countries around the world. The status and costs of procurement are affected by factors such as weather and other natural phenomena, the balance between supply and demand, exchange fluctuations and supplier issues. Furthermore, there is the risk that increases in transport costs will be further exacerbated going forward due to increasing personnel expenses in the logistics industry, which are caused by labor shortages, and rising crude oil prices. In the event that the Group is unable to stably secure the necessary amount of raw materials, or in the event that raw material procurement costs and costs to transport products rise, the Group's business performance may be negatively affected due to being unable to guarantee the stable supply of products and other factors.

In order to reduce the risks associated with these raw material procurement costs and transport costs becoming unstable, the Group prepares for unforeseen circumstances and secures multiple suppliers. Furthermore, the Group continuously monitors raw material prices, and efficiently uses raw materials, such as by reviewing product specifications as appropriate, upon confirming manufacturing processes and quality. Similarly, the Group continuously monitors crude oil prices and trends in the logistics industry, and reviews transport methods and streamlines them as appropriate. In addition, by reinforcing its relationship with suppliers, the Group increases its procurement abilities for key raw materials, and carries out the necessary response, such as working to improve the internal sourcing ratio for the procurement of tobacco leaves.

k. Supply chain risks

The Group has formulated a sustainability strategy, and each business has also set out its own focus areas and works continuously on a variety of sustainability issues. The tobacco business and the Processed Food Business in particular have "Supply Chain" as one of its focus areas, and appropriately maintaining and managing the supply chain is a significant matter for the continuation of business activities. The Group has expanded its business in various countries and regions in the world. It collaborates with stakeholders, such as suppliers, and works on procurement activities that take the environment and society into consideration. However, in the event that environmental or human rights issues occur or laws and regulations are violated in the supply chain, the Group's business performance could be negatively affected due to factors such as the impairment or decline of public trust in the Group.

Based on the JT Group Supplier Standards, the Group is working to establish a sustainable supply chain, such as by carrying out initiatives to introduce supplier screening in accordance with the evaluated ESG items and monitoring them regularly, and understanding potential risks related to compliance, human rights, the environment and occupational safety and health. Agricultural Labor Practices (ALP) were formulated in the tobacco business based on "tackling child labor," "respecting worker rights" and "ensuring workplace health and safety," which work to maintain and manage the tobacco leaf supply chain.

l. Litigation

The Group is a defendant in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products, or exposure to tobacco smoke. As of the fiscal year end date, there were smoking and health-related cases pending in which one or more members of the Group were named as defendant, including cases for which the Company may have certain indemnity obligations pursuant to the agreement for the Company's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations. In addition, the Group is also a defendant in lawsuits other than the smoking and health-related cases.

The Group is unable to predict the outcome of currently pending or future lawsuits. If these actions result in a decision unfavorable to the Group, its business could be materially affected by, for example, the payment of a substantial amount of monetary compensation. Moreover, regardless of the results of these lawsuits, critical media coverage may reduce social tolerance of smoking, strengthen public regulations concerning smoking and

prompt the filing of a number of similar lawsuits against the Group, forcing it to bear litigation costs and materially affecting its business performance. In addition to smoking and health-related litigation, the Group may be a party to further cases should litigation occur in the future, such as if any problems arise regarding product quality of the Group that lead to the Group becoming the target of claims seeking product liability. Such litigation cases may negatively affect the Group's business performance or manufacture, sale, and import and export of the Company's products, should their outcomes prove unfavorable.

The Group has prepared a system in order to deeply cooperate internally and externally where the Group responds to litigation cases pertaining to the Group in a timely and appropriate manner by quickly understanding the information regarding the case, sharing information to management and relevant departments, coordinating with an outside lawyer if necessary and considering policies to deal with the situation going forward.

Regarding major litigation cases to which the Group is a party, please refer to "V. Accounting, 1. Consolidated Financial Statements, (1) Consolidated Financial Statements, Notes to Consolidated Financial Statements, 38. Contingencies."

#### m. Difficulty in maintaining human resource competitiveness

The Group strives for "strengthening business foundations" as one basic strategy, and aims to maximize synergies by leveraging the global footprint as represented by the Group's operations in various countries and regions around the world, and the diversity of the Group's global workforce, which represents at least 100 nationalities, and by promoting collaboration on a global scale. On the other hand, in the particular case of tobacco business, the Group is aware of the negative social image placed on this business line. Mainly for that reason, it is becoming major issues for the Group to recruit and retain talented people. Should the Group be unable to sufficiently fulfill such needs as retaining human resources, future business operations may become difficult, thus having a negative impact on the Group's business performance.

The Group strongly believes that the quality of human resources is the key to business activity and performance. Furthermore, as the Group has adopted the "Human Resources Management Philosophy" based on the belief that a diversified employee base is a major factor of its competitiveness, the Group seeks to attract talented people worldwide, and further strengthen development and retention.

Specifically, by attracting experienced people, the Group immediately secures human resources who are needed in various fields, such as people who have a high level of expertise. Additionally, in the International Tobacco Business, the Group is focusing on attracting the generation known as Generation Z, which is the generation of people born between the latter half of the 1990s and 2001 as the Group believes that they have the skills to push the Group's innovation. Furthermore, the Group works to develop human resources by providing growth opportunities to all employees of the Group, such as by carrying out training applicable to all employees, including executives, which provides them with the necessary skills for their individual careers. At the same time, the Group maintains and improves a motivating work environment, which includes the promotion of diversity, provides a fair nomination and compensation system and operates fairly, and establishes systems and a corporate culture that respects diversity.

#### n. Infringement of intellectual property rights

In order to achieve "quality top-line growth," the Group utilizes various intellectual properties, enhances product and service added value and actively acquires the rights to these intellectual properties. Under such circumstances, if an outside party infringes the Group's intellectual property rights, the Group's technology and brands may not be sufficiently protected, which in turn could lead to negative effects on the Group's business strategies and financial position. Or, if it is acknowledged that the Group's products and services have infringed on the intellectual property rights of an outside party, the Group may risk having to pay compensation for damages, or becoming unable to provide the products and services, which could negatively affect the Group's business strategies and the financial position.

In order to avoid the risk of infringement of the Group's intellectual property rights by an outside party, the Group prepares measures to acquire the rights of intellectual properties and appropriately manage its intellectual property rights. Furthermore, in order to prevent the infringement of the intellectual property rights of an outside party before it occurs, the Group responds timely and appropriately, such as by investigating and monitoring the status of intellectual property rights.

o. Environmental regulations

The Group carries out research and development and production, the processes of which are subject to a wide variety of legal restraints both in Japan and overseas related to environmental protection with respect to hazardous substances, waste and other effects. In the future, if environmental pollution or a similar problem occurs as a result of the Group's business activities, or if environmental regulations are introduced or existing ones are changed, the Group's business performance may be negatively affected due to factors such as being liable for damages for environmental pollution, the decline of corporate reputation, the incurring of additional expenses for capital expenditures, etc. to respond to regulations or restrictions on existing business activities.

In order to prevent environmental pollution, the Group continuously monitors the establishment and revision of environment-related laws and regulations, thoroughly observes environment-related laws and regulations, such as by making them well known to relevant departments, and appropriately responds as necessary. For example, the Group confirms the status of compliance with environment-related laws and regulations annually with internal audits in accordance with ISO 14001, primarily at manufacturing facilities. In addition, the Group establishes an even stronger environmental management system by being audited by an outside agency once every three years.

Furthermore, the Operational Review and Business Assurance Division of the Company and the auditing divisions of the Group companies in Japan perform environmental audits, and make evaluations from an objective viewpoint. The results of these audits are reported to management and shared with relevant departments, which leads to the improvement of the Group's overall environmental management system.

p. Information security

In the operation of business, the Group utilizes various types of information technology to efficiently perform business and operations. To that end, in the event that damage to systems, or leaks of confidential information occur as a result of unforeseen circumstances, such as attacks by illicit access or computer viruses, or disasters, the business performance of the Group may be negatively affected due to temporary suspension of information systems, the decline of public trust, the loss of competitive advantage and the bearing of expenses to appropriately respond to these events.

The Group has clarified its position on initiatives for information security, put in place a variety of rules in relation to information security in order to comprehensively and continuously promote information security measures, and works to protect and manage information assets, such as the systems and data owned by the Group, in an appropriate manner. Furthermore, the Group works to reinforce information security from the aspect of both hardware and software. In regard to hardware, the Group continuously carries out technological and operational inspections and improvements related to security for key systems. In regard to software, the Group works to educate employees on security, such as by carrying out information security e-learning that is applicable to all employees.

## **(2) Risks Relating to the Group Businesses**

### **Risks relating to the Tobacco Business**

a. Decreasing tobacco demand

In the Japanese domestic tobacco market, with the aging population and declining birth rate, growing awareness about the health risks associated with smoking and the tightening of smoking-related regulations, as well as higher tobacco excise taxes, tobacco demand has continued to decline and the Company expects this downward trend to continue unabated into the future. Demand overseas could also decrease depending on the economic conditions, other societal conditions, trends in regulations, price rises, tax increases and other factors, although the trends in demand will vary from region to region. Should demand decrease, sales volume may decrease, and this may negatively affect the Group's business performance.

In the tobacco business, the Group strives to provide products that can capture changes in consumer preferences and behaviors and optimize our product portfolio. While pursuing self-sustaining growth by adopting a balanced approach to investing in markets in which it already has a strong base, as well as in markets with high growth potential, the Group takes the view that searching for and exploiting growth opportunities through the acquisition of external resources is also a valuable strategic option, and it is working to secure positions in multiple markets capable of generating continuous profit, rather than in just one specific market. With regard to issues such as tax increases and strengthened smoking regulations, the Group is implementing measures such as gathering information on regulatory trends with greater speed and accuracy, actively cooperating in



policymaking that leads to fair and balanced regulation by engaging in constructive dialogue with government-affiliated participants (including regulators) and other stakeholders, setting prices appropriately so as to minimize the impact of higher taxation, and pursuing further cost efficiency.

#### b. Taxes levied on tobacco

In countries around the world, including Japan, governments are discussing increases in tobacco excise taxes to secure public finances and promote public health, and are actually raising taxes in some cases. Some countries, including Japan, are also implementing increases in taxes such as consumption tax or value-added tax (VAT) with the aim of improving public finances.

It is difficult to predict changes in the types of taxes or tax rates imposed on tobacco products in various countries, and if tax hikes are implemented at an unexpected timing, frequency or rate of increase, or in a region where tax hikes were not anticipated, the Group may be unable to react to such tax hikes promptly and appropriately.

Increases in tobacco taxes may, if accompanied by a hike in retail prices, push down demand, move consumers toward lower priced brands, or cause or increase illicit trade such as smuggling and counterfeiting. On the other hand, if there is no retail price hike, such tax increases may cause the earnings structure of the tobacco business to deteriorate. As such, either case may negatively affect the Group's business performance.

In the tobacco business, the Group is implementing measures such as offering products that match the changing preferences and behaviors of consumers, optimizing its product portfolio, securing positions in multiple markets capable of generating continuous profit rather than in just one specific market, gathering information on trends pertaining to tax increases with greater speed and accuracy, engaging in constructive dialogue with governments and regulators, setting prices appropriately so as to minimize the impact of higher taxation, and pursuing further cost efficiency.

In Japan, the Act for Partial Amendment of the Income Tax Act, etc. (Act No. 7 of March 31, 2018) and the Act for Partial Amendment of the Local Tax Act, etc. (Act No. 3 of March 31, 2018) were established as part of the 2018 Tax Reform. In addition, the Act for Partial Amendment of the Income Tax Act, etc. (Act No. 8 of March 31, 2020) and the Act for Partial Amendment of the Local Tax Act, etc. (Act No. 5 of March 31, 2020) were established on March 27, 2020 as part of the 2019 Tax Reform. For details, see “(3) Other Factors Which May Materially Affect Investment Decisions, c. Legal matters relating to the business of filing company, (iii) Acts relating to tobacco excise taxes (including tobacco special excise taxes), (iv) Taxation methods applied to tobacco products other than cigarettes.”

#### c. Regulations on tobacco products

- Situation overseas

The regulatory environment for tobacco is getting stricter year by year, in the wake of the Framework Convention on Tobacco Control (FCTC), which came into force in February 2005.

The purpose of the FCTC is to control continuously and substantively the proliferation of smoking. Its provisions include price and tax measures; non-price measures to reduce demand (including protection from passive smoking, testing and measuring the contents and emissions of tobacco products and their information disclosure, product packaging and labeling, regulations on tobacco advertising, promotion and sponsorship), and measures related to the reduction of tobacco supply (including prevention of illicit trade and prohibition of sale of tobacco products to minors). The Japanese government ratified the framework in June 2004.

All Parties to the FCTC are obligated to develop, implement, periodically update and review strategies, plans and programs for tobacco control. However, each party, has a right to determine the content, scope and specific implementation method of their own tobacco control. After coming into force, the Parties of FCTC continue their discussions through regularly holding the Conferences of the Parties (COP) in order to develop the protocols (for which additional ratification, acceptance, accession and other are required to the FCTC Parties) and guidelines in view of implementation of each FCTC provision.

Specific regulations are also undertaken in each country. For example, Russia, a key market of the JT Group, enacted the comprehensive tobacco control law in February 2013 and has gradually been implementing it since June 2013. The law includes a retail display ban; restrictions on sales of tobacco products in certain retail stores; a ban on advertising, sponsorship and promotions; the introduction of minimal pricing; a ban on smoking in public places; and anti-illicit trade measures.

In addition, the EU revised the EU Tobacco Product Directive (EU TPD) announced in July 2001 and it entered into force in May 2014. The revised Directive includes the tightening of packaging and labeling regulations; restrictions on the use of additives including menthol for cigarettes and Fine Cut; regulations related to electronic cigarettes; and anti-illicit trade measures. Each member state has introduced their national regulations based on the revised Directive.

Furthermore, the Australian government introduced plain packaging in December 2012, which prohibits displaying logos, brand images or promotional text on tobacco packages. The regulation only allows product names to be displayed in the prescribed color, font, font size and font color. Various countries including France, U.K. and others have also introduced and legislated similar regulations, while other countries have been discussing or determining its implementation.

For example, there are signs of increasing regulations on electronic cigarettes, such as the introduction of regulations banning the sale of some flavored electronic cigarettes by the U.S. federal government.

Although it is difficult to accurately predict the content of future laws and regulations relating to sales activities, marketing, packaging and labeling, tobacco products and smoking, the Group expects various regulations, including those like the ones above, to spread across Japan and other countries.

- Situation in Japan

The Tobacco Business Act, related acts and statutes and voluntary standards set forth the regulations for the sale and promotion activities of tobacco products in Japan that include the indication of warning labels on tobacco product advertisements and packages that urge caution over the relationship between the consumption of tobacco products and health.

In November 2003, the Ordinance for Enforcement of the Tobacco Business Act was revised including the wording of the cautions over the relationship between the consumption of tobacco products and health indicated on tobacco product packages and, starting July 2005, all tobacco products sold in Japan have been in conformity to the revised regulations. In addition, the Japanese Minister of Finance has indicated a “Guideline for Advertising of Tobacco Products” (hereinafter, “Advertising Guideline”) based on the Tobacco Business Act, Article 39 (warning labels) and Article 40 (recommendations, etc. relating to advertising). The Advertising Guideline was revised in March 2004 in accordance with the revision of the Ordinance for Enforcement of the Tobacco Business Act mentioned above (for details, see (3) c. (i), Notes 2 and 3 below).

The Tobacco Institute of Japan (TIOJ) has established voluntary standards regarding the advertising and sales promotion activities for tobacco products. We comply with these standards together with all other TIOJ members. In February 2016 under the Financial System Council tobacco business subcommittee meeting, a new labeling sub-committee was established, which performed a specialized investigation in relation to means of the Advertising Guideline. The labeling sub-committee reported the results of its investigation to the tobacco business subcommittee in June 2016, and as a result of further discussions conducted within the tobacco business subcommittee, “Review of Warning Labels Regulations / Advertising Regulations” was published on December 28, 2018. Based on the aforementioned review and a promulgation of a partial amendment of the Ordinance for Enforcement of the Tobacco Business Act; the Advertising Guideline; and Related Notices of the Tobacco Business Act on June 14, 2019, the Tobacco Institute of Japan revised the voluntary standards on the same day (for details of the amendment of the Ordinance for Enforcement of the Tobacco Business Act and the Advertising Guideline, see (3) c. (i), Notes 4 and 5 below). There are four criteria in this revision: the revision of standards for tobacco products; establishment of new rules for T-Vapor products; establishment of new rules for T-Vapor devices; and establishment of new rules for business activity relating to tobacco and television advertising to advocate the improvement of smoking manners.

With regard to the caution on tobacco product packages, the revision required (a) caution statement changes on tobacco product packages by July 1, 2020 and (b) more restrictive advertisement measures for tobacco products. The changes in (a) included wording revision, which reflects the latest scientific knowledge, and increasing the area of the statements at least 50% on the surface. With regard to (b), the measures included more effective ways to prevent minors’ access to internet advertisements and new restrictions on the size and presentation methods for point-of-sale advertising.

The enactment of the Partial Amendment of the Health Promotion Act (Act No. 78 of July 25, 2018) (hereinafter, the “Act”) in July 2018 strengthened measures to prevent unwanted passive smoking at facilities used by numerous people. The Act classifies the facilities into three types in terms of measures to take: Facility Type 1 includes schools, hospitals and administrative agencies; Facility Type 2 includes restaurants, offices, factories and any other facilities that do not fall under Facility Type 1 or facilities whose main purpose is not for smoking; and other facilities that do not fall in Facility Type 1 or 2 whose main purpose is to provide a place for smoking (includes public smoking areas, bars that are mainly for smoking, and tobacco retailers where

on-premise smoking is allowed). Facility Type 1 prohibits smoking within its site but allows designated outdoor smoking areas if they meet all of the requirements. Facility Type 2 prohibits indoor smoking but allows designated smoking rooms, etc. after meeting certain criteria. Additionally, a restaurant can allow indoor smoking once it meets certain requirements. Facilities whose main purpose is to provide a place for smoking allow smoking within their sites. The Act was enacted fully on April 1, 2020, and the Group recognizes that the number of smoking places will diminish as a result. The Group forecasts a certain level of impact on its business performance while it is difficult to predict the anticipated changes in smoking environment.

- Impact on the Group's business performance

Although it is impossible to predict the content of future laws, regulations and industry guidelines relating to sales activities, marketing, packaging and labeling, tobacco products and smoking, the Group expects regulations like the above and new regulations (including those of local governments) to diffuse across Japan and other countries where the Group sells its products.

The Group's position is to support any regulation relating to tobacco that is appropriate and reasonable. Nevertheless, if regulations such as those mentioned above are tightened, or if the Group is unable to respond to this tightening of regulations in a timely and appropriate manner, subsequent declines in tobacco demand or market share, costs for compliance with new regulations or other factors may negatively affect the Group's business performance. In the tobacco business, the Group is implementing measures such as gathering information on regulatory trends with greater speed and accuracy, and engaging in constructive dialogue with governments, regulators, and various stakeholders.

#### d. Illicit trade such as smuggling and counterfeiting

The Group has formulated a sustainability strategy, and each business has also set out its own focus areas and works continuously on a variety of sustainability issues. In the tobacco business, the Group has selected Regulatory Environment and Illicit Trade as one of its focus areas, and is working to execute countermeasures. One of the most serious issues in the tobacco industry is the increase of illicit trade, including smuggling and counterfeit product distribution. Motivations for illicit trade are believed to include the high profit margin of tobacco products and cross-border price gaps arising from different taxation systems and tax levels among countries. As historical evidence shows, illicit trade in a market tends to increase after a steep tax increase.

Illicitly traded products not only significantly damage the credibility of brands and the companies that own those brands, but also negatively affect governments' tax revenues. Therefore, the Group and other tobacco companies are working together with governments to eliminate illicit trade.

The Group is making efforts towards countermeasures, such as by concluding cooperation agreements to counter illicit trade with the EU (including its member countries) and the governments of Canada and all its provinces and territories, respectively. Even so, growth in illicit trade such as smuggling and counterfeiting of tobacco products may negatively affect the Group's business performance because of consequences including damage to its brand equity or the need for substantial expenses for countermeasures and the like to eliminate illicit trade. In order to protect consumers and society, as well as the business and the reputation of the Group, the Group has formed an Anti-Illicit Trade team that works to prevent illicit trade. The Anti-Illicit Trade team works with the Group's various markets to prevent genuine products being diverted into illegal channels, and cooperates with law enforcement to remove illegal tobacco products from the marketplace. Making use of public-private partnerships, the team maintains proactive dialogues with governments and law enforcement authorities in various countries in relation to the threat posed by illicit trade, and has established programs around the world to educate law enforcement on how to recognize counterfeit products.

The Group also deploys and operates a Track and Trace system for tobacco products, enabling it to track and analyze the movement of products through the supply chain. For more than a decade, this Track and Trace system has played an important role in our compliance policy, and although it was at first a voluntary initiative, legislation has recently been drawn up to make such Track and Trace systems mandatory. In addition to systems already deployed in the United Arab Emirates, Saudi Arabia and Russia, an EU directive for the first regional-level tobacco products Track and Trace system applicable to all member states came into force in May 2019.

Furthermore, in accordance with our rigorous compliance policy, the Group implements measures to prevent illicit trade, such as by dealing only with reputable business partners, and raising awareness among consumers of the negative impact of purchasing unregulated products.

## Risks relating to the Pharmaceutical Business

### a. Research and development, manufacture and sale of pharmaceutical products

The Pharmaceutical Business engages in research and development so as to swiftly provide original and revolutionary new drugs to patients around the world. New drug development requires the Group to invest enormous amounts of time and money, and the hurdles to discovering new drugs become higher every year. In some cases development is delayed or canceled when the anticipated results in terms of efficacy and safety cannot be confirmed during development or when unexpected side effects occur during development. Such cases may have a negative impact on the performance of the Group by failing to achieve the expected investment returns, or by delaying said returns, amongst other effects.

In addition, although the pharmaceuticals thus developed undergo stringent examinations before being approved by the governmental agencies with jurisdiction in various countries around the world, if unexpected side effects and the like are discovered after the product goes on sale that subsequently develop into a suspension of sales or a product recall, such a situation could negatively impact the performance of the Group by causing a decline in revenue, the occurrence of expenses related to the suspension of sales or product recall, or the decline of public trust in the Group.

The Pharmaceutical Business maximizes effective use of its resources by focusing on fields of treatment where it can leverage the small-molecule drug knowledge and platform that it has built up over the years, and is also working to shorten research and development time, and reduce R&D costs, by utilizing AI and data science to improve the efficiency of drug discovery research. Furthermore, through collaborative initiatives with companies and academic institutions in Japan and overseas aimed at establishing proprietary drug discovery technology, the Pharmaceutical Business seeks to construct a stable earnings base by accelerating R&D, raising the hit rate for drugs discovered, and broadening the pipeline by actively licensing and adopting new compounds.

With regard to side effects, the Pharmaceutical Business collects and evaluates safety information after pharmaceutical products are launched, and takes other measures necessary to ensure the safety and appropriate use of its pharmaceutical products.

### b. Regulation and healthcare policy

The Pharmaceutical Business operates under regulations, imposed by the policies of various countries, that seek to ensure the quality, effectiveness and safety of pharmaceutical products. The environment in which the pharmaceutical industry operates is expected to remain challenging, due to such factors as attempts by various governments to control healthcare costs, and the drastic reform of the drug pricing system in Japan. In the event that pharmaceutical regulations are made more stringent, the Group may incur additional costs to ensure that products comply with strengthened rules. In the event of drug prices being lower than expected as a result of trends in healthcare systems or regulatory policies, including reform of drug price standards, Group revenue may decline. In either case there would be negative effects on the performance of the Group.

The Pharmaceutical Business is working on other appropriate measures to deal with these issues, in addition to following pharmaceutical regulations and drug price standards, such as continuous monitoring of regulatory trends to get a grasp of the details of amendments at an early stage. With regard to drug prices, in addition to continuously creating innovative products, the Pharmaceutical Business is putting together the evidence that demonstrates the scientific basis for the value they provide.

### c. Dependency on specific licensees/contract manufacturers

The Group's Pharmaceutical Business has been striving to make stable profit contribution to the Group through the promotion of R&D on next-generation strategic products and by maximizing the value of each product. With regard to research and development, the Group is further broadening pre-clinical research themes as well as constructing a high-precision research strategy that emphasizes "first in class" discoveries. Its aim is to use these to drive forward R&D for next-generation strategic products, while implementing initiatives at the perfect time to maximize the value of licensing activities for proprietary compounds, and cooperating closely with licensing partners. In addition, manufacture of each product is contracted to external manufacturers, and the Group seeks to maintain close relationships with these companies. In the event that agreements with these contract manufacturers are changed or terminated, or in the event that the partnership suffers from delays or

congestion, the returns expected at the point at which the agreement was concluded may not be achieved, or returns may be delayed, with a resulting negative impact on the performance of the Group.

When considering a partnership, the Pharmaceutical Business makes a judgment as to whether to approve or reject based on a multilateral analysis and evaluation. When concluding an agreement, it anticipates risks that could emerge, and engages in discussions to form a consensus on how to mitigate them. In addition, even during a partnership it seeks to enhance the quality of the relationship by working continuously to maintain and develop it further.

#### Risks relating to the Processed Food Business

##### a. Food safety and quality

The mission of the Processed Food Business is to provide consumers with safe and high-quality food. The frozen and ambient foods business, the seasonings business, and the bakery business that make up the three core operations are each responsible for food safety control functions, and take all possible measures to ensure food safety control during the operation of the business. However, in the event that problems related to food safety or quality occur that exceed those anticipated by the Group, in addition to a decline or impairment of public trust in the Group, costs related to product recalls and demands for compensatory damages may be incurred, which could negatively impact performance.

In addition to conducting continuous quality assurance activities aimed at providing safe and secure products from the four perspectives of Food Safety, Food Defense, Food Quality, and Food Communication, the Processed Food Business confirms their effectiveness through periodic audits. With the objective of constructing a management system platform to achieve the highest levels of food safety, the Company has drawn up policies, rules and guidelines related to food safety control for the Processed Food Business as a whole, and monitors the initiatives of each operating company in their operation. In addition, excluding one factory that began operations in fiscal 2020, all of the Group's factories inside and outside Japan, as well as the Group's business partners' factories that produce frozen foods, have achieved certification under the ISO 22000 or FSSC 22000 international standards for food safety management. The one remaining factory is currently in the process of obtaining certification for both ISO 22000 and FSSC 22000.

##### b. Food regulations

The Processed Food Business is subject to a variety of legal restrictions, such as the Food Safety Basic Act, the Food Sanitation Act, and the Food Labeling Act. The mission of the Processed Food Business is to provide consumers with safe and high-quality food, and the Group operates a thorough program of compliance to ensure conformity with all these legal restrictions. However, in the event that legal restrictions are introduced or changed, additional costs may be incurred to comply with these regulations, or existing business activities may be restricted, leading to a negative impact on the Group's business performance.

In addition to conducting advance preparations by continuously monitoring for regulatory introductions and amendments, gathering information as appropriate, and considering additional countermeasures, the Processed Food Business responds to circumstances as required.

### **(3) Other Factors Which May Materially Affect Investment Decisions**

##### a. Relations with the Japanese government and the Minister of Finance

The JT Act obligates the government to continue to hold more than one-third of all the Company's shares issued. As of December 31, 2020, the government held 33.35% of all the Company's shares issued. As a consequence, the Japanese government is able to have a substantial influence on proposals for ordinary resolutions at the Company's General Meetings of Shareholders such as the election of Members of the Board. Furthermore, the Japanese government has the veto power for special resolutions for such actions as mergers, capital reductions or amendments to the Articles of Incorporation.

In addition, the Minister of Finance has the authority to supervise the Company under the JT Act and Tobacco Business Act. Under the JT Act, the scope of the Company's businesses includes the "manufacture, sale and importation of tobacco products and ancillary businesses, as well as businesses required for attaining the objective of the Company," and "business required for attaining the objective of the Company" are subject to the Minister of Finance's approval. Consequently, the Minister of Finance's approval is required in order for the Company to engage in new businesses outside the scope of currently-approved businesses (for details, see c. (ii) below).

As mentioned above, in addition to the Japanese government's rights as a shareholder of the Company, the government has the authority to supervise the Company and other powers under the JT Act and Tobacco Business Act. Since it cannot be guaranteed that the interests of the government will always coincide with the interests of other shareholders, this may have a negative effect on the interests of other shareholders.

Under the "Act on Special Measures for Securing Financial Resources Necessary for Reconstruction from the Great East Japan Earthquake," which was promulgated on December 2, 2011, the government makes it a principle to secure revenue to fund reconstruction resources until the fiscal year ending March 31, 2023. To this end, it is required for an examination to be made of the feasibility of selling the Company's shares by reassessing the framework under which the government holds the shares, while taking into consideration the framework of the country's commitment to tobacco-related business based on the Tobacco Business Act and the like.

#### b. Purchasing of leaf tobacco

The Tobacco Business Act requires the Company to annually enter into purchase contracts with tobacco growers regarding the aggregate cultivation area for specific varieties of leaf tobacco and the prices for leaf tobacco by variety and grade. The Company must purchase all leaf tobacco produced pursuant to such contracts, except for any not suited for the manufacture of tobacco products. When the Company decides the aggregate cultivation area and the prices of leaf tobacco for its contracts with tobacco growers, it is required to respect the opinion of the Leaf Tobacco Council (hatabako shingi kai), which consists of members appointed by the Company with the approval of the Ministry of Finance from among the representatives of domestic leaf tobacco growers and academic appointees (for details, see c. (i) below). Much like many other agricultural products in Japan, production costs for domestically-grown leaf tobacco is higher than those of foreign-grown leaf tobacco to the extent that the purchasing price for the former (before redrying) is approximately three times that of the latter (after redrying). The obligation to purchase virtually all leaf tobacco produced in Japan may adversely impact the Group's relative competitiveness in Japan because other global tobacco companies use foreign-grown leaf tobacco only.

c. Legal matters relating to the business of filing company

(i) Tobacco Business Act (Act No. 68 of August 10, 1984)

	Description
1. Purpose	The object of this Act is, in consideration of the tax relating to tobacco products as a portion of the treasury revenue incidental to the abolishment of the tobacco monopoly system, to promote a sound development of the tobacco industry in our country by making necessary adjustments in the production and purchase of domestically produced leaf tobacco as raw material for tobacco products and in business activities etc. of manufacture and sale of the tobacco products, whereby it will contribute to ensuring treasury revenue and a sound development of the national economy. (Article 1)
2. Cultivation and purchase of domestically grown leaf tobacco for use as raw material	<p>(1) When intending to purchase the domestically produced leaf tobacco, Japan Tobacco Inc. (hereinafter, “JT”) shall enter into agreements in advance with those who intend to cultivate leaf tobacco for the purpose of selling it to JT regarding the cultivation area for each item of leaf tobacco and the prices for each item and each grade of the leaf tobacco. (Article 3)</p> <p>(2) JT shall purchase all leaf tobacco produced pursuant to such agreements, except those which are not suitable as raw materials for manufacture red tobacco. (Article 3)</p> <p>(3) In the case where JT intends to enter into an agreement, JT shall consult with the Leaf Tobacco Council that JT establishes, and respect its opinion concerning the total cultivation area and the prices of leaf tobacco. (Articles 4 and 7)</p> <p>(4) The Leaf Tobacco Council shall deliberate on the price of the leaf tobacco so that subsequent production of leaf tobacco is ensured, by taking into account the production costs, commodity prices and other economic conditions. (Article 4)</p> <p>(5) JT shall determine the regional breakdown of the aggregate cultivation area for the respective items of leaf tobacco seeking the opinion of the Japan Tobacco Growers Association (hereinafter, “JTGA”) and, within the scope of such regional breakdown, enter into agreements with growers. (Article 5)</p> <p>(6) If a member grower of a tobacco growers association entrusts JTGA with entering into an agreement regarding a fundamental matters of the agreements such as the price of leaf tobacco, JT shall establish said fundamental matters with JTGA and such agreement shall be deemed as a part of the agreements executed between JT and said grower. (Article 6)</p>
3. Manufacture of tobacco products	<p>(1) No tobacco products shall be manufactured by any party other than JT. (Article 8)</p> <p>(2) JT shall obtain the approval of the Minister of Finance on the maximum wholesale price for each item of tobacco products. (Article 9)</p> <p>(3) JT shall make efforts to ensure a smooth supply of tobacco products taking into account regional demand conditions for tobacco products. (Article 10)</p>
4. Sale of tobacco products	<p>(1) A party wanting to engage in the sale of tobacco products imported by themselves shall register with the Minister of Finance, who establishes necessary regulations relating to said registration and registered party (hereinafter, “Specified Distributor”). (Articles 11 to 19)</p> <p>(2) A party wanting to engage in the wholesaling of tobacco products shall, for the time being, register with the Minister of Finance, who establishes necessary regulations relating to said registration and registered party. (Articles 20 and 21)</p> <p>(3) A party wanting to engage in the retailing of tobacco products shall, for the time being, obtain the approval of the Minister of Finance, who establishes necessary regulations relating to said registration and registered party (hereinafter, “Retailer”). (Articles 22 to 32)</p> <p>(4) If JT and a Specified Distributor want to sell manufactured or imported tobacco products, the list price of each item, and any subsequent change thereof, shall be approved by the Minister of Finance for the time being. Necessary regulations are in place with respect to the approval: for example, the Minister of Finance shall grant approval unless it deems such price is unfair to consumers, etc. (Articles 33 to 35) <sup>(Note 1)</sup></p> <p>(5) A Retailer is only permitted to sell tobacco products at list prices that have been approved by the Minister of Finance. (Article 36)</p>

	Description
5. Other	<p>(1) JT or a Specified Distributor shall indicate the wording as prescribed by Ordinance of the Ministry of Finance for warning consumers of the relationship between the consumption of tobacco products and health prior to the commencement of sale of the tobacco products that it manufactured or imported. (Article 39) <sup>(Notes 2, 4)</sup></p> <p>(2) Advertisers of tobacco products shall give due consideration to the prevention of smoking by minors, etc. and make efforts lest such advertisement should be made to an excessive extent. The Minister of Finance may implement necessary measures with respect to advertisers. (Article 40) <sup>(Notes 3, 5)</sup></p>

Notes: 1. The so-called list price system is maintained for the time being as a means to prevent confusion in the distribution order, a well-established constant that materialized after the list price system was adopted in 1904.

Tobacco is a luxury item different from the so-called public property and public services and, in a distribution market completely liberalized after the opening of import markets and other factors, the Company and Specified Distributors stipulate prices on application (POA) to the Minister of Finance based on their respective, independent management decisions.

Concerning the approval of list prices, the Company understands that a government delegate gave the following explanation of the gist of the process at the 1984 Diet deliberations on the proposed Tobacco Business Act:

Pertaining to tobacco product list prices, under the Tobacco Business Act, in the event an application is made for the approval of list prices, the Minister of Finance may exceptionally deny approval if it deems such list price unfair to consumers or unfairly low in comparison with wholesale prices of domestic products or import prices of imported products. In all other cases, the Minister approves list prices in line with the spirit of Tobacco Business Act.

2. In November 2003, the Ordinance for Enforcement of the Tobacco Business Act was revised and the wording of warnings concerning tobacco consumption and health indicated on tobacco product packages was changed to specify risks related to eight items, four of which are diseases associated with direct smoking (lung cancer, heart attack, stroke and emphysema), while the other four are smoking by pregnant women, passive smoking, addiction to smoking and youth smoking. Each tobacco product package must indicate, on its main surfaces, a warning regarding at least one of the four items associated with direct smoking and at least one of the other four items. The Ordinance stipulates, among others, (1) that these warnings must be rotated throughout the year in ways to ensure that they receive equal exposure on each product item and each type of package and (2) that the display must occupy 30% or more of the main surfaces of the package. In addition, the Ordinance stipulates that when wording like “mild” and “light” are used on the package, they must be accompanied by a warning that clarifies that such words do not mean that the risk to their health is lower than other tobacco products so as to prevent consumers from misunderstanding the relationship between the consumption of tobacco products and health. The Company has been adhering to this rule since July 1, 2005.
3. In March 2004, the “Guideline for Advertising of Tobacco Products” was revised to stipulate that the outdoor advertising of tobacco products (posters, billboards, etc.) shall generally be prohibited. It also specifies matters concerning the presentation and content of the health warnings that accompany tobacco advertising.
4. In June 2019, the Ordinance for Enforcement of the Tobacco Business Act was revised and the wording of warnings concerning tobacco consumption and health indicated on tobacco product packages was changed. According to the revision of this Ordinance, new warnings were established for T-Vapor products. Also, the Ordinance stipulates that a tobacco product package must indicate, on its front main surface, warnings about the effects on others and, on its back main surface, warnings about the prevention of smoking by minors, (persons under 20 years of age) and the effects on the smoker. The display of these warnings must occupy 50% or more of each main surface of the package. In addition, the Ordinance stipulates that when wording like “mild” and “light” are used on the package, they must be accompanied by a warning on the front main surface of the package that clarifies that such words do not mean that the risk to their health is lower than other tobacco products. Because the display of nicotine and tar levels on tobacco product packages may mislead consumers into thinking that the displayed levels indicate a lower risk to their health, the Ordinance also stipulates that the package must indicate that the actual intake levels of nicotine and tar could vary from the displayed levels depending on the consumer’s smoking style. The display of these warnings is required for T-Vapor products and cigarettes with a certain volume (cigarette sales volume of 100 million or more from April 2018 to March 2019) shipped from April 1, 2020 and for other products shipped from July 1, 2020.
5. In June 2019, the “Guideline for Advertising of Tobacco Products” was revised to limit the locations where tobacco products can be advertised and, excluding distribution by mail, etc., where tobacco product samples, leaflets, brochures, pamphlets, etc. can be distributed to locations where tobacco products are sold, designated smoking areas and locations restricted to use by adults only. It also specifies matters concerning the presentation and content of the health warnings that accompany tobacco advertising and the matters concerning the devices used to heat T-Vapor products.



(ii) Act on Japan Tobacco Inc. (Act No. 69 of August 10, 1984)

	Description
1. Purpose	Japan Tobacco Inc. (“JT”) is a stock company whose purpose is to engage in business related to the manufacture, sale, and importation of tobacco products in order to attain the objectives set forth in Article 1 of the Tobacco Business Act. (Article 1)
2. Stock	<p>The Japanese government must continue to hold more than one-third of all Japan Tobacco Inc. (“JT”) shares issued (excluding shares of a class for which it is provided that the voting rights may not be exercised for all the matters that are subject to resolution at the General Meeting of Shareholders; the same shall apply to the following items). (Article 2, paragraph 1)</p> <p>Whenever JT intends to solicit subscribers for an issuance of shares or subscription rights to shares of JT, or deliver shares (excluding own shares), subscription rights to shares (excluding subscription rights to treasury shares), or issuance of bonds with subscription rights to shares (excluding bonds with subscription rights to treasury shares) at the time of share exchange or delivery, the approval of the Minister of Finance is required. (Article 2, paragraph 2)</p> <p>The disposal of JT shares held by the government shall be effectuated within the maximum range stipulated by resolution of the Diet based on the budget of the corresponding year. (Article 3)</p>
3. Scope of business	<p>JT shall engage in the following businesses in order to attain the objectives stated in 1 above.</p> <ol style="list-style-type: none"> <li>(1) business of manufacture, sale and importation of tobacco products</li> <li>(2) business incidental or relating to the business in the preceding item</li> <li>(3) other business required for attaining the object of JT</li> </ol> <p>JT shall obtain authorization from the Minister of Finance before engaging in any business corresponding to (3) above. (Article 5)</p>
4. Monitoring	<ol style="list-style-type: none"> <li>(1) The appointment or dismissal of Members of the Board, Executive Officers (<i>sikkoyaku at a company with committees</i>), and Audit &amp; Supervisory Board Members require authorization from the Minister of Finance. (Article 7)</li> <li>(2) Amendments to JT’s articles of incorporation, appropriations of surplus (except disposal of losses), and any merger, corporate split, or dissolution of JT require authorization from the Minister of Finance. (Article 8)</li> <li>(3) JT shall formulate a business plan prior to each business year and obtain authorization from the Minister of Finance. Any change thereof also requires authorization from same. (Article 9)</li> <li>(4) Within three months after the closing of each business year, JT shall issue its balance sheet, statement of income, and business report to the Minister of Finance. (Article 10)</li> <li>(5) Transfers of manufacturing facilities or similar material assets require authorization from the Minister of Finance. (Article 11)</li> <li>(6) The Minister of Finance shall monitor JT in accordance with this Act as well as the Tobacco Business Act and may implement necessary measures in the execution of same. (Articles 12 and 13)</li> </ol>

## (iii) Acts relating to tobacco excise taxes (including tobacco special excise taxes)

	Description			
	National Tobacco Excise Tax	National Tobacco Special Excise Tax	Local Tobacco Excise Tax	
1. Tax item <sup>(Note 1)</sup>	Tobacco Excise Tax	Tobacco Special Excise Tax	Prefectural Tobacco Excise Tax (also applies to Tokyo)	Municipal Tobacco Excise Tax (also applies to special wards)
2. Taxpayers <sup>(Note 2)</sup>	Manufacturers of tobacco products or those who removes tobacco products from bonded areas		Manufacturers of tobacco products, specified distributors or wholesalers selling to retailers	
3. Tax base <sup>(Note 3)</sup>	Number of cigarettes removed from the manufacturing site or bonded area (for tobacco products other than cigarettes, prescribed cigarette count conversion)		Number of cigarettes relating to sales to retailers (for tobacco products other than cigarettes, prescribed cigarette count conversion)	
4. Tax rate <sup>(Notes 4, 5)</sup>		¥6,302 per 1,000 cigarettes	¥820 per 1,000 cigarettes	¥1,000 per 1,000 cigarettes
	On and after October 1, 2021	¥6,802 per 1,000 cigarettes	¥820 per 1,000 cigarettes	¥1,070 per 1,000 cigarettes
5. Declaration and payment <sup>(Note 6)</sup>	Tobacco product manufacturers are to declare and pay taxes for each month's shipment by the end of the following month. Parties removing tobacco products from bonded areas are to declare and pay taxes by the time of extraction		For sales of tobacco products relating to sales locations of retailers located within a given prefecture, a declaration and payment of taxes is to be made to that prefecture for each month's transfer by the end of the following month	For sales of tobacco products relating to sales locations of retailers located within a given municipality, a declaration and payment of taxes is to be made to that municipality for each month's transfer by the end of the following month

- Notes: 1. Article 3 of the Tobacco Excise Tax Act, Article 4 of the Act Concerning Special Measures for Financing Debt Transferred to the General Accounts, and Article 1, paragraph 2 and Articles 4 and 5 of the Local Tax Act
2. Article 4 of the Tobacco Excise Tax Act, Article 5 of the Act Concerning Special Measures for Financing Debt Transferred to the General Accounts, and Article 74-2, paragraph 1 and Article 465, paragraph 1 of the Local Tax Act
3. Article 10 of the Tobacco Excise Tax Act, Article 7 of the Act Concerning Special Measures for Financing Debt Transferred to the General Accounts, and Articles 74-4 and 467 of the Local Tax Act
4. Article 11, paragraph 1 of the Tobacco Excise Tax Act, Article 8, paragraph 1 of the Act Concerning Special Measures for Financing Debt Transferred to the General Accounts, and Articles 74-5 and 468 of the Local Tax Act
5. Concerning "4. Tax rate"
- As a result of the 2018 Tax Reform, national and local tobacco excise tax rates were reviewed and revised in stages after October 1, 2018, and new tax rates were applied on October 1, 2020. Further changes to the tax rates are scheduled on and after October 1, 2021.
- As a result of the Act for Partial Amendment of the Income Tax Act, etc. (Act No. 9 of March 31, 2015) and the Act for Partial Amendment of the Local Tax Act, etc. (Act No. 2 of March 31, 2015), special tax rates for former third-class products (those equivalent to the type of tobacco products stipulated as third-class cigarettes in the Tobacco Product Price Act that was repealed on April 1, 1985) were abolished on October 1, 2019.
6. Articles 17 to 20 of the Tobacco Excise Tax Act, Article 12 of the Act Concerning Special Measures for Financing Debt Transferred to the General Accounts, and Articles 74-10 and 473 of the Local Tax Act
7. In the event the tax system relating to tobacco subject to high excise taxes is examined, on a general basis, as part of a revision of the tax system by the government each year and the tax system is revised, a decision is made upon the deliberation and resolution of the legislature subsequent to the determination of government policy through deliberation by the Tax System Council and other bodies. Relevant government policy is determined once cabinet approval of a bill is secured following the cabinet's approval of an outline of the tax reform proposal.

(iv) Taxation methods applied to tobacco products other than cigarettes

The tax base for the tobacco excise tax is held to be the number of cigarettes, but based on the fact that the number of tobacco products other than cigarettes is not understood, the following tobacco product categories are converted into the equivalent of single cigarettes, based on the respective category weights.

Classification	Tax base	Conversion method
Tobacco products for smoking		
Pipe tobacco	Number of cigarettes resulting from conversion by weight	Converted at the rate of 1 g per cigarette
Cigar tobacco		
Flake tobacco		Converted at the rate of 2 g per cigarette
Heated tobacco	Separate (refer to the figure below)	
Chewing tobacco products	Number of cigarettes resulting from conversion by weight	Converted at the rate of 2 g per cigarette
Snuff products		

Note: The review of tobacco excise tax caused by the 2020 Tax Reform resulted in a review of the tax base for little cigars (a cigar contains less than 1 g of tobacco per cigar). For details refer to Note 2 for [Main movements relating to the tobacco tax system and the Company's responses] below.

Heated tobacco products were categorized as “pipe tobacco” before the 2018 Tax Reform, and were converted to cigarettes at the rate of 1 g per cigarette, with the cigarette excise tax rate being applied to the resulting number. After the reform a new tax category was established for heated tobacco on October 1, 2018, with these tobacco products being converted to cigarettes at a rate prescribed by the new conversion methods described below. Moreover, with regard to the review of the form of excise taxation for such heated tobacco products, transitional measures have been devised to allow staged implementation between October 1, 2018 and October 1, 2022.

Tax base of heated tobacco			Conversion method
Conversion method before reform	Number of cigarettes resulting from conversion by weight	(A)	Heated tobacco is converted at the rate of 1 g per cigarette
Conversion method after reform	Number of cigarettes resulting from conversion by weight and price	(B)	The prescribed weight of heated tobacco <sup>(Note 1)</sup> of 0.4 g converts to 0.5 cigarettes
		(C)	Based on the average retail price per cigarette <sup>(Note 2)</sup> , the retail price of heated tobacco (excluding the equivalent of consumption tax) is converted to 0.5 cigarettes.

Notes: 1. Weight does not include weight of filter and certain other goods

2. Calculated by dividing the total of the national and local tobacco excise tax per cigarette, and a figure equivalent to tobacco special excise tax, by 60%

		Conversion volume during the transitional measures period (tax base)
On and before September 30, 2018		(A) × 1.0
Revision	October 2018	(A) × 0.8 + {(B) + (C)} × 0.2
	October 2019	(A) × 0.6 + {(B) + (C)} × 0.4
	October 2020	(A) × 0.4 + {(B) + (C)} × 0.6
	October 2021	(A) × 0.2 + {(B) + (C)} × 0.8
	October 2022	{(B) + (C)} × 1.0

[Main movements relating to the tobacco tax system and the Company's responses]

Month/Year	Item	Description	The Company's response
May 1986	1986 Tax Reform	Tax increase equivalent to ¥900 per 1,000 cigarettes	Fixed price revised by amount equivalent to tax increase
April 1989	1989 Tax Reform	Following the introduction of the consumption tax, "tobacco consumption tax" changed to "tobacco excise tax" and taxation formula unified to a unit tax	Basically, fixed price revision unnecessary
April 1997	1997 Tax Reform	[Revision of Local Tax Act] Local Tobacco Excise Tax revenue transferred from the Prefectural Tobacco Excise Tax to the Municipal Tobacco Excise Tax	Fixed price revision unnecessary
		[Revision of Consumption Tax Act] Consumption tax rate revised from 3% to 5%	Prices raised by ¥10 per pack for some brands in an effort to revise fixed prices overall by the amount equivalent to the consumption tax rate revision
December 1998	1998 Tax Reform	Act Concerning Special Measures for Financing Debt Transferred to the General Accounts established and ¥820 per 1,000 cigarettes of Tobacco Special Excise Tax introduced	Basically, price per cigarette raised by ¥1
May 1999	1999 Tax Reform	[Revision of Special Taxation Measures Act and Local Tax Act] Tax revenue transferred from Tobacco Excise Tax to Prefectural Tobacco Excise Tax and Municipal Tobacco Excise Tax	Fixed price revision unnecessary
July 2003	2003 Tax Reform	Acts revising portions of the Income Tax Act, Local Tax Act, among others, established and tax increase by ¥820 per 1,000 cigarettes	Price per cigarette raised by approx. ¥1
July 2006	2006 Tax Reform	Acts revising portions of the Income Tax Act, Local Tax Act, among others, established and tax increase by ¥852 per 1,000 cigarettes	Amount equivalent to tax increase shifted to fixed price of all brands with some prices increased higher than said amount
October 2010	2010 Tax Reform	Acts revising portions of the Income Tax Act, Local Tax Act, among others, established and tax increase by ¥3,500 per 1,000 cigarettes	With exception of some brands, prices increased higher than the amount equivalent to tax increase
April 2014	2014 Tax Reform	[Revision of Consumption Tax Act] Consumption tax rate revised from 5% to 8%	With exception of some brands, prices raised by ¥10 or ¥20 per pack to revise fixed prices overall by the amount equivalent to the consumption tax rate revision
April 2016	2015 Tax Reform	Acts revising portions of the Income Tax Act, Local Tax Act, among others, established and tax increase by ¥1,000 per 1,000 cigarettes for former third-class products	For former third-class products, prices raised by ¥30 to ¥50 per pack
April 2017	2015 Tax Reform	Based on 2015 Tax Reform, tax increase by ¥1,000 per 1,000 cigarettes for former third-class products	For former third-class products, prices raised by ¥30 per pack
April 2018	2015 Tax Reform	Based on 2015 Tax Reform, tax increase by ¥1,500 per 1,000 cigarettes for former third-class products	For former third-class products, prices raised by ¥40 per pack

Month/Year	Item	Description	The Company's response
October 2018	2018 Tax Reform	Tax increase based on 2018 Tax Reform (Note 1)	With exception of some brands, prices increased higher than the amount equivalent to tax increase
October 2019	2015 Tax Reform	Based on 2015 Tax Reform, tax increase by ¥3,932 per 1,000 cigarettes for former third-class products	For former third-class products, prices raised by ¥90 per pack
	2018 Tax Reform	Tax increase based on 2018 Tax Reform (Note 1)	With exception of some brands, prices increased by a margin lower than the amount equivalent to tax increase
	2019 Tax Reform	[Revision of Consumption Tax Act] Consumption tax rate revised from 8% to 10%	Prices raised by ¥10 per pack for some brands in an effort to revise fixed prices overall by the amount equivalent to the consumption tax rate revision
October 2020	2018 Tax Reform	Tax increase based on 2018 Tax Reform (Note 1)	With exception of some brands, prices increased higher than the amount equivalent to tax increase
	2020 Tax Reform	Tax increase based on 2020 Tax Reform (Note 2)	With exception of some brands, prices increased higher than the amount equivalent to tax increase

- Notes: 1. The review of tobacco excise tax caused by the 2018 Tax Reform resulted in an increase in the national and local tobacco excise tax rate of ¥3,000 per 1,000 cigarettes, with the establishment of a new tax category for heated tobacco, and a review of the form of excise taxation based on the characteristics of these products. These reviews, viewed from the perspective of mitigating radical change, etc., have been respectively devised as transitional measures, with the former implemented in three stages, in which each stage consists of a ¥1,000 increase per 1,000 cigarettes between October 2018 and October 2021 (with no increase in the rate of excise tax in October 2019), and with the latter implemented in five stages between October 2018 and October 2022.
2. In terms of revisions to the tobacco excise tax arising from the 2020 Tax Reform, the tax base for little cigars (a cigar contains less than 1 g of tobacco per cigar) was revised to specify that one little cigar be converted into the equivalent of one cigarette. Although the results of these reviews came into force on October 1, 2020, from the perspective of mitigating radical change, etc., the proposals apply only to cigars that contain less than 0.7 g of tobacco per cigar, and in this case, a method for converting one cigar into the equivalent of 0.7 cigarette shall be used as a transitional measure from October 1, 2020 to September 30, 2021.

### 3. Management Analysis of Financial Position, Operating Results and Cash Flows

Major notes concerning the operating results from the viewpoint of the management are as follows.

#### (Non-GAAP financial measures)

The Group also discloses certain non-GAAP financial measures that are not required or defined under IFRS, which is the accounting standard the Company applies. These non-GAAP financial measures are used internally to manage each of the business operations to understand their underlying performance, in view of the Group's target for mid- to long-term sustainable growth, and the Group believes that these financial measures are useful information for users of the financial statements to assess the Group's performance.

#### Adjusted operating profit

Adjusted operating profit presented is operating profit (loss) less amortization cost of acquired intangibles arising from business acquisitions and adjustment items (income and costs). Adjustment items (income and costs) are impairment losses on goodwill, restructuring income and costs, and other items.

Furthermore, growth rate in adjusted operating profit at constant FX is also presented as additional information. This is a financial measurement that excludes foreign exchange effects by translating and calculating adjusted operating profit for the current period in the International Tobacco Business using the foreign exchange rates of the same period of the previous year. The Group has set its group-wide target for annual average growth rate in adjusted operating profit at constant FX, at mid to high single digit over the mid- to long-term, and will continue to pursue this goal.

The Group makes accounting adjustments to the financial statements of subsidiaries that operate in hyperinflationary economies according to the requirements stipulated in IAS 29 "Financial Reporting in Hyperinflationary Economies" (hereinafter referred to as "IAS 29"). However, the impact of IAS 29 is not included in adjusted operating profit at constant FX.

#### (Core revenue from tobacco business)

Regarding tobacco business, core revenue is disclosed. Specifically, the Domestic Tobacco Business includes revenue from the domestic duty-free market as well as from markets in China, Hong Kong and Macau that are under the control of the Company's China Division, in addition to revenue related to RRP, little cigars and the like, but it excludes revenue related to imported tobacco delivery charges, among others. In addition, the International Tobacco Business includes revenue related to waterpipe tobacco products and RRP, but excludes revenue related to the distribution business and contract manufacturing, among others. Furthermore, growth rate in US dollar-based core revenue from the tobacco business at constant FX is also presented as additional information.

The Group makes accounting adjustments to the financial statements of subsidiaries that operate in hyperinflationary economies according to the requirements stipulated in IAS 29. However, the impact of IAS 29 is not included in core revenue from the tobacco business at constant FX.

#### (RRP)

Reduced-Risk Products (RRP) are products with potential to reduce the risks associated with smoking such as E-Vapor products and T-Vapor products.

E-Vapor products do not use tobacco leaf, instead using electrical heating of a liquid inside a device or specialized cartridge to generate vapor for the user to enjoy.

Conversely, T-Vapor products do use tobacco leaf, but instead of burning the leaf, they use methods such as heating the leaf to generate tobacco vapor (which includes compounds derived from the tobacco leaf) for the user to enjoy.

The Group is committed to developing, testing and bringing to market such new and innovative products for sustainable growth.

Analyses and examinations concerning the operating results from the viewpoint of the management are as follows.

## (1) Business Results

### a. Consolidated results

	(Billions of yen)		
	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Revenue	2,175.6	2,092.6	(3.8)%
Adjusted operating profit	515.9	487.0	(5.6)%
Operating profit	502.4	469.1	(6.6)%
Profit attributable to owners of the parent company	348.2	310.3	(10.9)%

#### <Revenue>

Revenue decreased by 3.8% from the previous fiscal year to ¥2,092.6 billion due to a revenue decline mainly in the Domestic Tobacco Business, Pharmaceutical Business and Processed Food Business. The spread of COVID-19 has affected the Group businesses, and the impact is expected to lower revenue by approximately ¥61.0 billion.

#### <Adjusted operating profit>

Adjusted operating profit at constant FX increased by 5.5% from the previous fiscal year driven by growth in the International Tobacco Business and the Pharmaceutical Business, partially offset by decreases in the Domestic Tobacco Business and the Processed Food Business. Adjusted operating profit including foreign exchange effects decreased by 5.6% from the previous fiscal year to ¥487.0 billion, mainly due to the unfavorable foreign exchange effects in the International Tobacco Business in addition to decreases in the Domestic Tobacco Business and the Processed Food Business.

#### <Operating profit>

Operating profit decreased by 6.6% from the previous fiscal year to ¥469.1 billion, despite the countering factor of an increase in proceeds from sales of real estate assets mainly due to the former JT head office building's sale, due to factors such as the disappearance of revenue relating to the termination of the six anti-HIV drugs license agreements in Japan in the Pharmaceutical Business during the previous fiscal year.

#### <Profit attributable to owners of the parent company>

Profit attributable to owners of the parent decreased by 10.9% from the previous fiscal year to ¥310.3 billion, due to a decline in operating profit, an increase in financing costs and other factors.

## b. Segment results

### Domestic Tobacco Business

(Billions of cigarettes, Billions of yen)			
Domestic Tobacco Business	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Cigarette industry volume <sup>(Note 1)</sup>	125.1	114.9	(8.2)%
Cigarette sales volume <sup>(Note 2)</sup>	75.5	68.7	(9.0)%
Core revenue	568.9	515.7	(9.3)%
Adjusted operating profit	187.2	168.1	(10.2)%

#### <Cigarette sales volume and RRP sales volume> <sup>(Note 3)</sup>

Cigarette industry volume decreased 8.2% from the previous year due to the natural decline trend, the growth in the RRP category, the impact of price revisions, full-scale implementation of the Partial Amendment of the Health Promotion Act in April 2020, as well as the spread of COVID-19. The Company's cigarette sales volume fell by 9.0% from the previous year due to a decline in cigarette industry volume as well as our cigarette market share loss. Cigarette market share of the Company decreased by 0.5 percentage points from the previous year to 59.8% due to intensified competition among low-end products.

Cigarette industry volume increased by 9.1% from the previous fiscal year to 40.2 billion cigarettes, and the share of the market was about 26% (shipment basis). The Company's RRP sales volume increased by 0.7 billion cigarettes from the previous fiscal year to 3.9 billion cigarette equivalent units, and in the RRP category, the market share of the Company was about 10% (consumer off-take basis).

Combined cigarette industry and RRP volume decreased by 4.2% from the same period of the previous year to 155.0 billion cigarettes, while the Company's sales volume decreased by 7.8% to 72.7 billion cigarettes, and the Company's market share declined by 1.8 percentage points to 46.9%.

The combined volume of cigarettes and RRP manufactured in Japan in the fiscal year ended December 31, 2020 decreased by 10.7 billion cigarettes, or 12.8%, from the previous fiscal year to 73.3 billion cigarettes.

#### <Core revenue from tobacco business and adjusted operating profit> <sup>(Note 3)</sup>

Core revenue from the tobacco business fell by 9.3% from the previous fiscal year, mainly due to an unfavorable cigarette sales volume variance, a decrease in RRP-related revenue, and lower sales in domestic Duty-Free and China businesses despite a positive cigarette price/mix variance. RRP-related revenue benefited from an increase in RRP sales volume, but the decline in device sales and the unfavorable cigarette price/mix variance attributed to the tax absorption following price revisions in October 2019 led to a decrease of ¥5.0 billion over the previous fiscal year, to ¥55.9 billion. Furthermore, we estimate that the negative impact of COVID-19 on core revenue from the tobacco business was approximately ¥30.0 billion, of which the effect on the domestic duty-free market and the Chinese business accounted for slightly over half.

Adjusted operating profit declined by 10.2% year on year, due lower core revenue from the tobacco business and increased investments in RRP, digital marketing and other areas. These factors outweighed the favorable comparison arising from the impairment loss related to infused tobacco capsule-manufacturing machines recorded in the previous year, and efficient cost management and prioritized investment activities implemented against the background of the prolonged impact of COVID-19.

- Notes: 1. Cigarette industry volume includes sales volume for the whole Japanese cigarette market. Note also that the figure stated above includes little cigars but excludes RRP and the like.
2. In addition to the figure stated above for sales volume, during the fiscal year ended December 31, 2020, 1.8 billion cigarettes were sold at duty-free shops in Japan, as well as at markets in China, Hong Kong and Macau that are under the control of the Company's China Division (4.0 billion cigarettes in the previous fiscal year). Note also that the figure stated above includes little cigars but excludes RRP and the like.
3. RRP sales volume is converted at the equivalent of 20 cigarettes per pack. The above figures do not include sales volume sold at duty-free shops in Japan. Also, RRP-related revenue includes revenue from duty-free shops in Japan and revenue from devices and associated accessories, etc.
4. Figures for cigarette industry volume and market share were estimated by the Company.



## International Tobacco Business

(Billions of cigarettes, Billions of yen)

International Tobacco Business	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Total shipment volume <sup>(Note 5)</sup>	445.8	435.7	(2.3)%
GFB shipment volume <sup>(Note 6)</sup>	277.0	282.0	1.8%
Core revenue	1,253.0	1,250.8	(0.2)%
Adjusted operating profit	340.8	340.9	0.0%

(Millions of US dollar)

International Tobacco Business (US dollar-based)	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Core revenue	11,496	11,724	2.0% [7.0%]
Adjusted operating profit	3,126	3,181	1.8% [16.8%]

\* The figures in parentheses “[ ]” show change from the previous fiscal year at constant FX (US dollar-based)

### <Total shipment volume and market share>

Total shipment volume fell by 2.3% from the previous year due to the impact of COVID-19 on duty-free sales and markets in emerging countries, as well as contractions in total demand in multiple markets, such as Russia. Excluding unfavorable inventory movements, total shipment volume declined by 1.7% despite market share grew strongly driven by GFBs. Market share continued to grow in various markets, including the key markets of Italy, Iran, the U.K., Canada, Spain, Taiwan, Germany, Romania, etc.

GFB shipment volume rose by 1.8% from the previous year, driven by Winston (+2.4%) and LD (+4.2%).

The volume manufactured overseas including outsourced manufacturing in the fiscal year ended December 31, 2020 decreased by 2.8 billion cigarettes, or 0.6%, from the previous fiscal year to 448.1 billion cigarettes.

### <Core revenue from tobacco business and adjusted operating profit>

Core revenue from the tobacco business was almost unchanged from the previous fiscal year as a result of unfavorable foreign exchange effects, despite the favorable pricing effects and volume effects. The impact from the spread of COVID-19 is expected to lower core revenue from the tobacco business by approximately ¥20.0 billion.

Despite unfavorable foreign exchange effects, US dollar-based core revenue from the tobacco business including foreign exchange effects increased by 2.0% from the previous year as a result of the effects of favorable pricing in the Canada, Germany, the Philippines, Romania, etc. and the volume effects due to a favorable market mix. At constant FX, it increased by 7.0% from the previous fiscal year.

Despite unfavorable foreign exchange effects, US dollar-based adjusted operating profit including foreign exchange effects increased by 1.8% from the previous year as a result of the effects of favorable pricing and the volume effects, etc. At constant FX, it increased by 16.8% from the previous fiscal year.

## The Regional Breakdown of International Tobacco Business <sup>(Note 7)</sup>

Results of International Tobacco Business in each region are as follows.

(Billions of cigarettes, Billions of yen, Millions of US dollar)

	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
<b>South and West Europe</b>			
Total shipment volume <sup>(Note 5)</sup>	64.9	66.3	2.2%
GFB shipment volume <sup>(Note 6)</sup>	52.8	55.7	5.5%
Core revenue	216.7	219.4	1.2%
Core revenue (US dollar-based)	1,987	2,052	3.3% [1.3%]
<b>North and Central Europe</b>			
Total shipment volume <sup>(Note 5)</sup>	55.9	63.4	13.5%
GFB shipment volume <sup>(Note 6)</sup>	28.5	33.3	16.8%
Core revenue	236.2	272.0	15.1%
Core revenue (US dollar-based)	2,167	2,549	17.6% [16.7%]
<b>CIS+</b>			
Total shipment volume <sup>(Note 5)</sup>	131.5	122.2	(7.1)%
GFB shipment volume <sup>(Note 6)</sup>	90.1	82.8	(8.1)%
Core revenue	309.6	294.3	(5.0)%
Core revenue (US dollar-based)	2,842	2,755	(3.1)% [4.9%]
<b>Rest-of-the-World</b>			
Total shipment volume <sup>(Note 5)</sup>	193.5	183.8	(5.0)%
GFB shipment volume <sup>(Note 6)</sup>	105.6	110.2	4.4%
Core revenue	490.5	465.2	(5.2)%
Core revenue (US dollar-based)	4,500	4,367	(2.9)% [6.2%]

\* The figures in parentheses “[ ]” show change from the previous fiscal year at constant FX (US dollar-based)

Notes: 5. Includes fine cut tobacco, cigars, pipe tobacco, snus, kretek and T-Vapor products, except for contract manufacturing products, waterpipe tobacco products and E-vapor products.

6. GFB (Global Flagship Brands) consists of four brands, which serve as flagships of the Group’s brand portfolio - Winston, Camel, MEVIUS, LD.

7. To make the Group’s International Tobacco Business more deeply understood, this segment has been divided into four regions (South and West Europe, North and Central Europe, CIS+ and Rest-of-the-World). South and West Europe includes France, Italy and Spain; North and Central Europe includes Germany and the U.K.; CIS+ includes Romania and Russia; and Rest-of-the-World includes Iran, Taiwan and Turkey.

\* The exchange rates of currencies against the US dollar for the fiscal year ended December 31, 2020 were as follows. <sup>(Note 8)</sup>

Foreign exchange rate per US dollar	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
USD/JPY	109.03	106.76	(2.27) 2.1% appreciation
USD/RUB	64.74	72.07	7.33 10.2% depreciation
USD/GBP	0.78	0.78	(0.00) 0.5% appreciation
USD/EUR	0.89	0.88	(0.02) 1.8% appreciation
USD/CHF	0.99	0.94	(0.05) 5.8% appreciation
USD/TWD	30.90	29.47	(1.43) 4.9% appreciation
USD/TRY	5.67	7.01	1.34 19.1% depreciation
USD/IRR	104,046		

Notes: 8. In accordance with IAS 29, the closing currency rates for the month ended December 2020 have been applied when converting financial statements of subsidiaries located in hyperinflationary economies to the US dollar. Similarly, the month-end rates are also applied upon conversions from the US dollar to the Japanese yen. (USD/IRR: 258,747, USD/JPY: 103.50)

## Pharmaceutical Business

(Billions of yen)

Pharmaceutical Business	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Revenue	88.5	79.0	(10.8)%
Adjusted operating profit	15.9	17.2	7.6%

### <Revenue and adjusted operating profit>

Revenue decreased by 10.8% from the previous year due mainly to lower royalty revenue overseas. The impact from the spread of COVID-19 on revenue is expected to be immaterial.

Adjusted operating profit increased by 7.6% from the previous year, despite the decline in revenue, due to the decrease in research and development expenses following the completion of trials for the clinical development of the product for which manufacturing and marketing application were submitted, and due to an increase in profit at Group company Torii Pharmaceutical.

## Processed Food Business

(Billions of yen)

Processed Food Business	Fiscal year ended December 31, 2019	Fiscal year ended December 31, 2020	Change
Revenue	158.6	149.3	(5.8)%
Adjusted operating profit	5.4	(0.8)	—

### <Revenue and adjusted operating profit>

Revenue was impacted by COVID-19, resulting in higher sales generated by increased demand for household products within frozen and ambient foods. However, declines in demand for food-service products within the frozen and ambient foods as well as the seasonings businesses, and the bakery business, led to lower sales and resulted in revenue falling 5.8% from the previous fiscal year. The impact from the spread of COVID-19 is expected to lower revenue by approximately ¥11.0 billion.

Adjusted operating profit decreased by ¥6.2 billion from the previous fiscal year, due to the decline in revenue, rising logistics costs in the frozen and ambient foods, and an impairment loss of assets such as factories and shops in the bakery business, partially offset by improvements in product mix.

## **(2) Financial Position and Cash Flow Position**

### **a. Financial position**

#### **Assets**

Total assets as of December 31, 2020 decreased by ¥171.7 billion from the end of the previous fiscal year to ¥5,381.4 billion. Although cash and equivalents increased, this was more than offset by the decrease in goodwill as a result of negative foreign currency impacts, and declines related to the amortization of acquired intangible assets arising from business acquisitions.

#### **Liabilities**

Total liabilities as of December 31, 2020 decreased by ¥27.6 billion from the end of the previous fiscal year to ¥2,781.9 billion. This was mainly due to repayment of short-term borrowings, redemption of bonds and decrease in tobacco excise tax payables, despite the proceeds from issuance of the subordinated bonds and borrowings of the subordinated loan.

#### **Equity**

Total equity as of December 31, 2020 decreased by ¥144.1 billion from the end of the previous fiscal year to ¥2,599.5 billion. This was mainly due to dividend payments and decrease in exchange differences on translation of foreign operations, despite an increase in retained earnings as a result of the recording of profit attributable to owners of the parent company.

### **b. Cash flow position**

Cash and cash equivalents at the end of the current fiscal year increased by ¥181.7 billion from the end of the previous fiscal year to ¥538.8 billion. Cash and cash equivalents at the end of the previous fiscal year was ¥357.2 billion.

#### **Cash flows from (used in) operating activities**

Net cash flows from operating activities during the current fiscal year were ¥519.8 billion, compared with ¥540.4 billion provided in the previous fiscal year. This was mainly due to the generation of a stable cash inflow from the tobacco business, despite payments of national and international tobacco excise taxes and income taxes.

#### **Cash flows from (used in) investing activities**

Net cash flows from investing activities during the current fiscal year were ¥5.4 billion, compared with ¥123.6 billion used in the previous fiscal year. This was mainly due to proceeds from sale of investment property and investments in associates despite the purchase of property, plant and equipment, and intangible assets.

#### **Cash flows from (used in) financing activities**

Net cash flows used in financing activities during the current fiscal year were ¥297.4 billion, compared with ¥333.8 billion used in the previous fiscal year. This was mainly due to the payment of dividends and repayments of borrowings despite proceeds from the issuance of deeply subordinated guaranteed fixed rate resettable capital securities and subordinated loan.

## **(3) Results of Production, Orders Received and Sales**

The Group conducts production and sales of broad and various products in the Domestic Tobacco Business, International Tobacco Business, Pharmaceutical Business and Processed Food Business. Moreover, the types, formats, content volumes, and packages of their products are broad, and major products are not based on a made-to-order basis. For this reason, size of production and orders received are presented neither in the amount of money nor in volume by segment.

Therefore, results of “production, orders received and sales” are presented in connection with the operating results by segment in “(1) Business Results.”

Regarding business partners which are the source for 10% or more of the Group’s total revenue, the revenue from such partners and the percentage of total revenue are as follows.

Business partner	Fiscal year ended December 31, 2019		Fiscal year ended December 31, 2020	
	Amount (Billions of yen)	Percentage	Amount (Billions of yen)	Percentage
Megapolis Group	235.1	10.8	210.8	10.1

Note: The Group's International Tobacco Business sells products to Megapolis Group, which runs logistics and wholesale businesses mainly in Russia.

#### (4) Significant Accounting Policies

##### a. Adoption of IFRS

Having acquired RJR Nabisco's non-U.S. tobacco operations in 1999 and Gallaher Group Plc in 2007, the Group has been growing steadily as a global company and now operates in at least 70 countries and territories, and sells products in at least 130 countries and territories. In this context, the Group has decided to opt for an early adoption of the IFRS from the fiscal year ended March 31, 2012. A decision based on the Japanese authorities' permission for the listed companies conducting financial and business activities internationally to adopt IFRS voluntarily from the year ended March 31, 2010. Upon the adoption of IFRS, the Group aims to diversify the group's sources of financing through international markets and to improve quality of business management.

##### b. Significant accounting estimates and judgment on estimates

Preparation of consolidated financial statements of the Group requires the management to make estimates and assumptions in order to measure income, expenses, assets and liabilities, and disclose contingencies as of the fiscal year end date. These estimates and assumptions are based on the best judgment of the management, considering past results and various factors deemed to be appropriate as of the fiscal year end date. Given their nature, actual results may differ from those estimates and assumptions.

The estimates and assumptions are continuously reviewed by the management. The effects of a change in the estimates and assumptions are recognized prospectively, including the period reviewed.

As for the estimates and assumptions that may have a material effect on the amounts recognized in the consolidated financial statements of the Group, please refer to "V. Accounting, 1. Consolidated Financial Statements, (1) Consolidated Financial Statements, Notes to Consolidated Financial Statements, 4. Significant Accounting Estimates and Judgments."

#### (5) Target Management Benchmarks

The Group considers the most important issue to be the pursuit of the 4S model, which represents its management principles, to achieve sustainable profit growth over the mid- to long-term. In order to measure the performance of the businesses that form the foundation for sustainable profit growth, the Group considers it appropriate to exclude foreign exchange effects, temporary factors and special factors, and have set a group-wide profit target of mid to high single digit annual average growth rate over the mid- to long-term in adjusted operating profit at constant FX.

Adjusted operating profit at constant FX in the fiscal year ended December 31, 2020 increased by 5.5% from the previous fiscal year, exceeding the previous year's results despite the challenging business environment.

Analyses and examinations concerning the operating results for the fiscal year ended December 31, 2020 are included in "II. Review of Operations, 3. Management Analysis of Financial Position, Operating Results and Cash Flows, (1) Business Results."

For details of management policies aimed at achieving group-wide profit targets, please refer to "II. Review of Operations, 1. Management Policy, Business Environment, Issues to Be Addressed, Etc."

#### (6) Factors Causing Significant Effects on Operating Results, Etc.

Along with the expansion of the International Tobacco Business and its contribution to the results, foreign exchange fluctuation greatly impacts consolidated financial statements. Adjusted operating profit at constant FX in the fiscal year ended December 31, 2020 increased by 5.5% from the previous fiscal year, while adjusted operating profit including foreign exchange effects decreased by 5.6% due to unfavorable foreign exchange effects. Unfavorable foreign exchange effects are also expected to arise in the fiscal year ending December 31, 2021.

In order to mitigate foreign exchange risk, the Group is working to implement a natural hedging strategy by matching revenue currencies to payment currencies. The Group hedges some foreign exchange risks using derivatives or foreign currency-denominated interest-bearing debt, etc.

With regard to factors causing significant effects on the Group's operating results, etc. including the above, please refer to "II. Review of Operations 2. Business and Other Risks."

## **(7) Basic Policies of Financing Activities**

The Group's basic policies of financing activities are as follows.

### **a. Group Cash Management Systems**

To maximize the total group cash efficiency, the Group gives first priority to utilizing internal financing mainly by the Group Cash Management Systems (CMS), where legally permissible and economically viable.

### **b. External financing**

Short-term working capital needs are normally financed through short-term borrowings from financial institutions or through commercial paper, or a combination of both; mid- to long-term financing is done through long-term borrowings from financial institutions, bond or equity, or a combination of those.

For secure and efficient financing, the Group continues to diversify its financing means as well as the financial institutions, and set up secure financing means, such as multiple committed facilities.

### **c. External investments**

Investments with financial institutions should be transacted ensuring safety, liquidity and optimal yield. Speculative dealings in pursuit of profit margin are not allowed.

### **d. Financial risk management**

The Group is exposed to financial risks such as credit risk, liquidity risk, foreign exchange risk, interest rate risk, and market price fluctuation risk. The Group manages such risks according to the risk management policies and procedures to avoid or mitigate such risks. The major financial risk management status is reported regularly to the President and Chief Executive Officer and the Board of Directors.

It is the Group's policy that derivatives are only used if it is intended to mitigate risks of transactions for actual business needs, and speculative and trading transactions are not allowed.

For more details on financial risk management, please refer to "V. Accounting, 1. Consolidated Financial Statements, (1) Consolidated Financial Statements, Notes to Consolidated Financial Statements, 33. Financial Instruments, (2) Financial Risk Management to (8) Market Price Fluctuation Risk."

## **(8) Analysis of Capital Resources and Liquidity of Funds**

### **a. Funding requirements**

Funds are mainly allocated for capital expenditure, working capital and acquiring external capital resources as well as the repayment of loans, the payment of interest and dividends, the acquisition of treasury shares and the payment of income taxes.

Scheduled material capital expenditures and approaches to procuring funds are as presented in "III. Facilities, 3. Plans for New Installation and Retirement of Facilities."

### **b. Resources of funds**

The necessary funds are mainly procured from net cash flows from operating activities, loans from financial institutions and bond and commercial paper issuances.

#### <Cash flows>

Please refer to “(2) Financial Position and Cash Flow Position, b. Cash flow position.”

#### <Interest-bearing debt>

Amounts of interest-bearing debt of the Group to be repaid or redeemed as of December 31, 2020 are as follows.

(Billions of yen)							
	Book value	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Short-term borrowings as loans	51.6	51.6	—	—	—	—	—
Long-term borrowings as loans (current portion)	12.2	12.2	—	—	—	—	—
Bonds (current portion)	77.6	77.6	—	—	—	—	—
Long-term borrowings as loans	192.7	—	41.9	11.6	20.1	0	120.1
Bonds	624.7	—	30.0	114.3	—	94.7	389.6
Total	958.9	141.5	71.9	125.9	20.1	94.8	509.7

Note: Lease obligations are excluded.

#### (Long-term debt)

Bonds issued (including the current portion) as of December 31, 2019 and as of December 31, 2020 accounted for ¥666.6 billion and ¥702.3 billion, respectively, and long-term borrowings as loans from financial institutions (including the current portion) accounted for ¥115.3 billion and ¥205.0 billion, respectively. Long-term lease liabilities totaled ¥40.2 billion as of December 31, 2019 and ¥49.4 billion as of December 31, 2020.

As of December 31, 2020, the long-term debt was rated A1 (negative) by Moody's Japan K.K., AA- (negative) by S&P Global Ratings Japan Inc., and AA (stable) by Rating and Investment Information, Inc. (R&I). These ratings are among the highest ratings for international tobacco companies.

These ratings are affected by a number of factors such as developments in the major business markets, the quality of execution of the business strategies, and general economic trends that are beyond the Group's control. The ratings may be withdrawn or revised at any time. Each rating should be evaluated separately from other ratings. Under the JT Act, bonds issued by the Company are secured by statutory preferential rights to the property of the Company. These rights give bondholders precedence over unsecured creditors in seeking repayment, with the exception of national and local taxes and other statutory obligations.

#### (Short-term debt)

Short-term borrowings from financial institutions totaled ¥192.6 billion as of December 31, 2019 and ¥51.6 billion as of December 31, 2020. There was no commercial paper outstanding on both period. Short-term lease liabilities totaled ¥13.5 billion as of December 31, 2019 and ¥17.1 billion as of December 31, 2020.

#### c. Liquidity

The Group has historically had, and expects to continue to have, significant cash flows from operating activities. The Group expects that cash generated from operating activities will continue to be stable and cover funds needed for regular business activities. As of December 31, 2020, the Group had ¥478.2 billion in committed lines of credit from major financial institutions both domestic and international, none of which was used. In addition, the Group has a commercial paper program, uncommitted lines of credit, a domestic bond shelf registration, and a euro MTN program.

## 4. Important Operational Contracts

No items to report.

## **5. Research and Development Activities**

Research and development activities are mainly undertaken at the Company's Tobacco Science Research Center and Central Pharmaceutical Research Institute.

Research and development expenses of the Group during the fiscal year ended December 31, 2020 amounts to ¥60.8 billion and the research objectives and research and development expenses by each segment are as follows. In January 2020, D-LAB was set up by the corporate divisions of the Company for the purpose of research and development, and the above-mentioned research and development expenses includes ¥6.5 billion relating to basic research not affiliated to any segment, consisting of costs and research and development expenses associated with this organization.

### **(1) Domestic and International Tobacco Businesses**

The Group is committed to strengthening its R&D capabilities to ensure a long-term competitive advantage. The focus areas in the R&D activities are the development of new leaf tobacco varieties, improvement of tobacco leaves and their processing, enhancement of aroma and taste, upgrading manufacturing technology, and continuous progress on RRP-related technologies. The Group has been striving to add value to the products in these focus areas in a cost efficient manner. It has established a global research platform in Japan, which focuses on the fundamental research and product technology development. To best meet consumers' needs and preferences, the market teams are continuously engaged in the product development. Research and development expenses relating to the Domestic Tobacco Business amounts to ¥19.1 billion with that of the International Tobacco Business amounting to ¥9.2 billion.

### **(2) Pharmaceutical Business**

R&D activities are the foundation of the Group's Pharmaceutical Business and are critical for its long-term growth and profitability. The R&D activities focus mainly on the fields of glucose and lipid metabolism, immune disorders and inflammation, and virus research. Research and development expenses for the Pharmaceutical Business is ¥25.2 billion.

### **(3) Processed Food Business**

Regarding R&D in the Processed Food Business, the Group devotes its efforts to the development of innovative products that meet consumers' needs and preferences. Research and development expenses for the Processed Food Business is ¥0.8 billion.



### III. Facilities

#### 1. Outline of Capital Expenditures

In the fiscal year ended December 31, 2020, the Group made capital expenditures totaling ¥112.9 billion.

In the Domestic Tobacco Business, the Group spent ¥21.1 billion, mainly on investments accompanying maintenance and upgrade of manufacturing processes, productivity improvements, adaptation to new products, improvements in product specifications, and others. In the International Tobacco Business, the Group invested ¥66.6 billion mainly for compliance with regulations in addition to improvements in product specifications. In the Pharmaceutical Business, the Group spent ¥9.1 billion on enhancing and strengthening research and development structures and the like. In the Processed Food Business, the Group invested ¥8.0 billion in improvement, maintenance and renewals of production capability.

\* Capital expenditures includes land; building and structures; machinery and vehicles; and other property, plant and equipment, as well as goodwill, right of trademark, software and other intangible assets, necessary for production improvements at factories and other facilities, strengthening competitiveness and executing business in a variety of fields, excluding assets acquired through business combinations.

The headquarters of the Company was relocated during the fiscal year ended December 31, 2020, and the following main facilities were sold.

Office and factory name (Location)	Segment	Description	Book value as of the end of the previous fiscal year (Millions of yen)	Sale period
The former JT head office building (Minato-ku, Tokyo)	General Administration	Other	40,810	November 2020

#### 2. Main Facilities

Main facilities of the Group (the Company and its consolidated subsidiaries) are as follows.

##### (1) Filing Company (the Company)

(As of December 31, 2020)

Office and factory name (Location)	Segment	Description	Book value (Millions of yen)						Number of employees (Person)
			Land		Buildings and structures	Machinery, equipment and vehicles	Tools, furniture and fixtures	Total	
			Size (thousand m <sup>2</sup> )	Amount					
Kita-kanto Factory (Utsunomiya-shi, Tochigi) <small>(Note 1)</small>	Domestic Tobacco	Tobacco manufacturing facilities	150	2,062	7,702	13,034	340	23,138	341
Tokai Factory (Iwata-shi, Shizuoka) <small>(Note 1)</small>	Domestic Tobacco	Tobacco manufacturing facilities	223	2,309	7,229	18,642	274	28,454	343
Kansai Factory (Fushimi-ku, Kyoto-shi, Kyoto) <small>(Note 1)</small>	Domestic Tobacco	Tobacco manufacturing facilities	116	5,831	9,657	17,444	413	33,345	364
Kyushu Factory (Chikushino-shi, Fukuoka)	Domestic Tobacco	Tobacco manufacturing facilities	166	4,042	3,064	10,488	220	17,814	216
Tobacco Science Research Center (Aoba-ku, Yokohama-shi, Kanagawa) <small>(Note 1)</small>	Domestic Tobacco	Research and development facilities	34	642	2,304	0	1,391	4,337	91
Central Pharmaceutical Research Institute (Takatsuki-shi, Osaka) <small>(Note 1)</small>	Pharmaceutical	Research and development facilities	75	2,687	19,559	232	2,999	25,477	617
Head Office (Minato-ku, Tokyo) <small>(Note 2)</small>	General administration	Other	—	—	15,811	53	1,765	17,629	1,449
Regional Sales Headquarters (15) (Municipality) <small>(Notes 1, 3)</small>	Domestic Tobacco (includes administration)	Other	28	904	3,165	1,039	340	5,448	2,955

## (2) Domestic Subsidiaries

(As of December 31, 2020)

Office and factory name (Location)	Segment	Description	Book value (Millions of yen)						Number of employees (Person)
			Land		Buildings and structures	Machinery, equipment and vehicles	Tools, furniture and fixtures	Total	
			Size (thousand m <sup>2</sup> )	Amount					
TS Network Co., Ltd. Head Office and other 24 distribution bases (Head Office: Taito-ku, Tokyo) <small>(Note 3)</small>	Domestic Tobacco	Distribution facilities	35	751	16,550	1,859	737	19,897	1,907
Japan Filter Technology, Co., Ltd. Head Office and other 3 factories (Head Office: Sumida-ku, Tokyo) <small>(Notes 1, 3)</small>	Domestic Tobacco	Material manufacturing facilities	114	714	4,532	7,195	343	12,783	545
Torii Pharmaceutical Co., Ltd. Headquarters, other regional sales headquarters, etc. (Head Office: Chuo-ku, Tokyo) <small>(Note 4)</small>	Pharmaceutical	Pharmaceuticals manufacturing facility and other	3	335	1,399	317	90	2,141	568
TableMark Co., Ltd. Head Office and other 8 factories (Head Office: Chuo-ku, Tokyo)	Processed Food	Frozen food production facilities	175	4,500	9,364	9,888	246	23,999	1,346

## (3) Foreign Subsidiaries

(As of December 31, 2020)

Office and factory name (Location)	Segment	Description	Book value (Millions of yen)						Number of employees (Person)
			Land		Buildings and structures	Machinery, equipment and vehicles	Tools, furniture and fixtures	Total	
			Size (thousand m²)	Amount					
JTI Polska Sp. z o. o. (Poland) <small>(Note 1)</small>	International Tobacco	Tobacco manufacturing facilities	532	243	11,825	41,994	1,051	55,114	2,353
LLC Petro (Russia) <small>(Note 3)</small>	International Tobacco	Tobacco manufacturing facilities	194	110	4,103	8,211	2,433	14,857	1,081
JT International Germany GmbH (Germany)	International Tobacco	Tobacco manufacturing facilities	346	302	13,310	19,714	1,736	35,063	1,909
JTI Tütün Ürünleri Sanayi A.Ş. (Turkey)	International Tobacco	Tobacco manufacturing facilities	232	480	1,369	10,057	121	12,027	719

Notes: 1. Companies have land leased to entities other than the group companies.

2. The headquarters of the Company was relocated during the fiscal year ended December 31, 2020, and the Head Office building (now the former JT head office building), which was described in the Annual Securities Report for the previous fiscal year as being owned by the Company, was sold.

3. Companies have land leased from entities other than the group companies.

4. During the fiscal year ended December 31, 2020, ownership of the Sakura Plant was transferred.

5. Book values include right-of-use assets.

### 3. Plans for New Installation and Retirement of Facilities

#### (1) Outline of Capital Expenditures

Regarding the mid- to long-term resource allocation of the Group, it will place top priority on business investments that will lead to sustainable profit growth in the mid- to long-term based on the Group's management principles. Of the reportable segments, the Group positions the Domestic and International Tobacco Businesses as the core business and profit growth engine and places top priority on business investments that will lead to their sustainable profit growth. On the other hand, with the aim of positioning the Pharmaceutical Business and the Processed Food Business as complementary drivers of profit growth for the Group as a whole, the focus will be on rebuilding their business foundations, and making the investments required to implement that.

Based on this policy, the Group plans capital expenditures (facility construction and expansion) totaling ¥147.5 billion in the fiscal year ending December 31, 2021.

As the Company and its consolidated subsidiaries have wide-ranging plans for capital expenditure, figures are disclosed by segment.

The Group's actual capital expenditures may differ significantly from the planned figures mentioned above as a result of a number of factors including those presented in "II. Review of Operations, 2. Business and Other Risks."

Segment	Capital expenditure plan for the fiscal year ending December 31, 2021 (Billions of yen)	Main purpose of investment	Funding
Domestic Tobacco Business	30.0	Expenditures for RRP-related investments and renovation for manufacturing facilities	Internally generated funds
International Tobacco Business	92.0	Expenditures for the improvements in product specifications, RRP-related investments, and renewal of facilities	Same as above
Pharmaceutical Business	5.0	Expenditures for the development and reinforcement of R&D capabilities	Same as above
Processed Food Business	14.5	Expenditures for the expansion of production capacity, and improvements, maintenance and upgrading of productivity	Same as above

\* Capital expenditures includes land; building and structures; machinery and vehicles; and other property, plant and equipment, as well as goodwill, right of trademark, software and other intangible assets, necessary for production improvements at factories and other facilities, strengthening competitiveness and executing business in a variety of fields, excluding assets acquired through business combinations.

#### (2) Sales or Retirement of Important Facilities, etc.

There were no other plans for sales or retirement of important facilities except for the regular renewal of facilities as of December 31, 2020.

Furthermore, as announced on February 9, 2021 in "JT Group Announces New Operating Model - Company Aims to Strengthen its Tobacco Business," the Company's Kyushu Tobacco Factory, and the Tagawa Factory of Group subsidiary Japan Filter Technology Co., Ltd., will be closed at the end of March 2022.

## IV. Filing Company

### 1. Information on the Company's Shares

#### (1) Total Number of Shares Authorized

##### a. Total number of shares authorized

Class	Total number of shares authorized (Share)
Ordinary shares	8,000,000,000
Total	8,000,000,000

##### b. Number of shares issued

Class	Number of shares issued (Share; as of December 31, 2020)	Number of shares issued (Share; as of the date of filing: March 24, 2021)	Name of financial instruments exchange where the stock of the Company is traded or the name of authorized financial instruments firms association where the Company is registered	Details
Ordinary shares	2,000,000,000	2,000,000,000	Tokyo Stock Exchange (First Section)	(Note 2)
Total	2,000,000,000	2,000,000,000	—	—

Notes: 1. The provisions of Article 2 of the JT Act prescribe that the Japanese government must continue to hold more than one-third of all shares issued by the Company (excluding shares of a class for which it is provided that the voting rights may not be exercised for all the matters that are subject to resolution at the General Meeting of Shareholders).

2. The Company's standard class of shares with no rights limitations. Its share trading unit is 100 shares.

## (2) Status of Subscription Rights to Shares

### a. Stock options

Subscription rights to shares issued pursuant to the Companies Act are as follows. Also, the matters presented below reflect the situation as of the last day of the Company's fiscal year (December 31, 2020). Matters that have undergone change between the last day of the Company's fiscal year and the last day of the end of the month before the date of filing (February 28, 2021) are presented in parentheses [ ], while other matters have undergone no change since the last day of the Company's fiscal year.

Note that the stock option plan was abolished in fiscal 2020 (excluding the stock options already granted). The granted stock options could be exercised when the stock option holder loses all positions as Member of the Board, Audit & Supervisory Board Member or Executive Officer. The Company does not plan to change this exercise condition going forward.

- Stock options based on resolutions taken at meetings of the Board of Directors held between December 21, 2007 and September 16, 2011

Resolution date	December 21, 2007	September 19, 2008	September 28, 2009	September 17, 2010	September 16, 2011
Positions and number of persons granted	Members of the Board 11 persons Executive Officers (excluding persons serving as Member of the Board) 16 persons	Members of the Board 11 persons Executive Officers (excluding persons serving as Member of the Board) 14 persons	Members of the Board 9 persons Executive Officers (excluding persons serving as Member of the Board) 14 persons	Members of the Board 9 persons Executive Officers (excluding persons serving as Member of the Board) 14 persons	Members of the Board 8 persons Executive Officers (excluding persons serving as Member of the Board) 15 persons
Number of subscription rights to shares	20 units	71 units	155 units [142 units]	194 units	208 units [160 units]
Class of shares to be issued upon exercise of subscription rights to shares	Ordinary shares (the Company's standard class of shares with no rights limitations)	Same as left	Same as left	Same as left	Same as left
Number of shares to be issued upon exercise of subscription rights to shares	4,000 shares (Notes 1, 6)	14,200 shares (Notes 1, 6)	31,000 shares [28,400 shares] (Notes 1, 6)	38,800 shares (Notes 1, 6)	41,600 shares [32,000 shares] (Notes 1, 6)
Paying due upon exercise of subscription rights to shares	¥1 per share	Same as left	Same as left	Same as left	Same as left
Exercise period of subscription rights to shares	From January 9, 2008 to January 8, 2038	From October 7, 2008 to October 6, 2038	From October 14, 2009 to October 13, 2039	From October 5, 2010 to October 4, 2040	From October 4, 2011 to October 3, 2041
Issue price of shares in cases where shares will be issued as a result of exercise of subscription rights to shares	¥581,269 per unit	¥285,904 per unit	¥197,517 per unit	¥198,386 per unit	¥277,947 per unit
Additional paid-in capital in issue price in cases where shares will be issued as a result of exercise of subscription rights to shares	(Note 2)	Same as left	Same as left	Same as left	Same as left
Conditions for exercising subscription rights to shares	(Note 3)	Same as left	Same as left	Same as left	Same as left
Assignment of subscription rights to shares	The approval of the Board of Directors is required for the assignment of subscription rights to shares.	Same as left	Same as left	Same as left	Same as left
Provisions for acquiring subscription rights to shares	(Note 4)	Same as left	Same as left	Same as left	Same as left

Resolution date	December 21, 2007	September 19, 2008	September 28, 2009	September 17, 2010	September 16, 2011
Matters regarding delivery of subscription rights to shares accompanied by reorganization	(Note 5)	Same as left	Same as left	Same as left	Same as left

Notes: 1. Number of shares to be issued upon exercise of subscription rights to shares

The class of shares to be issued upon exercise of subscription rights to shares shall be ordinary shares. The number of shares to be issued upon exercise of each subscription right to shares (hereinafter, “Number of Shares Granted”) shall be one. However, in cases where the Company conducts stock split (including stock allotment without contribution; hereinafter, the same shall apply to description of stock split) or stock consolidation of ordinary shares of the Company after the date on which the Company allots subscription rights to shares (hereinafter, “Allotment Date”), the Number of Shares Granted shall be adjusted according to the following formula.

$$\text{Number of Shares Granted after adjustment} = \text{Number of Shares Granted before adjustment} \times \text{Ratio of stock split or stock consolidation}$$

Any fraction of less than one share that occurs as a result of the above adjustment shall be rounded down to two decimal places.

In the case of a stock split, the Number of Shares Granted after adjustment shall be applied on and after the date following the base date (if the base date is not specified, on and after the effective date), while in the case of stock consolidation, it shall be applied on and after the effective date. However, in cases where stock split is conducted subject to approval of the proposal to reduce surplus and increase capital or reserve fund at the General Meeting of Shareholders of the Company and where the base date for stock split is set on or before the date of conclusion of that General Meeting of Shareholders, the Number of Shares Granted after adjustment shall be applied retrospectively to the date following that base date, on and after the date following the date of conclusion of that General Meeting of Shareholders.

In addition, in cases where the adjustment of the Number of Shares Granted is proper, the Company shall conduct adjustments deemed necessary after the Allotment Date. When adjusting the Number of Shares Granted, the Company shall notify Subscription rights to shares Holders or make public notice of necessary information by the date before the date on which the Number of Shares Granted after adjustment is applied. However, in cases where the notice or public notice by the date before the date of the application is impracticable, the Company shall later do so as soon as possible.

2. Additional paid-in capital in issue price in cases where shares will be issued as a result of exercise of subscription rights to shares

- a. Capital amount that will be increased in cases where shares will be issued as a result of the exercise of subscription rights to shares must be a half of the maximum capital increase amount obtained by the calculation pursuant to Article 17, paragraph 1 of the Regulation on Corporate Accounting. If the obtained figure has a fraction less than ¥1, the figure is rounded up to the nearest yen.
- b. Capital reserves that will be increased in cases where shares will be issued as a result of the exercise of subscription rights to shares must be the amount obtained by subtracting the capital amount to be increased as specified in a. above from the maximum capital increase amount described in a. above.

3. Conditions for exercising subscription rights to shares

- a. The person who is a holder of subscription rights to shares and is recorded in the registry of subscription rights to shares (hereinafter, “Subscription rights to shares Holder”) may exercise his/her subscription rights to shares only if he/she forfeit his/her all position as Member of the Board (including *sikkoyaku* at a company with committees), Audit & Supervisory Board Member and Executive Officer of the Company
- b. In cases where Subscription rights to shares Holders waive their subscription rights to shares, they cannot exercise those subscription rights to shares.

4. Provisions for acquiring subscription rights to shares

In cases where proposal a., b. or c. below is approved at the General Meeting of Shareholders of the Company (if a resolution by the General Meeting of Shareholders is not necessary, it is read as “in cases where the resolution of the Board of Directors or the decision by the representative Executive Officer (*sikkoyaku* at a company with committees) is made”), the Company may acquire subscription rights to shares on the date separately provided for by the Board of Directors. In this case, the Company shall, in exchange for acquiring each subscription right to shares, deliver money at the amount obtained by multiplying the value per share calculated according to the following formula by the Number of Shares Granted (if adjusted pursuant to Note 1 above, the Number of Shares Granted after adjustment) to the Subscription rights to shares Holders of respective such subscription rights to shares.

Value per share = Closing price for regular transactions of ordinary shares of the Company on the Tokyo Stock Exchange (if there is no closing price, the base price thereof on the following business day) on the date on which such proposal is approved at the General Meeting of Shareholders of the Company (if a resolution by the General Meeting of Shareholders is not necessary, it is read as “the resolution of the Board of Directors or the decision by the representative Executive Officer (*sikkoyaku* at a company with committees) is made”) – ¥1

- a. Proposal to ask approval of a contract of merger where the Company is not to be the surviving company
- b. Proposal to ask approval of a contract or plan of company split where the Company would be the split company
- c. Proposal to ask approval of a share exchange contract or share transfer plan where the Company becomes a wholly-owned subsidiary

5. Matters regarding delivery of subscription rights to shares accompanied by reorganization

In cases where the Company merges (limited to cases where the Company is to be extinguished as a result of the merger), splits and absorbs or splits and incorporates (limited to cases where the Company becomes the split company in either case), or exchanges or

transfers shares (limited to cases where the Company becomes a wholly-owned subsidiary in either case) (collectively, hereinafter, “Reorganization”), the Company shall, in each case, deliver subscription rights to shares of the companies as listed in Article 236, paragraph 1, item (viii), sub-items (a) to (e) of the Companies Act (hereinafter, the “Company Subject to Reorganization”) to the Subscription rights to shares Holders that have subscription rights to shares existing immediately before the effective date of the Reorganization, which is either the effective date of absorption-type merger when it is an absorption-type merger, the consolidation date of a company as a result of the consolidated-type merger when it is a consolidated-type merger, the effective date of absorption-type company split when it is an absorption-type company split, the incorporation date of a company as a result of the incorporation-type company split when it is an incorporation-type company split, the effective date of share exchange when it is a share exchange, or the incorporation date of a wholly-owning parent company as a result of the share transfer when it is a share transfer (hereinafter, “Remaining Subscription rights to shares”). However, it is subject to a condition that the provision that the subscription rights to shares of the Company Subject to Reorganization shall be delivered pursuant to the provisions of the items below, is specified in the absorption-type merger contract, consolidated-type merger contract, absorption-type company split contract, incorporation-type company split plan, share exchange contract or share transfer plan.

- a. Number of subscription rights to shares to be delivered of the Company Subject to Reorganization  
Subscription rights to shares whose number is identical to the number of the Remaining Subscription rights to shares held by Subscription rights to shares Holder
- b. Class of shares of the Company Subject to Reorganization to be issued upon exercise of subscription rights to shares  
Ordinary shares of the Company Subject to Reorganization
- c. Number of shares of the Company Subject to Reorganization to be issued upon exercise of subscription rights to shares  
To be determined in the same manner as Note 1 above, taking into consideration terms and other conditions of the Reorganization.
- d. Value of property to be contributed when subscription rights to shares are exercised  
The value of the property to be contributed when each subscription right to shares to be delivered is exercised shall be the amount obtained by multiplying the paid-in amount after Reorganization as specified below by the number of shares of the Company Subject to Reorganization to be issued upon exercise of each subscription right to shares, which is decided pursuant to c. above.  
The paid-in amount after Reorganization shall be ¥1 per share of the shares of the Company Subject to Reorganization that would be delivered by exercising the delivered subscription rights to shares.
- e. Period during which subscription rights to shares can be exercised  
From the effective date of the Reorganization to the expiration date of the period during which such subscription rights to shares can be exercised as specified in “Exercise period of subscription rights to shares” mentioned above.
- f. Matters regarding capital and capital reserves that will be increased in cases where shares will be issued as a result of the exercise of subscription rights to shares  
To be determined in the same manner as “Additional paid-in capital in issue price in cases where shares will be issued as a result of exercise of subscription rights to shares” mentioned above.
- g. Restrictions on transferring of subscription rights to shares  
Transferring the subscription rights to shares is subject to approval of the Board of Directors of the Company Subject to Reorganization
- h. Provisions for acquiring subscription rights to shares  
To be determined in the same manner as “Provisions for acquiring subscription rights to shares” mentioned above.
- i. Other conditions for exercising subscription rights to shares  
To be determined in the same manner as “Conditions for exercising subscription rights to shares” mentioned above.

6. The Company conducted a share split at a ratio of 200 to one ordinary share with July 1, 2012 as effective date. As a consequence, the number of shares to be issued upon exercise of the subscription rights to shares issued before this share split has been adjusted from one share to 200 shares and is presented accordingly.

- Stock options based on resolutions taken at meetings of the Board of Directors held between September 21, 2012 and June 14, 2019

Resolution date	September 21, 2012	September 20, 2013	September 19, 2014	July 17, 2015	June 17, 2016
Positions and number of persons granted	Members of the Board (excluding Outside Directors) 7 persons Executive Officers (excluding persons serving as Member of the Board) 17 persons	Members of the Board (excluding Outside Directors) 7 persons Executive Officers (excluding persons serving as Member of the Board) 19 persons	Members of the Board (excluding Outside Directors) 6 persons Executive Officers (excluding persons serving as Member of the Board) 19 persons	Members of the Board (excluding Outside Directors) 6 persons Executive Officers (excluding persons serving as Member of the Board) 18 persons	Members of the Board (excluding Outside Directors) 5 persons Executive Officers (excluding persons serving as Member of the Board) 18 persons
Number of subscription rights to shares	165 units	150 units	121 units	212 units	233 units
Class of shares to be issued upon exercise of subscription rights to shares	Ordinary shares (the Company's standard class of shares with no rights limitations)	Same as left	Same as left	Same as left	Same as left
Number of shares to be issued upon exercise of subscription rights to shares	33,000 shares (Note 1)	30,000 shares (Note 1)	24,200 shares (Note 1)	42,400 shares (Note 1)	46,600 shares (Note 1)
Paying due upon exercise of subscription rights to shares	¥1 per share	Same as left	Same as left	Same as left	Same as left
Exercise period of subscription rights to shares	From October 10, 2012 to October 9, 2042	From October 8, 2013 to October 7, 2043	From October 7, 2014 to October 6, 2044	From August 4, 2015 to August 3, 2045	From July 5, 2016 to July 4, 2046
Issue price of shares in cases where shares will be issued as a result of exercise of subscription rights to shares	¥320,000 per unit	¥513,400 per unit	¥483,200 per unit	¥711,200 per unit	¥572,600 per unit
Additional paid-in capital in issue price in cases where shares will be issued as a result of exercise of subscription rights to shares	(Note 2)	Same as left	Same as left	Same as left	Same as left
Conditions for exercising subscription rights to shares	(Note 3)	Same as left	Same as left	Same as left	Same as left
Assignment of subscription rights to shares	The approval of the Board of Directors is required for the assignment of subscription rights to shares.	Same as left	Same as left	Same as left	Same as left
Provisions for acquiring subscription rights to shares	(Note 4)	Same as left	Same as left	Same as left	Same as left
Matters regarding delivery of subscription rights to shares accompanied by reorganization	(Note 5)	Same as left	Same as left	Same as left	Same as left



Resolution date	June 14, 2017	June 15, 2018	June 14, 2019
Positions and number of persons granted	Members of the Board (excluding Outside Directors) 5 persons Executive Officers (excluding persons serving as Member of the Board) 19 persons	Members of the Board (excluding Outside Directors) 5 persons Executive Officers (excluding persons serving as Member of the Board) 18 persons	Members of the Board (excluding Outside Directors) 6 persons Executive Officers (excluding persons serving as Member of the Board) 20 persons
Number of subscription rights to shares	371 units	659 units	1,299 units
Class of shares to be issued upon exercise of subscription rights to shares	Ordinary shares (the Company's standard class of shares with no rights limitations)	Same as left	Same as left
Number of shares to be issued upon exercise of subscription rights to shares	74,200 shares (Note 1)	131,800 shares (Note 1)	259,800 shares (Note 1)
Paying due upon exercise of subscription rights to shares	¥1 per share	Same as left	Same as left
Exercise period of subscription rights to shares	From July 4, 2017 to July 3, 2047	From July 3, 2018 to July 2, 2048	From July 2, 2019 to July 1, 2049
Issue price of shares in cases where shares will be issued as a result of exercise of subscription rights to shares	¥482,200 per unit	¥300,000 per unit	¥188,000 per unit
Additional paid-in capital in issue price in cases where shares will be issued as a result of exercise of subscription rights to shares	(Note 2)	Same as left	Same as left
Conditions for exercising subscription rights to shares	(Note 3)	Same as left	Same as left
Assignment of subscription rights to shares	The approval of the Board of Directors is required for the assignment of subscription rights to shares.	Same as left	Same as left
Provisions for acquiring subscription rights to shares	(Note 4)	Same as left	Same as left
Matters regarding delivery of subscription rights to shares accompanied by reorganization	(Note 5)	Same as left	Same as left

Notes: 1. Number of shares to be issued upon exercise of subscription rights to shares  
The class of shares to be issued upon exercise of subscription rights to shares shall be ordinary shares. The number of shares to be issued upon exercise of each subscription right to shares (hereinafter, "Number of Shares Granted") shall be 200. However, in cases where the Company conducts stock split (including stock allotment without contribution; hereinafter, the same shall apply to description of stock split) or stock consolidation of ordinary shares of the Company after the date on which the Company allots subscription rights to shares (hereinafter, "Allotment Date"), the Number of Shares Granted shall be adjusted according to the following formula.

$$\text{Number of Shares Granted after adjustment} = \text{Number of Shares Granted before adjustment} \times \text{Ratio of stock split or stock consolidation}$$

Any fraction of less than one share that occurs as a result of the above adjustment shall be rounded down to two decimal places. In the case of a stock split, the Number of Shares Granted after adjustment shall be applied on and after the date following the base date (if the base date is not specified, on and after the effective date), while in the case of stock consolidation, it shall be applied on and after the effective date. However, in cases where stock split is conducted subject to approval of the proposal to reduce surplus and increase capital or reserve fund at the General Meeting of Shareholders of the Company and where the base date for stock split is set on or before the date of conclusion of that General Meeting of Shareholders, the Number of Shares Granted after adjustment shall be applied retrospectively to the date following that base date, on and after the date following the date of conclusion of that General Meeting of Shareholders. In addition, in cases where the adjustment of the Number of Shares Granted is proper, the Company shall conduct adjustments deemed necessary after the Allotment Date. When adjusting the Number of Shares Granted, the Company shall notify Subscription rights to shares Holders or make public notice of necessary information by the date before the date on which the Number of Shares Granted after adjustment is applied. However, in cases where the notice or public notice by the date before the date of the application is impracticable, the Company shall later do so as soon as possible.

2. to 5. Same as (Notes) 2-5 for stock options based on resolutions of the Board of Directors taken between December 21, 2007 and September 16, 2011.

**b. Details of rights plan**

No items to report.

**c. Other status of subscription rights to shares**

No items to report.

**(3) Exercise of Bond Certificates With Subscription Rights to Shares With Exercise Price Amendment Clause**

No items to report.

**(4) Trends in Total Number of Shares Issued and Share Capital**

Date	Fluctuation in the number of shares issued (Thousands of shares)	Balance of shares issued (Thousands of shares)	Fluctuation in share capital (Millions of yen)	Balance of share capital (Millions of yen)	Fluctuation in capital reserve (Millions of yen)	Balance of capital reserve (Millions of yen)
July 1, 2012	1,990,000	2,000,000	—	100,000	—	736,400

Note: The Company conducted a share split at a ratio of 200 to one share with July 1, 2012 as effective date. Consequently, the balance of shares issued increased by 1,990,000 thousand shares to 2,000,000 thousand shares.

**(5) Shareholder Composition**

(As of December 31, 2020)

Category	Shareholder composition (100 shares in one share unit)								Shares less than one unit (Share)
	Public sector	Financial institutions	Financial instruments business operators	Other corporations	Foreign investors		Individuals	Total	
					Companies	Individuals			
Number of shareholders (Person)	1	223	53	3,552	754	627	633,506	638,716	—
Number of shares held (Unit)	6,669,252	3,064,320	1,235,391	302,040	2,435,771	2,596	6,285,864	19,995,234	476,600
Holding rate of shares (%)	33.35	15.33	6.18	1.51	12.18	0.01	31.44	100.00	—

Notes: 1. 2,257,546 units of treasury shares are included in “Individuals.”

2. The number of “Other corporations” includes 336 units in the name of Japan Securities Depository Center, Inc.

## (6) Status of Major Shareholders

(As of December 31, 2020)

Name of shareholder	Address	Number of shares held (Share)	Percentage of number of shares held in the total number of shares issued (excluding treasury shares) (%)
Minister of Finance	1-1, Kasumigaseki 3-chome, Chiyoda-ku, Tokyo, Japan	666,925,200	37.59
The Master Trust Bank of Japan, Ltd. (Trust Account)	11-3, Hamamatsucho 2-chome, Minato-ku, Tokyo, Japan	77,183,500	4.35
SMBC Nikko Securities Inc.	3-1, Marunouchi 3-chome, Chiyoda-ku, Tokyo, Japan	58,303,600	3.29
Custody Bank of Japan, Ltd. (Trust Account)	8-12, Harumi 1-chome, Chuo-ku, Tokyo, Japan	48,009,500	2.71
Custody Bank of Japan, Ltd. as trustee for Mizuho Bank, Ltd. Retirement Benefit Trust Account re-entrusted by Mizuho Trust & Banking Co., Ltd.	8-12, Harumi 1-chome, Chuo-ku, Tokyo, Japan	23,660,000	1.33
State Street Bank West Client - Treaty 505234 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	1776 Heritage Drive, North Quincy, MA 02171, U.S.A. (Shinagawa Intercity Tower A, 15-1, Konan 2-chome, Minato-ku, Tokyo, Japan)	19,974,941	1.13
Barclays Securities Japan Limited	31F Roppongi Hills Mori Tower, 10-1, Roppongi 6-chome, Minato-ku, Tokyo, Japan	18,432,844	1.04
Custody Bank of Japan, Ltd. (Trust Account 5)	8-12, Harumi 1-chome, Chuo-ku, Tokyo, Japan	17,079,000	0.96
Custody Bank of Japan, Ltd. (Trust Account 6)	8-12, Harumi 1-chome, Chuo-ku, Tokyo, Japan	15,416,800	0.87
JAPAN SECURITIES FINANCE CO., LTD.	2-10, Nihonbashi-kayabacho 1-chome, Chuo-ku, Tokyo, Japan	14,114,400	0.80
Total	—	959,099,785	54.06

Note: In addition to the above, the Company held 225,754,671 shares of ordinary shares as treasury shares.

## (7) Status of Voting Rights

### a. Number of shares issued

(As of December 31, 2020)

Classification	Number of shares (Share)	Number of voting rights	Details
Shares without voting rights	—	—	—
Shares with restricted voting rights (Treasury shares)	—	—	—
Shares with restricted voting rights (Other)	—	—	—
Shares with full voting rights (Treasury shares)	Ordinary shares 225,754,600	—	(Note 2)
Shares with full voting rights (Other)	Ordinary shares 1,773,768,800	17,737,688	(Note 2)
Shares less than one unit	Ordinary shares 476,600	—	(Note 3)
Total number of shares issued	2,000,000,000	—	—
Total number of voting rights	—	17,737,688	—

Notes: 1. The number of “Shares with full voting rights (Other)” includes 33,600 shares in the name of Japan Securities Depository Center, Inc. “Number of voting rights” includes 336 units of voting rights related to shares with full voting rights in its name.

2. The Company’s standard class of shares with no rights limitations. Its share trading unit is 100 shares.

3. Includes 71 shares of treasury shares.

### b. Treasury shares

(As of December 31, 2020)

Name of shareholder	Address	Number of shares held under own name (Share)	Number of shares held under the name of others (Share)	Total number of shares held (Share)	Percentage of number of shares held in the total number of shares issued (%)
JAPAN TOBACCO INC.	1-1, Toranomon 4-chome, Minato-ku, Tokyo, Japan	225,754,600	—	225,754,600	11.29
Total	—	225,754,600	—	225,754,600	11.29

## 2. Acquisition of Treasury Shares

[Class of shares] Acquisition of ordinary shares falling under Article 155, item (vii) of the Companies Act

### (1) Acquisition by Resolution of the General Meeting of Shareholders

No items to report.

### (2) Acquisition by Resolution of the Board of Directors

No items to report.

### (3) Items Not Based on Resolutions of the General Meeting of Shareholders or Board of Directors

Category	Number of shares (Share)	Total value (Millions of yen)
Treasury shares acquired during this fiscal year ended December 31, 2020	330	1
Treasury shares acquired during the period from January 1, 2021 to the filing date of this Annual Securities Report	73	0

Note: The figure for treasury shares acquired during the period from January 1, 2021 to the filing date of this Annual Securities Report does not include the number of shares from purchases of shares less than one unit from March 1, 2021 until the filing date of this Annual Securities Report.

#### (4) Status of Disposal and Ownership of Acquired Treasury Shares

Category	Fiscal year ended December 31, 2020		From January 1, 2021 until the filing date of this Annual Securities Report	
	Number of shares (Share)	Total disposal value (Millions of yen)	Number of shares (Share)	Total disposal value (Millions of yen)
Acquired treasury shares offered for subscription	—	—	—	—
Acquired treasury shares that were cancelled	—	—	—	—
Acquired treasury shares transferred for merger, share exchange, share delivery and company split	—	—	—	—
Others				
(Restricted stock grants)	239,200	521	—	—
(Exercise of subscription rights to shares)	203,000	442	12,200	27
(Sales resulting from requests for sale of shares less than one unit)	25	0	—	—
Treasury shares held	225,754,671	—		—

Notes: 1. The number of disposed shares and total disposal value in the “From January 1, 2021 until the filing date of this Annual Securities Report” column does not include transfers by the exercise of subscription rights to shares performed from March 1, 2021 until the filing date of this Annual Securities Report, nor does it include sales of shares less than one unit during that period.

2. The number of treasury shares held in the “From January 1, 2021 until the filing date of this Annual Securities Report” column does not include transfers by the exercise of subscription rights to shares performed from March 1, 2021 until the filing date of this Annual Securities Report, nor does it include purchases and sales of shares less than one unit during that period.

### 3. Dividend Policy

With regard to the shareholder return policy for the current fiscal year, the Company aims to enhance shareholder returns in proportion to mid- to long-term profit growth, while maintaining a solid financial base<sup>(Note 1)</sup>.

Specifically, the Company will pursue the following:

- Stable and consistent growth in dividend per share<sup>(Note 2)</sup>
- Consider whether to execute the acquisition of treasury shares in view of factors including the medium-term outlook on business environment and financial positions
- Continue to monitor a trend in shareholder returns of global FMCG companies

Notes: 1. As its financial policy, the Company will maintain a solid financial base that secures stability in case of changes in business environment such as economic crises and flexibility enabling expeditious responses to business investment opportunities.  
2. Based on the mid- to long-term outlook of the growth rate of adjusted operating profit at constant FX, the Group will also take into account the Group's level of profit.

It is also a basic policy of the Company to pay an interim dividend and year-end dividend, with the former determined by the Board of Directors and the latter by the General Meeting of Shareholders. The Company's Articles of Incorporation stipulate that the Company may pay interim dividends to shareholders with the record date of June 30 each year upon a resolution by the Board of Directors.

In light of business performance in the current fiscal year ended December 31, 2020, the year-end dividend for the fiscal year ended December 31, 2020 was ¥77 per share. Therefore, the total annual dividend for the fiscal year ended December 31, 2020, including the interim dividend of ¥77, is ¥154 per share.

Also, internal reserves will be prepared not only for present and future business investments and to acquire external resources but also for the purchase of treasury shares and other objectives.

The dividend for the 36th term is as follows.

Resolution date	Total amount of dividends (Millions of yen)	Cash dividends per share (Yen)
The Board of Directors on July 31, 2020	136,617	77.00
Ordinary General Meeting of Shareholders held on March 24, 2021	136,617	77.00

From the fiscal year ending December 31, 2021, the Company has revised the shareholder return policy taking into consideration the key components of our resource allocation policy, "prioritizing business investments" and "balancing profit growth and shareholder returns." For details of the revised shareholder return policy, please refer to "II. Review of Operations, 1. Management Policy, Business Environment, Issues to Be Addressed, Etc. (3) Group-Wide Profit Targets and Policy on Shareholder Return."

## 4. Status of Corporate Governance

### (1) Outline of Corporate Governance

Whereas the following contains statements regarding the fiscal year ended December 31, 2020, the final day of that fiscal year, and the fiscal year ended December 31, 2019, the statements herein are current as of the filing date, unless otherwise indicated.

#### a. Basic concept on the corporate governance

The Company's belief is that corporate governance is the means for conducting transparent, fair, timely and decisive decision-making for pursuing the Group's management principle, the "4S model." Specifically, the 4S model aims "to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can."

The Company has set out the "JT Corporate Governance Policy," and strives to make enhancements based on its belief that it will enable the Group to achieve mid- to long-term sustainable profit growth and increase company value, which will contribute to the development of the Group's stakeholders and eventually the economic society as a whole.

The Company will continue to strive to make enhancements of the Group's corporate governance as one of the key challenges for its management.

#### b. Outline of corporate governance structure and reason for adoption of the structure

As a company with an Audit & Supervisory Board, the Company has strengthened the supervisory function of management while maintaining its objectivity and neutrality by means of the Audit & Supervisory Board carrying out appropriate audits of the execution of duties by Members of the Board and Executive Officers from an independent and fair standpoint. Based on the audit system of the Audit & Supervisory Board, while facilitating the prompt execution of business through the delegation of authority by reducing the size of the Board of Directors and introducing an Executive Officer system, the Company has established the JT Group Compliance Committee, which is largely composed of outside committee members, and the Advisory Panel on Nomination and Compensation, which is largely composed of the Independent Outside Directors, as voluntary structures and created an effective corporate governance system.

Since 2019, the Company has also continued to enhance corporate governance and improve the objectivity and transparency of management, such as by increasing the number of Outside Directors and Outside Audit & Supervisory Board Members by one each.

The Company has selected the current structure because it recognizes that, through initiatives like these, the corporate governance structure functions effectively regarding business execution and supervision.

The Board of Directors meets once a month in principle and on more occasions as necessary, in order to make decisions with regard to the matters specified by laws and regulations and other important matters, to supervise implementation of business and to receive reports from the Members of the Board on the status of implementation of business. In addition, the Chairperson of the Board has been positioned as a non-executive Director in order to concentrate on supervising management while also serving as the chairman of the Board of Directors. The Company appoints at least two Independent Outside Directors who possess the qualities to contribute to sustainable profit growth and enhancement of company value over the mid- to long-term from a viewpoint of strengthening the supervising function and management transparency. The Board of Directors has set forth in the Board of Directors Regulations matters to be discussed at the Board of Directors meetings. In addition, from the viewpoint of realizing swift decision making and high-quality implementation of business, the Board of Directors has set forth a clear decision-making process based on internal rules on the allocation of responsibilities and authorities (hereinafter referred to as the "Responsibility and Authority Regulations") concerning essential business matters as well as delegates authority as necessary to Executive Officers based on JT Group management strategies, under the Executive Officer system. In the fiscal year ended December 31, 2020, the Board of Directors convened 13 times, and all Members of the Board attended every meeting.

The Advisory Panel on Nomination and Compensation was established as an optional advisory body to the Board of Directors and integrates the functions of the previous Meeting for Talent Development and Compensation Advisory Panel. The purpose of establishing the panel is to further enhance the objectivity and transparency of the Board of Directors' decision making by having the panel support the development of a group of executive candidates, deliberate on the selection of Member of the Board and Audit & Supervisory Board Member candidates, deliberate on dismissal of Executive Directors and Members of the Board who



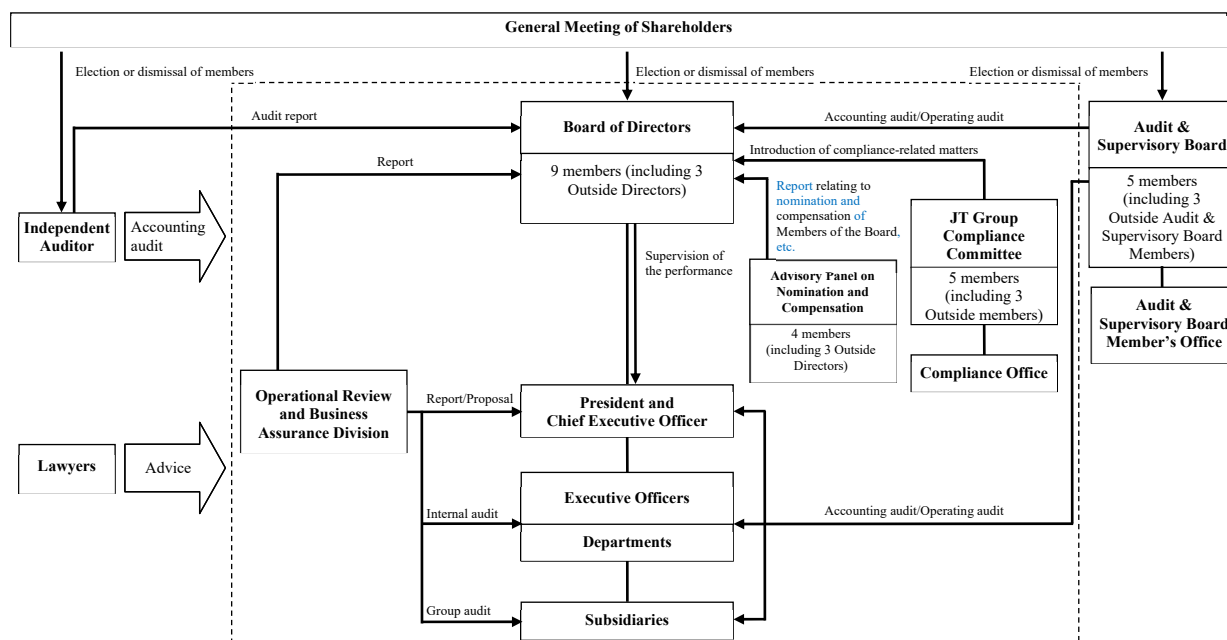
execute the business, and deliberate on matters regarding remuneration for Members of the Board and Executive Officers, then report to the Board of Directors. The Advisory Panel on Nomination and Compensation, which shall meet at least once a year, consists of four members: the Chairperson of the Board, who chairs the panel and who does not serve as an Executive Officer, and three Independent Outside Directors. In the fiscal year ended December 31, 2020, the Advisory Panel on Nomination and Compensation convened four times, and all members of the Panel attended every meeting.

As an organization that reports directly to the Board of Directors, the JT Group Compliance Committee deliberates the status of implementing the Compliance Action Plan for the fiscal year, the establishment, changes, etc. to compliance-related rules and the Code of Conduct, and matters relating to compliance for the entire JT Group in order to foster awareness and ensure thorough compliance among employees. The JT Group Compliance Committee is headed by the Chairperson of the Board and consists mainly of outside members. Meanwhile, the Company appoints an Executive Officer in charge of compliance who oversees the Compliance Office in an effort to establish and promote a group-wide, cross-sectional system and shed light on issues. The compliance promotion departments of the Company and its subsidiaries (meaning the Compliance Office within the Company, and corresponding departments within subsidiaries) distribute materials including the “JT Group Code of Conduct,” which explains the Code of Conduct, etc., to Members of the Board and employees of the Company and Directors, etc. and employees of subsidiaries (with Members of the Board, Directors, etc. and employees hereinafter collectively referred to as “directors and employees”), and work to enhance the effectiveness of the compliance system by enlightening directors and employees about compliance through training and other programs, etc. In the fiscal year ended December 31, 2020, the JT Group Compliance Committee convened three times, and all members of the Committee attended every meeting.

The Company has adopted the Audit & Supervisory Board system under which Audit & Supervisory Board Members of the Company (hereinafter “Audit & Supervisory Board Members,” with the terms “Audit & Supervisory Board,” “Audit & Supervisory Board Member’s Office,” and “Manager of the Audit & Supervisory Board Member’s Office” also referring to those items within the Company) assertively exercise authority as an independent body with the mandate of shareholders, which includes attending and speaking at the Board of Directors meetings and other important meetings as well as actively inspecting business sites. In addition, they also perform audits appropriately from an objective viewpoint in accordance with the characteristics of the duties of the Outside Audit & Supervisory Board Members and the standing Audit & Supervisory Board Members. The Audit & Supervisory Board Members work to ensure sound and sustainable growth and maintain and enhance public trust in the Company by examining the performance of duties by Members of the Board and Executive Officers.

The Audit & Supervisory Board, which meets as necessary, is composed of members with substantial knowledge of management, law, finance, accounting and other aspects of business. Standing Audit & Supervisory Board Member Ms. Ryoko Nagata has served as Senior Vice President, Head of Beverage Business Division and in charge of CSR, etc., and has abundant experience and wide-ranging insights with regard to the Group’s business operations from the perspective both of the business operations and the internal department. Furthermore, standing Audit & Supervisory Board Member Mr. Hiroshi Yamamoto has knowledge of finance and accounting as well as insight into corporate governance in the Group’s business operations having served as the Company’s Vice President of the Operational Review and Business Assurance. In the fiscal year ended December 31, 2020, the Audit & Supervisory Board convened 13 times, and all of the Audit & Supervisory Board Members attended every meeting.

The status of the development of the Company’s corporate governance system is represented as the following schematic depiction.



As of the filing date, the members of the Company's corporate governance system are as follows:

Name of body	Members
Board of Directors	Chairman: Yasutake Tango, Chairperson of the Board Members: Mutsuo Iwai, Masamichi Terabatake, Naohiro Minami, Kiyohide Hirowatari, Kazuhito Yamashita, Main Kohda <sup>(*)</sup> , Yukiko Nagashima <sup>(*)</sup> , Masato Kitera <sup>(*)</sup>
Audit & Supervisory Board	Chairman: Ryoko Nagata, Standing Audit & Supervisory Board Member Members: Hiroshi Yamamoto, Toru Mimura <sup>(*)</sup> , Hiroshi Obayashi <sup>(*)</sup> , Koji Yoshikuni <sup>(*)</sup>
Advisory Panel on Nomination and Compensation	Chairman: Yasutake Tango, Chairperson of the Board Members: Main Kohda <sup>(*)</sup> , Yukiko Nagashima <sup>(*)</sup> , Masato Kitera <sup>(*)</sup>
JT Group Compliance Committee	Chairman: Yasutake Tango, Chairperson of the Board Members: Masamichi Terabatake, and 3 outside committee members

(\*) Outside Director

(\*) Standing Outside Audit and Supervisory Board Member

(\*) Outside Audit & Supervisory Board Member

c. Implementation status of internal control system, risk management system and systems necessary to ensure the properness of operations in subsidiaries

The Company has always endeavored to run an internal control system of the Company and the Group through initiatives in such areas as compliance, internal audits, and risk management. Moreover, the Company has created the systems required under the Companies Act and the Regulation for Enforcement of the Companies Act by implementing measures aimed at ensuring the effectiveness of audits by Audit & Supervisory Board Members. The Company will work to maintain and enhance the systems in each company while consecutively reviewing and revising the current system as necessary, and ensure appropriate implementation of business. For the foreign subsidiaries, the Company builds and operates the necessary system in conformity with the following provisions concerning subsidiaries, in principle, while complying with the laws and regulations in the country in which the subsidiary is incorporated.

- Systems to ensure that the performance of duties by directors and employees of the Company and its subsidiaries conforms to laws, regulations, and the Articles of Incorporation

Regarding the internal reporting system (whistle-blower system), each of the Company and its subsidiaries has a counter inside and outside the company through which employees and others may consult or report in case that they detect any conduct, etc. that may violate laws and regulations. Compliance promotion departments that receive a report or request for consultation investigate the details and take necessary action, while working to prevent recurrence of the issue. The Company will bring matters of particular importance involving the Group to the JT Group Compliance Committee, and will request deliberation or will report on the issue.

Under the system for excluding anti-social elements, the Company and its subsidiaries are resolved to fight against them, not to comply with an unreasonable demand and not to have any relations with them. Designating the General Administration Division of the Company as the department assuming the responsibility for supervising efforts to exclude anti-social elements at the Group level, the Company cooperates with police, lawyers and other relevant organizations and parties to gather and share information in order to deal with such elements in an organized way. The Company also consistently makes enlightening activities to eliminate anti-social forces by making directors and employees of the Company and its subsidiaries informed about the rules not to have any relations with anti-social groups and organizations and by educating the directors and employees through providing relevant training as necessary.

In order to ensure the reliability of financial reporting of the Group, the Company is operating a relevant internal control system that it has established in accordance with the Financial Instruments and Exchange Act. By allocating a sufficient level of staff to the task of evaluating financial results and reporting them, the company is striving to maintain and improve the reliability of its financial reporting.

- Procedures and arrangements for storage and management of information on the performance of duties by the Members of the Board of the Company

The Company makes sure to properly store and manage the minutes of General Meetings of Shareholders and meetings of the Board of Directors in line with laws and regulations. The Company makes sure that the information on important matters relating to business execution and decision-making including the conclusion of corporate contracts is stored and managed by the relevant departments and divisions as specified by the Responsibility and Authority Regulations, and establishes rules on managing the processes of decision-making, procurement and accounting.

- System for reporting matters concerning the performance of duties by Directors, etc. of subsidiaries to the Company

The Company makes subsidiaries to regularly report important information to the Company's departments and divisions that are in charge of the subsidiaries.

- Rules on management of risk of loss of the Company and its subsidiaries, and procedures/arrangements for other matters

The Company has established internal policies, rules and manuals relating to the Group for the management of risk of loss relating to monetary and financial affairs, and ensures that relevant reports are made to the President and Chief Executive Officer and the Board of Directors on a quarterly basis via Chief Financial Officer. With regard to the risk of loss relating to other affairs, in accordance with authority delegated to each department and division as per the Responsibility and Authority Regulations, responsible departments and divisions take on a supervisory role creating all types of committees to conduct proper management.

The Company works to achieve an integrated understanding of all risks that may affect the Group, and to manage them accordingly. This risk management is coordinated by the person in charge of risk management promotion, who determines which risks are significant, and reports them to the President and Chief Executive Officer. Executive Officers also take the lead role in drawing up measures to address significant risks. After submitting reports to the person in charge of risk management promotion and to the President and Chief Executive Officer, the Executive Officers promote and execute these measures, and provide progress reports on them to the same individuals. With regard to risk management process, please refer to "II. Review of Operations 2. Business and Other Risks."

In cooperation with the internal audit functions of subsidiaries, the Operational Review and Business Assurance Division of the Company examines and evaluates the internal control systems, etc. of the Group companies in light of the level of importance and the risks involved, and from an objective standpoint that is independent of organizations responsible for business execution. It provides reports and counsel to the President and Chief Executive Officer and also reports to the Board of Directors.

To prepare for possible emergencies, the Company has produced a manual for crisis management and disaster response. In the event of an emergency or a disaster, the Company is ready to establish an emergency project system, and make prompt and proper responses under the leadership of senior management and through close cooperation between the relevant departments and divisions and subsidiaries. Events to which a response has

been made and the details of such events shall be reported to the Board of Directors in a timely and appropriate manner.

- System to ensure that Members of the Board of the Company and Directors, etc. of its subsidiaries can perform their duties efficiently

The Board of Directors of the Company meets once a month in principle and on more occasions as necessary, in order to make decisions with regard to the matters specified by laws and regulations and other important matters and to supervise business execution. The Board of Directors of the Company receives reports from Members of the Board of the Company on the status of business execution at least once every three months. For important management issues, particularly management policy and basic plans regarding overall business operations of the Company, in addition to matters to be referred to the Board of Directors of the Company, a clear decision-making process is stipulated in the Responsibility and Authority Regulations to have a system that enables to realize swift decision-making and high-quality business execution. The Company has adopted the Executive Officer System, under which Executive Officers appointed by the Company's Board of Directors execute business properly by exercising the authority delegated to them in their respective areas, in accordance with JT Group management strategies decided by the Board. In order to manage business operations in ways that contribute to the business efficiency and flexibility of the Company, basic matters concerning the Company's organization, allocation of duties to officers and staff and the roles of individual divisions are specified by the relevant internal rules.

The Company has been constructing an efficient system for business execution within the Group through the formulation, etc. of rules and policies that apply to the Group.

- Systems necessary to ensure the properness of operations in the Company and the Group

The Group has set itself the mission of creating, developing and nurturing its unique brands to win consumer trust, while understanding and respecting the environment and the diversity of societies and individuals, and there is a group-wide consensus on the mission. The Company has specified the functions and rules common for the Group to effectuate group management that optimizes the operations of the entire Group as a whole. Moreover, the Company has been putting in place systems for compliance (including the internal reporting system), internal audits, financial affairs management, etc. in cooperation with its subsidiaries.

- Matters for employees assisting Audit & Supervisory Board Members in their duties in the event such employees were requested by Audit & Supervisory Board Members

The Company has allocated sufficient staff to the Audit & Supervisory Board Member's Office (five persons as of December 31, 2020) as an organization supporting the Audit & Supervisory Board Members in performing their duties. In addition, the Company makes sure to review and reform the staffing structure as necessary based on consultations with the Audit & Supervisory Board.

- Matters relating to the independence of employees belonging to the Audit & Supervisory Board Member's Office from the Company's Members of the Board, and matters relating to the assurance of the effectiveness of instruction by Audit & Supervisory Board Members to those employees

The evaluation of the Manager of the Audit & Supervisory Board Member's Office is made by the Audit & Supervisory Board and the evaluation of the other employees assigned to the Audit & Supervisory Board Member's Office is made by the Manager of the Audit & Supervisory Board Member's Office based on the advice of the Audit & Supervisory Board. The transfer and discipline of employees assigned to the Audit & Supervisory Board Member's Office is to be deliberated in advance with the Audit & Supervisory Board.

The Company makes the employees belonging to the Audit & Supervisory Board Member's Office follow the direction and orders of Audit & Supervisory Board Members in assisting the duties of the latter, and not be assigned to other concurrent positions relating to the business execution of the Company.

- System for reporting by directors and employees of the Company and its subsidiaries or persons reported by directors and employees of its subsidiaries to the Audit & Supervisory Board and Audit & Supervisory Board Members

When directors and employees of the Company and its subsidiaries detect any evidence of malfeasance in financial documents or serious breaches of laws and regulations or the Company's Articles of Incorporation, they are due to report them to the Audit & Supervisory Board, along with other relevant matters that could affect the Company's management. In addition, when directors and employees of the Company and its subsidiaries are asked by Audit & Supervisory Board Members to compile important documents for their perusal, to accept field audits and to submit reports, they are due to respond to the request in a prompt and appropriate manner.

The Compliance Office makes reports regularly to Audit & Supervisory Board Members on the status of whistleblowing involving the Group, and makes non-regular reports as necessary.

- System to ensure that persons reporting to Audit & Supervisory Board Members are not subject to disadvantageous treatment due to having reported

The Company thoroughly communicates within the Group that persons engaging in consultation or whistleblowing are not to be subject to any disadvantageous treatment for reason of those actions.

- Matters concerning policies for the prepayment of expenses involving the performance of duties by Audit & Supervisory Board Members, procedures for reimbursement, and the handling of other expenses or debts involving the performance of those duties

When an Audit & Supervisory Board Member has made claim to the Company for the prepayment of expenses, etc. in accordance with Article 388 of the Companies Act, the Company will promptly handle the relevant expenses or debt, with the exception of cases in which the Company deems the claimed expenses or debt to be unnecessary to the performance of the duties of the Audit & Supervisory Board Member.

The Company makes a budget covering audit-related expenses so as to secure effectiveness of audits by Audit & Supervisory Board Members. The Company also bears the portion of miscellaneous expenses for audits by Audit & Supervisory Board Members that are in excess of budget, with the exception of cases in which the Company deems the expenses to be unnecessary to the performance of duties.

- Other systems to ensure effective auditing by Audit & Supervisory Board Members

Audit & Supervisory Board Members are allowed to attend not only meetings of the Board of Directors of the Company but also other important meetings of the Company. The Operational Review and Business Assurance Division and the Compliance Office maintain cooperation with Audit & Supervisory Board Members by exchanging information.

#### d. Other matters regarding corporate governance

- Evaluation of effectiveness of the Board of Directors

With regard to the effectiveness of the Board of Directors, in addition to annual questionnaire-based self-evaluations by Members of the Board and Audit & Supervisory Board Members from the standpoint of such themes as business operation systems and supervisory functions of the Board of Directors, and dialogue with shareholders and investors, before compiling the results the Board of Directors Secretariat also conducts individual interviews with the aim of supplementing the results of the evaluations. The results of the self-evaluations are assessed and analyzed at the Board of Directors, leading to further improvements in its effectiveness. Furthermore, we take advice from external institutions when creating the questionnaire and analyzing the results, in order to ensure objectivity and further improve the evaluation of effectiveness.

### Major items evaluated

Business operation systems of the Board of Directors	Composition (internal/external ratio, diversity); status of operations (frequency of holding meetings, appropriateness of topics of discussion, advance explanations); systems for support and cooperation (cooperation between Members of the Board and Audit & Supervisory Board Members / the internal auditing division, etc., utilization of committees, sharing of information outside the Board of Directors); status of discussions (fair and prompt decision-making that follows the management principles of the Company, free and open-minded discussion), etc.
Supervisory functions of the Board of Directors	Systems for reporting the status of business execution, risk management systems, penetration of compliance awareness, decision-making process for executive remuneration, succession planning, etc.
Dialogue with shareholders and investors	Sharing of shareholder and investor views, status of development of system for engaging in dialogue, etc.

In the evaluation of effectiveness conducted for fiscal 2019, the items undergoing evaluation obtained good results on the whole, allowing the Company to confirm that the effectiveness of the Board of Directors is improving and the Board of Directors is functioning effectively. Conversely, in addition to identifying issues related to the operation of the Board of Directors aimed at further improving its effectiveness, and issues related to better sharing of information that could contribute to further enhancements in the quality of decision-making by the Board of Directors, the following measures for improvement, which also took into account the impacts of COVID-19, were implemented throughout 2020.

#### *Effective and efficient operation of the Board of Directors aimed at further enhancements in its capabilities*

- More detailed advance explanations for critical matters, and more substantial deliberation and discussion
- Remote hosting of some meetings of the Board of Directors, and the use of digital versions of proposal materials and minutes

#### *Better sharing of information that could contribute to further enhancements in the quality of decision-making*

- Enhanced sharing of information in relation to the following matters
  - Details and status of investigations into important policies related to mid- to long-term strategy
  - Status of operations in important countries or regions
  - Status of dialogue with shareholders/investors
  - Sustainability strategy for the Company as a whole and individual businesses, progress towards the same, and results of external evaluation, etc.
  - The impacts of COVID-19 on employees and individual businesses, measures taken in response, and status of the same

The fiscal 2020 effectiveness evaluation recognized that there had been improvements from fiscal 2019 in the main initiatives for the year (effective and efficient operation of the Board of Directors / better sharing of information), in addition to which the items undergoing evaluation again achieved good results, on the whole.

On the other hand, in order to make an ongoing contribution to enhanced effectiveness, the Company will target continuous improvements from 2021 onwards, focusing on the following newly identified issues.

Main issues	Policy for improvements going forward
Measures to maintain and improve the quality and amount of communication between Members of the Board (in light of reduced opportunities for face-to-face meetings due to the impacts of COVID-19)	Further enhancement of discussions, exchanges of opinions, and information sharing under themes, such as the progress of key policies in the mid- to long-term strategy, status of each stakeholder who contributes to the further pursuit of the 4S model, and corporate governance
Discussions that delve deeper into topics related to corporate governance	

The Company will continue to implement improvements required to further enhance effectiveness, including the above-mentioned activities.

- Policy for ensuring the effectiveness of the governance system for the listed subsidiary

The Company believes it is an indispensable prerequisite for the subsidiary to maintain independence in terms of management and to duly protect its minority shareholders' interests in order for, not only the subsidiary, but also for the Group to grow in value. Therefore, the Company is striving to build an appropriate governance system for the subsidiary as a listed subsidiary. The Company has instituted the Group's Responsibility and Authority Regulations as an internal decision-making rules. The listed subsidiary has opted to adopt these regulations, thereby gaining autonomy in terms of decision-making authority. Such autonomy ensures its independence as a listed subsidiary. Torii Pharmaceutical is a consolidated subsidiary of the Company and is listed on the Tokyo Stock Exchange. Torii Pharmaceutical is upgrading the effectiveness of its governance system, which effectively utilizes Independent Outside Directors, by transiting to a majority-independent Board of Directors, which was approved at its Annual General Meeting of Shareholders on March 26, 2020.

- Succession planning

The Company places priority on fostering successive generations of executives who will manage its future operations, expanding its pool of executive candidates and improving quality thereof.

To develop a steady stream of highly skilled, highly qualified leaders capable of excelling in the global arena, the Company aims to upgrade its executive development program, succession plan and succession planning process with input from both external consultants and the Independent Outside Directors on the Advisory Panel on Nomination and Compensation. Senior management, having the President at the core, are deeply involved in selecting executive candidates and supporting their growth.

The Company expands its executive talent pool by selecting groups of human resources who have the potential for being future executive candidates by organizational rank through Group-wide recruitment and recommendations from management, particularly executive officers. The Company develops selected personnel mainly through diverse and challenging job assignments based on individualized development plans formulated with input from outsourced objective assessments and periodic discussions with management.

- Key points of the partial exemption of liability and liability limitation agreement

The Company's Articles of Incorporation stipulate that the Company may enter into an agreement with Members of the Board (excluding those who are Executive Directors, etc.) and Audit & Supervisory Board Members to limit the scope of their liabilities in advance to the extent permitted by the Companies Act and the Company may exempt Members of the Board and Audit & Supervisory Board Members from liabilities to the extent permitted by the same act. This provision is intended to enable Members of the Board and Audit & Supervisory Board Members to fulfill their expected role and make it easier to appoint the right persons from a broad choice both within and outside the company. As of the date of submission, the Company has such liability limiting agreements with its Members of the Board (excluding those who are Executive Directors, etc.) and Audit & Supervisory Board Members.

- Number of Members of the Board

The Company's Articles of Incorporation stipulate that the number of Members of the Board must be 15 or less.

- Nomination of Member of the Board Candidates and Election and Dismissal of Directors

With regard to candidates for Members of the Board, the JT Corporate Governance Policy stipulates that the proposed list of candidates created by the President shall be deliberated by the Advisory Panel on Nomination and Compensation, the content and results of which are reported to the Board of Directors, and that after appropriate opportunities to receive advice from Independent Outside Directors have been secured, a decision shall be made by resolution of the Board of Directors. The Company's Articles of Incorporation stipulate that

Members of the Board must be appointed by a majority of the shareholder votes cast on an occasion where shareholders representing at least one-third of the total voting rights are present.

With regard to the dismissal of Executive Directors and Members of the Board who execute the business, the JT Corporate Governance Policy stipulates that in cases where such persons do not meet the required qualifications or have become unable to perform their duties, a decision shall be made by resolution of the Board of Directors after securing appropriate opportunities for receiving advice from Independent Outside Directors by having those Members of the Board who are not subject to dismissal request the Advisory Panel on Nomination and Compensation to deliberate on the proposal for dismissal, and then having the panel report the content and results of its deliberations to the Board of Directors. In relation to resolutions pertaining to the dismissal of Directors, there are no provisions in the Articles of Incorporation that differ from those of the Companies Act.

Further, when bringing up the agenda item on the appointment of Member of the Board candidates at a General Meeting of Shareholders, and when the Board of Directors has resolved to dismiss a Member of the Board who execute the business, the Company shall disclose the reasons for the appointment of individual candidates and for the dismissal.

- Matters to be decided by the Board of Directors without referral to General Meeting of Shareholders

*Acquisition of treasury shares*

In order to enable flexible management that meets changes in business environment, the Company's Articles of Incorporation stipulate that the Company may acquire treasury shares through means such as market transaction upon a resolution by the Board of Directors under Article 165, paragraph 2 of the Companies Act.

*Interim dividends*

In order to enable profits to be returned to shareholders in a flexible manner, the Company's Articles of Incorporation stipulate that the Company may pay interim dividends to shareholders, upon a resolution by the Board of Directors under Article 454, paragraph 5 of the Companies Act.

- Requirements for special resolutions at General Meeting of Shareholders

In order to facilitate the smooth conduct of General Meeting of Shareholders with an easier quorum requirement for special resolutions, the Company's Articles of Incorporation stipulate that a resolution as specified by Article 309, paragraph 2 of the Companies Act is valid if it is supported by at least two-thirds of the votes cast at a General Meeting of Shareholders attended by shareholders representing at least one-third of the Company's total voting rights (compared with the usual requirement of "at least half").

- Measures regarding transactions that involve possible conflict of interest between the Company and specified shareholders to avoid harming the interests of shareholders (excluding the shareholder who is a party to such a transaction)

The Company requires resolution by the Board of Directors with respect to gaining approval for uncustomary transactions between the Company and its major shareholders.



## (2) Status of Officers

### a. Officers

There are eleven male officers and three female officers (21.4% of the officers are women).

Title	Name	Date of birth	Summary of career	Term of office	Number of shares held (Share)
Chairperson of the Board	Yasutake Tango	March 21, 1951	<p>April 1974 Entered Ministry of Finance</p> <p>October 2006 Director-General of the Financial Bureau</p> <p>July 2007 Deputy Vice Minister</p> <p>July 2008 Director-General of the Budget Bureau</p> <p>July 2009 Administrative Vice Minister</p> <p>December 2010 Corporate Auditor, The Yomiuri Shimbun Holdings</p> <p>December 2012 Special Advisor to the Cabinet</p> <p>June 2014 Chairperson of the Board, the Company (Current Position)</p> <p>June 2015 Outside Director, The Ogaki Kyoritsu Bank, Ltd. (Current Position)</p> <p>June 2020 Outside Director, Audit and Supervisory Committee Member, Mitsubishi UFJ Trust and Banking Corporation (Current Position)</p> <p>(Significant Concurrent Positions outside the Company)</p> <p>Outside Director, The Ogaki Kyoritsu Bank, Ltd.</p> <p>Outside Director, Audit and Supervisory Committee Member, Mitsubishi UFJ Trust and Banking Corporation</p>	2 years since March 2020	19,400
Deputy Chairperson of the Board	Mutsuo Iwai	October 29, 1960	<p>April 1983 Joined the Company (Japan Tobacco and Salt Public Corporation)</p> <p>June 2003 Vice President, Corporate Planning Division</p> <p>July 2004 Vice President, Corporate Strategy Division</p> <p>June 2005 Senior Vice President and Vice President, Food Business Division, Food Business</p> <p>June 2006 Member of the Board and Executive Vice President, President, Food Business</p> <p>June 2008 Executive Vice President, Chief Strategy Officer</p> <p>June 2010 Member of the Board and Senior Vice President, Chief Strategy Officer and Assistant to CEO in Food Business</p> <p>June 2011 Member of the Board Executive Vice President, JT International S.A.</p> <p>June 2013 Senior Executive Vice President, and Chief Strategy Officer</p> <p>January 2016 Executive Vice President, President, Tobacco Business</p> <p>March 2016 Representative Director and Executive Vice President</p> <p>January 2020 Member of the Board</p> <p>March 2020 Deputy Chairperson of the Board, the Company (Current Position)</p> <p>June 2020 Outside Director, Benesse Holdings, Inc. (Current Position)</p> <p>(Significant Concurrent Positions outside the Company)</p> <p>Outside Director, Benesse Holdings, Inc.</p>	2 years since March 2020	31,600

Title	Name	Date of birth	Summary of career			Term of office	Number of shares held (Share)
* Representative Director and President, Chief Executive Officer	Masamichi Terabatake	November 26, 1965	April 1989	Joined the Company		2 years since March 2020	77,800
			July 2005	Vice President, Secretary's Office			
			July 2008	Vice President, Corporate Strategy Division			
			June 2011	Senior Vice President, Chief Strategy Officer and in charge of Food Business			
			June 2012	Senior Vice President, Chief Strategy Officer			
			June 2013	Member of the Board Executive Vice President, JT International S.A.			
			January 2018	President and Chief Executive Officer, the Company			
			March 2018	Representative Director and President, Chief Executive Officer (Current Position) (Significant Concurrent Positions outside the Company) Chairman and Managing Director, JT International Group Holding B.V.			
* Representative Director and Executive Vice President	Naohiro Minami	January 21, 1964	April 1986	Joined the Company		2 years since March 2020	31,700
			December 2005	Controller			
			July 2010	Deputy Financial Officer and Controller			
			June 2012	Senior Vice President, Chief Financial Officer and Controller			
			July 2012	Senior Vice President, Chief Financial Officer			
			January 2018	Executive Vice President			
			March 2018	Representative Director and Executive Vice President (Current Position) (Significant Concurrent Positions outside the Company) Supervisory Board member, JT International Holding B.V.			
* Representative Director and Executive Vice President	Kiyohide Hirowatari	November 11, 1965	April 1989	Joined the Company		2 years since March 2020	28,500
			July 2010	Vice President, Legal Division			
			June 2012	Senior Vice President, Chief Legal Officer and Vice President, Legal Division			
			July 2014	Senior Vice President, Chief Legal Officer			
			January 2015	Senior Vice President, Head of Tobacco Business Planning Division, Tobacco Business			
			January 2017	Senior Vice President, Human Resources			
			January 2018	Executive Vice President			
			March 2018	Representative Director and Executive Vice President (Current Position)			
* Member of the Board	Kazuhito Yamashita	February 4, 1963	April 1986	Joined the Company		2 years since March 2020	20,100
			May 2007	Vice President, Corporate, Scientific & Regulatory Affairs Division, Tobacco Business Headquarters			
			July 2009	Vice President, Corporate Affairs Division, Tobacco Business Headquarters			
			June 2010	Senior Vice President, Chief Corporate, Scientific & Regulatory Affairs Officer, Tobacco Business			
			January 2015	Senior Vice President, Head of China Division, Tobacco Business			
			January 2019	Senior Vice President, Chief Sustainability Officer, Compliance and General Affairs			
			March 2019	Member of the Board and Senior Vice President (Current Position)			

Title	Name	Date of birth	Summary of career	Term of office	Number of shares held (Share)
Member of the Board	Main Kohda	April 25, 1951	<p>September 1995 Started independently as Novelist (Current Position)</p> <p>January 2003 Member of Financial System Council, Ministry of Finance Japan</p> <p>April 2004 Visiting professor, Faculty of Economics, Shiga University</p> <p>March 2005 Member of the Council for Transport Policy, Ministry of Land, Infrastructure, Transport and Tourism</p> <p>November 2006 Member of the Tax Commission, Cabinet Office, Government of Japan</p> <p>June 2010 Member of the Board of Governors, Japan Broadcasting Corporation</p> <p>June 2012 Outside Director, the Company (Current Position)</p> <p>June 2013 Outside Director, LIXIL Group Corporation</p> <p>June 2016 Outside Director, Japan Exchange Group, Inc. (Current Position)</p> <p>June 2018 Outside Director, MITSUBISHI MOTORS CORPORATION (Current Position)</p> <p>(Significant Concurrent Positions outside the Company)</p> <p>Novelist</p> <p>Outside Director, Japan Exchange Group, Inc.</p> <p>Outside Director, MITSUBISHI MOTORS CORPORATION</p>	2 years since March 2020	0
Member of the Board	Yukiko Nagashima	April 4, 1961	<p>April 1985 Joined Recruit Co., Ltd. (Current Recruit Holdings Co., Ltd.)</p> <p>April 2006 Corporate Executive Officer, Recruit Co., Ltd.</p> <p>January 2008 President and Representative Director, Recruit Staffing Co., Ltd.</p> <p>October 2012 Corporate Executive Officer, Recruit Holdings Co., Ltd.</p> <p>June 2016 Standing Audit and Supervisory Board Member, Recruit Holdings Co., Ltd. (Current Position)</p> <p>April 2018 Standing Audit and Supervisory Board Member, Recruit Co., Ltd. (Current Position)</p> <p>March 2019 Outside Director, the Company (Current Position)</p> <p>(Significant Concurrent Positions outside the Company)</p> <p>Standing Audit and Supervisory Board Member, Recruit Holdings Co., Ltd.</p> <p>Standing Audit and Supervisory Board Member, Recruit Co., Ltd.</p>	2 years since March 2020	0

Title	Name	Date of birth	Summary of career		Term of office	Number of shares held (Share)
Member of the Board	Masato Kitera	October 10, 1952	April 1976	Joined the Ministry of Foreign Affairs	1 year since March 2021	0
			January 2008	Director-General for Sub-Saharan African Affairs, Middle Eastern and African Affairs Bureau, and Secretary-General, TICAD IV, Ministry of Foreign Affairs		
			July 2008	Director-General, International Cooperation Bureau, Ministry of Foreign Affairs		
			January 2010	Deputy Vice Minister		
			September 2012	Assistant Chief Cabinet Secretary		
			November 2012	Ambassador of Japan to the People's Republic of China		
			April 2016	Ambassador of Japan to the Republic of France		
			June 2016	Ambassador of Japan to the Republic of France, Andorra and Monaco		
			April 2020	Advisor, the Company		
			June 2020	External Director, Marubeni Corporation (Current Position)		
				Outside Director, NIPPON STEEL CORPORATION (Current Position)		
			March 2021	Outside Director, the Company (Current Position)		
			(Significant Concurrent Positions outside the Company)			
			External Director, Marubeni Corporation			
			Outside Director, NIPPON STEEL CORPORATION			
Audit & Supervisory Board Member	Ryoko Nagata	July 14, 1963	April 1987	Joined the Company	4 years since March 2019	12,400
			April 2001	Vice President, Head of Products Division, Food Business Division, Food Business Headquarters		
			June 2008	Senior Vice President, Head of Beverage Business Division, Food Business Headquarters and Products Division, Food Business Division, Food Business		
			July 2008	Senior Vice President, Head of Beverage Business Division, Food Business Headquarters		
			July 2010	Senior Vice President, Head of Beverage Business Division		
			June 2013	Senior Vice President, CSR		
			January 2018	Senior Vice President, Assistant to President		
			March 2018	Standing Audit & Supervisory Board Member (Current Position)		
Audit & Supervisory Board Member	Hiroshi Yamamoto	November 29, 1963	April 1987	Joined the Company	4 years since March 2019	2,600
			July 2008	Vice President, NTM Procurement Division, Tobacco Business		
			June 2012	Vice President, Operational Review and Business Assurance Division		
			March 2019	Standing Audit & Supervisory Board Member (Current Position)		

Title	Name	Date of birth	Summary of career			Term of office	Number of shares held (Share)
Audit & Supervisory Board Member	Toru Mimura	December 26, 1955	April 1979	Entered Ministry of Finance		4 years since March 2019	0
			July 2010	Deputy Director-General of the Planning and Coordination Bureau, and Secretary-General of the Executive Bureau, Certified Public Accountants and Auditing Oversight Board, Financial Services Agency			
			July 2011	Director General, Kinki Local Finance Bureau, Ministry of Finance			
			January 2012	Deputy Director-General, Minister’s Secretariat, Ministry of Defense			
			September 2012	Director General, Bureau of Personnel and Education, Ministry of Defense			
			July 2013	Director General, National Institute for Defense Studies, Ministry of Defense			
			July 2014	Director General, Bureau of Finance and Equipment, Ministry of Defense			
			October 2015	Vice-Minister of Defense for International Affairs, Ministry of Defense			
			September 2016	Chairman, Sompo Japan Nipponkoa Research Institute Inc.			
			October 2017	Director, Eltes Co., Ltd.			
			March 2018	Registered as Attorney at Law			
			March 2019	Standing Outside Audit & Supervisory Board Member, the Company (Current Position)			
			(Significant Concurrent Positions outside the Company)				
Attorney at Law, Shiba International Law Offices							
Audit & Supervisory Board Member	Hiroshi Obayashi	June 17, 1947	April 1970	Judicial Apprentice		4 years since March 2019	0
			April 1972	Appointed as Public Prosecutor			
			May 2001	Director-General of the Rehabilitation Bureau, Ministry of Justice			
			January 2002	Deputy Vice Minister			
			June 2004	Director-General of the Criminal Affairs Bureau, Ministry of Justice			
			June 2006	Vice-Minister of Justice, Ministry of Justice			
			July 2007	Superintending Prosecutor, Sapporo High Public Prosecutors’ Office			
			July 2008	Superintending Prosecutor, Tokyo High Public Prosecutors Office			
			June 2010	Prosecutor-General			
			March 2011	Registered as Attorney at Law			
			April 2011	Outside Audit & Supervisory Board Member, Daiwa Securities Co., Ltd. (Current Position)			
			June 2013	Outside Director, Mitsubishi Electric Corporation (Current Position)			
			June 2014	Outside Audit & Supervisory Board Member, NIPPON STEEL & SUMITOMO METAL CORPORATION (Current NIPPON STEEL CORPORATION)			
			March 2015	Outside Audit & Supervisory Board Member, the Company (Current Position)			
			June 2020	Outside Director, Audit & Supervisory Committee Member, NIPPON STEEL CORPORATION (Current Position)			
			(Significant Concurrent Positions outside the Company)				
Attorney at Law, Obayashi Law Office							
Outside Audit & Supervisory Board Member, Daiwa Securities Co., Ltd.							
Outside Director, Mitsubishi Electric Corporation							
Outside Director, Audit & Supervisory Committee Member, NIPPON STEEL CORPORATION							

Title	Name	Date of birth	Summary of career		Term of office	Number of shares held (Share)
Audit & Supervisory Board Member	Koji Yoshikuni	September 7, 1952	April 1975	Joined Japan Broadcasting Corporation	4 years since March 2019	0
			June 2003	Director Responsible for Finance of News Department, Japan Broadcasting Corporation		
			June 2005	Executive Director, Yokohama Broadcasting Station, Japan Broadcasting Corporation		
			June 2007	Chief of Secretariat for Board of Governors, Japan Broadcasting Corporation		
			February 2010	Senior Director, Japan Broadcasting Corporation		
			April 2012	Executive Director, Japan Broadcasting Corporation		
			April 2017	Vice President, the Graduate School of Project Design Auditor, Hosei University (Current position)		
			March 2019	Outside Audit & Supervisory Board Member, the Company (Current Position)		
			April 2019	President, the Graduate School of Information & Communication (Current Position)		
Total						224,100

Notes: 1. Members of the Board Main Kohda, Yukiko Nagashima and Masato Kitera are Outside Directors.

2. Standing Audit & Supervisory Board Member Toru Mimura and Audit & Supervisory Board Members Hiroshi Obayashi and Koji Yoshikuni are Outside Audit & Supervisory Board Members.

3. Persons with the title marked with \* concurrently serve as Executive Officer.

4. The Company has introduced the Executive Officer System in June 2001 in order to realize prompt and proper decision-making and business execution. The following 25 persons were appointed effective March 24, 2021.

Title	Name	Post
President	Masamichi Terabatake	Chief Executive Officer
Executive Vice President	Naohiro Minami	Chief Financial Officer and Communications
Executive Vice President	Kiyohide Hirowatari	Corporate, Pharmaceutical Business and Food Business
Senior Vice President	Kazuhito Yamashita	Chief Sustainability Officer, Compliance and General Affairs
Senior Vice President	Junichi Fukuchi	Chief Executive Officer of Japanese Tobacco Business, Tobacco Business Planning, Tobacco Business
Senior Vice President	Yuki Maeda	Chief Financial Officer of Japanese Tobacco Business, Tobacco Business
Senior Vice President	Eiichi Kiyokawa	Sales, Tobacco Business
Senior Vice President	Kenji Ogura	Scientific & Regulatory Affairs, Tobacco Business
Senior Vice President	Chigusa Ogawa	Leaf Procurement, Tobacco Business
Senior Vice President	Yasuhiro Nakajima	Head of RRP Japan Office, Tobacco Business
Senior Vice President	Shuichi Hirosue	Marketing, Tobacco Business
Senior Vice President	Hiroyuki Miki	R&D, Tobacco Business
Senior Vice President	Akihiro Koyanagi	Manufacturing, Tobacco Business
Senior Vice President	Toru Oguchi	Head of China Division, Tobacco Business
Senior Vice President	Toru Hijikata	Quality Assurance, Tobacco Business
Senior Vice President	Muneaki Fujimoto	President, Pharmaceutical Business
Senior Vice President	Shigenori Ohkawa	Head of Central Pharmaceutical Research Institute, Pharmaceutical Business
Senior Vice President	Hiromasa Furukawa	Food Business
Senior Vice President	Kei Nakano	Corporate Strategy
Senior Vice President	Takehisa Shibayama	Digitalization
Senior Vice President	Takanori Kikuchi	General Affairs
Senior Vice President	Koichi Mori	Human Resources
Senior Vice President	Hiroyuki Fukuda	Communications
Senior Vice President	Osamu Hirose	Legal
Senior Vice President	Hisato Imokawa	Sustainability Management

Note: President and Chief Executive Officer Masamichi Terabatake also serves as President, Tobacco Business.

#### b. Status of Outside Directors and Outside Audit & Supervisory Board Members

- Numbers of Outside Directors and Outside Audit & Supervisory Board Members as well as their human, capital, business or other relationships of interest

The Company has three Outside Directors and three Outside Audit & Supervisory Board Members.

Outside Director Ms. Main Kohda previously served as a Member of the Board of Governors of Japan Broadcasting Corporation (“NHK”), and now concurrently serves as an Outside Director of Japan Exchange Group, Inc. Although the Company has relationships involving payments with both organizations, the amount paid came to less than 0.001% of NHK’s consolidated total operating income in the fiscal year ended March 2020 and less than 0.005% of consolidated operating revenue for Japan Exchange Group, Inc. in the fiscal year ended March 2020, and the amount paid to each came to less than 0.001% of the Company’s consolidated revenue for the fiscal year ended December 31, 2020. Also, the payment relationship with NHK is for a certain level of receiving fees, which are based on the Broadcast Act and non-negotiable, and are not therefore categorized as business transactions. The Company has therefore concluded that there is no risk of a special relationship of interest arising.

Outside Director Ms. Yukiko Nagashima is a standing Audit and Supervisory Board Member of Recruit Holdings Co., Ltd. Although the Company has a business relationship with Recruit Holdings Co., Ltd. in the area of recruitment, etc., the value of the business was less than 0.01% of the consolidated revenue for Recruit Holdings Co., Ltd. in the fiscal year ended March 2020 and less than 0.01% of the Company’s consolidated revenue in the fiscal year ended December 31, 2020, and the Company has therefore concluded that there is no risk of a special relationship of interest arising.

Outside Director Mr. Masato Kitera is an External Director of Marubeni Corporation. Although the Company has a business relationship with Marubeni Corporation for materials procurement, etc., the value of the business was less than 0.001% of the consolidated revenue for Marubeni Corporation in the fiscal year ended March 2020 and less than 0.001% of the Company’s consolidated revenue in the fiscal year ended December 31, 2020. Furthermore, Mr. Masato Kitera received remuneration as a part-time advisor

of the Company from April 30, 2020, but this agreement has expired due to his election at the Ordinary General Meeting of Shareholders held on March 24, 2021. This remuneration was paid to him as consideration for his advice on the management and business of the Company based on the experience and insight he possesses, and satisfies the independence criteria (not more than ¥10 million) prescribed by the Company. The Company has therefore concluded that there is no risk of a special relationship of interest arising.

Outside Audit and Supervisory Board Member Mr. Toru Mimura previously served as a Director of Eltes Co., Ltd. Although the Company has a business relationship with Eltes Co., Ltd. in the area of web surveys, etc., the value of the business was less than 1.2% of the consolidated revenue for Eltes Co., Ltd. in the fiscal year ended February 2020 and less than 0.002% of the Company's consolidated revenue in the fiscal year ended December 31, 2020, and the Company has therefore concluded that there is no risk of a special relationship of interest arising.

Outside Audit and Supervisory Board Member Mr. Hiroshi Obayashi concurrently serves as an Outside Director of Mitsubishi Electric Corporation and an Outside Audit & Supervisory Board Member of Daiwa Securities Co., Ltd. Daiwa Securities Co., Ltd. holds shares of the Company, but this constitutes less than 0.01% of the total shares. In addition, although the Company has business relationships with both companies, the value of the business was less than 0.001% of the consolidated revenue for Mitsubishi Electric Corporation in the fiscal year ended March 2020, less than 0.001% of the consolidated operating revenue for Daiwa Securities Co., Ltd. in the fiscal year ended March 2020 and the amount paid to each came to less than 0.001% of the Company's consolidated revenue for the fiscal year ended December 31, 2020, and the Company has therefore concluded that there is no risk of a special relationship of interest arising.

Outside Audit and Supervisory Board Member Mr. Koji Yoshikuni previously worked for NHK. The payments involved in the relationship with NHK are as described above, and the Company has concluded that there is no risk of a special relationship of interest arising.

Other than the above, there are no human, capital, business or other relationships of interest that should be reported between the Company and the Outside Directors and Outside Audit & Supervisory Board Members.

- Outside Directors appointed and functions and roles of Outside Directors in corporate governance of the filing company

The Company has appointed Ms. Main Kohda, Ms. Yukiko Nagashima and Mr. Masato Kitera as Outside Directors. The Company expects that Ms. Kohda will draw on her high insight into international finance, her broad experience serving on governmental advisory bodies and other such forums, and also draw on her deep insight and objective point of view developed through her activities as a novelist. The Company also anticipates that Ms. Nagashima will leverage her experience acquired through her deep involvement in emerging businesses and corporate management, her experience as a Member of the Audit and Supervisory Boards, and also her high degree of knowledge cultivated through the perspectives of both management and auditing. Furthermore, the Company counts on Mr. Kitera to make use of his abundant international experience and knowledge concerning international affairs, gained through his long diplomatic career including his important positions as a government officer mostly in the Ministry of Foreign Affairs. Accordingly, as well as expecting that all their experiences will be reflected in the management of the Company through their active provision of proposals and advice to the Board of Directors, the Company believes that they will supervise implementation of business from a fair and independent standpoint.

- Outside Audit & Supervisory Board Members appointed and functions and roles of Outside Audit & Supervisory Board Members in corporate governance of the filing company

Outside Audit & Supervisory Board Members are appointed in light of their significant experience in their respective backgrounds and broad perspective. The Company has appointed Mr. Toru Mimura, Mr. Hiroshi Obayashi and Mr. Koji Yoshikuni as Outside Audit & Supervisory Board Members. Mr. Mimura has developed extensive knowledge of such fields as finance, global risk management, geopolitics and company law through his extensive experience over many years of serving in a wide range of important positions in ministries and agencies, in addition to his role as research institute chairman. Mr. Obayashi has gained extensive experience in the legal circles and developed insightful perspectives based on experience as an Outside Director and Outside Audit & Supervisory Board Member across a wide range of industries. Mr. Yoshikuni has served in such roles at Japan Broadcasting Corporation as the Director Responsible for Finance of News Department, Chief of Secretariat for Board of Governors, and Executive Director. In



addition to his knowledge of politics and economics cultivated over long years in his journalistic career, his perspective is also informed by his management experience, characterized by thorough acquaintance with all business operations and internal departments. The Company expects that their experiences, perspectives and knowledge will be reflected in their audit activity, and the Company believes that they will maintain objective and neutral oversight of the management of the Company by conducting audits from a fair and independent standpoint.

- Independence of Outside Directors and Outside Audit & Supervisory Board Members

At the Board of Directors on April 26, 2012, the Company established a Criteria for Evaluating the Independence of Outside Executives. According to the Criteria, Independent Directors/Audit & Supervisory Board Members must not fall under any of the following categories.

1. A person who belongs or belonged to the Company or an affiliate or sister company of the Company
2. A person who belongs to a company or any other form of organization of which the Company is a major shareholder
3. A person who is a major shareholder of the Company or who belongs to a company or any other form of organization which is a major shareholder of the Company
4. A person who is a major supplier or customer of the Company (if the supplier or customer is a company or any other form of organization, a person who belongs thereto)
5. A major creditor of the Company including a major loan lender (if the creditor is a company or any other form of organization, a person who belongs thereto)
6. A certified public accountant who serves as an independent auditor or an audit advisor of the Company, or a person who belongs to an auditing firm which serves as an independent auditor or an audit advisor of the Company
7. A person who receives a large amount of fees from the Company in exchange for providing professional services for legal, financial and tax affairs or business consulting services (if the recipient of such fee is a company or any other form of organization, a person who belongs thereto)
8. A person who receives a large amount of donation from the Company (if the recipient of such donation is a company or any other form of organization, a person who belongs thereto)
9. A person who has fit any of the descriptions in 2 to 8 above in the recent past
10. A close relative of a person who fits any of the following descriptions:
  - (i) A person who fits any of the descriptions in 2 to 8 above (if such descriptions apply to a company or any other form of organization, a person who performs important duties thereof)
  - (ii) A member of the board, audit & supervisory board member, audit advisor, executive officer or employee of the Company or an affiliate or sister company of the Company
  - (iii) A person who has fit the descriptions in (i) or (ii) in the recent past.

Note:

- A company or any other form of organization of which the Company is a major shareholder  
A company or any other form of organization, in which the Company holds more than 10% of all shares issued
- A major shareholder of the Company, or a company or any other form of organization which is a major shareholder of the Company  
A person, or a company or any other form of organization, that holds more than 10% of all shares of the Company issued
- A major supplier or customer of the Company  
A person whose business with the Company accounts for more than 2% of the consolidated revenue of the Company, or a person whose business with the Company accounts for more than 2% of the consolidated revenue of the person

- A major creditor of the Company including a major loan lender  
A financial institution listed in the “Major Lenders” section of the Company’s Business Report, and a financial institution listed as a lender or a lead managing underwriter in materials released at the time of major M&A deals in the past, and at other times
- A person who receives a large amount of fees from the Company in exchange for providing professional services for legal, financial and tax affairs or business consulting services  
A person who receives fees of more than ¥10 million in a fiscal year from the Company in exchange for providing professional services for legal, financial and tax affairs or business consulting services.  
For a company or any other form of organization, this shall be 2% or more of total income in a fiscal year. However, even if the fees do not exceed 2%, in cases where consideration for services in which such professionals are directly involved exceeds ¥10 million, it shall be considered a large amount.
- A person who receives a large amount of donation from the Company  
A person who receives a donation of more than ¥10 million in a fiscal year from the Company. In cases where the recipient is a company or any other form of organization, a person belonging to an organization that receives a donation of ¥10 million in a fiscal year or the equivalent to 2% of the organization’s total annual income or consolidated revenue, whichever is the greater amount.
- A close relative  
A spouse or a relative within the second degree of kinship
- A person who performs important duties  
A person of head of division or executive rank
- Retrospective measure (criteria for judging “in the recent past”)  
The retrospective period shall be the past five years

Notwithstanding the above mentioned notes, as a result of investigations into the past and present state of employment of a candidate, it is judged that the person is in effect independent, that person may become an Outside Member of the Board or an Outside Audit & Supervisory Board Member after receiving the approval of the Board of Directors. In such cases, the grounds for the decision shall be disclosed publicly.

In light of the above set of criteria, the Company has designated Ms. Main Kohda, Ms. Yukiko Nagashima and Mr. Masato Kitera, who are Outside Directors, and Mr. Toru Mimura, Mr. Hiroshi Obayashi and Mr. Koji Yoshikuni, who are Outside Audit & Supervisory Board Members, as independent officers as defined by financial instruments exchanges.

To ensure that supervisory tasks and audits are conducted appropriately, information is shared regarding supervision and audit results and other steps are taken to ensure cooperation among operations involving supervision or audits performed by Outside Directors or Outside Audit & Supervisory Board Members, and operations involving internal audits, audits by Audit & Supervisory Board Members and audits by the Independent Auditor. To ensure appropriate implementation of business, information is exchanged as necessary and other means of cooperation are implemented among operations involving supervision or audits performed by Outside Directors or Outside Audit & Supervisory Board Members, and the Company’s Internal Control Division.

### **(3) Implementation status of audits**

#### **a. Status of audits by Audit & Supervisory Board Members**

##### **i. Organization, members and procedures for audits by Audit & Supervisory Board**

For the organization, members and procedures for audits by Audit & Supervisory Board, please refer to “(1) Outline of Corporate Governance, b. Outline of corporate governance structure and reason for adoption of the structure” and “(2) Status of Officers, b. Status of Outside Directors and Outside Audit & Supervisory Board

Members, Outside Audit & Supervisory Board Members appointed and functions and roles of Outside Audit & Supervisory Board Members in corporate governance of the filing company.”

ii. Status of Audit & Supervisory Board Members and Audit & Supervisory Board activities

During the fiscal year ended December 31, 2020, the Audit & Supervisory Board meeting was held a total of 13 times, with attendance at meetings for individual Audit & Supervisory Board Members being as follows:

Classification	Name	Attendance at meetings of the Audit & Supervisory Board
Audit & Supervisory Board Member	Ryoko Nagata	13/13 (100%)
Audit & Supervisory Board Member	Hiroshi Yamamoto	13/13 (100%)
Standing Outside Audit and Supervisory Board Member	Toru Mimura	13/13 (100%)
Outside Audit & Supervisory Board Member	Hiroshi Obayashi	13/13 (100%)
Outside Audit & Supervisory Board Member	Koji Yoshikuni	13/13 (100%)

The major items considered by the Audit & Supervisory Board included the auditing policies, legality of the business report and accompanying supplemental schedules, as well as the appropriateness of execution of duties by directors, the state of the rollout and operation of the internal control system, and the reasonableness of the methods used by the Independent Auditor, and of the results thus obtained.

Other activities conducted by Audit & Supervisory Board Members were the exchange of opinions with the Board of Directors of the Company, attendance at important meetings of the Board of Directors, the reading of documents for important resolutions, etc., surveys of operations and the status of assets at the Company and its subsidiaries, the exchange of opinions with directors and Audit & Supervisory Board Members of subsidiaries, and checking progress reports and the reported results for audits implemented by the Independent Auditor.

b. Status of internal audit

The internal audit system is an entity independent of the organizations responsible for business execution that reports directly to the President and is overseen by the Operational Review and Business Assurance Division (21 employees as of December 31, 2020) of the Company. The internal audit system uses an objective position to examine and evaluate systems for supervising and managing the overall operations and the status of business execution from the viewpoints of legality and rationality, in order to protect the Company’s assets and improve management efficiency. The Operational Review and Business Assurance Division has the authority to observe all activities, inspect all records and question all personnel of the entire Group without restrictions in order to fulfill its responsibilities. Moreover, in coordination with the internal audit functions of all subsidiaries, the Operational Review and Business Assurance Division also undertakes the planning and performance of the Group’s internal audit systems and policies, and supplements the internal audit functions of subsidiaries.

The Company’s Vice President of the Operational Review and Business Assurance has an obligation to report the results of audits to the President and Chief Executive Officer, and reports to the Board of Directors every year.

c. Implementation status of accounting audits

The Company, in order to ensure the Independent Auditor’s appropriate audit, secures sufficient time for audit enabling high-quality audit and provide the Independent Auditor with opportunities to contact Members of the Board and Executive Officers, as well as provide appropriate auditing environment enabling sufficient cooperation between the Independent Auditor and Audit & Supervisory Board Members, the internal auditing division and Outside Directors. Further, in the event that an Independent Auditor indicates a deficiency or problem or discovers misconduct, the Company shall appropriately take measures correspondingly.

While Audit & Supervisory Board Members, internal audit organizations including the Operational Review and Business Assurance Division, and the Independent Auditor conduct audits individually, they endeavor to enhance their cooperation in order to ensure appropriate audits, for example by sharing information on the results of their respective audits. Also, Audit & Supervisory Board Members, internal audit organizations including the Operational Review and Business Assurance Division, and the Independent Auditor cooperate

with the Company's Internal Control Division to ensure appropriate implementation of business by exchanging information when necessary.

i. Name of auditing firm

Deloitte Touche Tohmatsu LLC

ii. Continuous audit period

36 years

iii. Certified public accountants

Yukitaka Maruchi, Yasuhiko Haga, Yoichi Matsushita

iv. Assistants for the audit work

Certified public accountants: 9 persons, People who have passed the Certified Public Accountants Examination: 7 persons, Others: 16 persons

v. Policy and reasons for selecting the Independent Auditor

The Audit & Supervisory Board has established the "Standards for Evaluating and Selecting Independent Auditor." The evaluation and selection of Independent Auditor are conducted in accordance with said standards, and are based on a comprehensive judgment, considering the various factors such as independence from the Company, degree of expertise, adequate experience, size and overseas network which enables efficient implementation of accounting services corresponding to the Company's broad range of business, well established auditing system, fair and reasonable audit plans and expenses.

In the case that an Independent Auditor is adjudged to fall within any of the items listed in Article 340, paragraph 1 of the Companies Act, with the agreement of all of the Audit & Supervisory Board Members, the Company shall dismiss the Independent Auditor. Additionally, apart from the above, should an incident occur casting serious doubt on the ability of the Independent Auditor to continue to perform its duties, the Audit & Supervisory Board shall decide the content of proposal and submit such proposal to the General Meeting of Shareholders that the Independent Auditor should be dismissed or should not be reappointed.

vi. Evaluation of the Independent Auditor by the Audit & Supervisory Board

The Audit & Supervisory Board of the Company conducts evaluations of the Independent Auditor. Evaluation items are established in relation to the independence and expertise of the Independent Auditor, as well as the appropriateness and reasonableness of their audit activities. The materials required to evaluate each item are obtained from the relevant departments within the Company and from the Independent Auditor, and through reports, in order to assess audit quality.

d. Audit fees

i. Audit fees paid to certified public accountants

(Millions of yen)

Classification	Fiscal year ended December 31, 2019		Fiscal year ended December 31, 2020	
	Fees for audit attestation services	Fees for non-audit services	Fees for audit attestation services	Fees for non-audit services
The Company	325	95	330	85
Consolidated subsidiaries	115	32	115	42
Total	440	127	445	127

Note: Fees paid to Deloitte Touche Tohmatsu LLC.

Details of non-audit services for the Company are as follows.

*Fiscal year ended December 31, 2019*

Non-audit services for which fees are paid by the Company to certified public accountants include the advisory services relating to sustainability management and the issuance of the comfort letter in relation to the bond issuing.

*Fiscal year ended December 31, 2020*

Non-audit services for which fees are paid by the Company to certified public accountants include the advisory services relating to sustainability management and the issuance of the comfort letter in relation to the bond issuing.

In addition, details of non-audit services for consolidated subsidiaries are as follows.

*Fiscal year ended December 31, 2019*

Non-audit services for which fees are paid by consolidated subsidiaries of the Company to certified public accountants include the enhancement of the governance system.

*Fiscal year ended December 31, 2020*

Non-audit services for which fees are paid by consolidated subsidiaries of the Company to certified public accountants include the enhancement of the governance system and support for the introduction of risk management.

ii. Audit fees paid to certified public accountants and organizations that belong to the same network (excluding i.)

(Millions of yen)

Classification	Fiscal year ended December 31, 2019		Fiscal year ended December 31, 2020	
	Fees for audit attestation services	Fees for non-audit services	Fees for audit attestation services	Fees for non-audit services
The Company	—	144	—	217
Consolidated subsidiaries	782	1,230	790	1,037
Total	782	1,374	790	1,254

Note: Fees paid to member firms of Deloitte Touche Tohmatsu Limited.

Details of non-audit services for the Company are as follows.

*Fiscal year ended December 31, 2019*

Non-audit services for which fees are paid by the Company to Deloitte Touche Tohmatsu Limited member firms include consulting services.

*Fiscal year ended December 31, 2020*

Non-audit services for which fees are paid by the Company to Deloitte Touche Tohmatsu Limited member firms include consulting services.

In addition, details of non-audit services for consolidated subsidiaries are as follows.

*Fiscal year ended December 31, 2019*

Non-audit services for which fees are paid by consolidated subsidiaries of the Company to Deloitte Touche Tohmatsu Limited member firms include tax consulting.

*Fiscal year ended December 31, 2020*

Non-audit services for which fees are paid by consolidated subsidiaries of the Company to Deloitte Touche Tohmatsu Limited member firms include tax consulting.

iii. Other important fees for audit attestation services

No items to report.

iv. Policy for determining audit fees

The audit fee is determined through the necessary and sufficient negotiations with auditors based on the audit plan and audit fee estimates provided by them.

More specifically, the audit fee is determined based on the overall information by confirming that the focused audit areas under the audit plan and the scope of group-wide audit and review considering changes in consolidation status are appropriately reflected in the audit hours, and comparing the actual hours to planning in the prior audits.

Consent from the Audit & Supervisory Board is acquired before the determination of the audit fee to ensure the independence of auditors.

v. Reasons for approval of the Independent Auditor's remuneration by the Audit & Supervisory Board:

When the Company concluded an audit contract with Independent Auditor, the Audit & Supervisory Board Members obtained necessary materials and received reports from the Members of the Board, relevant internal departments, and the Independent Auditor, and performed verification to confirm that the amount of remuneration to be paid to the Independent Auditor, the persons in charge of the audits, and other details of the audit contract were appropriate.

Based upon this verification, the Audit & Supervisory Board checked and examined matters including the content of the Independent Auditor's accounting plan, the status of the performance of the auditing duties, and the basis for calculation of the remuneration estimate, and, as a result, determined that approval was fair and reasonable.

#### **(4) Remuneration for Members of the Board and Audit & Supervisory Board Members**

- a. Policy concerning the remuneration amount for Members of the Board and Audit & Supervisory Board Members or the remuneration calculation method thereof

i. Executive remuneration policy and method for determining remuneration amount

In order to achieve sustainable profit growth and increase of company value over the mid- to long-term by pursuing the Group's management principles of "4S model," the Advisory Panel on Nomination and Compensation reviews and provides advice on the policy, framework and calculation method for remuneration of the Company's Members of the Board and Executive Officers in response to inquiries from the Board of Directors. It also monitors whether our executive remuneration level is reasonable.

In light of reports by the Advisory Panel on Nomination and Compensation, the Company's basic concept of remuneration for Members of the Board and Audit & Supervisory Board Members is as follows:

- Set the remuneration at an adequate level to retain personnel with superior capabilities.
- Link the remuneration to company performance so as to motivate executives to achieve their performance targets.
- Link the remuneration to company value in the mid- to long-term.
- Ensure transparency by implementing an objective and quantitative framework.

The amount of remuneration for Members of the Board is benchmarked based on a survey of remuneration of directors conducted by third parties, based on the remuneration levels of major domestic manufacturers that are expanding overseas with the similar size and profits. Specifically, after benchmarking the level of base salary of the directors and the percentage of variable remuneration for annual bonuses and mid- and long-term incentives, the amount of remuneration for each Member of the Board is decided by a resolution of the Company's Board of Directors, based on the deliberations of the Advisory Panel on Nomination and Compensation and within the maximum remuneration approved at the General Meeting of Shareholders. The remuneration of Audit & Supervisory Board Members is also benchmarked in the same way, and is determined by deliberation among the Audit & Supervisory Board Members within the maximum remuneration approved at the General Meeting of Shareholders.

ii. Executive Remuneration Structure

The remuneration for Members of the Board and Audit & Supervisory Board Members is made of four components. In addition to the monthly "base salary," there is an "executive bonus," which reflects the Company's business performance in the relevant fiscal year, a "restricted stock remuneration" and "performance share units," which are linked to the mid- to long-term company value of the Company. The Restricted Stock Remuneration Plan and the Performance Share Unit Plan were introduced in 2020 in order to strengthen the efforts to enhance the mid- to long-term company value and to further promote shared value with shareholders.

The composition of remuneration by member category is as follows:

- Remuneration for the Members of the Board who also serve as Executive Officers

For Members of the Board who also serve as Executive Officers (hereinafter referred to as "Eligible Directors"), remuneration consists of "base salary," "executive bonus," "restricted stock remuneration" and "performance share unit remuneration" as they are required to achieve results by executing their duties on a daily basis.

If the "executive bonus" and "performance share unit remuneration" are paid at the standard amount, the composition ratio for each type of remuneration is as follows.

	Base Salary	Short-Term Incentive Plan	Mid- and Long-Term Incentive Plan	
Ratio *1	Base Salary C. 33-42%	Executive Bonus C. 31-35%	Restricted Stock Remuneration *2	Performance Share Units *2
			C. 25-33%	
Payment Format	Cash		Shares	Shares & Cash *3

- \*1 The composition ratios vary depending on the duties of the Members of the Board. The ranges are indicated in the illustration.
- \*2 The ratio of restricted stock remuneration and performance share units is about 3 to 1.
- \*3 Under the Performance Share Unit Plan, 50% is paid as cash towards tax payment.
- \*4 The above illustration is based on certain assumptions of the Company's performance and the share price. The ratios may fluctuate depending on the Company's performance and the share price.

- Remuneration for the Members of the Board who do not serve as Executive Officers (excluding Outside Directors)

For Members of the Board (excluding Outside Directors) who do not serve as Executive Officers, remuneration is not linked to business performance but is composed of "base salary" alone, as they are required to make decisions on the JT Group management strategies aimed at enhancing corporate value and to fulfill supervisory functions including monitoring the implementation of mid- to long-term growth strategies, etc.

- Remuneration for the Outside Directors

Remuneration for the Outside Directors is composed of "base salary" alone and is not linked to business performance to ensure their independence.

- Remuneration for the Audit & Supervisory Board Members

Remuneration for the Audit & Supervisory Board Members is composed of "base salary" alone in light of their key responsibility to conduct audits.

(Composition of remuneration by member category)

		Base salary	Executive bonus	Restricted stock remuneration	Performance share units
Members of the Board (excluding Outside Directors)	Executive Officer	Applicable	Applicable	Applicable	Applicable
	Not an Executive Officer	Applicable	Not applicable	Not applicable	Not applicable
Outside Directors		Applicable	Not applicable	Not applicable	Not applicable
Audit & Supervisory Board Members		Applicable	Not applicable	Not applicable	Not applicable

### iii. Executive Remuneration Details

- Base salary

Executives will be remunerated with monthly base salary as per their responsibilities. Eligible Directors will be individually evaluated for achievement of their performance targets through execution of their duties that will lead to the Company's sustainable profit growth. Performance targets are set through interviews with the Company's President and Chief Executive Officer at the beginning of the fiscal year and evaluated at the end of year. The base salary for the following fiscal year will be set within certain range reflecting the individual performance evaluations. However, an individual performance evaluation will not be applicable for the Company's President and Chief Executive Officer.

- Executive bonus

Executive bonuses for Eligible Directors will be paid as monetary remuneration reflecting the performance



of a fiscal year. Adjusted operating profit at constant FX and profit results will be the key performance indicators (KPI) for the calculation of executive bonuses, which will be used to measure the performance of the business itself, which is the foundation of sustainable profit growth, as well as the achievement rate of profit growth, from the viewpoint of providing shared value with the shareholders. Executive bonus will comprise of adjusted operating profit at constant FX and profit in the ratio of 75% and 25%, respectively. Performance-linked payout will be based on the KPI achievement in the range of 0% - 200%. In a case where a Member of the Board who is a recipient of executive bonus has carried out certain wrongful behavior, the officer involved will be required to refund a part of the executive bonus already paid.

KPIs related to executive bonuses that were used to evaluate Group performance in the fiscal year ended December 31, 2020, and actual results, were as follows.

KPIs for Group performance (consolidated)	(Billions of yen)	
	Fiscal year ended December 31, 2020	
	Target	Result
Adjusted operating profit at constant FX	516.0	544.5
Profit attributable to owners of the parent company	305.0	310.3

- Restricted Stock Remuneration Plan

The Restricted Stock Remuneration Plan is designed to strengthen the shared value with shareholders and to enhance the corporate value over the mid- to long-term. Monetary remuneration claims are provided to Eligible Directors as remuneration associated with restricted stock in each fiscal year based on resolution of the Company's Board of Directors, and each Eligible Director receives allotment of ordinary shares of the Company by providing all the monetary remuneration claims by means of contribution in kind (the allotment is made by means of disposal of treasury shares). In disposal of ordinary shares of the Company due to this Plan, a restricted stock allotment agreement shall be concluded between the Company and each Eligible Director.

The monetary compensation towards the purchase of the Company's restricted stock will be decided based on the closing price of the Company's share at the Tokyo Stock Exchange as of the business day immediately preceding the resolution by the Board of Directors. However, if the Company share does not trade at the Tokyo Stock Exchange on the day prior to the resolution of the Company's Board of Directors, the closing price of the immediately preceding trading day will be used. This price of share will be decided by the Company's Board of Directors within a scope that is not particularly advantageous to the Eligible Directors who will receive the restricted stock.

In addition, the allocation of monetary remuneration claims to the Eligible Directors, assumes that such director accepts the compensation as contribution in kind and enters into the restricted stock allotment agreement.

The specific details of the Plan are as follows. Any other matters regarding the Plan shall be determined by the Company's Board of Directors.

(1) The total amount of monetary remuneration claims and number of shares

The total amount of monetary remuneration claims for all Eligible Directors together shall not exceed ¥210 million per year or the total number of ordinary shares allotted by the Company shall not exceed 115,200 shares per year. If there is a stock split, stock consolidation, or any other event requiring adjustment to the total number of share to be allocated after this Restricted Stock Remuneration Plan has been approved in the 35th Ordinary General Meeting of Shareholders (March 19, 2020), the relevant total number shall be adjusted accordingly within a reasonable range.

(2) Transfer restriction period and details

The restriction period will be 30 years ("Restriction Period"). During this period restrictions will be applied on the allotted shares ("Allotted Shares"), so that each Eligible Director is prohibited to transfer the Allotted Shares, pledge them, mortgage them, or use any arrangement to dispose them.

(3) Removal of transfer restrictions

In case any Eligible Director retires due to expiration of the term or resigns due to reasons deemed reasonable by the Company's Board of Directors, from a position as Member of the Board or any other positions separately specified by the Company's Board of Directors during the Restriction Period, the transfer restrictions will be removed on all the Allotted Shares.

(4) Revocation of Allotted Shares without any compensation

Allotted Shares will be revoked by the Company if an Eligible Director violates any laws and regulations or falls under any other event specified by the Company's Board of Directors during the Restriction Period, the Company retains the right to acquire all or part of the Allotted Shares without any compensation.

(5) Handling in the case of reorganization

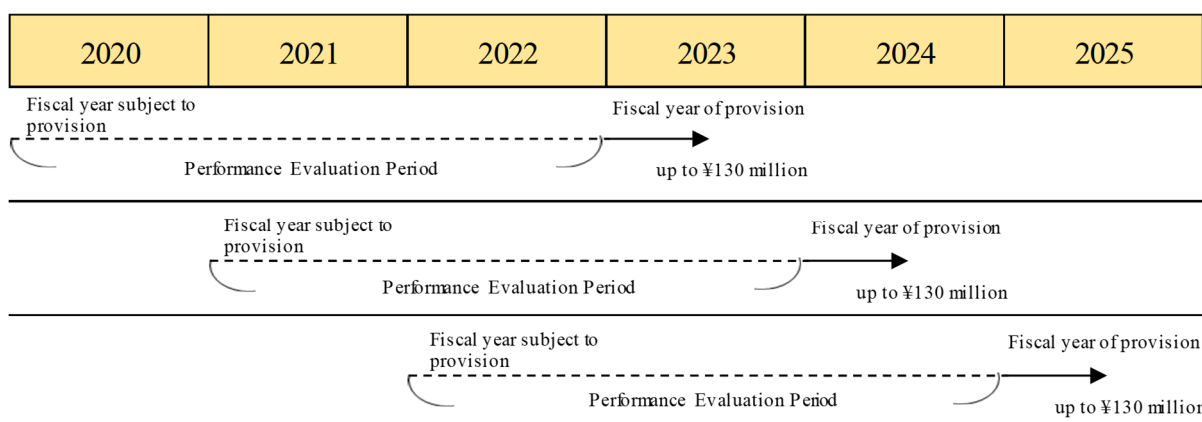
During the Restriction Period, if the Company becomes defunct due to merger or organization restructuring, the transfer restrictions for Allotted Shares will be removed following the resolution of the Company's Board of Directors before the effective date of such reorganization.

- Performance Share Unit Plan

The Performance Share Unit Plan is a performance-linked stock compensation system that aims to strengthen the shared value with shareholders, to enhance the corporate value over the mid- to long-term and to commit to achieving business results over the mid-term. The Plan offers monetary remuneration claims and cash to deliver the Company's ordinary shares, to the Eligible Directors. The monetary remuneration claims and cash are calculated after the performance evaluation period that is aligned with the duration of the Company's three-year Business Plan that starts from the fiscal year subject to provision (the "Performance Evaluation Period")\* in accordance with the rate of achievement of performance and other targets during the Performance Evaluation Period, which are determined through deliberations of the Advisory Panel on Nomination and Compensation of the Company. Thus, the monetary remuneration claims to deliver ordinary shares of the Company and cash are provided to Eligible Directors after the Performance Evaluation Period expires, in principle. Each of the Eligible Directors will receive the allocation of Company's ordinary shares by paying all of the monetary remuneration claims in kind (the allotment is made by means of disposal of treasury shares).

The monetary compensation towards the purchase of the Company's ordinary shares will be decided based on the closing price of the Company's share at the Tokyo Stock Exchange as of the business day immediately preceding the resolution by the Board of Directors. However, if the Company share does not trade at the Tokyo Stock Exchange on the day prior to the resolution of the Company's Board of Directors, the closing price of the immediately preceding trading day will be used. This price of share will be decided by the Company's Board of Directors within a scope that is not particularly advantageous to the Eligible Directors who will receive the performance share units. In addition, since monetary remuneration claims and cash to deliver the Company's ordinary shares are granted according to the above achievement rate of performance and other targets, the allocation of the monetary remuneration claims and cash to the Eligible Directors, the amount of the claims and cash to deliver the Company's ordinary shares, and the number of shares delivered are not decided by the expiration of the Performance Evaluation Period.

\*The first Performance Share Unit Plan is effective from the fiscal year of 2020 ending in 2022, with a three-year evaluation period. This Performance Share Unit Plan will be effective beyond 2021 and new evaluation period will start every year, further the remuneration will be decided with the limits approved in the Ordinary General Meeting of Shareholders.



The specific details of the Plan are as follows. Any other matters regarding the Plan shall be determined by the Company's Board of Directors.

(1) The total amount of monetary remuneration claims and cash and number of shares

The total amount of monetary remuneration claims and cash for all Eligible Directors together shall not

exceed ¥130 million per year or the total number of ordinary shares allotted by the Company shall not exceed 76,800 shares per year. If there is a stock split, stock consolidation, or any other event requiring adjustment to the total number of shares to be allocated has been approved in the 35th Ordinary General Meeting of Shareholders (March 19, 2020), the relevant total number shall be adjusted accordingly within a reasonable range.

(2) Share allotment and cash calculation methodology

The Company determines performance indicators and others such as performance-linked figures for the Plan which are necessary to specifically calculate the number of shares to be distributed, reviewed by the Advisory Panel on Nomination and Compensation of the Company. Profit has been set as the KPI for the Performance Evaluation Period that began from fiscal 2020 and fiscal 2021 from the perspective of providing shared value with shareholders. In the specific calculation, the number of shares of the Company to be distributed to each Eligible Director is calculated based on the formula in i) below (however, any fraction of less than one share shall be rounded down), and the amount of cash to be paid as funds for tax payment to each Eligible Director is calculated based on the formula in ii) below. In the case of retirement or new appointment or alike during the Performance Evaluation Period, the number of shares of the Company or the amount of cash to be delivered to the Eligible Director, or his/her heir, may be adjusted reasonably as stipulated by the Company's Board of Directors. In case that the above total number of Company shares allotted to the Eligible Directors is exceeded by allotting the number of shares of the Company calculated based on the formula in i) to each Eligible Director, the number of shares to be allotted to each Eligible Director shall be reduced by a reasonable method specified by the Company's Board of Directors, including a pro-rata basis, within a range not exceeding the maximum number of shares.

i) Number of Company shares to be distributed to each Eligible Director

Basic number of share units (\*1) X ratio of provision (\*2) X 50%

ii) Amount of monetary benefits to be paid to each Eligible Director

(Basic number of share units (\*1) X ratio of provision (\*2) – number of shares of the Company calculated in i) above) X share price at the time of delivery (\*3)

\*1 The number is determined by the Company's Board of Directors in accordance with duties of each Eligible Director and other factors.

\*2 Payment ratio for the KPI is set in the range of 0 - 200% according to the achievement rate of each numerical target during the Performance Evaluation Period.

\*3 The share price will be set as the closing price of the Company's ordinary shares at the Tokyo Stock Exchange as of the business day immediately preceding the resolution by the Board of Directors for the allotment of shares of the Company on the basis of the Plan after the Performance Evaluation Period expires. However, if the Company share does not trade at the Tokyo Stock Exchange on the day prior to the resolution of the Company's Board of Directors, the closing price of the immediately preceding trading day will be used. This price of share will be decided by the Company's Board of Directors within a scope that is not particularly advantageous to the Eligible Directors.

(3) Pre-requisites for distribution

The Company shall provide the monetary remuneration claims and cash to Eligible Directors, and Eligible Directors are required to purchase the Company's ordinary shares with all the monetary remuneration claims received as contribution in kind, after the Performance Evaluation Period expires and the following conditions for distribution of Company's ordinary shares are met.

- i) Remaining in his/her term of office as Member of the Board, Executive Officer or any other positions separately specified by the Board of Directors during the fiscal year subject to provision
- ii) Non-existence of certain illegal acts
- iii) Other requirements considered necessary, which are stipulated by the Board of Directors

(4) Handling in the case of reorganization

During the Performance Evaluation Period, if the Company becomes defunct due to merger or organization restructuring, the Company's Board of Directors may, prior to the effective date of the said organizational restructuring, decide to pay towards performance share units in accordance with the duration from the commencement date of the Performance Evaluation Period to the date of approval for the said organizational restructuring. However, in lieu of the aforementioned allocation of the Company's ordinary shares, cash will be reasonably calculated by the Company's Board of Directors as the amount equivalent to the said ordinary shares, within the limit of the remuneration for the Performance Share Unit Plan.

iv. Overview of the Resolutions on Total Executive Remuneration at the Ordinary General Meeting of Shareholders

At the 35th Ordinary General Meeting of Shareholders (held on March 19, 2020), approval was obtained for an upper limit to remuneration, consisting of base salary and executive bonuses, for the Company's Members of the Board (9 persons as of the filing date) of ¥1.1 billion per year for all Directors (including ¥80 million per year for Outside Directors). In addition, approval was obtained for the adoption of the Restricted Stock Remuneration Plan and Performance Share Unit Plan for those Members of the Board who also serve as Executive Officers (4 persons as of the filing date), after abolishing the previous stock option plan, and for upper limits of remuneration of ¥210 million per year for the Restricted Stock Remuneration Plan (equivalent to 115,200 shares), and not more than ¥130 million per year (equivalent to 76,800 shares) for the Performance Share Unit Plan, respectively.

The 35th Ordinary General Meeting of Shareholders (March 19, 2020)				
	Remuneration amount	Members of the Board (excl. Outside Directors)		Outside Directors
		Executive Officer	Not an Executive Officer	
Base salary	up to ¥1.1 billion (incl. ¥80 million for Outside Directors)	Applicable	Applicable	Applicable
Executive bonus		Applicable	Not applicable	Not applicable
Restricted stock remuneration	up to ¥210 million (up to 115,200 shares)	Applicable	Not applicable	Not applicable
Performance share units	up to ¥130 million (up to 76,800 shares)	Applicable	Not applicable	Not applicable
Total remuneration amount	up to ¥1.44 billion			

At the 34th Ordinary General Meeting of Shareholders (held on March 20, 2019), approval was obtained for an upper limit to remuneration for the Company's Audit & Supervisory Board Members (5 persons as of the filing date) of ¥240 million per year as a total for all Audit & Supervisory Board Members.

- v. Details of the activities of the Board of Directors and the Advisory Panel on Nomination and Compensation in relation to determining remuneration for Members of the Board and Audit & Supervisory Board Members

Details of activities related to determining remuneration for Members of the Board and Audit & Supervisory Board Members were as follows

Name	Number of meetings	Details of activities
Advisory Panel on Nomination and Compensation	4	Confirming the resolution tabled at the Ordinary General Meeting of Shareholders in relation to the executive remuneration plan revision, confirming the level of remuneration, etc.
Board of Directors	3	Introduction of new stock compensation system and determination of remuneration amount for Directors, revision and formulation of rules for executive remuneration associated with the executive remuneration plan revision, decisions related to the payment of a monetary remuneration claim for the allotment of restricted stock, etc.

- (ii) Total amount of remuneration and other payments, total amount of remuneration and other payments by type, and number of Members of the Board and Audit & Supervisory Board Members to be paid, by member category for the fiscal year ended December 31, 2020

Category	Total amount of remuneration and other payments (Millions of yen)	Total amount of remuneration and other payments by type (Millions of yen)					Number to be paid (Person)
		Base salary	Executive bonus	Stock option grants	Restricted stock remuneration	Performance share units	
Members of the Board (excluding Outside Directors)	1,193	504	438	30	188	33	6
Audit & Supervisory Board Members (excluding Outside Audit & Supervisory Board Members)	88	88	—	—	—	—	2
Outside Directors and Outside Audit & Supervisory Board Members	135	135	—	—	—	—	6
Total	1,416	727	438	30	188	33	14

- Notes: 1. For executive bonuses, the amounts planned to be paid are shown.  
2. For stock option grants, the recorded amount of stock option expenses for the period under review is shown (following a resolution of the 35th Ordinary General Meeting of Shareholders held on March 19, 2020, the previous stock option plan was abolished and the Restricted Stock Remuneration Plan and Performance Share Unit Plan were adopted).  
3. For performance share units, the recorded amount of expenses is shown.

- (iii) Total amount of consolidated remuneration and other payments for individuals whose consolidated remuneration and other payments amount to ¥100 million or more for the fiscal year ended December 31, 2020

Name	Category	Company	Amount of consolidated remuneration and other payments by type (Millions of yen)					Total (Millions of yen)
			Base salary	Executive bonus	Stock option grants	Restricted stock remuneration	Performance share units	
Masamichi Terabatake	Representative Director	Filing company	156	224	9	107	19	515
Naohiro Minami	Representative Director	Filing company	57	72	4	28	5	166
Kiyohide Hirowatari	Representative Director	Filing company	61	86	4	30	5	186
Kazuhito Yamashita	Member of the Board	Filing company	49	57	3	24	4	137

## (5) Share Ownership

### a. Basic concept and criteria for investment stock category

The Company categorizes stocks that are held exclusively for the purpose of profiting through fluctuations in share prices or from the receipt of dividends as “investment stocks held purely for the purpose of financial investment,” and all others as “investment stocks held for purposes other than financial investment” (strategic shareholdings).

### b. Investment stocks held for purposes other than financial investment

#### i. Shareholding policy, methods used to verify the reasonableness of shareholdings, and details of verification by the Board of Directors, etc. in relation to the suitability of holding individual issues

The Company has drawn up a policy regarding strategic holdings of listed stocks as well as criteria for the exercise of voting rights, as follows, and operates them appropriately.

- The Company maintains strategic shareholdings only in cases where it has concluded that they will contribute to mid- to long-term sustainable profit growth and to increases in corporate value.
- Such shareholdings are subject to detailed investigations, such as whether the purpose of holding each issue is appropriate, and whether the benefits and risks associated with the shareholding are reasonable in the light of capital costs, and the suitability of holding is subject to verification by the Board of Directors every year.
- In cases where, as a result of this verification, a stock is recognized to be lacking the rationale for holding, the stock is sold as and when appropriate.
- The Company exercises its voting rights in relation to strategic shareholdings after coming to a comprehensive judgment regarding the purpose of the shareholding and whether the value of the stock held is impaired.

#### ii. Number of issues and balance sheet amount

(Fiscal year ended December 31, 2020)

	Number of issues (Issue)	Balance sheet amount (Millions of yen)
Unlisted stocks	43	1,596
Stocks other than unlisted stocks	8	11,723

(Issues for which the number of shares increased in the fiscal year ended December 31, 2020)

	Number of issues (Issue)	Total acquisition cost associated with the increase in the number of shares (Millions of yen)	Reason for increase in the number of shares
Unlisted stocks	2	170	Establishment and strengthening of cooperative relationships for the pursuit and development of seeds in the medium to long term
Stocks other than unlisted stocks	—	—	

(Issues for which the number of shares decreased in the fiscal year ended December 31, 2020)

	Number of issues (Issue)	Total sales proceeds associated with the decrease in the number of shares (Millions of yen)
Unlisted stocks	—	—
Stocks other than unlisted stocks	3	2,953

iii. Number of shares for each specified investment stock and stock deemed to be held, and information related to balance sheet amount, etc.

Specified investment stocks

Issue	Fiscal year ended December 31, 2020	Fiscal year ended December 31, 2019	Purpose of the shareholding, quantitative effects of the shareholding, and the reason for increase in number of shares	Shares of the Company held
	Number of shares (Share)	Number of shares (Share)		
	Balance sheet amount (Millions of yen)	Balance sheet amount (Millions of yen)		
Seven & i Holdings Co., Ltd.	852,000	852,000	Dealings with the Company are ongoing, expressed in such ways as cooperation with the sales and sales promotion activities of the Domestic Tobacco Business, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	None
	3,117	3,411		
DOUTOR-NICHIRETS Holdings Co., Ltd.	1,320,000	1,320,000	Dealings with the Company are ongoing, expressed in such ways as cooperating with the Domestic Tobacco Business in the area of setting up environments divided into smoking and non-smoking zones, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	None
	1,958	2,859		
Japan Airport Terminal Co., Ltd.	400,000	400,000	Dealings with the Company are ongoing, expressed in such ways as cooperating with the Domestic Tobacco Business in the area of setting up environments divided into smoking and non-smoking zones, and in selling tobacco products in duty-free stores in airports and in urban locations. Shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	None
	2,500	2,436		
Central Japan Railway Company	100,000	100,000	Dealings with the Company are ongoing, expressed in such ways as cooperating with the Domestic Tobacco Business in the area of setting up environments divided into smoking and non-smoking zones, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	Yes
	1,459	2,200		



Yoshimura Food Holdings K.K.	1,052,500	1,052,500	The two companies exchange human resources and a variety of information with a view to enhancing corporate value, and shares are held for the purpose of maintaining and strengthening the stable long-term cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	None
	814	1,250		
NIPPON EXPRESS CO., LTD.	173,040	173,040	As a service provider that collaborates with the Domestic Tobacco Business in the area of distribution, dealings with the Company for the transportation of product are ongoing, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	Yes
	1,199	1,111		
Daicel Corporation	602,000	602,000	As a supplier for the tobacco products of the Domestic Tobacco Business, dealings with the Company for the procurement of materials are ongoing, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	Yes
	453	631		
Tokyo Automatic Machinery Works, Ltd.	134,700	134,700	As a supplier of tobacco production machinery to the Domestic Tobacco Business, dealings with the Company in relation to the procurement and maintenance of machinery and parts are ongoing, and shares are held for the purpose of maintaining and strengthening the stable long-term transactional and cooperative relationship. Although it is difficult to quantify the effects of the relationship, the suitability of the shareholding has been verified by the Board of Directors.	Yes
	223	212		
OKAMURA CORPORATION	—	1,206,000	As a result of the verification process conducted by the Board of Directors, all shares have been sold.	None
	—	1,343		
West Japan Railway Company	—	133,000	As a result of the verification process conducted by the Board of Directors, all shares have been sold.	None
	—	1,256		
Nifco Inc.	—	220,000	As a result of the verification process conducted by the Board of Directors, all shares have been sold.	None
	—	660		

Note: The approach used to verify each individual shareholding is as described in “b. Investment stocks whose purpose of holding is other than for financial investment, i. Shareholding policy, methods used to verify the reasonableness of shareholdings, and details of verification by the Board of Directors, etc. in relation to the suitability of holding individual issues” above.

Stocks deemed to be held

No items to report for the fiscal years ended December 31, 2019 and 2020.

c. Investment stocks held purely for the purpose of financial investment

No items to report for the fiscal years ended December 31, 2019 and 2020.

## **V. Accounting**

### **1. Preparation Policy of the Consolidated and Nonconsolidated Financial Statements**

- (1) The consolidated financial statements of Japan Tobacco Inc. (hereinafter referred to as the “Company”) are prepared in accordance with International Financial Reporting Standards (hereinafter referred to as “IFRS”) pursuant to the provisions of Article 93 of the Ordinance on Terminology, Forms and Preparation Methods of Consolidated Financial Statements (Ordinance of the Ministry of Finance No. 28 of 1976; hereinafter referred to as the Ordinance on CFS).
- (2) The nonconsolidated financial statements of the Company are prepared based on the Ordinance on Terminology, Forms, and Preparation Methods of Financial Statements (Ordinance of the Ministry of Finance No. 59 of 1963; hereinafter referred to as the Ordinance on FS). The Company is categorized as a company allowed to file specified financial statements, and prepares the nonconsolidated financial statements in accordance with the provisions of Article 127 of the Ordinance on FS.
- (3) Figures stated in the consolidated and nonconsolidated financial statements are rounded to the nearest million yen.

### **2. Audit Certification**

In accordance with the provisions of Article 193-2 (1) of the Financial Instruments and Exchange Act, the consolidated financial statements and the nonconsolidated financial statements for the year ended December 31, 2020 were audited by Deloitte Touche Tohmatsu LLC.

### **3. Special Effort to Ensure the Appropriateness of Consolidated Financial Statements, and Development of a System for Fair Preparation of Consolidated Financial Statements, in accordance with IFRS**

The Company is making special effort to ensure the appropriateness of consolidated financial statements, and developing a system for the appropriate preparation of consolidated financial statements, in accordance with IFRS. The content thereof is as follows:

- (1) In order to develop a system, which is capable of responding to changes of accounting standards adequately, we strive to accumulate expert knowledge by assigning employees with sufficient knowledge on IFRS, and participating in organizations, such as the Financial Accounting Standards Foundation and attending their seminars.
- (2) In order to prepare appropriate consolidated financial statements in accordance with IFRS, we established IFRS Group Accounting Guidelines and we comply with them. The IFRS Group Accounting Guidelines are revised and updated as needed after obtaining press releases and standards issued by the International Accounting Standards Board, understanding the latest standards and examining their impact on our results.

# 1. Consolidated Financial Statements

## (1) Consolidated Financial Statements

### A. Consolidated Statement of Financial Position

As of December 31, 2019 and 2020

		(Millions of yen)
	2019	2020
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents (Note 7)	357,158	538,844
Trade and other receivables (Note 8)	458,513	412,144
Inventories (Note 9)	583,695	539,762
Other financial assets (Note 10)	21,943	18,828
Other current assets (Note 11)	504,334	493,992
Subtotal	1,925,643	2,003,570
Non-current assets held for sale (Note 12)	30	348
Total current assets	1,925,673	2,003,919
<b>Non-current assets</b>		
Property, plant and equipment (Notes 13, 15)	803,239	759,290
Goodwill (Note 14)	2,002,595	1,909,392
Intangible assets (Note 14)	440,434	363,604
Investment property (Note 16)	16,588	4,744
Retirement benefit assets (Note 22)	67,377	70,528
Investments accounted for using the equity method	52,903	40,230
Other financial assets (Note 10)	109,568	107,143
Deferred tax assets (Note 17)	134,696	122,534
Total non-current assets	3,627,397	3,377,464
<b>Total assets</b>	<b>5,553,071</b>	<b>5,381,382</b>

		(Millions of yen)
	2019	2020
<b>Liabilities and equity</b>		
<b>Liabilities</b>		
<b>Current liabilities</b>		
Trade and other payables (Note 18)	408,597	436,540
Bonds and borrowings (Note 19)	284,135	141,469
Income tax payables	69,543	46,462
Other financial liabilities (Note 19)	21,862	27,588
Provisions (Note 20)	18,289	19,420
Other current liabilities (Note 21)	699,331	652,314
Total current liabilities	1,501,757	1,323,793
<b>Non-current liabilities</b>		
Bonds and borrowings (Note 19)	690,367	817,412
Other financial liabilities (Note 19)	41,062	50,164
Retirement benefit liabilities (Note 22)	320,614	331,752
Provisions (Note 20)	40,164	31,338
Other non-current liabilities (Note 21)	135,066	162,982
Deferred tax liabilities (Note 17)	80,430	64,447
Total non-current liabilities	1,307,702	1,458,095
Total liabilities	2,809,459	2,781,888
<b>Equity</b>		
Share capital (Note 23)	100,000	100,000
Capital surplus (Note 23)	736,400	736,400
Treasury shares (Note 23)	(492,469)	(491,507)
Other components of equity (Note 23)	(431,741)	(605,776)
Retained earnings	2,750,506	2,783,718
Equity attributable to owners of the parent company	2,662,696	2,522,834
Non-controlling interests	80,916	76,660
Total equity	2,743,611	2,599,495
<b>Total liabilities and equity</b>	<b>5,553,071</b>	<b>5,381,382</b>

**B. Consolidated Statement of Income**  
**Years Ended December 31, 2019 and 2020**

		(Millions of yen)
	2019	2020
Revenue (Notes 6, 25)	2,175,626	2,092,561
Cost of sales (Notes 14, 22)	(942,299)	(898,001)
Gross profit	1,233,326	1,194,560
Other operating income (Note 26)	95,725	54,924
Share of profit in investments accounted for using the equity method	5,011	4,042
Selling, general and administrative expenses (Notes 12, 13, 14, 16, 22, 27, 32)	(831,707)	(784,472)
Operating profit (Note 6)	502,355	469,054
Financial income (Notes 28, 33)	8,402	12,353
Financial costs (Notes 22, 28, 33)	(45,526)	(61,344)
Profit before income taxes	465,232	420,063
Income taxes (Note 17)	(103,609)	(108,034)
Profit for the period	361,622	312,029
<b>Attributable to</b>		
Owners of the parent company	348,190	310,253
Non-controlling interests	13,432	1,775
Profit for the period	361,622	312,029
<b>Earnings per share</b>		
Basic (Yen) (Note 30)	195.97	174.88
Diluted (Yen) (Note 30)	195.87	174.80

**Reconciliation from “Operating profit” to “Adjusted operating profit”**

		(Millions of yen)
	2019	2020
Operating profit	502,355	469,054
Amortization cost of acquired intangibles arising from business acquisitions	69,623	63,160
Adjustment items (income)	(84,467)	(51,978)
Adjustment items (costs)	28,415	6,716
Adjusted operating profit (Note 6)	515,927	486,952

**C. Consolidated Statement of Comprehensive Income**  
**Years Ended December 31, 2019 and 2020**

	2019	(Millions of yen) 2020
Profit for the period	361,622	312,029
<b>Other comprehensive income</b>		
<b>Items that will not be reclassified to profit or loss</b>		
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income (Notes 29, 33)	(2,484)	(2,702)
Remeasurements of defined benefit plans (Notes 22, 29)	(2,811)	(5,957)
Total of items that will not be reclassified to profit or loss	(5,295)	(8,659)
<b>Items that may be reclassified subsequently to profit or loss</b>		
Exchange differences on translation of foreign operations (Notes 29, 33)	9,879	(170,711)
Net gain (loss) on derivatives designated as cash flow hedges (Notes 29, 33)	(391)	224
Total of items that may be reclassified subsequently to profit or loss	9,489	(170,486)
Other comprehensive income (loss), net of taxes	4,194	(179,145)
Comprehensive income (loss) for the period	365,816	132,883
<b>Attributable to</b>		
Owners of the parent company	352,953	131,965
Non-controlling interests	12,863	919
Comprehensive income (loss) for the period	365,816	132,883

**D. Consolidated Statement of Changes in Equity**  
**Years Ended December 31, 2019 and 2020**

(Millions of yen)

	Equity attributable to owners of the parent company						
	Share capital	Capital surplus	Treasury shares	Subscription rights to shares	Other components of equity		
					Exchange differences on translation of foreign operations	Net gain (loss) on derivatives designated as cash flow hedges	Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income
<b>As of January 1, 2019</b>	100,000	736,400	(442,829)	1,547	(454,918)	443	29,570
Profit for the period	—	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	10,553	(391)	(2,486)
Comprehensive income (loss) for the period	—	—	—	—	10,553	(391)	(2,486)
Acquisition of treasury shares (Note 23)	—	—	(50,001)	—	—	—	—
Disposal of treasury shares (Note 23)	—	—	361	(281)	—	—	—
Share-based payments (Note 32)	—	—	—	290	—	—	—
Dividends (Note 24)	—	—	—	—	—	—	—
Changes in the scope of consolidation	—	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	—	—	—	—	—
Transfer from other components of equity to retained earnings	—	—	—	—	—	—	(15,883)
Other increase (decrease)	—	—	—	—	—	(185)	—
Total transactions with the owners	—	—	(49,640)	10	—	(185)	(15,883)
<b>As of December 31, 2019</b>	100,000	736,400	(492,469)	1,556	(444,366)	(132)	11,201
Profit for the period	—	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	(170,009)	224	(2,577)
Comprehensive income (loss) for the period	—	—	—	—	(170,009)	224	(2,577)
Acquisition of treasury shares (Note 23)	—	—	(1)	—	—	—	—
Disposal of treasury shares (Note 23)	—	—	963	(334)	—	—	—
Share-based payments (Note 32)	—	—	—	30	—	—	—
Dividends (Note 24)	—	—	—	—	—	—	—
Changes in the scope of consolidation	—	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	—	—	—	—	—
Transfer from other components of equity to retained earnings	—	—	—	—	—	—	(1,399)
Other increase (decrease)	—	—	—	—	—	30	—
Total transactions with the owners	—	—	962	(304)	—	30	(1,399)
<b>As of December 31, 2020</b>	100,000	736,400	(491,507)	1,252	(614,374)	122	7,224



(Millions of yen)

	Equity attributable to owners of the parent company					
	Other components of equity				Non-controlling interests	Total equity
	Remeasurements of defined benefit plans	Total	Retained earnings	Total		
As of January 1, 2019	—	(423,357)	2,660,381	2,630,594	69,851	2,700,445
Profit for the period	—	—	348,190	348,190	13,432	361,622
Other comprehensive income (loss)	(2,913)	4,763	—	4,763	(569)	4,194
Comprehensive income (loss) for the period	(2,913)	4,763	348,190	352,953	12,863	365,816
Acquisition of treasury shares (Note 23)	—	—	—	(50,001)	—	(50,001)
Disposal of treasury shares (Note 23)	—	(281)	(80)	0	—	0
Share-based payments (Note 32)	—	290	(19)	271	47	319
Dividends (Note 24)	—	—	(270,936)	(270,936)	(2,051)	(272,987)
Changes in the scope of consolidation	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	(1)	(1)	206	205
Transfer from other components of equity to retained earnings	2,913	(12,971)	12,971	—	—	—
Other increase (decrease)	—	(185)	—	(185)	—	(185)
Total transactions with the owners	2,913	(13,146)	(258,065)	(320,851)	(1,798)	(322,650)
As of December 31, 2019	—	(431,741)	2,750,506	2,662,696	80,916	2,743,611
Profit for the period	—	—	310,253	310,253	1,775	312,029
Other comprehensive income (loss)	(5,927)	(178,289)	—	(178,289)	(857)	(179,145)
Comprehensive income (loss) for the period	(5,927)	(178,289)	310,253	131,965	919	132,883
Acquisition of treasury shares (Note 23)	—	—	—	(1)	—	(1)
Disposal of treasury shares (Note 23)	—	(334)	(629)	0	—	0
Share-based payments (Note 32)	—	30	469	498	35	533
Dividends (Note 24)	—	—	(273,200)	(273,200)	(1,276)	(274,476)
Changes in the scope of consolidation	—	—	—	—	8	8
Changes in the ownership interest in a subsidiary without a loss of control	—	—	846	846	(3,941)	(3,095)
Transfer from other components of equity to retained earnings	5,927	4,528	(4,528)	—	—	—
Other increase (decrease)	—	30	—	30	—	30
Total transactions with the owners	5,927	4,254	(277,042)	(271,826)	(5,174)	(277,000)
As of December 31, 2020	—	(605,776)	2,783,718	2,522,834	76,660	2,599,495

**E. Consolidated Statement of Cash Flows**  
**Years Ended December 31, 2019 and 2020**

	2019	(Millions of yen) 2020
<b>Cash flows from operating activities</b>		
Profit before income taxes	465,232	420,063
Depreciation and amortization	183,852	179,654
Impairment losses	16,124	12,571
Interest and dividend income	(7,944)	(7,318)
Interest expense	27,557	22,535
Share of profit in investments accounted for using the equity method	(5,011)	(4,042)
(Gains) losses on sale and disposal of property, plant and equipment, intangible assets and investment property	(8,299)	(40,821)
(Increase) decrease in trade and other receivables	10,673	21,554
(Increase) decrease in inventories	(9,046)	748
Increase (decrease) in trade and other payables	28,294	39,288
Increase (decrease) in retirement benefit liabilities	(9,526)	(5,788)
(Increase) decrease in prepaid tobacco excise taxes	(21,864)	(29,996)
Increase (decrease) in tobacco excise tax payables	3,891	(18,038)
Increase (decrease) in consumption tax payables	29,592	9,762
Other	(7,005)	49,132
Subtotal	696,521	649,305
Interest and dividends received	15,340	14,589
Interest paid	(24,346)	(19,549)
Income taxes paid	(147,105)	(124,511)
Net cash flows from operating activities	540,410	519,833
<b>Cash flows from investing activities</b>		
Purchase of securities	(45,401)	(39,991)
Proceeds from sale and redemption of securities	77,200	49,802
Purchase of property, plant and equipment	(111,366)	(85,319)
Proceeds from sale of investment property	15,863	86,263
Purchase of intangible assets	(22,004)	(23,301)
Payments into time deposits	(218)	(491)
Proceeds from withdrawal of time deposits	409	334
Subsequent payments for past fiscal years' business combinations	(40,127)	(1,140)
Proceeds from sale of investments in associates	—	17,413
Other	2,073	1,785
Net cash flows from investing activities	(123,571)	5,354

		(Millions of yen)
	2019	2020
<b>Cash flows from financing activities</b>		
Dividends paid to owners of the parent company (Note 24)	(270,871)	(273,134)
Dividends paid to non-controlling interests	(1,913)	(1,404)
Capital contribution from non-controlling interests	358	117
Increase (decrease) in short-term borrowings and commercial paper (Note 31)	(44,976)	(132,462)
Proceeds from long-term borrowings (Note 31)	—	100,101
Repayments of long-term borrowings (Note 31)	(11,568)	(11,948)
Proceeds from issuance of bonds (Note 31)	59,435	122,201
Redemption of bonds (Note 31)	—	(80,000)
Repayments of lease liabilities (Note 31)	(14,294)	(17,741)
Acquisition of treasury shares	(50,001)	(1)
Payments for acquisition of interests in subsidiaries from non-controlling interests	(1)	(3,132)
Other	0	0
Net cash flows from financing activities	(333,832)	(297,404)
<b>Net increase (decrease) in cash and cash equivalents</b>	83,008	227,784
<b>Cash and cash equivalents at the beginning of the period</b>	282,063	357,158
<b>Effect of exchange rate changes on cash and cash equivalents</b>	(7,913)	(46,098)
<b>Cash and cash equivalents at the end of the period (Note 7)</b>	357,158	538,844

**Notes to Consolidated Financial Statements**  
**Years ended December 31, 2019 and 2020**

**1. Reporting Entity**

Japan Tobacco Inc. (hereinafter referred to as the “Company”) is a joint stock corporation under the Companies Act of Japan, pursuant to the Japan Tobacco Inc. Act, with its principal places of business located in Japan since its incorporation. The addresses of the Company’s registered head office and principal business offices are available on the Company’s website (<https://www.jt.com/>).

The details of businesses and principal business activities of the Company and its subsidiaries (hereinafter referred to as the “Group”) are stated in “6. Operating Segments.”

The Group’s consolidated financial statements for the year ended December 31, 2020 were approved on March 24, 2021 by Masamichi Terabatake, President and Chief Executive Officer.

**2. Basis of Preparation**

**(1) Compliance with IFRS**

The Group’s consolidated financial statements, which satisfy the requirements concerning the “Specified Company applying Designated International Financial Reporting Standards” prescribed in Article 1-2 of the “Regulations for Consolidated Financial Statements,” are prepared in accordance with IFRS pursuant to the provision of Article 93 of the same regulations.

**(2) Basis of Measurement**

Except for the financial instruments, stated in “3. Significant Accounting Policies,” and the accounting adjustments, stated in “37. Hyperinflationary Accounting Adjustments,” the Group’s consolidated financial statements are prepared on the historical cost basis.

**(3) Functional Currency and Presentation Currency**

The Group’s consolidated financial statements are presented in Japanese yen, which is the functional currency of the Company. The units are in millions of yen, and figures less than one million yen are rounded to the nearest million yen.

### 3. Significant Accounting Policies

#### (1) Basis of Consolidation

The consolidated financial statements include financial statements of the Company and its subsidiaries, and interests in investments in associates and joint arrangements.

##### A. Subsidiaries

A subsidiary is an entity that is controlled by the Group and the Group has control over the entity if it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The acquisition date of a subsidiary is the date on which the Group obtains control of the subsidiary, and the subsidiary is included in the consolidation from the date of acquisition until the date on which the Group loses control.

In cases where the accounting policies applied by a subsidiary are different from those applied by the Group, adjustments are made to the subsidiary's financial statements, if necessary.

All intergroup balances, transactions, income and expenses are eliminated on consolidation.

Comprehensive income for subsidiaries is attributed to owners of the parent company and non-controlling interests even if this results in the non-controlling interests having a deficit balance.

##### B. Associates

An associate is an entity over which the Group has significant influence. The Group has significant influence over the entity if it has the power to participate in the financial and operating policy decisions of the investee but it does not have control or joint control over the investee. Investments in associates are accounted for using the equity method from the date on which the Group has the significant influence until the date on which it ceases to have the significant influence.

##### C. Joint Arrangements

A joint arrangement is a contractual arrangement in which two or more parties have joint control. Depending upon the rights and obligations of the parties to the arrangement, the Group classifies a joint arrangement into a joint operation whereby the Group has rights to the assets and obligations for the liabilities relating to the arrangement, and a joint venture whereby the Group has rights to the net assets of the arrangement only. The Group recognizes the assets, liabilities, revenues and expenses relating to its interest in a joint operation while a joint venture is accounted for using the equity method.

## (2) Business Combination

Business combinations are accounted for using the acquisition method. Consideration transferred in a business combination is measured as the sum of the acquisition-date fair value of the assets transferred, the liabilities assumed and equity instruments issued by the Company in exchange for control over an acquiree. Any excess of the consideration of acquisition over the fair value of identifiable assets and liabilities is recognized as goodwill in the consolidated statement of financial position. If the consideration of acquisition is lower than the fair value of the identifiable assets and liabilities, the difference is immediately recognized as profit in the consolidated statement of income. If the amount of initial accounting for a business combination is not determined by the end of the reporting period in which the combination occurs, the provisional amounts for the items for which the accounting is incomplete are reported and are adjusted during the measurement period, which is one year from the acquisition date. Acquisition-related costs incurred are recognized as expenses. The additional acquisition of non-controlling interests after obtaining control is accounted for as a capital transaction. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in retained earnings and no goodwill is recognized with respect to such transaction.

## (3) Foreign Currency Translation

Consolidated financial statements of the Group are presented in Japanese yen, which is the functional currency of the Company. Each company in the Group specifies its own functional currency and measures transactions based on it. Foreign currency transactions are translated into the functional currency at the rates of exchange prevailing at the dates of transactions or an approximation of the rate. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rates of exchange prevailing at year end. Differences arising from the translation and settlement are recognized as profit or loss. However, exchange differences arising from the translation of financial instruments designated as hedging instruments for net investment in foreign operations (foreign subsidiaries), financial assets measured at fair value through other comprehensive income, and cash flow hedges are recognized as other comprehensive income.

The assets and liabilities of foreign operations are translated into Japanese yen at the rates of exchange prevailing at year end, while income and expenses of foreign operations are translated into Japanese yen at the rates of exchange prevailing at the dates of transactions or an approximation of the rate. The resulting translation differences are recognized as other comprehensive income. However, the income and expenses of the Group's subsidiaries in the hyperinflationary economy are translated into Japanese yen at the rates of exchange prevailing at the fiscal year end date in accordance with the hyperinflationary accounting. In cases where foreign operations are disposed of, the cumulative amount of translation differences related to the foreign operations is recognized as profit or loss in the period of disposition.

#### (4) Financial Instruments

##### A. Financial Assets

###### (i) Initial Recognition and Measurement

Financial assets are classified into financial assets measured at fair value through profit or loss, fair value through other comprehensive income, and amortized cost. The Group determines the classification at initial recognition. Financial assets are classified as financial assets measured at amortized cost if both of the following conditions are met. Otherwise, they are classified as financial assets measured at fair value.

- The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

For financial assets measured at fair value, each equity instrument is designated as measured at fair value through profit or loss or as measured at fair value through other comprehensive income, except for equity instruments held for trading purposes that must be measured at fair value through profit or loss. Such designations are applied consistently.

All financial assets are measured at fair value plus transaction costs that are attributable to the financial assets, except for the case of being classified in the category of financial assets measured at fair value through profit or loss.

###### (ii) Subsequent Measurement

After initial recognition, financial assets are measured based on the following classifications:

###### (a) Financial Assets Measured at Amortized Cost

Financial assets measured at amortized cost are measured at amortized cost using the effective interest method.

###### (b) Other Financial Assets

Financial assets other than those measured at amortized cost are measured at fair value.

Changes in the fair value of financial assets measured at fair value are recognized as profit or loss.

However, changes in the fair value of equity instruments designated as measured at fair value through other comprehensive income are recognized as other comprehensive income and the amount in other comprehensive income is transferred to retained earnings when equity instruments are derecognized or the decline in its fair value compared to its acquisition cost is significant. Dividends on the financial assets are recognized in profit or loss for the year.

###### (iii) Derecognition

Financial assets are derecognized when the rights to receive benefits from them expire or are transferred, or when substantially all the risks and rewards of the ownership are transferred.

## B. Impairment of Financial Assets

With respect to financial assets measured at amortized cost, the Group recognizes an allowance for doubtful accounts for expected credit losses. The expected credit losses are calculated based on historical loss experience or future recoverable amounts.

An allowance for doubtful accounts for trade receivables is always recognized in an amount equal to the full lifetime expected credit losses. In principle, with respect to financial assets except for trade receivables, an allowance for doubtful accounts is measured at an amount equal to the 12-month expected credit losses. However, the allowance for doubtful accounts is measured at an amount equal to the full lifetime expected credit losses if a credit risk on the financial asset has increased significantly since initial recognition.

The Group assesses whether a credit risk on a financial asset has increased significantly based on a change of the default risk considering past due information, financial difficulties of obligors or downgrades of the internal credit rating.

The Group assesses a whole or part of the financial asset which is deemed extremely difficult to be collected as a default and recognizes it as a credit-impaired financial asset. If the Group reasonably determines that a whole or part of the financial asset is uncollectible, the carrying amounts of financial assets are written-off directly.

The expected credit losses on trade receivables which are not assessed as credit-impaired financial assets are measured collectively by an asset group consisting of a number of homogeneous counterparties.

An allowance for doubtful accounts for financial assets is recognized in profit or loss. If an event which causes a reduction in the allowance for doubtful accounts occurs, a reversal of an allowance for doubtful accounts is recognized in profit or loss.

## C. Financial Liabilities

### (i) Initial Recognition and Measurement

Financial liabilities are classified into financial liabilities measured at fair value through profit or loss and financial liabilities measured at amortized cost. The Group determines the classification at initial recognition.

All financial liabilities are measured at fair value at initial recognition. However, financial liabilities measured at amortized cost are measured at cost after deducting transaction costs that are directly attributable to the financial liabilities.

### (ii) Subsequent Measurement

After initial recognition, financial liabilities are measured based on the following classifications:

#### (a) Financial Liabilities Measured at Fair Value through Profit or Loss

Financial liabilities measured at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated as measured at fair value through profit or loss at initial recognition.

#### (b) Financial Liabilities Measured at Amortized Cost

After initial recognition, financial liabilities measured at amortized cost are measured at amortized cost using the effective interest method. Amortization under the effective interest method and gains or losses on derecognition are recognized as profit or loss in the consolidated statement of income.

After initial recognition, financial guarantee contracts are measured at the higher of:

- The amount of an allowance for doubtful accounts calculated in accordance with “B Impairment of Financial Assets” above, and
- The amount initially measured less cumulative revenue recognized in accordance with IFRS 15 “Revenue from Contracts with Customers.”

### (iii) Derecognition

Financial liabilities are derecognized when the obligation is discharged, canceled or expired.

## D. Offsetting of Financial Instruments

Financial assets and financial liabilities are offset and presented as a net amount in the consolidated statement of financial position only when there is a legally enforceable right to set off the recognized amounts and the Group intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.



#### E. Derivatives and Hedge Accounting

The Group utilizes derivatives, including forward foreign exchange contracts and interest rate swap contracts, to hedge foreign exchange and interest rate risks. These derivatives are initially measured at fair value when the contract is entered into, and are subsequently remeasured at fair value. Changes in the fair value of derivatives are recognized as profit or loss in the consolidated statement of income. However, the gains or losses on the hedging instrument relating to the effective portion of cash flow hedges and hedges of net investment in foreign operations are recognized as other comprehensive income in the consolidated statement of comprehensive income.

At the inception of the hedge, the Group formally designates and documents the hedging relationship to which hedge accounting is applied and the objectives and strategies of risk management for undertaking the hedge. The documentation includes identification of the hedging instruments, the hedged items, the nature of the risks being hedged and how the hedging relationship's effectiveness is assessed. These hedges are assessed on an ongoing basis to determine whether the hedging relationship is effective prospectively, even though it is expected that there is an economic relationship between the hedged item and the hedging instrument, that the effect of credit risk does not dominate the value changes that result from that economic relationship, and that the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of the hedged item.

If a hedging relationship ceases to meet the hedge effectiveness requirement relating to the hedge ratio due to changes in an economic relationship between the hedged item and the hedging instrument but the risk management objective remains the same, the Group would adjust the hedge ratio so that it meets the qualifying criteria again. The Group discontinues hedge accounting for the portion that does not meet the requirement when the hedging relationship ceases to meet the qualifying criteria even after adjusting the hedge ratio.

Hedges that meet the stringent requirements for hedge accounting are classified in the following categories and accounted for in accordance with IFRS 9 "Financial Instruments."

##### (i) Fair Value Hedge

The gain or loss on the hedging instrument is recognized as profit or loss in the consolidated statement of income. However, changes in the fair value of the hedging instrument are recognized as other comprehensive income in the consolidated statement of comprehensive income if the hedging instrument hedges an equity instrument designated as at fair value through other comprehensive income. Regarding the hedging gain or loss on the hedged item, the carrying amount of the hedged item is adjusted and the change is recognized as profit or loss in the consolidated statement of income. However, changes in the fair value of an equity instrument which the Group elected to present in other comprehensive income are recognized as other comprehensive income.

##### (ii) Cash Flow Hedge

The effective portion of gains or losses on hedging instruments is recognized as other comprehensive income in the consolidated statement of comprehensive income, while the ineffective portion is recognized immediately as profit or loss in the consolidated statement of income.

The amounts of hedging instruments recognized in other comprehensive income are reclassified to profit or loss when the transactions of the hedged items affect profit or loss. In cases where hedged items result in the recognition of non-financial assets or liabilities, the amounts recognized as other comprehensive income are accounted for as adjustments to the original carrying amount of non-financial assets or liabilities.

If the hedged future cash flows are no longer expected to occur, any related cumulative gain or loss that has been recognized in equity as other comprehensive income is reclassified to profit or loss. If the hedged future cash flows are still expected to occur, amounts that have been recognized in other comprehensive income are continued to be recognized in other comprehensive income until the future cash flows occur.

##### (iii) Hedge of Net Investment in Foreign Operations

Translation differences resulting from the hedge of net investment in foreign operations are accounted for similarly to a cash flow hedge. The effective portion of gains or losses on hedging instruments is recognized as other comprehensive income in the consolidated statement of comprehensive income, while the ineffective portion is recognized as profit or loss in the consolidated statement of income. At the time of the disposal of the foreign operations, any related cumulative gain or loss that has been recognized in equity as other comprehensive income is reclassified to profit or loss.

#### F. Fair Value of Financial Instruments

Fair value of financial instruments that are traded in active financial markets at year end refers to quoted prices or dealer quotations.

If there is no active market, fair value of financial instruments is determined using appropriate valuation models.

#### (5) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, demand deposits, and short-term investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value and due within three months from the date of acquisition.

#### (6) Inventories

The cost of inventories includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Inventories are measured at the lower of cost or net realizable value, and the costs are determined by using the weighted-average method. Net realizable value is determined as the estimated selling price in the ordinary course of business less the estimated costs of completion and estimated costs necessary to make the sale.

Leaf tobacco which is stored for more than 12 months before being used for production is included in current assets since it is held within the normal operating cycle.

#### (7) Property, Plant and Equipment

Property, plant and equipment is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

The acquisition cost includes any costs directly attributable to the acquisition of the asset and dismantlement, removal and restoration costs, as well as borrowing costs eligible for capitalization.

Except for assets that are not subject to depreciation such as land, assets are depreciated using the straight-line method over their estimated useful lives. The estimated useful lives of major asset items are as follows:

- Buildings and structures: 38 to 50 years
- Machinery and vehicles: 10 to 15 years

The estimated useful lives and depreciation method are reviewed at each year end and if there are any changes made to the estimated useful lives and depreciation method, such changes are applied prospectively as changes in estimate.

## (8) Goodwill and Intangible Assets

### A. Goodwill

Goodwill is stated at acquisition cost less accumulated impairment losses.

Goodwill is not amortized. It is allocated to cash-generating units that are identified according to locations and types of businesses and tested for impairment annually or whenever there is any indication of impairment. Impairment losses on goodwill are recognized in the consolidated statement of income and no subsequent reversal is made.

### B. Intangible Assets

Intangible assets are measured by using the cost model and are stated at cost less accumulated amortization and accumulated impairment losses.

Intangible assets acquired separately are measured at cost at the initial recognition, and the costs of intangible assets acquired through business combinations are recognized at fair value at the acquisition date. Expenditures on internally generated intangible assets are recognized as expense in the period when incurred, except for development expenses that satisfy the capitalization criteria.

Intangible assets with finite useful lives are amortized using the straight-line method over their estimated useful lives and are tested for impairment whenever there is any indication of impairment. The estimated useful lives and amortization method of intangible assets with finite useful lives are reviewed at each year end, and the effect of any changes in estimate would be accounted for on a prospective basis.

The estimated useful lives of major intangible assets with finite useful lives are as follows:

- Trademarks: 10 to 20 years
- Software: 5 years

Intangible assets with indefinite useful lives and intangible assets that are not ready to use are not amortized, but they are tested for impairment individually or by cash-generating unit annually or whenever there is any indication of impairment.

## (9) Leases

At inception of a contract, the Group assesses whether the contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Group elects not to recognize right-of-use assets and lease liabilities for short-term leases within 12 months and leases of low-value assets. If a contract is, or contains, a lease, except for short-term leases and leases of low-value assets, the Group recognizes right-of-use assets and lease liabilities on the consolidated statement of financial position at the commencement date. The Group recognizes the lease payments associated with short-term leases and leases of low-value assets as an expense on a straight-line basis over the lease term.

Right-of-use asset is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

An acquisition cost of a right-of-use asset includes the amount of the initial measurement of the lease liability, any lease payments made at or before the commencement date, and any initial direct costs. The right-of-use asset is depreciated using the straight-line method over its estimated useful life or lease term, whichever is shorter. The lease liability is initially measured at the present value of the lease payment that is not paid at the commencement date. The lease payments are apportioned between the financial cost and the reduction in the lease liability based on the effective interest method. The financial costs are recognized in the consolidated statement of income.

## (10) Investment Property

Investment property is property held to earn rentals or for capital appreciation or both.

Investment property is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

(11) Impairment of Non-financial Assets

The Group assesses for each year whether there is any indication that an asset may be impaired. If any such indication exists, or in cases where the impairment test is required to be performed each year, the recoverable amount of the asset is estimated. In cases that the recoverable amount cannot be estimated for each asset, it is estimated by the cash-generating unit to which the asset belongs. The recoverable amount of an asset or a cash-generating unit is determined at the higher of its fair value less costs of disposal or its value in use. If the carrying amount of the asset or cash-generating unit exceeds the recoverable amount, impairment losses are recognized and the carrying amount is reduced to the recoverable amount. In determining the value in use, estimated future cash flows are discounted to the present value, using pretax discount rates that reflect current market assessments of the time value of money and the risks specific to the asset. In determining the fair value less costs of disposal, the Group uses an appropriate valuation model supported by available fair value indicators.

The Group assesses whether there is any indication that an impairment loss recognized in prior years for an asset other than goodwill may no longer exist or may have decreased, such as any changes in assumptions used for the determination of the recoverable amount. If any such indication exists, the recoverable amount of the asset or cash-generating unit is estimated. In cases that the recoverable amount exceeds the carrying amount of the asset or cash-generating unit, impairment losses are reversed up to the lower of the estimated recoverable amount or the carrying amount (net of depreciation) that would have been determined if no impairment losses had been recognized in prior years.

(12) Non-current Assets Held for Sale

An asset or asset group for which the value is expected to be recovered through a sales transaction rather than through continuing use is classified into a non-current asset or disposal group held for sale when the following conditions are met: it is highly probable that the asset or asset group will be sold within one year, the asset or asset group is available for immediate sale in its present condition, and the Group management commits to the sale plan. In such cases, the non-current asset is not depreciated or amortized and is measured at the lower of its carrying amount or its fair value less costs of disposal.

(13) Post-employment Benefits

The Group sponsors defined benefit plans and defined contribution plans as employee retirement benefit plans.

The Company is obligated to bear pension expenses for a mutual assistance association incurred with respect to services in or before June 1956 (prior to the enforcement of the Act on the Mutual Aid Association of Public Corporation Employees). Such obligations are calculated and included in liabilities related to the retirement benefits. For each plan, the Group calculates the present value of defined benefit obligations, related current service cost and past service cost using the projected unit credit method. For a discount rate, a discount period is determined based on the period until the expected date of benefit payment in each year, and the discount rate is determined by reference to market yields for the period corresponding to the discount period at the end of the year on high quality corporate bonds or government bonds. Liabilities or assets for defined benefit plans are calculated by the present value of the defined benefit obligation, deducting the fair value of any plan assets (including adjustments for the asset ceiling for defined benefit plans and minimum funding requirements, if necessary). Expected interest costs and interest income are recognized as financial costs.

Remeasurements of defined benefit plans are recognized in full as other comprehensive income in the period when they are incurred and transferred to retained earnings immediately. Past service costs are recognized as profit or loss in the period when incurred.

The cost for retirement benefits for defined contribution plans is recognized as an expense at the time of contribution.

#### (14) Share-based Payments

The Group has a share option plan and a restricted stock remuneration plan as an equity-settled share-based payment plan. Share options are estimated at fair value at the grant date and are recognized as an expense over the vesting period in the consolidated statement of income after considering the number of share options that are expected to be eventually vested. The corresponding amount is recognized as an increase in equity in the consolidated statement of financial position. Restricted stock remuneration is estimated at fair value at the grant date and is recognized as an expense from the grant date over the vesting period in the consolidated statement of income, and the corresponding amount is recognized as an increase in equity in the consolidated statement of financial position.

The Group has a performance share unit plan as a share-based payment plan with cash alternatives. Performance share units are accounted as a cash-settled share-based payment transaction if, and to the extent that, the entity has incurred a liability to settle in cash or other assets, or as an equity-settled share-based payment transaction if, and to the extent that, no such liability has been incurred. A portion as an equity-settled share-based payment transaction is estimated at fair value of granted shares of the Company and is recognized as an expense over the vesting period in the consolidated statement of income, and the corresponding amount is recognized as an increase in equity in the consolidated statement of financial position. As for a portion as a cash-settled share-based payment transaction, the services received and liability incurred are estimated at fair value of the liability and are recognized as an expense over the vesting period in the consolidated statement of income, and the corresponding amount is recognized as an increase in liability in the consolidated statement of financial position.

The fair value of the liability is remeasured at the end of reporting period and at the date of settlement with any changes in fair value recognized in profit or loss.

#### (15) Provisions

The Group has present obligations (legal or constructive) resulting from past events and recognizes provisions when it is probable that the obligations are required to be settled and the amount of the obligations can be estimated reliably. Where the effect of the time value of money is material, the amount of provisions is measured at the present value of the expenditures expected to be required to settle the obligations. In calculating the present value, the Group uses the pretax discount rate reflecting current market assessments of the time value of money and the risks specific to the liability.

In accordance with IAS 37 “Provisions, Contingent Liabilities and Contingent Assets,” the Group recognizes a provision for restructuring when it has a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main scheme to those affected by it. Restructuring provisions include only the direct expenditures arising from the restructuring, which meet both of the following criteria:

- necessarily entailed by the restructuring;
- not associated with the ongoing activities of the entity.

(16) Revenue

A. Revenue from Contracts with Customers

Revenue is recognized based on the following five-step approach.

Step 1: Identify the contract with a customer

Step 2: Identify the performance obligations in the contract

Step 3: Determine the transaction price

Step 4: Allocate the transaction price to the performance obligations in the contract

Step 5: Recognize revenue when the entity satisfies a performance obligation

The Group mainly engages in the sale of tobacco products, prescription drugs, and processed foods. Revenue is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax.

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The amount after deducting the tobacco excise taxes and other transactions is presented as "Revenue" in the consolidated statement of income.

B. Interest Income

Interest income is recognized using the effective interest rate method.

C. Dividend Income

Dividend income is recognized when the shareholders' right to receive payment is established.

(17) Government Grants

Government grants are recognized at fair value when there is a reasonable assurance that the Group will comply with the conditions attached to them and receive the grants.

In the case that the government grants are related to expense items, they are recognized in profit or loss on a systematic basis over the period in which the related costs for which the grants are intended to compensate are recognized. With regard to government grants for assets, the amount of the grants is deducted from the acquisition cost of the assets.

(18) Borrowing Costs

With respect to assets that necessarily take a substantial period of time to get ready for their intended use or sale, the borrowing costs that are directly attributable to the acquisition, construction or production of the assets are capitalized as part of the acquisition cost of the assets. Other borrowing costs are recognized as an expense in the period when they are incurred.

#### (19) Income Taxes

Income taxes in the consolidated statement of income are presented as the total of current income taxes and deferred income taxes.

Current income taxes are measured at the amount that is expected to be paid to or refunded from the taxation authorities. For the calculation of the tax amount, the Group uses the tax rates and tax laws that have been enacted or substantively enacted by the end of the year. The current income taxes are recognized in profit or loss, except for taxes arising from items that are recognized in other comprehensive income or directly in equity and taxes arising from business combinations.

Deferred income taxes are calculated based on the temporary differences between the tax base for assets and liabilities and the carrying amount at year end. Deferred tax assets are recognized for deductible temporary differences, carryforward of unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which they can be utilized. Deferred tax liabilities are recognized for taxable temporary differences.

The deferred tax assets or liabilities are not recognized for the following temporary differences:

- the initial recognition of goodwill
- the initial recognition of assets or liabilities in transactions that are not business combinations and at the time of transaction, affect neither accounting profit nor taxable profit or tax loss
- deductible temporary differences arising from investments in subsidiaries and associates, and interests in joint ventures to the extent that it is probable that the timing of the reversal of the temporary difference in the foreseeable future and it is not probable that future taxable profits will be available against which they can be utilized
- taxable temporary differences arising from investments in subsidiaries and associates, and interests in joint ventures to the extent that the timing of the reversal of the temporary difference is controlled and that it is probable the temporary difference will not reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted by year end.

Assets and liabilities are recognized as estimated amounts if uncertain tax position of income taxes arising from interpretation of tax laws and regulations is probable.

The Company and certain subsidiaries apply for the consolidated taxation system.

#### (20) Treasury Shares

Treasury shares are recognized at cost and deducted from equity. No gain or loss is recognized on the purchase, sale or cancellation of the treasury shares. Any difference between the carrying amount and the consideration paid is recognized in capital surplus.

#### (21) Earnings per Share

Basic earnings per share are calculated by dividing profit or loss attributable to ordinary shareholders of the parent company by the weighted-average number of ordinary shares outstanding during the year, adjusted by the number of treasury shares. Diluted earnings per share are calculated by adjusting the effects of dilutive potential ordinary shares.

#### (22) Dividends

Dividend distributions to the shareholders of the Company are recognized as liabilities in the period in which, for year end dividends, the Annual Shareholders' Meeting approves the distribution and, for interim dividends, the Board of Directors approves the distribution.

(23) Contingencies

A. Contingent Liabilities

The Group discloses contingent liabilities in the notes to consolidated financial statements if it has possible obligations at year end, whose existence cannot be confirmed at that date, or if the obligations do not meet the recognition criteria of a provision described in “20. Provisions.”

B. Contingent Assets

The Group discloses contingent assets in the notes to consolidated financial statements if an inflow of future economic benefits to the Group is probable, but not virtually certain at year end.

(24) Adjusted Financial Measures

The adjusted financial measures are calculated by adding certain adjustment items to the non-adjusted financial data or by deducting the items from the non-adjusted financial data.

The adjustment items are determined by management’s judgment, taking into consideration the nature and frequency of the income and costs such that they provide effective comparative information on the Group performance and that they reflect the way of managing our business appropriately. Adjusted financial measures are presented in the consolidated statement of income and “6. Operating Segments.”

The adjusted financial measures are not defined under IFRS and are not comparable with equivalent indicators for other entities.



**(Changes in Accounting Policies)**

The Group has adopted the following new accounting standards, amended standards and new interpretations from the year ended December 31, 2020.

IFRS		Description of new standards and amendments
IFRS 3	Business Combinations	Amendments to definition of “business”
IFRS 16	Leases	Amendments to permit a practical expedient for COVID-19-related rent concessions

The adoption of the above standards and interpretations does not have a material impact on the consolidated financial statements.

Part of the consolidated financial statements for the year ended December 31, 2019 has been reclassified to conform with the presentation for the year ended December 31, 2020.

#### 4. Significant Accounting Estimates and Judgments

Preparation of consolidated financial statements of the Group requires management estimates and assumptions in order to measure income, expenses, assets and liabilities, and disclose contingencies as of the year end. These estimates and assumptions are based on the best judgment of management in light of historical experience and various factors deemed to be reasonable as of the year end. Given their nature, actual results may differ from those estimates and assumptions. The estimates and assumptions are continuously reviewed by management. The effects of a change in estimates and assumptions are recognized in the period of the change or the period of the change and future periods. Among the above estimates and assumptions, the following are items that may have a material effect on the amounts recognized in the consolidated financial statements of the Group:

##### A. Impairment of Property, Plant and Equipment, Goodwill, Intangible Assets and Investment Properties

With regard to property, plant and equipment, goodwill, intangible assets and investment properties, if there is any indication that the recoverable amount has declined below the carrying amount, the Group performs an impairment test.

Such indications include, but are not limited to significant changes with adverse effect on the results of past or projected business performance, significant changes in the use of acquired assets or in overall business strategy, and significant deteriorations in industry or economic trends. With regard to goodwill, an impairment test is conducted at least once a year, regardless of whether there are any indicators of impairment.

An impairment test is performed by comparing the carrying amount to the recoverable amount of the asset under assessment. If the recoverable amount is below the carrying amount, impairment losses are recognized. The recoverable amount is calculated based primarily on a discounted cash flow model. Certain assumptions must be made for the useful lives and future cash flows of the assets, the applicable discount rates as well as long-term growth rates. These assumptions are based on the best estimates and judgments made by management. However, there is a possibility that these assumptions will be affected by changes in uncertain future economic conditions, which may have a material impact on the consolidated financial statements in future periods.

The method for calculating the recoverable amount is described in “13. Property, Plant and Equipment,” “14. Goodwill and Intangible Assets” and “16. Investment Property.” With regard to goodwill, the sensitivity analysis is described in “14. Goodwill and Intangible Assets.”

##### B. Post-employment Benefits

The Group has various types of retirement benefit plans, including defined benefit plans. In addition, the mutual pension benefits plan of the Company is one of the public pension systems under the jurisdiction of the government of Japan and the Company is legally obligated to bear a part of the pension costs of the plan.

The present value of defined benefit obligations on each of these plans and the related service costs are calculated based on actuarial assumptions. These actuarial assumptions make use of estimates and judgments on a number of variables, including discount rates and inflation rate.

The Group obtains advice from external pension actuaries with respect to the appropriateness of their actuarial assumptions including the aforementioned variables.

The actuarial assumptions are determined based on the best estimates and judgments made by management. However, there is a possibility that these assumptions will be affected by changes in uncertain future economic conditions, or by the publication or amendment of related laws, which may have a material impact on the consolidated financial statements in future periods.

These actuarial assumptions and the related sensitivity analysis are described in “22. Employee Benefits.”

#### C. Provisions

The Group recognizes various provisions, including provisions for asset retirement obligations and restructuring, in the consolidated statement of financial position.

These provisions are recognized based on best estimates of the expenditure required to settle the obligations, taking into account the pertinent risks and uncertainties which exist at the year-end for those obligations.

Expenditures required to settle the obligations are calculated by taking possible results into account comprehensively; however, they may be affected by the occurrence of unexpected events or changes in conditions which may have a material impact on the consolidated financial statements in future periods.

The nature and amount of recognized provisions are described in “20. Provisions.”

#### D. Income Taxes

The Group operates business activities around the world, and it recognizes current tax liabilities and income taxes as the estimated amounts to be paid to the tax authorities, based on the estimation in accordance with their laws and regulations.

Calculating current tax liabilities and income taxes requires estimates and judgment on various factors, including the interpretation of tax regulations by taxable entities and the tax authority in the jurisdiction or the experience of past tax audits.

Therefore, there may be differences between the amount recognized as tax liabilities and income taxes and the amount of actual tax liabilities and income taxes. These differences may have a material impact on the consolidated financial statements in future periods.

In addition, deferred tax assets are recognized to the extent that it is probable that taxable income will be available against which deductible temporary differences can be utilized.

In recognizing the deferred tax assets, when judging the possibility of the future taxable income, we reasonably estimate the timing and amount of future taxable income based on the business plan.

The timing when taxable income arises and the amount of such income may be affected by changes in uncertain future economic conditions. Therefore, this may have a material impact on the consolidated financial statements in future periods.

The content and amount related to income taxes are described in “17. Income Taxes.”

#### E. Contingencies

With regard to contingencies, any items that may have a material impact on business in the future are disclosed in light of all the available evidence as of the year end and by taking into account the probability of these contingencies and their impact on financial reporting.

The content of contingencies is described in “38. Contingencies.”

The spread of COVID-19 has affected the Group businesses in the current fiscal year, causing a decrease in duty-free sales in the tobacco business and changes in consumer trends in the Domestic Tobacco Business and the Processed Food Business.

The Group anticipates that although the impact of the spread of COVID-19 will continue to certain extent from 2021 onward, the economies of countries around the world will gradually recover. At present, there is no material impact on accounting estimates and judgements.

## 5. New Accounting Standards Not Yet Adopted by the Group

By the date of approval of the consolidated financial statements, new accounting standards, amended standards and new interpretations that have been issued, but have not been early adopted by the Group are as follows.

The implications from adoption of these standards and interpretations are assessed by the Group; however, we evaluate that none of them will have a material impact on our operating results and financial condition.

	IFRS	Mandatory adoption (From the year beginning)	To be adopted by the Group	Description of new standards and amendments
IFRS 1	First-time Adoption of International Financial Reporting Standards	January 1, 2022	Year ending December 2022	Amendments to accounting treatment for measurement of cumulative translation differences if a subsidiary becomes a first-time adopter of IFRS later than its parent
IFRS 3	Business Combinations	January 1, 2022	Year ending December 2022	Amendments to update references to the conceptual framework
IFRS 4	Insurance Contracts	January 1, 2021	Year ending December 2021	Amendments to replace an existing interest rate benchmark with an alternative benchmark rate
IFRS 7	Financial Instruments Disclosures	January 1, 2021	Year ending December 2021	Amendments to replace an existing interest rate benchmark with an alternative benchmark rate
IFRS 9	Financial Instruments	January 1, 2021	Year ending December 2021	Amendments to replace an existing interest rate benchmark with an alternative benchmark rate
		January 1, 2022	Year ending December 2022	Clarifying fees and costs to be included in the 10 per cent test for derecognition of financial liabilities
IFRS 16	Leases	January 1, 2021	Year ending December 2021	Amendments to replace an existing interest rate benchmark with an alternative benchmark rate
IFRS 17	Insurance Contracts	January 1, 2023	Year ending December 2023	Amendments to accounting treatment for insurance contracts
IAS 1	Presentation of Financial Statements	January 1, 2023	Year ending December 2023	Clarifying classification of liabilities into current liabilities or non-current liabilities Amendments to require companies to disclose their material accounting policy information rather than their significant accounting policies
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	January 1, 2023	Year ending December 2023	Amendments to clarify how companies should distinguish changes in accounting policies from changes in accounting estimates
IAS 16	Property, Plant and Equipment	January 1, 2022	Year ending December 2022	Amendments to accounting treatment regarding proceeds from selling items produced while bringing the asset to the condition to be capable of operating in the manner intended
IAS 37	Provisions, Contingent Liabilities and Contingent Assets	January 1, 2022	Year ending December 2022	Clarifying the cost of fulfilling a contract for the purpose of assessing whether the contract is onerous
IAS 39	Financial Instruments Recognition and Measurement	January 1, 2021	Year ending December 2021	Amendments to replace an existing interest rate benchmark with an alternative benchmark rate

IFRS		Mandatory adoption (From the year beginning)	To be adopted by the Group	Description of new standards and amendments
IAS 41	Agriculture	January 1, 2022	Year ending December 2022	Removal of the requirement to use pre-tax exclude taxation cash flows when measuring the fair value of a biological assets
IFRS 10 IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	Not yet determined	Not yet determined	Amendments to accounting treatment for sale or contribution of assets between an investor and its associate or joint venture

## 6. Operating Segments

### (1) Outline of Reportable Segments

The reportable segments of the Group are determined based on the operating segments that are components of the Group for which separate financial information is available and are evaluated regularly by the Board of Directors in deciding how to allocate resources and in assessing performance.

The Group is mainly engaged in the manufacture and sale of tobacco products, prescription drugs and processed foods. With respect to tobacco products, operations are managed separately for domestic and overseas markets. The reportable segments of the Group are composed of four segments: “Domestic Tobacco Business,” “International Tobacco Business,” “Pharmaceutical Business,” and “Processed Food Business.” They are determined by the type of products sold, their characteristics, and their markets.

The “Domestic Tobacco Business” manufactures and sells tobacco products in domestic areas (which include duty-free shops in Japan and markets in China, Hong Kong, and Macau where the Company’s China Division operates). The “International Tobacco Business” manufactures and sells tobacco products overseas mainly through JT International S.A., which controls manufacturing and sales operations. The “Pharmaceutical Business” consists of research and development, and the manufacture and sale of prescription drugs. The “Processed Food Business” consists of the manufacture and sale of frozen and ambient processed foods, bakery products and seasonings.

## (2) Revenues and Performances of Reportable Segments

Revenues and performances of reportable segments are as follows. The Board of Directors assesses segment performance and determines resource allocation after reviewing revenues and adjusted operating profit. Since financial income, financial costs and income taxes are managed by the Group head office, these income and expense categories are excluded from segmental performance. Transactions within segments are primarily based upon prevailing market prices.

Year ended December 31, 2019

(Millions of yen)

	Reportable Segments					Other (Note 2)	Elimination	Consolidated
	Domestic Tobacco	International Tobacco	Pharma- ceuticals	Processed Food	Total			
Revenue								
External revenue	611,494	1,310,877	88,528	158,586	2,169,485	6,140	—	2,175,626
Intersegment revenue	7,270	27,626	—	1	34,897	7,333	(42,229)	—
Total revenue	<u>618,764</u>	<u>1,338,503</u>	<u>88,528</u>	<u>158,587</u>	<u>2,204,382</u>	<u>13,473</u>	<u>(42,229)</u>	<u>2,175,626</u>
Segment profit (loss)								
Adjusted operating profit (Note 1)	<u>187,180</u>	<u>340,752</u>	<u>15,943</u>	<u>5,432</u>	<u>549,308</u>	<u>(33,478)</u>	<u>97</u>	<u>515,927</u>
Other items								
Depreciation and amortization (Note 3)	59,276	108,378	5,936	7,586	181,176	2,909	(233)	183,852
Impairment losses on other than financial assets	7,751	5,765	1,471	220	15,207	917	—	16,124
Reversal of impairment losses on other than financial assets	—	91	—	—	91	—	—	91
Share of profit (loss) in investments accounted for using the equity method	16	4,863	—	10	4,889	122	—	5,011
Capital expenditures (Note 4)	34,793	78,295	6,979	6,142	126,209	5,609	(383)	131,434

Year ended December 31, 2020

(Millions of yen)

	Reportable Segments					Other (Note 2)	Elimination	Consolidated
	Domestic Tobacco	International Tobacco	Pharma- ceuticals	Processed Food	Total			
Revenue								
External revenue	555,568	1,306,233	78,957	149,329	2,090,087	2,474	—	2,092,561
Intersegment revenue	7,674	24,606	—	1	32,282	5,317	(37,599)	—
Total revenue	<u>563,242</u>	<u>1,330,839</u>	<u>78,957</u>	<u>149,330</u>	<u>2,122,369</u>	<u>7,791</u>	<u>(37,599)</u>	<u>2,092,561</u>
Segment profit (loss)								
Adjusted operating profit (Note 1)	<u>168,069</u>	<u>340,867</u>	<u>17,161</u>	<u>(793)</u>	<u>525,304</u>	<u>(38,201)</u>	<u>(152)</u>	<u>486,952</u>
Other items								
Depreciation and amortization (Note 3)	56,576	105,654	5,427	7,554	175,210	4,679	(234)	179,654
Impairment losses on other than financial assets	—	7,538	—	3,841	11,378	1,193	—	12,571
Reversal of impairment losses on other than financial assets	—	49	—	—	49	—	—	49
Share of profit (loss) in investments accounted for using the equity method	15	3,963	—	21	3,999	42	—	4,042
Capital expenditures (Note 4)	21,053	66,598	9,087	7,972	104,709	8,301	(127)	112,883

# Reconciliation from “Adjusted operating profit” to “Profit before income taxes”

Year ended December 31, 2019

(Millions of yen)

	Reportable Segments					Other (Note 2)	Elimination	Consolidated
	Domestic Tobacco	International Tobacco	Pharma- ceuticals	Processed Food	Total			
Adjusted operating profit (Note 1)	187,180	340,752	15,943	5,432	549,308	(33,478)	97	515,927
Amortization cost of acquired intangibles arising from business acquisitions	(16,245)	(53,378)	—	—	(69,623)	—	—	(69,623)
Adjustment items (income) (Note 5)	24	8,776	61,018	461	70,278	14,189	—	84,467
Adjustment items (costs) (Note 6)	—	(22,141)	(4,264)	(365)	(26,770)	(1,646)	—	(28,415)
Operating profit (loss)	170,960	274,008	72,697	5,528	523,193	(20,935)	97	502,355
Financial income								8,402
Financial costs								(45,526)
Profit before income taxes								465,232

Year ended December 31, 2020

(Millions of yen)

	Reportable Segments					Other (Note 2)	Elimination	Consolidated
	Domestic Tobacco	International Tobacco	Pharma- ceuticals	Processed Food	Total			
Adjusted operating profit (Note 1)	168,069	340,867	17,161	(793)	525,304	(38,201)	(152)	486,952
Amortization cost of acquired intangibles arising from business acquisitions	(16,245)	(46,915)	—	—	(63,160)	—	—	(63,160)
Adjustment items (income) (Note 5)	—	5,774	150	1	5,926	46,053	—	51,978
Adjustment items (costs) (Note 6)	—	(3,280)	(822)	(44)	(4,147)	(2,569)	—	(6,716)
Operating profit (loss)	151,824	296,446	16,488	(836)	463,923	5,283	(152)	469,054
Financial income								12,353
Financial costs								(61,344)
Profit before income taxes								420,063

(Note 1) For adjusted operating profit, amortization cost of acquired intangibles arising from business acquisitions, and adjustment items (income and costs) are excluded from operating profit (loss).

(Note 2) “Other” includes business activities relating to real estate rental and corporate expenditure relating to corporate communication and operation of the head office.

(Note 3) Depreciation of right-of-use assets included in “Depreciation and amortization ” is as follows:

(Millions of yen)

	2019	2020
Domestic Tobacco	3,649	3,641
International Tobacco	10,314	11,923
Pharmaceuticals	456	439
Processed Food	741	867
Other	616	2,797
Depreciation of right-of-use assets	15,778	19,667

(Note 4) The increase of right-of-use assets is excluded.



(Note 5) The breakdown of “Adjustment items (income)” is as follows:

		(Millions of yen)
	2019	2020
Gain on transfer of pharmaceutical licenses	60,518	—
Gain on sale of the former JT Building	—	41,265
Restructuring incomes	15,197	4,803
Other	8,752	5,910
Adjustment items (income)	<u>84,467</u>	<u>51,978</u>

Restructuring incomes for the years ended December 31, 2019 and 2020 mainly relate to gains on sale of real estate. The breakdown of restructuring incomes is described in “26. Other Operating Income.” Other (income) for the year ended December 31, 2019 and 2020 mainly relate to gains on fair value adjustment after the measurement period for assets and liabilities acquired in a business combination in the “International Tobacco Business.”

(Note 6) The breakdown of “Adjustment items (costs)” is as follows:

		(Millions of yen)
	2019	2020
Restructuring costs	26,182	3,116
Other	2,233	3,600
Adjustment items (costs)	<u>28,415</u>	<u>6,716</u>

Restructuring costs for the year ended December 31, 2019 mainly relate to business operation transformation in the “International Tobacco Business” and business restructuring in the “Pharmaceutical Business.” The breakdown of restructuring costs is described in “27. Selling, General and Administrative Expenses.” Other (costs) for the year ended December 31, 2019 mainly relates to disposal of real estate.

(3) Geographic Information

The regional breakdown of non-current assets as of December 31 is as follows:

Non-current Assets

(Millions of yen)

	2019	2020
Japan	812,083	751,673
Overseas	2,450,772	2,285,357
Consolidated	3,262,855	3,037,030

(Note) Non-current assets, exclusive of financial instruments, deferred tax assets and retirement benefits assets, are segmented by the location of the assets.

The regional breakdown of external revenue for each year is as follows:

External Revenue

(Millions of yen)

	2019	2020
Japan	789,279	727,845
Overseas	1,386,347	1,364,716
Consolidated	2,175,626	2,092,561

(Note) Revenue is segmented by the sales destination.

(4) Major customers Information

The “International Tobacco Business” of the Group sells products to the Megapolis Group that engages in distribution and wholesale business in Russia and other countries. The external revenues from the Megapolis Group were ¥235,093 million (10.8% of consolidated revenue) for the year ended December 31, 2019 and ¥210,834 million (10.1% of consolidated revenue) for the year ended December 31, 2020.

## 7. Cash and Cash Equivalents

The breakdown of “Cash and cash equivalents” as of December 31 is as follows:

		(Millions of yen)
	2019	2020
Cash and deposits	260,908	483,844
Short-term investments	96,249	55,000
Total	357,158	538,844

Cash and cash equivalents are classified as financial assets measured at amortized cost.

The Group’s Iranian subsidiaries’ ability to remit funds outside of Iran is restricted mainly due to international sanctions imposed on Iran. “Cash and cash equivalents” include ¥48,675 million as of December 31, 2019 and ¥42,807 million as of December 31, 2020 held by the Group’s Iranian subsidiaries.

JTI-Macdonald Corp. (hereinafter referred to as “JTI-Mac”), the Company’s Canadian subsidiary, is subject to certain restrictions on the use of funds other than in the ordinary course of business due to the adoption of the “Companies’ Creditors Arrangement Act .” “Cash and cash equivalents” include ¥19,085 million as of December 31, 2019 and ¥43,735 million as of December 31, 2020 held by JTI-Mac.

## 8. Trade and Other Receivables

The breakdown of “Trade and other receivables” as of December 31 is as follows:

		(Millions of yen)
	2019	2020
Note and account receivables	432,874	404,720
Other	28,113	9,347
Allowance for doubtful accounts	(2,475)	(1,923)
Total	458,513	412,144

Trade and other receivables are presented net of allowance for doubtful accounts in the consolidated statement of financial position.

Trade and other receivables are classified as financial assets measured at amortized cost.

## 9. Inventories

The breakdown of “Inventories” as of December 31 is as follows:

		(Millions of yen)
	2019	2020
Merchandise and finished goods	142,343	130,718
Leaf tobacco (Note )	365,700	334,797
Other	75,652	74,247
Total	583,695	539,762

(Note) Leaf tobacco includes those products that will be used after 12 months from the end of each year, but they are included in inventories since they are held within the normal operating cycle.

## 10. Other Financial Assets

(1) The breakdown of “Other financial assets” as of December 31 is as follows:

(Millions of yen)

	2019	2020
Derivative assets	2,564	8,608
Equity securities	32,747	26,704
Debt securities	18,616	18,776
Time deposits	761	928
Other	82,757	76,830
Allowance for doubtful accounts	(5,935)	(5,875)
Total	131,511	125,971
Current assets	21,943	18,828
Non-current assets	109,568	107,143
Total	131,511	125,971

Other financial assets are presented net of allowance for doubtful accounts in the consolidated statement of financial position.

Derivative assets are classified as financial assets measured at fair value through profit or loss excluding those to which hedge accounting is applied, equity securities are classified as financial assets measured at fair value through other comprehensive income, and time deposits and debt securities are classified as financial assets measured at amortized cost.

(2) Names of major securities held as financial assets measured at fair value through other comprehensive income and their fair values as of December 31 are as follows:

(Millions of yen)

Company name	2019	2020
Seven & i Holdings Co., Ltd.	3,424	3,129
Japan Airport Terminal Co., Ltd.	2,436	2,500
DOUTOR•NICHIRE Holdings Co., Ltd.	2,892	1,980
KATO SANGYO CO., LTD.	2,032	1,968
Mitsubishi Shokuhin Co., Ltd.	1,860	1,720
Central Japan Railway Company	2,200	1,459
NIPPON EXPRESS CO., Ltd.	1,111	1,199
Yoshimura Food Holdings K.K.	1,250	814
Daicel Corporation	891	640
Kanemi Co., Ltd.	638	624

Equity securities are held mainly for strengthening relationships with investees. Therefore, they are designated as financial assets measured at fair value through other comprehensive income.

In order to pursue the efficiency of assets held and to use them effectively, sales of financial assets measured at fair value through other comprehensive income have been carried out (derecognition).

The fair value at the time of sale and cumulative gain or loss that is recognized in equity through other comprehensive income for each year is as follows:

	(Millions of yen)	
	2019	2020
Fair value	30,765	2,978
Cumulative gain or loss recognized in equity as other comprehensive income (Note)	(15,883)	(1,399)

(Note) The figure represents the amount transferred to retained earnings.

The cumulative gain or loss recognized in equity as other comprehensive income is transferred to retained earnings when an equity instrument is sold or the decline in its fair value compared to its acquisition cost is significant.

### 11. Other Current Assets

The breakdown of “Other current assets” as of December 31 is as follows:

		(Millions of yen)
	2019	2020
Prepaid tobacco excise taxes	337,166	336,109
Prepaid expenses	22,172	15,680
Consumption tax receivables	15,243	14,960
Other	129,753	127,242
Total	504,334	493,992

### 12. Non-current Assets Held for Sale

The breakdown of “Non-current assets held for sale” as of December 31 is as follows:

Breakdown of Major Assets

		(Millions of yen)
	2019	2020
Non-current assets held for sale		
Property, plant and equipment	14	348
Other	17	0
Total	30	348

“Non-current assets held for sale” are mainly idle properties which are currently actively marketed for sale.

With regard to such assets and assets sold, impairment losses of ¥31 million are recognized in “Selling, general and administrative expenses” in the consolidated statement of income for the year ended December 31, 2020.

### 13. Property, Plant and Equipment

#### (1) Schedule of Property, Plant and Equipment

The schedules of the carrying amount, acquisition cost, and accumulated depreciation and accumulated impairment losses of “Property, plant and equipment” are as follows:

	(Millions of yen)				
Carrying Amount	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of December 31, 2018	362,586	288,587	44,333	63,335	758,841
Cumulative effect of changes in accounting policies	36,440	4,548	85	—	41,073
As of January 1, 2019, after cumulative effect of changes in accounting policies	399,027	293,135	44,418	63,335	799,914
Individual acquisition	29,054	47,247	15,808	41,371	133,480
Transfer to investment property	(1,095)	—	(21)	—	(1,116)
Transfer to non-current assets held for sale	(14)	—	—	—	(14)
Depreciation	(28,049)	(55,775)	(15,196)	—	(99,021)
Impairment losses	(1,930)	(9,506)	(304)	(44)	(11,784)
Reversal of impairment losses	—	91	—	—	91
Sale or disposal	(739)	(5,148)	(2,084)	(21)	(7,991)
Exchange differences on translation of foreign operations	(741)	(1,550)	(81)	(1,280)	(3,652)
Other	9,461	30,172	1,357	(47,657)	(6,668)
As of December 31, 2019	404,973	298,665	43,897	55,704	803,239
Individual acquisition	45,618	33,073	11,434	34,242	124,367
Transfer to investment property	(979)	—	(1)	—	(980)
Transfer to non-current assets held for sale	(29,059)	(379)	(474)	(50)	(29,962)
Depreciation	(31,160)	(56,278)	(13,658)	—	(101,096)
Impairment losses	(4,405)	(4,089)	(386)	(10)	(8,891)
Reversal of impairment losses	—	34	2	—	36
Sale or disposal	(733)	(3,437)	(1,081)	(148)	(5,399)
Exchange differences on translation of foreign operations	(8,552)	(8,667)	(998)	(1,880)	(20,097)
Other	5,721	29,707	850	(38,205)	(1,927)
As of December 31, 2020	381,424	288,629	39,583	49,653	759,290

	(Millions of yen)				
Acquisition Cost	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of January 1, 2019	707,874	778,384	152,878	63,443	1,702,578
As of December 31, 2019	734,009	826,909	156,328	55,709	1,772,954
As of December 31, 2020	686,208	826,889	152,000	49,653	1,714,751

	(Millions of yen)				
Accumulated Depreciation and Accumulated Impairment Losses	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of January 1, 2019	308,847	485,249	108,460	107	902,664
As of December 31, 2019	329,036	528,244	112,431	5	969,715
As of December 31, 2020	304,783	538,261	112,417	—	955,461

## (2) Impairment Losses

The grouping of property, plant and equipment for impairment test is the smallest cash-generating unit that independently generates cash inflows.

The Group recognized impairment losses of ¥11,784 million in the year ended December 31, 2019, and ¥8,891 million in the year ended December 31, 2020 in “Selling, general and administrative expenses” in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2019 represent losses incurred to reduce the carrying amounts to the recoverable amounts for buildings, structures, machinery and vehicles, due to the decision to demolish individual items, etc.

The recoverable amounts of these assets are calculated mainly by their values in use, which are estimated at “zero.” Impairment losses recognized in the year ended December 31, 2020 represent losses incurred to reduce the carrying amounts to the recoverable amounts for land, buildings, structures, machinery and vehicles, due to the decision to demolish individual items, etc.

The recoverable amounts of these assets are calculated mainly by their values in use.



#### 14. Goodwill and Intangible Assets

##### (1) Schedule of Goodwill and Intangible Assets

The schedules of carrying amount, acquisition cost, and accumulated amortization and accumulated impairment losses of “Goodwill” and “Intangible assets” are as follows:

	(Millions of yen)				
Carrying Amount	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2019	2,008,416	421,276	31,919	49,882	2,511,492
Individual acquisition	—	4	8,778	13,112	21,893
Amortization (Note)	—	(63,380)	(11,500)	(9,418)	(84,298)
Impairment losses	—	(791)	(130)	(2,501)	(3,423)
Sale or disposal	—	(6)	(300)	(83)	(389)
Exchange differences on translation of foreign operations	(665)	3,536	(129)	121	2,863
Other	(5,155)	3	2,934	(2,891)	(5,109)
As of December 31, 2019	2,002,595	360,641	31,572	48,221	2,443,029
Individual acquisition	—	447	7,176	15,601	23,224
Amortization (Note)	—	(57,737)	(11,905)	(8,555)	(78,196)
Transfer to non-current assets held for sale	—	—	(20)	(0)	(20)
Impairment losses	—	(55)	(117)	(3,219)	(3,390)
Reversal of impairment losses	—	—	13	—	13
Sale or disposal	—	(7)	(798)	(236)	(1,041)
Exchange differences on translation of foreign operations	(93,203)	(15,928)	(486)	(1,216)	(110,833)
Other	—	(17)	5,829	(5,602)	210
As of December 31, 2020	1,909,392	287,344	31,264	44,995	2,272,996

(Note) The amortization of intangible assets is included in “Cost of sales” and “Selling, general and administrative expenses” in the consolidated statement of income.

	(Millions of yen)				
Acquisition Cost	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2019	2,008,416	1,078,596	157,191	94,698	3,338,901
As of December 31, 2019	2,002,595	1,087,865	141,954	103,762	3,336,175
As of December 31, 2020	1,909,392	1,057,235	149,251	110,884	3,226,763

	(Millions of yen)				
Accumulated Amortization and Accumulated Impairment Losses	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2019	—	657,320	125,272	44,817	827,409
As of December 31, 2019	—	727,224	110,382	55,540	893,146
As of December 31, 2020	—	769,891	117,987	65,889	953,767

## (2) Material Goodwill and Intangible Assets

Goodwill and intangible assets recognized in the consolidated statement of financial position are mainly composed of goodwill and trademarks in the JTIH Group. The carrying amounts of goodwill as of December 31, 2019 and 2020 were ¥1,711,335 million and ¥1,618,133 million, respectively. The carrying amounts of trademarks as of December 31, 2019 and 2020 were ¥261,969 million and ¥205,223 million, respectively.

The majority of goodwill and trademark in the JTIH Group was recognized as a result of the acquisitions of RJR Nabisco's non-U.S. tobacco operations in 1999 and Gallaher in 2007.

Other than the above, goodwill and trademark in Domestic Tobacco business were recognized as a result of the acquisition of Natural American Spirit's non-U.S. tobacco operations in 2016. The carrying amounts of goodwill as of December 31, 2019 and 2020 were ¥265,891 million and ¥265,891 million, respectively. The carrying amounts of trademarks as of December 31, 2019 and 2020 were ¥98,669 million and ¥82,120 million, respectively.

The trademarks are amortized using the straight-line method and the remaining amortization period is mainly from 5 to 6 years.

## (3) Impairment Test for Goodwill

For the year ended December 31, 2020, the carrying amount of the majority of goodwill is allocated to the domestic tobacco cash-generating unit of ¥265,891 million (¥265,891 million for the year ended December 31, 2019), the international tobacco cash-generating unit of ¥1,618,133 million (¥1,711,335 million for the year ended December 31, 2019) and the processed food cash-generating unit of ¥25,368 million (¥25,368 million for the year ended December 31, 2019). Details of the result of impairment tests are as follows:

### A. Domestic Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, given the current domestic tobacco market situation, the Group calculates the value in use by using cash flows with a growth rate from (1.3%) in the fourth year to 0% in the ninth year, and the same growth rate as the ninth year from the tenth year as a continued growth rate. In the prior period, the Group's estimated growth rate of 0% is applied only from the fourth year of cash-flows onwards.

The pre-tax discount rate is 4.9% (2019: 4.3%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

### B. International Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 4.6% in the fourth year (2019: 5.7%) to 2.8% in the ninth year (2019: 3.3%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The pre-tax discount rate is 9.0% (2019: 11.0%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

### C. Processed Food Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 2.2% in the fourth year (2019: 2.5%) to 1.1% in the ninth year (2019: 1.3%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The pre-tax discount rate is 3.9% (2019: 3.8%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

### (4) Impairment Losses

Goodwill is allocated to cash-generating units that are identified according to locations and types of businesses. The grouping of intangible assets for impairment test is the smallest cash-generating unit that independently generates cash inflow.

The Group recognized impairment losses of ¥3,423 million for the year ended December 31, 2019, and ¥3,390 million for the year ended December 31, 2020 in “Selling, general and administrative expenses” in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2019 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of trademarks, software and other intangible assets since the recoverable amounts were lower than the carrying amounts.

The recoverable amounts of these assets are calculated mainly by their values in use.

Impairment losses recognized in the year ended December 31, 2020 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of trademarks, software and other intangible assets since the recoverable amounts were lower than the carrying amounts.

The recoverable amounts of these assets are calculated mainly by their values in use.

## 15. Lease Transactions

The Group leases buildings, factory sites, vehicles and other assets as a lessee. Some of the lease contracts have renewal options or escalation clauses. There are no restrictions on additional debt and further leasing imposed by the lease arrangements.

### (1) Addition, Depreciation and Carrying Amount of Right-of-use Assets

The breakdown of addition, depreciation and carrying amount of right-of-use assets is as follows:

Year ended December 31, 2019

	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	(Millions of yen) Total
Addition	14,645	9,404	72	24,121
Depreciation	10,449	5,210	119	15,778

As of December 31, 2019

	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	(Millions of yen) Total
Carrying amount	43,772	12,813	126	56,711

Year ended December 31, 2020

	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	(Millions of yen) Total
Addition	29,796	4,813	165	34,773
Depreciation	14,149	5,435	84	19,667

As of December 31, 2020

	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	(Millions of yen) Total
Carrying amount	57,011	10,732	103	67,847

### (2) Expense Items Related to Lease

The breakdown of expense items related to lease is as follows:

	2019	2020
Financial cost on lease liabilities	1,506	1,462
Expense relating to short-term lease or leases of low-value assets	9,440	7,519
Expense relating to variable lease payments	2,182	1,654
Total cash outflow for leases	16,003	19,315

## 16. Investment Property

### (1) Schedule of Investment Property

The schedule of the carrying amount of “Investment property” for each year is as follows:

(Millions of yen)

	2019	2020
As of January 1	17,558	16,588
Expenditure after acquisition	182	65
Transfer from property, plant and equipment	1,116	980
Transfer to non-current assets held for sale	(403)	(12,033)
Transfer to property, plant and equipment	(370)	(223)
Depreciation	(533)	(362)
Impairment losses	(917)	(259)
Sale or disposal	(34)	(11)
Exchange differences on translation of foreign operations	(10)	3
Other	—	(3)
As of December 31	16,588	4,744
Acquisition cost as of January 1	38,355	40,262
Accumulated depreciation and accumulated impairment losses as of January 1	20,797	23,674
Acquisition cost as of December 31	40,262	14,074
Accumulated depreciation and accumulated impairment losses as of December 31	23,674	9,331

### (2) Fair Value

The fair value of investment property is determined based on a valuation conducted by an external real estate appraiser. The valuation is made in accordance with the appraisal standards of the country where the investment property is located and based on market evidence of transaction prices for similar assets.

The fair value hierarchy of investment property is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market

Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly

Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

The fair value of investment property based on the fair value hierarchy as of December 31 is as follows:

As of December 31, 2019

(Millions of yen)

	Level 1	Level 2	Level 3	Total
Investment property	—	34,788	1,416	36,204

As of December 31, 2020

(Millions of yen)

	Level 1	Level 2	Level 3	Total
Investment property	—	12,467	1,489	13,956

### (3) Impairment Losses

The grouping of investment properties for impairment test is based on the smallest cash-generating unit that independently generates cash inflows. Impairment tests for idle properties are carried out individually.

The Group recognized impairment losses of ¥917 million for the year ended December 31, 2019, and ¥259 million for the year ended December 31, 2020 in “Selling, general and administrative expenses” in the consolidated statement of income.

Impairment losses recognized for the year ended December 31, 2019 represent the difference between the recoverable amount and the carrying amount for buildings as it was decided to demolish certain idle properties. The recoverable amounts of these assets are calculated mainly by their values in use, which are estimated at “zero.”

Impairment losses recognized for the year ended December 31, 2020 represent the difference between the recoverable amount and the carrying amount for buildings as it was decided to demolish certain idle properties. The recoverable amounts of these assets are calculated mainly by their values in use, which are estimated at “zero.”

## 17. Income Taxes

### (1) Deferred Tax Assets and Deferred Tax Liabilities

The breakdown and schedule of “Deferred tax assets” and “Deferred tax liabilities” by major causes of their occurrence for each year are as follows:

Year ended December 31, 2019

(Millions of yen)					
Deferred Tax Assets	As of January 1, 2019	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2019
Fixed assets (Note 2)	120,129	(2,528)	—	16	117,616
Retirement benefits	72,248	(3,996)	3,854	(572)	71,534
Carryforward of unused tax losses	53,126	(10,070)	—	(648)	42,409
Other	84,215	2,635	1,103	(22)	87,931
Subtotal	329,717	(13,959)	4,957	(1,225)	319,490
Valuation allowance	(65,986)	15,011	(1,438)	349	(52,064)
Total	263,731	1,053	3,519	(877)	267,426

(Millions of yen)					
Deferred Tax Liabilities	As of January 1, 2019	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2019
Fixed assets (Note 2)	(99,298)	5,824	—	(495)	(93,968)
Retirement benefits	(10,125)	375	(1,708)	(174)	(11,632)
Other	(117,697)	3,938	6,773	(574)	(107,561)
Total	(227,120)	10,137	5,065	(1,243)	(213,160)

Year ended December 31, 2020

(Millions of yen)

Deferred Tax Assets	As of January 1, 2020	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2020
Fixed assets (Note 2)	117,616	(12,394)	—	(332)	104,890
Retirement benefits	71,534	(2,590)	3,243	841	73,028
Carryforward of unused tax losses	42,409	8,645	—	(4,966)	46,087
Other	87,931	10,770	(1,626)	(3,354)	93,722
Subtotal	319,490	4,431	1,617	(7,811)	317,726
Valuation allowance	(52,064)	(12,815)	(921)	4,356	(61,443)
Total	267,426	(8,384)	696	(3,455)	256,283

(Millions of yen)

Deferred Tax Liabilities	As of January 1, 2020	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2020
Fixed assets (Note 2)	(93,968)	11,990	—	2,443	(79,535)
Retirement benefits	(11,632)	(826)	(1,704)	(5)	(14,166)
Other	(107,561)	328	1,275	1,462	(104,496)
Total	(213,160)	11,492	(429)	3,900	(198,197)

(Note 1) “Other” includes exchange differences on translation of foreign operations.

(Note 2) “Fixed assets” include property, plant and equipment, goodwill, intangible assets and investment property.

The deferred tax assets are recognized for the amount considered to be recoverable on deductible temporary differences, carryforward of unused tax losses and tax credits by taking taxable temporary differences and future taxable profits plan into account. The carryforward of unused tax losses, for which the deferred tax assets are not recognized, was ¥31,555 million (including ¥19,252 million, for which the carryforward expires after five years) as of December 31, 2019, and ¥38,953 million (including ¥20,743 million, for which the carryforward expires after five years) as of December 31, 2020. Tax credits, for which the deferred tax assets are not recognized, were ¥4,201 million (including ¥3,931 million, for which the carryforward expires after five years) as of December 31, 2019, and ¥5,132 million (including ¥4,705 million, for which the carryforward expires after five years) as of December 31, 2020.

## (2) Income Taxes

The breakdown of “Income taxes” for each year is as follows:

(Millions of yen)

	2019	2020
Current income taxes	114,799	111,142
Deferred income taxes	(11,189)	(3,108)
Total income taxes	103,609	108,034

Deferred income taxes decreased by ¥4,498 million and increased by ¥1,624 million for the years ended December 31, 2019 and 2020, respectively, due to the effect of changes in tax rates in Japan and other countries.



(3) Reconciliation of the Effective Tax Rate

The breakdown of major items that caused differences between the effective statutory tax rate and the average actual tax rate for each year is as follows:

The Company is subject mainly to corporate tax, inhabitant tax and enterprise tax, and the effective statutory tax rate for each year calculated based on these taxes was 30.43%. Foreign subsidiaries are subject to income taxes at their locations.

	2019	2020
		(%)
Effective statutory tax rate	30.43	30.43
Different tax rates applied to foreign subsidiaries	(9.08)	(8.81)
Non-deductible expenses	1.48	1.53
Dividend income	2.04	2.40
Valuation allowance	(2.90)	3.16
Tax credits	(1.66)	(1.04)
Withholding tax in foreign countries	1.79	1.25
Tax contingencies	1.21	(1.11)
Other	(1.05)	(2.10)
Average actual tax rate	22.27	25.72

**18. Trade and Other Payables**

The breakdown of “Trade and other payables” as of December 31 is as follows:

	2019	2020
		(Millions of yen)
Accounts payable	229,914	233,723
Other payables	69,439	72,588
Other	109,245	130,228
Total	408,597	436,540

Trade and other payables are classified as financial liabilities measured at amortized cost.

## 19. Bonds and Borrowings (Including Other Financial Liabilities)

### (1) Breakdown of Financial Liabilities

The breakdown of “Bonds and borrowings” and “Other financial liabilities” as of December 31 is as follows:

(Millions of yen)			
	2019	2020	Due
Derivative liabilities	7,739	10,334	—
Short-term borrowings	192,581	51,633	—
Current portion of long-term borrowings	11,554	12,226	—
Current portion of bonds (Note 2)	80,000	77,609	—
Long-term borrowings (Note 1)	103,743	192,729	2022 - 2080
Bonds (Note 2)	586,623	624,683	—
Lease liabilities	53,705	66,531	—
Other	1,479	887	—
Total	<u>1,037,425</u>	<u>1,036,633</u>	
Current liabilities	305,997	169,057	
Non-current liabilities	<u>731,428</u>	<u>867,576</u>	
Total	<u>1,037,425</u>	<u>1,036,633</u>	

(Note 1) ¥99,085 million of the long-term borrowings is subordinated loans.(Due: 2080. The Company may, at its option, repay early all or a portion of the principal on any interest payment date on or after the interest payment date in January 2025)

(Note 2) The summary of the issuing conditions of the bonds is as follows:

Company	Name of bond	Date of issuance	As of December 31, 2019	(Millions of yen)	(%)	Collateral	Date of maturity
				As of December 31, 2020	Interest rate		
Japan Tobacco Inc.	8th domestic straight bond	December 9, 2010	20,000 (20,000)	—	1.300	Yes	December 9, 2020
Japan Tobacco Inc.	9th domestic straight bond	July 15, 2015	60,000 (60,000)	—	0.217	Yes	July 15, 2020
Japan Tobacco Inc.	10th domestic straight bond	July 15, 2015	30,000	30,000	0.358	Yes	July 15, 2022
Japan Tobacco Inc.	11th domestic straight bond	July 15, 2015	25,000	25,000	0.599	Yes	July 15, 2025
Japan Tobacco Inc.	12th domestic straight bond	September 10, 2018	60,000	60,000	0.110	Yes	September 8, 2023
Japan Tobacco Inc.	13th domestic straight bond	September 10, 2018	30,000	30,000	0.355	Yes	September 8, 2028
Japan Tobacco Inc.	14th domestic straight bond	September 10, 2018	10,000	10,000	0.758	Yes	September 10, 2038
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	82,095 [USD 750 mil.]	77,609 (77,609) [USD 750 mil.]	2.000	Yes	April 13, 2021
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	54,580 [USD 500 mil.]	51,589 [USD 500 mil.]	2.800	Yes	April 13, 2026
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	57,198 [USD 525 mil.]	54,109 [USD 525 mil.]	3.500	No	September 28, 2023
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	54,172 [USD 500 mil.]	51,231 [USD 500 mil.]	3.875	No	September 28, 2028
JT International Financial Services B.V.	Straight bond in EUR	September 28, 2018	66,772 [EUR 550 mil.]	69,233 [EUR 550 mil.]	1.125	No	September 28, 2025
JT International Financial Services B.V.	Straight bond in EUR	November 26, 2019	60,639 [EUR 500 mil.]	62,842 [EUR 500 mil.]	1.000	No	November 26, 2029
JT International Financial Services B.V.	Straight bond in GBP	September 28, 2018	56,168 [GBP 400 mil.]	54,850 [GBP 400 mil.]	2.750	No	September 28, 2033
JT International Financial Services B.V.	Subordinated bond in EUR	October 7, 2020	— [—]	62,934 [EUR 500 mil.]	2.375	No	April 7, 2081 (Note 3)
JT International Financial Services B.V.	Subordinated bond in EUR	October 7, 2020	— [—]	62,896 [EUR 500 mil.]	2.875	No	October 7, 2083 (Note 4)
Total			666,623 (80,000)	702,292 (77,609)			

(Note 1) The figure in parentheses ( ) represents the amount of the current portion of the bond.

(Note 2) The figure in parentheses [ ] represents the amount of foreign currency-denominated bond.

(Note 3) The Issuer may redeem the Bond at its own discretion in the 3-month period ending on and including April 7, 2026 and on each interest payment date thereafter.

(Note 4) The Issuer may redeem the Bond at its own discretion in the 3-month period ending on and including January 7, 2029 and on each interest payment date thereafter.

Derivative liabilities are classified as financial liabilities measured at fair value through profit or loss excluding those to which hedge accounting is applied, and bonds and borrowings are classified as financial liabilities measured at amortized cost.

There are no financial covenants that have a significant impact on the bonds and borrowings of the Group.

## (2) Assets Pledged as Collateral for Liabilities

Pursuant to the provisions of Article 6 of the Japan Tobacco Inc. Act, the Company's properties are pledged as general collateral for bonds issued by the Company. Bondholders are entitled to claim satisfaction in preference to unsecured creditors of the Company properties (with the exception of national and local taxes and certain other statutory obligations).

## 20. Provisions

The breakdown and schedule of “Provisions” for each year are as follows:

Year ended December 31, 2019

	(Millions of yen)				
	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2019	3,579	322	3,668	34,689	42,258
Provisions	2	25,393	4,000	16,225	45,621
Interest cost associated with passage of time	29	—	—	—	29
Provisions used	(9)	(2,874)	(3,668)	(4,204)	(10,754)
Provisions reversed	(4)	(95)	—	(18,406)	(18,506)
Exchange differences on translation of foreign operations	—	490	—	(685)	(195)
As of December 31, 2019	<u>3,598</u>	<u>23,236</u>	<u>4,000</u>	<u>27,619</u>	<u>58,453</u>
Current liabilities	—	7,565	4,000	6,723	18,289
Non-current liabilities	3,598	15,671	—	20,896	40,164
Total	<u>3,598</u>	<u>23,236</u>	<u>4,000</u>	<u>27,619</u>	<u>58,453</u>

Year ended December 31, 2020

	(Millions of yen)				
	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2020	3,598	23,236	4,000	27,619	58,453
Provisions	1,887	4,254	3,697	15,949	25,787
Interest cost associated with passage of time	29	—	—	—	29
Provisions used	(173)	(7,246)	(4,000)	(5,362)	(16,782)
Provisions reversed	(108)	(2,046)	—	(10,675)	(12,828)
Exchange differences on translation of foreign operations	—	(538)	—	(3,363)	(3,901)
As of December 31, 2020	<u>5,232</u>	<u>17,660</u>	<u>3,697</u>	<u>24,169</u>	<u>50,758</u>
Current liabilities	43	10,637	3,697	5,043	19,420
Non-current liabilities	5,189	7,023	—	19,125	31,338
Total	<u>5,232</u>	<u>17,660</u>	<u>3,697</u>	<u>24,169</u>	<u>50,758</u>

### A. Asset Retirement Provisions

In order to settle the obligation of restoring and of removing hazardous substances from plant facilities and premises that the Group uses, the probable amount to be paid in the future is recognized based on past performances. These expenses are expected to be paid after one year or more; however, they may be affected by future business plans.

### B. Restructuring Provisions

These provisions are mainly related to business integration and measures for the rationalization of the “International Tobacco Business.” The timing of the payment may be affected by future business plans.

### C. Provisions for Sales Rebates

These provisions are for contracts which reward the customers with discounts when the sales volume or sales amount in a given period exceeds a specified volume or amount and correspond to “Refund liabilities” in IFRS 15 “Revenue from Contracts with Customers.” They are expected to be paid within one year.

## 21. Other Liabilities

The breakdown of “Other current liabilities” and “Other non-current liabilities” as of December 31 is as follows:

(Millions of yen)

	2019	2020
Tobacco excise tax payables	302,965	268,608
Tobacco special excise tax payables	10,060	8,536
Tobacco local excise tax payables	163,387	158,905
Consumption tax payables	124,693	129,782
Bonus to employees	49,473	56,955
Employees' unused paid vacations liabilities	19,488	20,297
Other	164,331	172,213
Total	834,397	815,295
Current liabilities	699,331	652,314
Non-current liabilities	135,066	162,982
Total	834,397	815,295

## 22. Employee Benefits

### (1) Post-employment Benefits

The Group sponsors funded or unfunded defined benefit plans and defined contribution plans as employee retirement benefit plans. The benefits of defined benefit plans are predetermined based on conditions, such as points employees have gained in compensation for each year of service, the payment rate, years of service, and average salaries in their final years of service before retirement.

The Company is obligated to bear pension costs for a mutual assistance association incurred with respect to services in or before June 1956 (prior to enforcement of the Act on the Mutual Aid Association of Public Corporation Employees). Such obligations are recognized as liabilities at their present value using the actuarial valuation method and are included in retirement benefit liabilities. Special termination benefits may be provided to employees on their early retirements under certain circumstances.

The funded defined benefit plans are administrated by the Group or the fund that is legally separated from the Group in accordance with statutory requirements. The Group, or the board of the pension fund and the trustee of the plan, are required by law to act in the best interests of the plan participants, and are responsible for managing the plan assets in accordance with the designated investment strategy.

The Group's main defined benefit plans expose the Group to actuarial risks, such as investment risk, interest rate risk, inflation risk, and longevity risk.

#### (i) Investment risk

The present value of the defined benefit obligations is calculated using a discount rate set with reference to a yield on high quality corporate bonds or government bonds. If the return on the plan assets is below this yield, there is a possibility that the plan is underfunded.

#### (ii) Interest rate risk

A decrease in a yield on high quality corporate bonds or government bonds will increase the present value of the defined benefit obligations. However, this will be partially offset by an increase in the fair value of the debt instruments (plan assets).

#### (iii) Inflation risk

The level of benefit for certain defined benefit plans of the Group is linked to inflation. Accordingly, a rise in inflation will increase the present value of the defined benefit obligations.

(iv) Longevity risk

Some defined benefit plans of the Group provide a lifetime annuity, and the Group is obligated to provide pension benefits to the plan participants for the rest of their lives after their retirements. The present value of the defined benefit obligations is calculated by reference to the best estimate of the mortality of plan participants during or after employment. An increase in average life expectancy of the plan participants will increase the defined benefit obligations.

A. Schedule of Defined Benefit Obligations

The schedule of the defined benefit obligations is as follows:

	Japan (Note 3)	Overseas	(Millions of yen) Total
As of January 1, 2019 (Notes 1, 2)	216,223	484,964	701,187
Current service cost	9,940	9,099	19,039
Past service cost and settlement	—	(4,190)	(4,190)
Interest expense	1,000	10,287	11,288
Contributions by plan participants	—	1,727	1,727
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	1,135	(4,668)	(3,533)
Actuarial gains and losses arising from changes in financial assumptions	(1,282)	46,336	45,053
Actuarial gains and losses arising from experience adjustments	(2,914)	(2,463)	(5,378)
Benefits paid	(23,507)	(21,110)	(44,617)
Exchange differences on translation of foreign operations	—	(284)	(284)
Other	—	(608)	(608)
As of December 31, 2019 (Notes 1, 2)	200,595	519,089	719,684
Current service cost	9,510	10,014	19,524
Past service cost and settlement	—	3,047	3,047
Interest expense	1,135	7,585	8,720
Contributions by plan participants	—	1,966	1,966
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	(284)	(2,110)	(2,394)
Actuarial gains and losses arising from changes in financial assumptions	(3,618)	39,629	36,012
Actuarial gains and losses arising from experience adjustments	(678)	4,374	3,696
Benefits paid	(21,434)	(19,864)	(41,298)
Exchange differences on translation of foreign operations	—	2,621	2,621
Other	(629)	(8)	(637)
As of December 31, 2020 (Notes 1, 2)	184,597	566,343	750,940

(Note 1) The Group's weighted-average duration of the defined benefit obligations is 6.9 years for Japan and 15.5 years for overseas (2019 : 6.9 years for Japan and 15.5 years for overseas).

(Note 2) The Group's breakdown of the defined benefit obligation by plan participant is as follows:

(Millions of yen)

	As of December 31, 2019			As of December 31, 2020		
	Japan	Overseas	Total	Japan	Overseas	Total
Active members	135,200	172,637	307,837	129,281	198,735	328,016
Deferred members	10,427	76,190	86,617	7,830	81,218	89,048
Pensioners	54,968	270,263	325,230	47,485	286,391	333,876
Total	<u>200,595</u>	<u>519,089</u>	<u>719,684</u>	<u>184,597</u>	<u>566,343</u>	<u>750,940</u>

(Note 3) The schedule of mutual pension benefits obligations included in the category of Japan is as follows:

(Millions of yen)

	2019	2020
As of January 1	36,675	31,090
Interest expense	110	124
Remeasurement gains and losses	(1,661)	(1,596)
Benefits paid	(4,034)	(3,565)
As of December 31	<u>31,090</u>	<u>26,054</u>

#### B. Schedule of Plan Assets

The schedule of the plan assets is as follows:

(Millions of yen)

	Japan	Overseas	Total
As of January 1, 2019	62,788	373,702	436,489
Interest income	296	8,207	8,503
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	1,064	30,122	31,185
Contributions by the employer (Notes 1, 2)	959	6,465	7,424
Contributions by plan participants	—	1,727	1,727
Benefits paid	(7,114)	(16,402)	(23,516)
Exchange differences on translation of foreign operations	—	4,634	4,634
As of December 31, 2019	<u>57,992</u>	<u>408,455</u>	<u>466,447</u>
Interest income	333	6,215	6,548
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	380	29,438	29,817
Contributions by the employer (Notes 1, 2)	879	7,536	8,414
Contributions by plan participants	—	1,966	1,966
Benefits paid	(5,560)	(15,100)	(20,660)
Exchange differences on translation of foreign operations	—	(2,246)	(2,246)
Other	(571)	—	(571)
As of December 31, 2020	<u>53,453</u>	<u>436,263</u>	<u>489,715</u>

(Note 1) Pursuant to laws and regulations, the Group and the pension fund review the financial condition of the pension plan regularly and recalculate contributions for allocating future benefit and keeping the balance of the pension financing when the plan is underfunded.

(Note 2) The Group plans to pay contributions of ¥5,154 million in the year ending December 31, 2021.



### C. Reconciliation of Defined Benefit Obligations and Plan Assets

The reconciliation of the defined benefit obligations and plan assets to the net defined benefit liabilities (assets) recognized in the consolidated statement of financial position as of December 31 is as follows:

As of December 31, 2019

	(Millions of yen)		
	Japan	Overseas	Total
Present value of the funded defined benefit obligations	53,201	366,845	420,046
Fair value of the plan assets	(57,992)	(408,455)	(466,447)
Subtotal	(4,791)	(41,610)	(46,401)
Present value of the unfunded defined benefit obligations	147,394	152,244	299,638
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	142,603	110,635	253,237
Retirement benefit liabilities	148,915	171,699	320,614
Retirement benefit assets	(6,312)	(61,064)	(67,377)
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	142,603	110,635	253,237

As of December 31, 2020

	(Millions of yen)		
	Japan	Overseas	Total
Present value of the funded defined benefit obligations	48,531	397,336	445,868
Fair value of the plan assets	(53,453)	(436,263)	(489,715)
Subtotal	(4,921)	(38,926)	(43,847)
Present value of the unfunded defined benefit obligations	136,065	169,007	305,072
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	131,144	130,080	261,225
Retirement benefit liabilities	137,262	194,490	331,752
Retirement benefit assets	(6,118)	(64,410)	(70,528)
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	131,144	130,080	261,225

#### D. Major Breakdown of Plan Assets

The breakdown of plan assets by major category as of December 31 is as follows:

(Millions of yen)

Japan						
	As of December 31, 2019			As of December 31, 2020		
	Market price in an active market		Total	Market price in an active market		Total
	Quoted	Unquoted		Quoted	Unquoted	
Cash and cash equivalents	7,794	—	7,794	7,569	—	7,569
Equity instruments	3,078	—	3,078	3,524	—	3,524
Japan	1,509	—	1,509	1,653	—	1,653
Overseas	1,569	—	1,569	1,871	—	1,871
Debt instruments	8,819	—	8,819	7,550	—	7,550
Japan	7,572	—	7,572	6,299	—	6,299
Overseas	1,247	—	1,247	1,250	—	1,250
General account of life insurance companies (Note)	—	36,496	36,496	—	33,048	33,048
Other	785	1,019	1,804	751	1,011	1,762
Total	<u>20,477</u>	<u>37,515</u>	<u>57,992</u>	<u>19,394</u>	<u>34,059</u>	<u>53,453</u>

(Millions of yen)

Overseas						
	As of December 31, 2019			As of December 31, 2020		
	Market price in an active market		Total	Market price in an active market		Total
	Quoted	Unquoted		Quoted	Unquoted	
Cash and cash equivalents	15,622	—	15,622	33,999	—	33,999
Equity instruments	59,536	0	59,537	63,683	0	63,683
United Kingdom	4,242	—	4,242	3,805	—	3,805
North America	23,397	—	23,397	23,876	—	23,876
Other	31,897	0	31,897	36,001	0	36,001
Debt instruments	294,759	5,334	300,093	296,597	6,079	302,676
United Kingdom	210,452	—	210,452	206,048	—	206,048
North America	33,186	—	33,186	31,588	0	31,588
Other	51,122	5,334	56,456	58,962	6,079	65,040
Real estate	13,060	66	13,126	15,673	68	15,740
Other	10,395	9,683	20,078	10,571	9,592	20,164
Total	<u>393,372</u>	<u>15,083</u>	<u>408,455</u>	<u>420,524</u>	<u>15,739</u>	<u>436,263</u>

(Millions of yen)

	Total					
	As of December 31, 2019			As of December 31, 2020		
	Market price in an active market		Total	Market price in an active market		Total
	Quoted	Unquoted		Quoted	Unquoted	
Cash and cash equivalents	23,416	—	23,416	41,568	—	41,568
Equity instruments	62,614	0	62,615	67,206	0	67,207
Debt instruments	303,578	5,334	308,913	304,147	6,079	310,226
Real estate	13,060	66	13,126	15,673	68	15,740
General account of life insurance companies (Note)	—	36,496	36,496	—	33,048	33,048
Other	11,180	10,702	21,882	11,323	10,604	21,926
Total	413,849	52,598	466,447	439,917	49,798	489,715

(Note) A certain interest rate and principal for the general account of life insurance are guaranteed by life insurance companies.

The investment strategy for the Group's major plans is as follows:

(Japan)

The Company's pension fund is managed in accordance with the internal policy for securing stable profits in the middle- and long-term in order to ensure the redemption of the plan liability. Concretely, by setting a target rate of return and composition ratio of plan assets by asset category within the risk tolerance that is annually assessed, the Company invests plan assets consistently with the composition ratio. When reviewing the composition ratio, the Company considers introducing an asset investment which has a high correlation with the liability.

When an unexpected situation occurs in the market environment, it is temporarily allowed to make a weighted adjustment to the risk assets, complying with company policy.

(Overseas)

The investment strategy for the foreign subsidiaries' funded pension plans is decided properly by the trustee of the plan and the management of overseas subsidiaries according to local legislation. The Company's objective for the foreign subsidiaries' funded pension plans is to manage risks arising from its defined benefit obligation, and meanwhile to achieve a return on assets in excess of the movement in the value of the defined benefit obligation.

The majority of the plan assets have been allocated to liability matching bonds and the remaining parts of the plan assets are mainly invested in equities targeting long-term return.

## E. Matters Related to Actuarial Assumptions

The major items of actuarial assumptions as of December 31 are as follows:

As of December 31, 2019

	(%)			
	Japan		Overseas	
Discount rate	0.6		1.5	
Inflation rate	—		2.3	

	(years)			
	Japan		Overseas	
	Males	Females	Males	Females
Average life expectancy at retirement (Note 1)				
Current pensioners	23.6 (Note 2)	29.3 (Note 2)	21.8 (Note 3)	24.0 (Note 3)
Future pensioners			23.1 (Note 4)	25.3 (Note 4)

As of December 31, 2020

	(%)			
	Japan		Overseas	
Discount rate	0.8		1.0	
Inflation rate	—		2.3	

	(years)			
	Japan		Overseas	
	Males	Females	Males	Females
Average life expectancy at retirement (Note 1)				
Current pensioners	24.5 (Note 2)	29.7 (Note 2)	21.9 (Note 3)	24.2 (Note 3)
Future pensioners			23.2 (Note 4)	25.5 (Note 4)

(Note 1) The average life expectancies underlie the values of the defined benefit obligations on major plans. Assumptions regarding future mortality rate are based on published statistics and mortality tables.

(Note 2) Life expectancy for a pensioner currently aged 60. Regardless of the plan participant's current age, the Group performs actuarial calculations based on the assumption that life expectancy remains the same.

(Note 3) Life expectancy for a pensioner currently aged 65.

(Note 4) Life expectancy at the age of 65 for an active member currently aged 50.

(Note 5) The valuation of defined benefit obligations reflects a judgment on uncertain future events. The sensitivities of defined benefit obligations due to changes in major assumptions as of December 31 are as follows. Each of these sensitivities assumes that other variables remain fixed; however, in fact, they do not always change independently. Negative figures represent a decrease in pension plan obligations, while positive figures represent an increase.

As of December 31, 2019

			(Millions of yen)
	Change in assumptions	Japan	Overseas
Discount rate	Increase by 0.5%	(6,438)	(38,101)
	Decrease by 0.5%	6,917	42,460
Inflation rate	Increase by 0.5%	—	25,757
	Decrease by 0.5%	—	(24,052)
Mortality rate	Extended 1 year	3,834	20,155
	Shortened 1 year	(3,696)	(19,764)

As of December 31, 2020

			(Millions of yen)
	Change in assumptions	Japan	Overseas
Discount rate	Increase by 0.5%	(5,821)	(41,376)
	Decrease by 0.5%	6,252	46,245
Inflation rate	Increase by 0.5%	—	31,073
	Decrease by 0.5%	—	(28,236)
Mortality rate	Extended 1 year	3,367	21,707
	Shortened 1 year	(3,231)	(21,346)

#### F. Breakdown of Defined Benefit Cost

The breakdown of defined benefit cost for each year is as follows:

Year ended December 31, 2019

	(Millions of yen)		
	Japan	Overseas	Total
Current service cost	9,940	9,099	19,039
Past service cost and gains and losses on settlement	—	(4,190)	(4,190)
Interest expense (income)	704	2,080	2,785
Defined benefit cost through profit or loss	10,645	6,989	17,634
Actuarial gains and losses arising from changes in demographic assumptions	1,135	(4,668)	(3,533)
Actuarial gains and losses arising from changes in financial assumptions	(1,282)	46,336	45,053
Actuarial gains and losses arising from experience adjustments	(2,914)	(2,463)	(5,378)
Return on plan assets (excluding amounts included in interest income)	(1,064)	(30,122)	(31,185)
Defined benefit cost through other comprehensive income	(4,126)	9,083	4,957
Total of defined benefit cost	6,519	16,072	22,591

Year ended December 31, 2020

	(Millions of yen)		
	Japan	Overseas	Total
Current service cost	9,510	10,014	19,524
Past service cost and gains and losses on settlement	—	3,047	3,047
Interest expense (income)	802	1,370	2,172
Defined benefit cost through profit or loss	10,312	14,431	24,742
Actuarial gains and losses arising from changes in demographic assumptions	(284)	(2,110)	(2,394)
Actuarial gains and losses arising from changes in financial assumptions	(3,618)	39,629	36,012
Actuarial gains and losses arising from experience adjustments	(678)	4,374	3,696
Return on plan assets (excluding amounts included in interest income)	(380)	(29,438)	(29,817)
Defined benefit cost through other comprehensive income	(4,960)	12,456	7,496
Total of defined benefit cost	5,352	26,886	32,238

(Note 1) The net amount of interest expense and interest income is included in “Financial costs.” Other expenses are included in “Cost of sales” and “Selling, general and administrative expenses.”

(Note 2) Contributions to the defined contribution plans were ¥9,269 million for the year ended December 31, 2019 and ¥9,698 million for the year ended December 31, 2020 and were not included in the table above.

(2) Other Employee Benefit Expenses

The employee benefit expenses other than post-employment benefits that are included in the consolidated statement of income for each year are as follows:

(Millions of yen)

	2019	2020
Remuneration and salary	239,305	241,549
Bonus to employees	80,973	97,676
Legal welfare expenses	44,607	45,458
Welfare expenses	38,620	38,258
Termination benefits	24,541	85

## 23. Equity and Other Equity Items

### (1) Share Capital and Capital Surplus

#### A. Authorized Shares

The number of authorized shares as of December 31, 2019 and 2020 is 8,000,000 thousand ordinary shares.

#### B. Fully Paid Issued Shares

The schedule of the number of issued shares and share capital is as follows:

	(Thousands of shares)		(Millions of yen)
	Number of ordinary issued shares	Share capital	Capital surplus
As of January 1, 2019	2,000,000	100,000	736,400
Increase (decrease)	—	—	—
As of December 31, 2019	2,000,000	100,000	736,400
Increase (decrease)	—	—	—
As of December 31, 2020	2,000,000	100,000	736,400

(Note) The shares issued by the Company are non-par value ordinary shares that have no restriction on any content of rights.

### (2) Treasury Shares

The schedule of the number of treasury shares and its amount as of each year end is as follows:

	(Thousands of shares)	(Millions of yen)
	Number of shares	Amount
As of January 1, 2019	208,577	442,829
Increase (decrease) (Note 2)	17,620	49,640
As of December 31, 2019	226,197	492,469
Increase (decrease) (Note 2)	(442)	(962)
As of December 31, 2020	225,755	491,507

(Note 1) The Company adopts share option plans, restricted stock remuneration plans and performance share unit plans and utilizes treasury shares for delivery of shares due to their exercises. Contract conditions and amounts are described in “32. Share-based Payments.”

(Note 2) The number of treasury shares purchased based on the resolution made by the Board of Directors is 17,788 thousand shares and the total purchase cost is ¥50,000 million for the year ended December 31, 2019. Purchases of shares less than one unit are 0 thousand shares for the year ended December 31, 2019 and 0 thousand shares for the year ended December 31, 2020. Sale of shares less than one unit is 0 thousand shares for the year ended December 31, 2020. The number of shares delivered upon exercise of share options is 168 thousand shares for the year ended December 31, 2019 and 203 thousand shares for the year ended December 31, 2020. The number of shares disposed for restricted stock remuneration is 239 thousand shares for the year ended December 31, 2020.



(3) Other Components of Equity

A. Subscription Rights to Shares

The Company adopts share option plans and issues subscription rights to shares based on the Companies Act. Contract conditions and amount are described in “32. Share-based Payments.”

B. Exchange Differences on Translation of Foreign Operations

Exchange differences on translation of foreign operations are composed of foreign currency translation difference that occurs when consolidating financial statements of foreign subsidiaries prepared in foreign currencies, and the effective portion of net gain (loss) on the hedging instruments designated as hedge of net investment.

C. Net Gain (Loss) on Derivatives Designated as Cash Flow Hedges

The Group uses derivatives for hedging to avoid the risk of fluctuation in future cash flows. This is the effective portion of changes in the fair value of hedging instruments designated as cash flow hedges.

D. Net Gain (Loss) on Revaluation of Financial Assets Measured at Fair Value through Other Comprehensive Income

This is the valuation difference in the fair value of financial assets measured at fair value through other comprehensive income.

E. Remeasurements of Defined Benefit Plans

Remeasurements of defined benefit plans comprise actuarial gains and losses, the return on plan assets excluding amounts included in interest income, and any change in the effect of the asset ceiling excluding amounts included in interest income. In addition, actuarial gains and losses are the effects of differences between the actuarial assumptions at the beginning of the year and what has actually occurred, and the effects of changes in actuarial assumptions. Remeasurements are recognized as other comprehensive income when they occur and are transferred immediately from other components of equity to retained earnings.

## 24. Dividends

Dividends paid for each year are as follows:

Year ended December 31, 2019

		(Millions of yen)	(Yen)		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 20, 2019)	Ordinary shares	134,357	75	December 31, 2018	March 22, 2019
Board of Directors (July 31, 2019)	Ordinary shares	136,579	77	June 30, 2019	September 2, 2019

Year ended December 31, 2020

		(Millions of yen)	(Yen)		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 19, 2020)	Ordinary shares	136,583	77	December 31, 2019	March 23, 2020
Board of Directors (July 31, 2020)	Ordinary shares	136,617	77	June 30, 2020	September 1, 2020

Dividends for which the effective date falls in the following year are as follows:

Year ended December 31, 2019

		(Millions of yen)	(Yen)		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 19, 2020)	Ordinary shares	136,583	77	December 31, 2019	March 23, 2020

Year ended December 31, 2020

		(Millions of yen)	(Yen)		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 24, 2021)	Ordinary shares	136,617	77	December 31, 2020	March 25, 2021

## 25. Revenue

### (1) Disaggregation of Revenue

The disaggregation of “Revenue” for each year is as follows. The amounts are presented after eliminations of intercompany transactions.

Year ended December 31, 2019

(Millions of yen)

	Reportable Segments				Other	Consolidated
	Domestic Tobacco (Note 2)	International Tobacco (Note 3)	Pharmaceuticals	Processed Food		
Core revenue from tobacco business (Note 1)	568,880	1,253,022	—	—	—	1,821,902
Other	42,614	57,855	88,528	158,586	6,140	353,724
Total	611,494	1,310,877	88,528	158,586	6,140	2,175,626

Year ended December 31, 2020

(Millions of yen)

	Reportable Segments				Other	Consolidated
	Domestic Tobacco (Note 2)	International Tobacco (Note 3)	Pharmaceuticals	Processed Food		
Core revenue from tobacco business (Note 1)	515,745	1,250,808	—	—	—	1,766,554
Other	39,822	55,425	78,957	149,329	2,474	326,007
Total	555,568	1,306,233	78,957	149,329	2,474	2,092,561

(Note 1) The “Domestic Tobacco Business” does not include revenue related to imported tobacco delivery charges. In addition, the “International Tobacco Business” does not include revenue related to the distribution business and contract manufacturing.

(Note 2) Revenues from RRP in core revenue from the “Domestic Tobacco Business” were ¥60,932 million and ¥55,891 million for the year ended December 31, 2019 and 2020, respectively. RRP represents Reduced-Risk Products with potential to reduce the health risks associated with smoking.

(Note 3) Core revenue by cluster from the “International Tobacco Business” is as follows:

(Millions of yen)

	2019	2020
South and West Europe	216,653	219,359
North and Central Europe	236,210	271,976
CIS+	309,646	294,283
Rest-of-the-World	490,513	465,190
Total	1,253,022	1,250,808

South and West Europe includes France, Italy and Spain. North and Central Europe includes Germany and the United Kingdom. CIS+ includes Romania and Russia. Rest-of-the-World includes Iran, Taiwan and Turkey.

#### A. Domestic and International Tobacco Businesses

Domestic and international tobacco businesses engage in the sale of tobacco products.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financing components.

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting the tobacco excise taxes and other transactions is presented as “Revenue” in the consolidated statement of income.

#### B. Pharmaceutical Business

Pharmaceutical business mainly engages in the sale of prescription drugs and licensing.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Revenue from licensing is generated by licensing out the rights to develop and market of each compound to licensees in the development stage, and the Group receives upfront income, milestone revenue and sales-based royalties. Upfront income is recognized at the time the customer obtains control of the license. Milestone revenue is recognized at the time the milestone agreed between the parties such as the progress of development is achieved. Sales-based royalties are measured based on the Group’s licensees’ sales, and recognized by taking into consideration the timing of occurrence.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

#### C. Processed Foods Business

Processed foods business engages in the sale of frozen and ambient processed foods, bakery products and seasonings.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

Transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting these transactions is presented as “Revenue” in the consolidated statement of income.

#### (2) Transaction Price Allocated to the Remaining Performance Obligations

The Group uses the practical expedient and does not disclose information on the remaining performance obligations because it has no significant transactions with initial expected contractual terms exceeding one year. There are no significant amounts of considerations from contracts with customers that are not included in transaction prices.

(3) Gross Turnover

The reconciliation from “Gross turnover” to “Revenue” for each year is as follows:

(Millions of yen)

	2019	2020
Gross turnover	7,581,071	7,555,062
Tobacco excise taxes and agency transaction amount	(5,405,446)	(5,462,501)
Revenue	2,175,626	2,092,561

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting the tobacco excise taxes and other transactions is presented as “Revenue” in the consolidated statement of income.

Gross turnover is an item that the Group discloses voluntarily and is not “Revenue” as defined by IFRS.

## 26. Other Operating Income

The breakdown of “Other operating income” for each year is as follows:

		(Millions of yen)
	2019	2020
Gain on transfer of pharmaceutical licenses	60,518	—
Gain on sale of the former JT building	—	41,265
Gain on sale of property, plant and equipment, intangible assets and investment property (Note)	15,605	5,332
Other (Note)	19,603	8,327
Total	95,725	54,924

(Note) The amount of restructuring incomes included in each account is as follows:

		(Millions of yen)
	2019	2020
Gain on sale of property, plant and equipment, intangible assets and investment property	14,626	4,744
Other	571	60
Total	15,197	4,803

## 27. Selling, General and Administrative Expenses

The breakdown of “Selling, general and administrative expenses” for each year is as follows:

(Millions of yen)

	2019	2020
Advertising expenses	33,467	27,254
Promotion expenses	102,095	92,149
Commission	55,469	57,614
Employee benefit expenses (Note 2)	309,623	307,181
Research and development expenses (Note 1)	64,079	60,847
Depreciation and amortization	106,094	103,666
Impairment losses on other than financial assets (Note 2)	16,124	12,571
Losses on sale and disposal of property, plant and equipment, intangible assets and investment property (Note 2)	9,432	7,591
Other (Note 2)	135,324	115,598
Total	831,707	784,472

(Note 1) All research and development expenses are included in “Selling, general and administrative expenses.”

(Note 2) The amount of restructuring costs included in each account is as follows:

(Millions of yen)

	2019	2020
Employee benefit expenses	24,378	323
Impairment losses on other than financial assets	411	332
Losses on sale and disposal of property, plant and equipment, intangible assets and investment property	329	361
Other	1,064	2,100
Total	26,182	3,116

## 28. Financial Income and Financial Costs

The breakdown of “Financial income” and “Financial costs” for each year is as follows:

(Millions of yen)

<b>Financial Income</b>	<b>2019</b>	<b>2020</b>
Dividend income		
Financial assets measured at fair value through other comprehensive income		
Investments derecognized during the year	1,275	46
Investments held at the end of the year	654	882
Interest income		
Financial assets measured at amortized cost		
Deposits and bonds	6,014	6,389
Gain on net monetary position	—	3,143
Other	459	1,893
<b>Total</b>	<b>8,402</b>	<b>12,353</b>

(Millions of yen)

<b>Financial Costs</b>	<b>2019</b>	<b>2020</b>
Interest expenses		
Financial liabilities measured at amortized cost		
Bonds and borrowings	26,019	21,039
Other	1,538	1,495
Foreign exchange losses (Note 1)	13,297	35,812
Employee benefit expenses (Note 2)	2,785	2,172
Other	1,887	826
<b>Total</b>	<b>45,526</b>	<b>61,344</b>

(Note 1) Valuation gain (loss) of currency derivatives is included in foreign exchange losses.

(Note 2) The employee benefit expenses are the net amount of interest cost and interest income related to employee benefits.



## 29. Other Comprehensive Income

Amount arising during the year, reclassification adjustments to profit or loss and tax effects for each component of “Other comprehensive income” for each year are as follows:

Year ended December 31, 2019

	(Millions of yen)				
	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	(2,209)	—	(2,209)	(274)	(2,484)
Remeasurements of defined benefit plans	(4,957)	—	(4,957)	2,146	(2,811)
Total of items that will not be reclassified to profit or loss	(7,166)	—	(7,166)	1,871	(5,295)
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	7,521	2,591	10,112	(233)	9,879
Net gain (loss) on derivatives designated as cash flow hedges	(882)	320	(561)	171	(391)
Total of items that may be reclassified subsequently to profit or loss	6,639	2,911	9,550	(62)	9,489
Total	(527)	2,911	2,384	1,810	4,194

Year ended December 31, 2020

					(Millions of yen)
	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	(3,886)	—	(3,886)	1,184	(2,702)
Remeasurements of defined benefit plans	(7,496)	—	(7,496)	1,539	(5,957)
Total of items that will not be reclassified to profit or loss	(11,383)	—	(11,383)	2,723	(8,659)
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	(167,963)	(1)	(167,964)	(2,746)	(170,711)
Net gain (loss) on derivatives designated as cash flow hedges	170	152	323	(98)	224
Total of items that may be reclassified subsequently to profit or loss	(167,793)	151	(167,642)	(2,844)	(170,486)
Total	<u>(179,175)</u>	<u>151</u>	<u>(179,024)</u>	<u>(121)</u>	<u>(179,145)</u>

### 30. Earnings per Share

#### (1) Basis of Calculating Basic Earnings per Share

##### A. Profit Attributable to Ordinary Shareholders of the Parent Company

		(Millions of yen)
	2019	2020
Profit for the period attributable to owners of the parent company	348,190	310,253
Profit not attributable to ordinary shareholders of the parent company	—	—
Profit for the period used for calculation of basic earnings per share	348,190	310,253

##### B. Weighted-average Number of Ordinary Shares Outstanding During the Period

		(Thousands of shares)
	2019	2020
Weighted-average number of shares during the period	1,776,782	1,774,128

#### (2) Basis of Calculating Diluted Earnings per Share

##### A. Profit Attributable to Diluted Ordinary Shareholders

		(Millions of yen)
	2019	2020
Profit for the period used for calculation of basic earnings per share	348,190	310,253
Adjustment	—	(0)
Profit for the period used for calculation of diluted earnings per share	348,190	310,253

##### B. Weighted-average Number of Diluted Ordinary Shares Outstanding During the Period

		(Thousands of shares)
	2019	2020
Weighted-average number of ordinary shares during the period	1,776,782	1,774,128
Increased number of ordinary shares under subscription rights to shares	857	792
Weighted-average number of diluted ordinary shares during the period	1,777,639	1,774,921

### 31. Reconciliation of Liabilities Arising from Financing Activities

Reconciliation of liabilities arising from financing activities for each year is as follows:

Year ended December 31, 2019

	As of January 1, 2019	Cash flows	Non-cash changes		As of December 31, 2019
			Foreign exchange movement	Other	
Short-term borrowings and commercial paper	238,023	(44,976)	(1,563)	1,097	192,581
Long-term borrowings (Note)	129,313	(11,568)	(2,475)	27	115,297
Bonds (Note)	610,444	59,435	(3,579)	324	666,623
Lease liabilities	48,840	(14,294)	(394)	19,552	53,705
Total	<u>1,026,621</u>	<u>(11,403)</u>	<u>(8,011)</u>	<u>21,000</u>	<u>1,028,206</u>

Year ended December 31, 2020

	As of January 1, 2020	Cash flows	Non-cash changes		As of December 31, 2020
			Foreign exchange movement	Other	
Short-term borrowings and commercial paper	192,581	(132,462)	(8,525)	39	51,633
Long-term borrowings (Note)	115,297	88,153	1,280	225	204,955
Bonds (Note)	666,623	42,201	(7,000)	468	702,292
Lease liabilities	53,705	(17,741)	(641)	31,209	66,531
Total	<u>1,028,206</u>	<u>(19,849)</u>	<u>(14,886)</u>	<u>31,941</u>	<u>1,025,412</u>

(Note) Current portion is included.

## 32. Share-based Payments

The explanation of the share-based payments of the Company and the Group is as follows.

### (1) Share Option

The Company and Torii Pharmaceutical adopt share option plans. Share options are granted by the resolutions of the Board of Directors based on the approvals at the Annual Shareholders' Meeting.

The outline of the share option plan of the Company is as follows. Due to the introduction of the restricted stock remuneration plan and the performance share unit plan, share option plans are abolished except share options already allotted and new share options will not be issued after 2020.

#### A. Share Option Contract Conditions of the Company

Positions of persons granted	: Directors and Executive Officers
Settlement	: Issuance of shares
Effective period of granted share option	: 30 years after the date of grant
Vesting conditions	: None

Conditions related to the exercise of share options are as follows:

(i) The subscription rights to shares become exercisable when a holder of a subscription right to shares no longer holds a position as a director, an audit & supervisory board member or an executive officer. In the subscription rights to shares allocation contract with holders of such rights, it is provided for that the rights become exercisable from the date following the date on which they no longer hold their positions.

(ii) In the case where any holders of subscription rights to shares waive such rights, they cannot exercise them.

#### B. Changes in the Number of Share Options of the Company

(Shares)

	2019			2020		
	Directors	Executive Officers	Total	Directors	Executive Officers	Total
Balance as of January 1	195,400	634,000	829,400	361,000	613,600	974,600
Granted	126,000	187,200	313,200	—	—	—
Exercised	—	(168,000)	(168,000)	—	(203,000)	(203,000)
Transferred	39,600	(39,600)	—	—	—	—
Balance as of December 31	361,000	613,600	974,600	361,000	410,600	771,600
Exercisable balance as of December 31	—	153,400	153,400	—	85,200	85,200

(Note 1) The number of share options is presented as the number of underlying shares.

(Note 2) All share options are granted with an exercise price of ¥1 per share.

(Note 3) Share options are granted to 6 directors and 20 executive officers for the year ended December 31, 2019.

“Transferred” included in the “Changes in the Number of Share Options” represents the number of share options for persons granted whose management position changed during the period.

(Note 4) The weighted-average fair value per share of share options granted during the period was ¥940 for the year ended December 31, 2019.

(Note 5) The weighted-average share prices of share options at the time of exercise during the period were ¥2,544 and ¥2,256 for the years ended December 31, 2019 and 2020, respectively.

(Note 6) The weighted-average remaining contract years of unexercised share options at the end of each period were 26.4 years and 25.6 years for the years ended December 31, 2019 and 2020, respectively.

### C. Method of Measuring Fair Value of Share Options Granted During the Period of the Company

#### (i) Valuation Model

Black-Scholes Model

#### (ii) Main Assumptions and Estimation

	2019	2020
Share price	¥2,401	—
Volatility of share price (Note 1)	31.2%	—
Estimated remaining period (Note 2)	15years	—
Estimated dividends (Note 3)	¥150/share	—
Risk free interest rate (Note 4)	0.07%	—

(Note 1) Calculated based on daily share prices quoted for the past 15 years.

(Note 2) Because of the difficulty of a reasonable estimation due to insufficient data, the remaining period is estimated based on the assumption that share option rights would be exercised at a midpoint of the exercise period.

(Note 3) Based on the latest dividends paid.

(Note 4) The yield on government bonds for a period of the expected remaining period.

#### (2) Restricted Stock Remuneration

The Company has the restricted stock remuneration plan, which delivers the Company's ordinary shares which are subject to a certain transfer restriction period, to Directors also serving as Executive Officers and Executive Officers of the Company (hereinafter referred to as "Eligible Directors and Executive Officers"). The plan aims to further strengthen the initiatives to enhance the corporate value over the mid to long-term and to further develop the shared value with shareholders.

The Company enters into the restricted stocks allotment agreement with the Eligible Directors and Executive Officers and the Company's ordinary shares shall be delivered if the Eligible Directors and Executive Officers, who continue to serve for a stipulated period, pay all of the monetary compensation claims provided by the Company by the method of contribution in kind. The transfer restriction period is 30 years from the grant date. With regard to the allotted restricted stocks (hereinafter referred to as "Allotted Shares") the restricted stock allotment agreement says that each Eligible Directors and Executive Officers is prohibited to transfer Allotted Shares to a third party, pledge them, mortgage them, or use any arrangement to dispose them, that the Company can acquire Allotted Shares without any compensation on certain conditions and so on. In case any Eligible Directors and Executive Officers who receive allotment retire due to expiration of the term or resign due to reasons deemed reasonable by the Company's Board of Directors, from a position as Member of the Board or any other positions separately specified by the Company's Board of Directors even during the transfer restriction period, the transfer restrictions shall be removed on all Allotted Shares held by him/her.

#### Details of Restricted Stock Remuneration

	2019	2020
Grant date	—	May 26, 2020
Number of allotted shares	—	Directors: 94,200
		Executive Officers: 145,000
Fair value at the grant date	—	¥2,001
Calculation methodology of fair value	—	Calculated based on the closing price of the Company's ordinary share at the Tokyo Stock Exchange as of the previous business day of the resolution of the share allotment by the Board of Directors

(3) Performance Share Unit Remuneration

The Company has the performance share unit remuneration plan, which varies the number of allotted shares depending on the degree of the achievement of predetermined performance target, for Directors also serving as Executive Officers and Executive Officers of the Company (hereinafter referred to as "Eligible Directors and Executive Officers"). The plan aims to further strengthen the initiatives to enhance the corporate value over the mid to long-term and to further develop the shared value with shareholders as with the restricted stock remuneration. The Eligible Directors and Executive Officers shall be paid monetary compensation claims and monies for the delivery of the Company's ordinary shares in accordance with the rate of achievement, etc. of numerical targets such as performance during the performance evaluation period as determined through deliberations by the Advisory Panel on Nomination and Compensation of the Company after the performance evaluation period of 3 consecutive fiscal years on the condition that they continue to serve as Directors, etc. of the Company for a stipulated period. They shall receive the delivery of the Company's ordinary shares by paying all of such monetary compensation claims by the method of contribution in kind. The number of allotted shares and the amount of cash to be paid are calculated by multiplying basic number of share units determined in accordance with duties of each Eligible Directors and Executive Officers by the payment ratio calculated based on the rate of achievement, etc. of numerical targets such as performance during the performance evaluation period in the range of 0% - 200%. The fair value in the plan is estimated based on the market price of the Company's share, which is not revised in consideration of the estimated dividend. The weighted average fair value at the reporting date for the year ended December 31, 2020 is ¥2,102.

(4) Share-based Payment Expenses

The costs included in "Selling, general and administrative expenses" in the consolidated statement of income are as follows.

	(Millions of yen)	
	2019	2020
Share options (equity-settled)	291	30
Restricted stock remuneration (equity-settled)	—	479
Performance share unit remuneration (cash-settled)	—	84

(5) Liabilities Arising from Share-based Payment

The liabilities included in "Other non-current liabilities" in the consolidated statement of financial position as of December 31 are as follows.

	(Millions of yen)	
	2019	2020
Carrying amounts of liability	—	84

### 33. Financial Instruments

#### (1) Capital Management

The Group's management principle is pursuit of the "4S" model: balancing the interests of consumers, shareholders, employees and wider society, and fulfilling our responsibilities towards them, aiming to exceed their expectations. The Group believes that sustainable profit growth in the mid- to long-term based on this principle will increase the Group's value in the mid- to long-term, and is consequently in the best interest of all stakeholders, including our shareholders.

For that reason, as its financial policy, the Group maintains a strong financial base that secures stability in the case of changes in business environment such as economic crises, and flexibility enabling expeditious responses to business investment opportunities.

The Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to the owners of the parent company). The amounts as of December 31 are as follows:

	2019	2020
		(Millions of yen)
Interest-bearing debt (Note)	974,502	958,881
Cash and cash equivalents	(357,158)	(538,844)
Net interest-bearing debt	617,344	420,037
Capital (equity attributable to owners of the parent company)	2,662,696	2,522,834

(Note) Lease liabilities are excluded.

There are specific rules for shares of the Company under the Japan Tobacco Inc. Act, as follows:

The Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by the Annual Shareholders' Meeting) (Article 2 (1)).

In cases where the Company intends to solicit persons to subscribe for shares to be issued or subscription rights to shares or where the Company intends to deliver shares (excluding treasury shares), subscription rights to shares (excluding its own subscription rights to shares) or bonds with subscription rights to shares (excluding its own bonds with subscription rights to shares) when exchanging with shares, the Company shall obtain the approval of the Minister of Finance (Article 2 (2)).

Disposal of shares owned by the Japanese government shall be within the limits on the number of shares decided by the Diet in the relevant annual budget (Article 3).

The Group monitors financial indicators in order to maintain a well-balanced capital structure that ensures an appropriate return on equity and a stable and flexible financial condition for future investment. We monitor credit ratings for financial stability and flexibility, and ROE (return on equity) for profitability, while focusing on changes in the domestic and overseas environment.

#### (2) Financial Risk Management

The Group is exposed to financial risks (credit risk, liquidity risk, foreign exchange risk, interest rate risk, and market price fluctuation risk) in the process of its management activities and it manages risks based on a specific policy in order to avoid or reduce said risks. The results of risk management are regularly reported by the Treasury Division to the president and the Board of Directors of the Company.

The Group policy limits derivatives to transactions for the purpose of mitigating risks from transactions based on actual demand. Therefore, we do not transact derivatives for speculation purposes or trading purposes.



### (3) Credit Risk

Receivables, such as note and account receivables, acquired from the operating activities of the Group are exposed to customer credit risk.

The Group holds mainly debt securities for surplus investment and equity securities of customers and suppliers to strengthen relationships with them; those securities are exposed to the issuer's credit risk.

In addition, through derivative transactions that the Group conducts in order to hedge foreign exchange fluctuation risks and interest rate fluctuation risks, we are exposed to the credit risk of the financial institutions which are counterparties to these transactions.

In principle, the Group sets credit lines or transaction conditions with respect to trade receivables for counterparties based on the Credit Management Guidelines in order to control the credit risk relating to counterparties. In addition, the receivable balances of counterparties with high credit risk are monitored. The Treasury Division of the Company regularly monitors the status of the occurrence and collection of bad debts, and reports them to the president and the Board of Directors of the Company.

With regard to the investment of cash surpluses and derivatives, the Group invests in debt securities and other financial instruments with a certain credit rating and transacts with financial institutions with a high credit rating in principle in order to prevent credit risks from occurring and based on the Group Financial Operation Basic Policy. In addition, the Treasury Division of the Company regularly monitors the performance of these transactions and reports the results to the president and the Board of Directors of the Company.

The maximum exposure pertaining to credit risks for financial assets is the carrying amount after considering impairment in the consolidated financial statements.

There is no excessive concentration of the credit risks to certain counterparties.

The Group reviews collectability of trade receivables depending on the credit conditions of counterparties and recognizes allowance for doubtful accounts. The schedule of the allowance for doubtful accounts is as follows.

(Millions of yen)

		Other financial assets			
	Trade receivables	Measured at an amount equal to the 12-month expected credit losses	Measured at an amount equal to the full lifetime expected credit losses		Total
			Non-credit-impaired financial assets	Credit-impaired financial assets	
As of January 1, 2019	1,650	—	269	5,839	7,758
Addition	1,163	—	18	1	1,182
Decrease (intended use)	(218)	—	—	(0)	(219)
Decrease (reversal)	(20)	—	(57)	(78)	(155)
Other	(100)	—	—	(56)	(156)
As of December 31, 2019	2,475	—	230	5,705	8,409
Addition	785	—	10	2	797
Decrease (intended use)	(1,003)	—	(0)	(55)	(1,059)
Decrease (reversal)	(52)	—	(31)	(23)	(107)
Other	(281)	—	(117)	155	(244)
As of December 31, 2020	1,923	—	92	5,783	7,798

(Note) There is no significant change in the carrying amounts of financial assets which affects the change in the allowance for doubtful accounts.

#### (4) Liquidity Risk

The Group raises funds by borrowings, commercial paper and bonds; however, these liabilities are exposed to the liquidity risk that we would not be able to repay liabilities on the due date due to the deterioration of the financing environment.

In accordance with the Group Financial Operation Basic Policy, the Group establishes a finance plan based on the annual business plan and the Treasury Division of the Company regularly monitors and collects information on the balance of liquidity-in-hand and interest-bearing debt and reports it to the president and the Board of Directors of the Company. In addition, the Group keeps necessary credit facilities to manage liquidity risk by having commitment lines with several financial institutions.

The financial liability balance (including derivative financial instruments) by maturity as of December 31 is as follows:

As of December 31, 2019

(Millions of yen)

	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	408,597	408,597	408,597	—	—	—	—	—
Short-term borrowings	192,581	192,581	192,581	—	—	—	—	—
Current portion of long-term borrowings	11,554	11,554	11,554	—	—	—	—	—
Long-term borrowings	103,743	103,847	—	11,209	41,211	11,175	20,064	20,187
Current portion of bonds	80,000	80,000	80,000	—	—	—	—	—
Bonds	586,623	590,133	—	82,170	30,000	117,519	—	360,444
Lease liabilities	53,705	58,189	15,289	10,985	6,482	4,183	2,751	18,497
Subtotal	1,436,804	1,444,901	708,022	104,364	77,694	132,877	22,815	399,128
Derivative financial liabilities								
Foreign exchange forward contract	7,739	7,739	7,739	—	—	—	—	—
Subtotal	7,739	7,739	7,739	—	—	—	—	—
Total	1,444,543	1,452,640	715,761	104,364	77,694	132,877	22,815	399,128

As of December 31, 2020

(Millions of yen)

	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	436,540	436,540	436,540	—	—	—	—	—
Short-term borrowings	51,633	51,633	51,633	—	—	—	—	—
Current portion of long-term borrowings	12,226	12,226	12,226	—	—	—	—	—
Long-term borrowings	192,729	193,722	—	41,911	11,560	20,064	49	120,140
Current portion of bonds	77,609	77,625	77,625	—	—	—	—	—
Bonds	624,683	628,628	—	30,000	114,338	—	94,728	389,563
Lease liabilities	66,531	70,383	19,031	12,896	9,336	7,132	3,223	18,764
Subtotal	1,461,952	1,470,757	597,055	84,807	135,233	27,196	98,000	528,467
Derivative financial liabilities								
Foreign exchange forward contract	10,334	10,334	10,334	—	—	—	—	—
Subtotal	10,334	10,334	10,334	—	—	—	—	—
Total	1,472,286	1,481,091	607,389	84,807	135,233	27,196	98,000	528,467

The total of commitment lines and withdrawal as of December 31 are as follows:

(Millions of yen)

	2019	2020
Total committed line of credit	470,411	478,200
Withdrawing	—	—
Unused balance	470,411	478,200

#### (5) Foreign Exchange Risk

The Group operates businesses globally and, therefore, is exposed to the following risks due to foreign exchange fluctuation:

(i) The risk where the profit or loss and cash flow in each functional currency of the Group is influenced by foreign exchange fluctuation as a result of external transactions and intergroup transactions, including the payment and receipt of dividends, in currencies that are different from each functional currency of the Group.

(ii) The risk that the equity of the Group is influenced by foreign exchange fluctuation when equity denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

(iii) The risk that the profit or loss of the Group is influenced by foreign exchange fluctuation when profit or loss denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

The Group hedges against risk (i) using derivatives or foreign currency-denominated interest-bearing debts for example, when future cash flow is projected or when receivables and payables are fixed, and some of them are designated as cash flow hedges. The Group hedges against risk (ii) using foreign currency-denominated interest-bearing debts for example, and part of these are designated as net investment hedges. The Group does not hedge against risk (iii) in principle.

In order to mitigate risks mentioned above resulting from the foreign exchange fluctuation, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Treasury Committee of the Company, the Group establishes and implements a foreign currency hedge policy, taking into consideration the impact on the Group's performance and the current conditions of the foreign exchange market in a comprehensive manner. The Treasury Division of the Company regularly reports the performances to the president and the Board of Directors of the Company.

#### Foreign Exchange Sensitivity Analysis

In cases where each currency other than the functional currency that denominates the financial instruments held by the Group as of each year end increases by 10% in value against the functional currency, the impact on profit before income taxes in the consolidated statement of income is as follows:

The impact from the translation of functional currency-denominated financial instruments, and assets, liabilities, income and expenses of foreign operations into Japanese yen is not included. Also, it is based on the assumption that currencies other than the currencies used for the calculation do not fluctuate.

	(Millions of yen)	
	2019	2020
Profit before income taxes	(1,594)	(3,960)

(6) Interest Rate Risk

Interest rate risk within the Group arises from interest-bearing debts after deducting cash equivalents. Borrowings and bonds with floating rates are exposed to interest rate fluctuation risk.

In order to reduce the interest rate fluctuation risk related to borrowings and bonds, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Treasury Committee of the Company, the Group establishes and implements an interest rate hedging policy, taking into consideration the impact on the Group's performance and the current condition of the interest rates in a comprehensive manner. The Treasury Division of the Company reports the performances to the president and the Board of Directors of the Company.

Interest Rate Sensitivity Analysis

In cases where the interest rate of financial instruments held by the Group as of each year end increases by 100bp, the impact on profit before income taxes in the consolidated statement of income is as follows:

The analysis is subject to financial instruments affected by interest rate fluctuation and based on the assumption that other factors, including the impacts of foreign exchange fluctuation, are constant.

	(Millions of yen)	
	2019	2020
Profit before income taxes	(566)	1,743

(7) Hedging Transactions

The Group's policy for hedging transactions is stated in "3. Significant Accounting Policies."

A. Cash Flow Hedges

The details of hedging instruments designated as cash flow hedges are as follows:

As of December 31, 2019

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen)		Average rate, etc.
			Assets	Liabilities	
Foreign exchange risk					
Foreign exchange forward contract					
JPY / USD	USD 187 mil.	—	41	227	¥ 106.67

As of December 31, 2020

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen)		Average rate, etc.
			Assets	Liabilities	
Foreign exchange risk					
Foreign exchange forward contract					
JPY / USD	USD 218 mil.	—	324	176	¥ 105.31

(Note) Carrying amounts of derivatives are presented as "Other financial assets" or "Other financial liabilities" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current assets" or "Non-current liabilities."

The schedule of net gains (losses) on hedging instrument designated as cash flow hedges is as follows:

(Millions of yen)

	Effective portion of changes in the fair value of cash flow hedges
	Foreign exchange risk
As of January 1, 2019	443
Other comprehensive income	
Amount arising (Note 1)	(882)
Reclassification adjustments (Note 2)	320
Tax effects	171
Other	(185)
As of December 31, 2019	(132)
Other comprehensive income	
Amount arising (Note 1)	170
Reclassification adjustments (Note 2)	152
Tax effects	(98)
Other	30
As of December 31, 2020	122

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.

(Note 2) The amount, which is reclassified when the hedged item affects profit or loss, is recognized in "Revenue," "Financial income" or "Financial costs" in the consolidated statement of income. The amount of hedge ineffectiveness is immaterial.

## B. Hedge of Net Investment in Foreign Operations

The details of hedging instruments designated as hedge of net investment are mainly as follows:

As of December 31, 2019

	Contract amount		Over one year		Carrying amount (Note) (Millions of yen)		Average rate, etc.	
					Assets	Liabilities		
Bonds in USD	USD	1,250 mil.	USD	1,250 mil.	—	136,675	¥	109.41
Bonds in EUR	EUR	567 mil.	EUR	567 mil.	—	69,132	\$	1.11
Bonds in GBP	GBP	400 mil.	GBP	400 mil.	—	56,089	\$	1.32
Foreign exchange forward contract								
EUR / RUB	RUB	29,502 mil.		—	—	930	€	0.014
JPY / USD	USD	400 mil.		—	—	749	¥	106.68
USD / TWD	TWD	7,518 mil.		—	—	399	\$	0.033
GBP / USD	USD	245 mil.		—	15	395	£	0.77
EUR / USD	USD	183 mil.		—	—	358	€	0.89

As of December 31, 2020

	Contract amount		Over one year		Carrying amount (Note) (Millions of yen)		Average rate, etc.	
					Assets	Liabilities		
Bonds in USD	USD	1,250 mil.	USD	500 mil.	—	129,198	¥	109.41
Bonds in EUR	EUR	1,321 mil.	EUR	1,321 mil.	—	166,119	\$	1.16
Bonds in GBP	GBP	400 mil.	GBP	400 mil.	—	54,704	\$	1.32
Foreign exchange forward contract								
EUR / RUB	RUB	20,294 mil.		—	543	289	€	0.011
JPY / USD	USD	300 mil.		—	519	—	¥	105.03
GBP / USD	USD	523 mil.		—	—	1,682	£	0.76

(Note) Carrying amounts of bonds are presented as “Bonds and borrowings” in the consolidated statement of financial position, and the portion with over one year maturity is classified as “Non-current liabilities.” Carrying amounts of derivatives are presented as “Other financial assets” or “Other financial liabilities” in the consolidated statement of financial position, and the portion with over one year maturity is classified as “Non-current assets” or “Non-current liabilities.”

The schedule of net gains (losses) on hedging instrument designated as hedge of net investment in foreign operations is as follows:

	(Millions of yen)	
	2019	2020
As of January 1	17,842	10,338
Other comprehensive income		
Amount arising (Note 1)	(7,271)	3,887
Tax effects	(233)	(2,746)
As of December 31 (Note 2)	10,338	11,480

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.

(Note 2) Net gain arising from the hedging instruments for which hedge accounting is discontinued were ¥14,683 million and ¥21,026 million as of December 31, 2019 and 2020 respectively those which are included in the exchange differences on translation of foreign operations.

(8) Market Price Fluctuation Risk

With respect to securities, the Group regularly assesses the fair value and financial conditions of the issuers, and each relevant department reviews the portfolio held by taking into account the relationship with counterparty entities as necessary.

(9) Fair Value of Financial Instruments

The fair value hierarchy of financial instruments is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market

Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly

Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

A. Financial Instruments Measured at Amortized Cost

The carrying amount and fair value hierarchy of financial instruments measured at amortized cost as of December 31 are as follows:

As of December 31, 2019

(Millions of yen)

	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	115,297	—	116,804	—	116,804
Bonds (Note)	666,623	683,650	—	—	683,650

As of December 31, 2020

(Millions of yen)

	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	204,955	—	206,953	—	206,953
Bonds (Note)	702,292	750,417	—	—	750,417

(Note) Current portion is included.

With regard to short-term financial assets and short-term financial liabilities measured at amortized cost, their fair value approximates the carrying amount.

The fair value of long-term borrowings is calculated based on the present value which is obtained by discounting the total of the principal and interest by the interest rate assumed in a case where the same loan is newly made.



## B. Financial Instruments Measured at Fair Value

The fair value hierarchy of financial instruments measured at fair value as of December 31 is as follows:

As of December 31, 2019

				(Millions of yen)
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	—	2,564	—	2,564
Equity securities	25,829	—	6,919	32,747
Other	442	17,673	5,008	23,123
Total	<u>26,270</u>	<u>20,238</u>	<u>11,927</u>	<u>58,435</u>
Derivative liabilities	—	7,739	—	7,739
Total	<u>—</u>	<u>7,739</u>	<u>—</u>	<u>7,739</u>

As of December 31, 2020

				(Millions of yen)
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	—	8,608	—	8,608
Equity securities	19,604	—	7,100	26,704
Other	451	8,650	5,357	14,457
Total	<u>20,055</u>	<u>17,257</u>	<u>12,457</u>	<u>49,769</u>
Derivative liabilities	—	10,334	—	10,334
Total	<u>—</u>	<u>10,334</u>	<u>—</u>	<u>10,334</u>

(Note) The schedule of financial instruments that are classified in Level 3 is as follows:

		(Millions of yen)
	2019	2020
As of January 1	10,351	11,927
Total gain (loss)		
Profit or loss (Note 1)	209	(930)
Other comprehensive income (Note 2)	(182)	(804)
Purchases	1,660	2,674
Sales	(140)	(410)
Other	29	—
As of December 31	<u>11,927</u>	<u>12,457</u>

(Note 1) Gains and losses included in profit or loss for the years ended December 31, 2019 and 2020 are related to financial assets measured at fair value through profit or loss as of the year end. These gains and losses are included in “Financial income” and “Financial costs.”

(Note 2) Gains and losses included in other comprehensive income for the years ended December 31, 2019 and 2020 are related to financial assets measured at fair value through other comprehensive income as of the year end. These gains and losses are included in “Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income.”

### 34. Related Parties

Based on the Japan Tobacco Inc. Act, the Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by Annual Shareholders' Meeting). As of December 31, 2020, the Japanese government held 33.35% of all outstanding shares of the Company.

#### (1) Related-party Transactions

Related-party transactions are conducted under the same conditions as regular business transactions.

The Group's revenue from CJSC TK Megapolis, the local Russian distribution affiliate, was ¥202,780 million and ¥177,170 million for the years ended December 31, 2019 and 2020, respectively. The Group held trade receivables of ¥38,640 million and ¥27,668 million from CJSC TK Megapolis as of December 31, 2019 and 2020, respectively.

#### (2) Remuneration for Directors and Audit and Supervisory Board Members

Remuneration for directors and audit and supervisory board members for each year is as follows:

	(Millions of yen)	
	2019	2020
Remuneration and bonuses	673	1,139
Share-based payments	115	251
Total	788	1,390

### 35. Subsidiaries, Associates and Others

(The composition of the Group)

The composition of the Group by reportable segment as of December 31 is as follows:

Reportable Segments	2019		2020	
	Number of subsidiaries	Number of entities accounted for using the equity method (Note)	Number of subsidiaries	Number of entities accounted for using the equity method (Note)
Domestic Tobacco	13	1	13	1
International Tobacco	171	7	173	8
Pharmaceuticals	2	—	2	—
Processed Food	28	3	28	2
Other	17	2	19	2
Total	231	13	235	13

(Note) No associates or joint ventures are considered to be material to the Group.

There is no significant change in the composition of the Group for the year ended December 31, 2020.

Regarding the restrictions on the ability to use the assets of the Group, please refer to "7. Cash and Cash Equivalents."

### 36. Commitments

#### (1) Commitments for the Acquisition of Assets

Commitments for the acquisition of assets as of December 31 are as follows:

		(Millions of yen)
	2019	2020
Acquisition of property, plant and equipment	35,747	33,768
Acquisition of intangible assets	1,602	3,130
Total	37,348	36,897

#### (2) Procurement of Domestic Leaf Tobacco

With regard to the procurement of domestic leaf tobacco by the Company, based on the Tobacco Business Act, the Company enters into purchase contracts with domestic leaf tobacco growers every year, and the contracts determine the area under cultivation by type of tobacco and the prices by type and quality of tobacco leaf. Under the contracts, the Company is obligated to purchase all domestic leaf tobacco produced pursuant to such contracts, except for any domestic leaf tobacco not suited for the manufacture of tobacco products.

### 37. Hyperinflationary Accounting Adjustments

As required by IAS 29, the Group's consolidated financial statements include the financial statements of the subsidiaries in the hyperinflationary economy, restated in terms of the measuring unit current at the end of the reporting period.

For the restatement of financial statements of the subsidiaries in Iran, the Group applies the conversion coefficient derived from the Consumer Price Index of Iran published by the Statistical Centre of Iran.

Consumer Price Index and corresponding conversion coefficients of Iran are presented below.

End of reporting period	Consumer Price Index	Conversion coefficient
31 December 2015	93	300
31 December 2016	102	276
31 December 2017	112	251
31 December 2018	152	185
31 December 2019	194	145
31 December 2020	281	100

The Group's subsidiaries in the hyperinflationary economy have restated their non-monetary items held at historical cost, such as property, plant and equipment, by applying the conversion coefficient at the acquisition date. Monetary items and non-monetary items held at current cost are not restated, as they are considered to be expressed in terms of the measuring unit current at the end of the reporting period.

For the purpose of consolidation, the financial statements of the Group's subsidiaries in the hyperinflationary economy are translated using the spot exchange rates at the end of the reporting period.

### 38. Contingencies

#### Contingent Liabilities

The Company and some of its subsidiaries are defendants in legal proceedings. Provisions are not accounted for in matters where it is not practicable to reasonably estimate the final outcomes.

The Company and some of its subsidiaries, who are defendants in such legal proceedings, believe that our defenses asserted in these proceedings are based on substantial evidence and implement the system for the response to action with the assistance of external lawyers.

#### (1) Smoking/Vaping and Health Related Litigation

The Company and some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking or vaping, the marketing of tobacco products, or exposure to tobacco smoke. As of December 31, 2020, there were a total of 21 smoking and health related cases pending in which one or more members of the Group were named as a defendant or for which the Company may have certain indemnity obligations pursuant to the agreement such as for the Company's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations. The major ongoing smoking and health related cases are as follows:

On March 8, 2019, JTI-Macdonald Corp. (hereinafter referred to as "JTI-Mac"), the Company's Canadian subsidiary, filed for protection from its creditors under the Companies' Creditors Arrangement Act (CCAA). The Ontario Superior Court has granted the CCAA application and extended protection in favor of JTI-Mac (hereinafter referred to as "CCAA Proceedings"). All of the below Canadian matters against JTI-Mac have been stayed by the CCAA Proceedings, under which JTI-Mac carries on business in the ordinary course.

##### A. Individual Claim

There is one individual case brought against the Company's indemnitee in South Africa.

##### South Africa Individual Claim (Joselowitz):

The individual claim was brought against the Company's indemnitee in South Africa in October 2000. Plaintiff seeks compensatory and punitive damages, alleging that the Company's indemnitee marketed products which it knew to be dangerous to health, manipulated nicotine content to foster addiction, failed to comply with South African labeling requirements and participated in a clandestine worldwide operation to encourage children to smoke. This case has been dormant since February 2001.

In addition, there is one individual case (which is currently dormant) brought against the Company's subsidiary in Ireland and one ongoing individual case brought against the Company's subsidiaries in the United States.

##### B. Class Actions

There are eight ongoing class actions in Canada against the Company's subsidiary and/or indemnitees.

##### Canada Quebec Class Action (Cecilia Letourneau):

This class action was brought in September 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥371.1 billion (approximately CAD 4.6 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥371.1 billion (approximately CAD 4.6 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of defendants by substantively upholding the first instance judgment and ordering a punitive damage award against the appellants of approximately ¥13.0 billion (approximately CAD 161 million), in which the share of the total damage award against JTI-Mac is approximately ¥1.2 billion (approximately CAD 15 million). The time limit for seeking leave to appeal the decision to the Supreme Court of Canada is suspended during the CCAA Proceedings. Enforcement of the judgement is stayed by the CCAA Proceedings.

Canada Quebec Class Action (Conseil Québécois sur le tabac et la santé):

This class action was brought in November 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥1,005.4 billion (approximately CAD 12.4 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥65.5 billion (approximately CAD 0.8 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of the defendants by substantively upholding the first instance judgment and ordering a compensatory damage award jointly and severally against the defendants of approximately ¥1,093.5 billion (approximately CAD 13.5 billion), in which the share of the total damage award against JTI-Mac is approximately ¥142.2 billion (approximately CAD 1.8 billion), and a punitive damage award of approximately ¥3 million (approximately CAD 0.04 million) per defendants. The time limit for seeking leave to appeal the decision to the Supreme Court of Canada is suspended during the CCAA Proceedings. Enforcement of the judgement is stayed by the CCAA Proceedings.

The Quebec Court of Appeal rendered one judgment for both class actions against the defendants and ordered them to make an initial deposit of approximately ¥93.9 billion (approximately CAD 1.2 billion), in which the share of JTI-Mac is approximately ¥11.8 billion (approximately CAD 145 million). The obligation to pay the initial deposit is stayed by the CCAA Proceedings.

Canada Saskatchewan Class Action (Adams):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Manitoba Class Action (Kunta):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Nova Scotia Class Action (Semple):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada British Columbia Class Action (Bourassa):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada British Columbia Class Action (McDermid):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Ontario Class Action (Jacklin):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2012. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

C. Health-Care Cost Recovery Litigation

There are 10 ongoing health-care cost recovery cases in Canada pending against the Company's subsidiary and indemnitees brought by all the Canadian provinces (except three Canadian territories). These provinces filed lawsuits under their own provincial legislation which was enacted exclusively for the purpose of authorizing the provincial government to file a direct action against tobacco manufacturers to recoup the health-care costs the government has allegedly incurred and will incur, resulting from "tobacco related wrongs."

Canada British Columbia Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of British Columbia in January 2001 against tobacco industry members including JTI-Mac and the Company's indemnitees based on its provincial legislation, the "Tobacco Damages and Health-Care Costs Recovery Act." The claim amount is unspecified. In 2001, several defendants challenged the legislation's constitutionality, which was ultimately rejected by the Supreme Court of Canada in September 2005. The action remains pending in the first instance. The case is stayed by the CCAA Proceedings.

Canada New Brunswick Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of New Brunswick in March 2008 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Ontario Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Ontario in September 2009 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of ¥26,673.9 billion (CAD 330 billion). The case is stayed by the CCAA Proceedings.

Canada Newfoundland and Labrador Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Newfoundland and Labrador in February 2011 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Manitoba Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Manitoba in May 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Quebec Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Quebec in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total amount of the claim approximately ¥4,902.9 billion (approximately CAD 60.7 billion). The case is stayed by the CCAA Proceedings.

Canada Alberta Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Alberta in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of at least ¥808.3 billion (CAD 10.0 billion). The case is stayed by the CCAA Proceedings.

Canada Saskatchewan Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Saskatchewan in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Prince Edward Island Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Prince Edward Island in September 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Nova Scotia Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Nova Scotia in January 2015 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

(2) Other Legal Proceedings

The Company and some of its subsidiaries are also engaged in other legal proceedings such as commercial and tax disputes.

(Note) The amount of damages sought denominated in foreign currencies is translated into Japanese yen at the rates as of December 31, 2020.

### 39. Subsequent Events

To strengthen our response to changes in the business environment and to aim for sustainable growth in the tobacco business, the Group decided to strengthen the operating system of the tobacco business towards further enhancement of its competitiveness and profitability on February 9, 2021.

Rapid changes in the tobacco industry include the perception of smoking and health, heightened tobacco regulations and tax reforms in various countries, increasingly diverse consumer preferences and expansion as well as intense competition in product development in the Reduced Risk Products (RRP) category. Having closely reviewed the business environment from a long-term perspective, the Group concluded that a revision of its strategic focus in its tobacco business is necessary. The Group's objective going forward is to operate with a stronger consumer-centric mindset and prioritize investments in heated tobacco sticks in the RRP category while maintaining necessary investments towards combustible products. The combination of the two tobacco businesses will enable efficient and effective deployment of resources within the Group.

In the Japanese market, the Group also plans to implement various measures, intending the enhancement of its competitiveness to maximize the value offered to its customers and strengthening its business foundation, considering the latest industry volume decline and the highly uncertain business environment.

#### **Consolidate the existing tobacco businesses into one tobacco business**

##### ■ Objectives:

- Strengthen the competitiveness in the growing RRP category by leveraging global resources
- Simplify the organization structure to improve speed in decision-making while building an effective and efficient organization structure
- Maximize the value offered to consumers through timely resource allocation in a prioritized manner, from a global perspective
- Unify the tobacco business operations further into one team to proactively offer a portfolio of products and services to anticipate the needs of individual markets
- Share and deploy best practices on a global basis to accelerate the learnings across different categories and markets

##### ■ Actions:

- Consolidate the headquarter functions of the tobacco business, including the Japan market, currently in Tokyo into the existing headquarters of the international tobacco business in Geneva
  - Strategy development functions, performance management functions and decision-making processes for the tobacco business will be consolidated
- Operate the Japanese market as a key market in a new unified tobacco business
- Consolidate the reporting lines of supply chain functions of the global tobacco business (manufacturing, leaf procurement, quality assurance, etc.) following the successful consolidation of the R&D functions

The consolidation of the tobacco businesses is scheduled for January 2022.

#### **Strengthen the competitiveness in the Japanese market**

##### ■ Objective:

- Establish an organizational structure to enhance consumer satisfaction

##### ■ Actions:

- Reform the Japanese Market Head-office and sales organization to address the changes in the operating environment, diverse consumer needs in a prompt and effective manner
  - Reform the Japan Market Head-office in January 2022 to further strengthen the marketing and sales function
  - Reform the sales organization structure to further promote sales activities to address consumer needs in each of the regions, from April 2022:
    - Restructure the sales organization from 3-tier structure (Market HQ - Regional sales office - branch) to 2-tier structure (Market HQ - New sales office)
    - Migrate from a system of 15 regional sales offices and 145 branches to a new system of 47 new sales offices

#### **Redefine the organizational structure in the Japanese market to correspond to the operating environment**

##### ■ Objective:

- Ensure competitiveness and adjust the operating model to meet domestic sales volumes



■ Actions:

- The Company's measures

- Optimization of workforce reflecting the reorganization of the sales operations and optimization of administrative tasks from April 2022
- The Company's Kyushu Tobacco Factory (Chikushino city, Fukuoka) will be closed at the end of March 2022
- Optimize Leaf procurement footprint

Integrate the Chu-Shikoku Leaf Tobacco Branch (Takamatsu city, Kagawa) and Minami-Kyushu Leaf Tobacco Branch (Miyakonojo city, Miyazaki) into the West Japan Leaf Services Headquarters (Koshi city, Kumamoto) from April 2022

- Group subsidiary measures

- Filter factory Closure

Japan Filter Technology Co., Ltd. Tagawa Factory (Tagawa city, Fukuoka) (hereinafter, "JFT Tagawa factory") will be closed at the end of March 2022

- Liquidation of JT Engineering Inc.

Tobacco related functions will be consolidated into the Company from April 2023. JT Engineering Inc. is expected to be liquidated after termination of System Integration services and external business services

**Optimization of the Company's workforce**

■ Objective:

- Optimization of workforce in line with the initiatives to strengthen competitiveness and redefine the organizational structure in the Japanese market

■ Actions:

- Offer voluntary retirement program and seek retirement of about 1,000 employees
- Remove field partner organizational structure (part-timers who support the sales activities); as a result, early retirement packages will be offered for about 1,600 field partners
- Offer voluntary retirement program and seek retirement of about 150 senior employees (contractors or part-timers who are reemployed after their retirement)
- The above voluntary retirement and field partner organization restructuring measures are expected to be completed at the end of March 2022

In addition, early retirement package will be offered for certain employees of the group companies, following the closure of the Company's Kyushu and JFT Tagawa factories.

The impact of these initiatives on the consolidated financial statements for fiscal year ending December 31, 2021 is expected to be about JPY 37 billion as a one-time expense, which is due to the factory closures and the offering of voluntary retirement programs.

(2) Others

A. Quarterly Information for the Year ended December 31, 2020

(Millions of yen)

	Q1 January 1, 2020 to March 31, 2020	Q2 January 1, 2020 to June 30, 2020	Q3 January 1, 2020 to September 30, 2020	2020 January 1, 2020 to December 31, 2020
Revenue	519,620	1,030,218	1,592,097	2,092,561
Profit before income taxes for the period (year)	115,102	225,961	345,558	420,063
Profit attributable to owners of the parent company for the period (year)	86,373	172,495	257,948	310,253
Basic earnings per share for the period (year) (yen)	48.69	97.23	145.40	174.88

	Q1 January 1, 2020 to March 31, 2020	Q2 April 1, 2020 to June 30, 2020	Q3 July 1, 2020 to September 30, 2020	Q4 October 1, 2020 to December 31, 2020
Basic earnings per share for the quarter (yen)	48.69	48.54	48.16	29.48

B. Significant Lawsuits

The significant lawsuits of the Group are as stated in “38. Contingencies” in the notes to consolidated financial statements.

# 1. Nonconsolidated Financial Statements

## (1) Nonconsolidated Financial Statements

### A. Nonconsolidated Balance Sheet

As of December 31, 2019 and 2020

(Millions of yen)

	2019	2020
<b>Assets</b>		
<b>Current assets</b>		
Cash and deposits	80,282	299,366
Accounts receivable-trade *2	43,174	34,815
Securities	40,000	20,000
Merchandise and finished goods	32,756	27,142
Semi-finished goods	68,416	76,402
Work in process	2,262	2,247
Raw materials and supplies	40,120	32,234
Advance payments-trade	2,093	1,886
Prepaid expenses	9,893	4,850
Short-term loans receivable from subsidiaries and affiliates	99,536	43,406
Other *2,*3	59,091	19,455
Allowance for doubtful accounts	(26)	(25)
Total current assets	477,597	561,777
<b>Noncurrent assets</b>		
Property, plant and equipment		
Buildings	92,396	80,030
Structures	2,686	2,375
Machinery and equipment	59,262	51,567
Vehicles	1,827	1,307
Tools, furniture and fixtures	16,586	14,221
Land	71,279	48,909
Construction in progress	2,503	445
Total property, plant and equipment	246,540	198,854
Intangible assets		
Patent right	224	154
Right of trademark	98,896	82,120
Software	19,581	18,299
Goodwill	214,626	178,855
Other	2,705	2,662
Total intangible assets	336,031	282,089
Investments and other assets		
Investment securities	22,566	16,862
Shares of subsidiaries and affiliates	1,482,083	1,487,617
Long-term loans receivable from subsidiaries and affiliates	17,040	17,792
Long-term prepaid expenses	9,268	9,090
Deferred tax assets	13,053	13,514
Other	11,841	14,118
Allowance for doubtful accounts	(1,663)	(3,783)
Total investments and other assets	1,554,189	1,555,210
Total noncurrent assets	2,136,759	2,036,153
<b>Total assets</b>	<b>2,614,357</b>	<b>2,597,930</b>

(Millions of yen)

		2019		2020
<b>Liabilities</b>				
<b>Current liabilities</b>				
Accounts payable-trade	*2	10,304	*2	7,069
Current portion of bonds	*1	80,000	*1	77,624
Lease obligations	*2	2,769	*2	2,450
Accounts payable-other	*2	60,869	*2	51,780
National tobacco excise taxes payable		71,178		65,605
National tobacco special excise taxes payable		10,060		8,536
Local tobacco excise taxes payable		81,718		74,707
Income taxes payable		10,555		29,527
Accrued consumption taxes		32,758		37,973
Cash management system deposits received	*4	323,313	*4	326,353
Provision for bonuses		4,726		6,330
Other		7,806		5,914
Total current liabilities		696,054		693,867
<b>Noncurrent liabilities</b>				
Bonds payable	*1	291,904	*1	206,717
Long-term loans payable		70,000		170,000
Lease obligations	*2	6,113	*2	4,529
Provision for retirement benefits		129,322		128,333
Other	*2	3,598	*2	4,472
Total noncurrent liabilities		500,937		514,051
Total liabilities		1,196,991		1,207,918

	(Millions of yen)	
	2019	2020
<b>Net assets</b>		
Shareholders' equity		
Capital stock	100,000	100,000
Capital surplus		
Legal capital surplus	736,400	736,400
Total capital surplus	736,400	736,400
Retained earnings		
Legal retained earnings	18,776	18,776
Other retained earnings		
Reserve for investment loss on developing new business	378	377
Reserve for reduction entry	45,373	41,711
Special account for reduction entry	1,747	327
Retained earnings brought forward	992,930	966,416
Total retained earnings	1,059,205	1,027,608
Treasury shares	(492,469)	(491,507)
Total shareholders' equity	1,403,136	1,372,501
Valuation and translation adjustments		
Valuation difference on available-for-sale securities	7,283	4,069
Deferred gains or losses on hedges	5,390	12,189
Total valuation and translation adjustments	12,673	16,259
Subscription rights to shares	1,556	1,252
Total net assets	1,417,365	1,390,011
<b>Total liabilities and net assets</b>	2,614,357	2,597,930

**B. Nonconsolidated Statement of Income**  
**Years Ended December 31, 2019 and 2020**

(Millions of yen)

	2019		2020	
Net sales	*1,*6	660,805	*1,*6	596,887
Cost of sales	*6	195,933	*6	166,144
<b>Gross profit</b>		464,872		430,742
Selling, general and administrative expenses	*2,*6	335,858	*2,*6	329,792
<b>Operating income</b>		129,014		100,950
Non-operating income				
Interest income	*6	210	*6	1,224
Dividends income	*6	148,354	*6	142,558
Other	*6	7,812	*6	7,548
Total non-operating income		156,376		151,329
Non-operating expenses				
Interest expenses	*6	519	*6	1,634
Interest on bonds		4,084		3,895
Other	*6	1,819	*6	6,260
Total non-operating expenses		6,422		11,789
<b>Ordinary income</b>		278,968		240,491
Extraordinary income				
Gain on sales of noncurrent assets	*3	14,202	*3	4,861
Gain on transfer of licenses	*6	18,381		—
Gain on sale of the former JT building		—	*7	45,806
Other		23,912		2,426
Total extraordinary income		56,495		53,094
Extraordinary losses				
Loss on sales of noncurrent assets	*4	52	*4	289
Loss on retirement of noncurrent assets	*5,*6	7,025	*5,*6	5,551
Impairment loss		8,521		999
Loss on liquidation of subsidiaries		20,524		—
Other		3,461		2,051
Total extraordinary losses		39,584		8,889
<b>Income before income taxes</b>		295,879		284,695
Income taxes-current		37,329		44,675
Income taxes-deferred		(3,920)		(1,732)
Total income taxes		33,409		42,943
<b>Net income</b>		262,469		241,752

**C. Nonconsolidated Statement of Changes in Net Assets**  
**Years ended December 31, 2019 and 2020**

(Millions of yen)

(Millions of yen)

	Shareholders' equity								
	Capital stock	Capital surplus		Retained earnings					Total retained earnings
		Legal capital surplus	Total capital surplus	Legal retained earnings	Other retained earnings				
					Reserve for investment loss on developing new business	Reserve for reduction entry	Special account for reduction entry	Retained earnings brought forward	
As of January 1, 2019	100,000	736,400	736,400	18,776	287	41,753	10,179	996,757	1,067,752
Changes of items during the period									
Provision of reserve for investment loss on developing new business					378			(378)	—
Reversal of reserve for investment loss on developing new business					(287)			287	—
Provision of reserve for reduction entry						8,395		(8,395)	—
Reversal of reserve for reduction entry						(4,775)		4,775	—
Provision of special account for reduction entry							1,747	(1,747)	—
Reversal of special account for reduction entry							(10,179)	10,179	—
Dividends from surplus								(270,936)	(270,936)
Net income								262,469	262,469
Purchase of treasury shares									
Disposal of treasury shares								(80)	(80)
Net changes of items other than shareholders' equity									
Total changes of items during the period	—	—	—	—	91	3,620	(8,432)	(3,826)	(8,547)
As of December 31, 2019	100,000	736,400	736,400	18,776	378	45,373	1,747	992,930	1,059,205

(Millions of yen)

	Shareholders' equity		Valuation and translation adjustments			Subscription rights to shares	Total net assets
	Treasury shares	Total shareholders' equity	Valuation difference on available-for-sale securities	Deferred gains or losses on hedges	Total valuation and translation adjustments		
<b>As of January 1, 2019</b>	(442,829)	1,461,323	25,815	4,877	30,693	1,547	1,493,562
Changes of items during the period							
Provision of reserve for investment loss on developing new business		—					—
Reversal of reserve for investment loss on developing new business		—					—
Provision of reserve for reduction entry		—					—
Reversal of reserve for reduction entry		—					—
Provision of special account for reduction entry		—					—
Reversal of special account for reduction entry		—					—
Dividends from surplus		(270,936)					(270,936)
Net income		262,469					262,469
Purchase of treasury shares	(50,001)	(50,001)					(50,001)
Disposal of treasury shares	361	281					281
Net changes of items other than shareholders' equity			(18,533)	513	(18,020)	10	(18,010)
Total changes of items during the period	(49,640)	(58,187)	(18,533)	513	(18,020)	10	(76,197)
<b>As of December 31, 2019</b>	(492,469)	1,403,136	7,283	5,390	12,673	1,556	1,417,365

(Millions of yen)

(Millions of yen)

	Shareholders' equity								
	Capital stock	Capital surplus		Retained earnings					Total retained earnings
		Legal capital surplus	Total capital surplus	Legal retained earnings	Other retained earnings				
					Reserve for investment loss on developing new business	Reserve for reduction entry	Special account for reduction entry	Retained earnings brought forward	
As of January 1, 2020	100,000	736,400	736,400	18,776	378	45,373	1,747	992,930	1,059,205
Changes of items during the period									
Provision of reserve for investment loss on developing new business					377			(377)	—
Reversal of reserve for investment loss on developing new business					(378)			378	—
Provision of reserve for reduction entry						2,924		(2,924)	—
Reversal of reserve for reduction entry						(6,586)		6,586	—
Provision of special account for reduction entry							327	(327)	—
Reversal of special account for reduction entry							(1,747)	1,747	—
Dividends from surplus								(273,200)	(273,200)
Net income								241,752	241,752
Purchase of treasury shares									
Disposal of treasury shares								(150)	(150)
Net changes of items other than shareholders' equity									
Total changes of items during the period	—	—	—	—	(1)	(3,662)	(1,421)	(26,514)	(31,597)
As of December 31, 2020	100,000	736,400	736,400	18,776	377	41,711	327	966,416	1,027,608

(Millions of yen)

	Shareholders' equity		Valuation and translation adjustments			Subscription rights to shares	Total net assets
	Treasury shares	Total shareholders' equity	Valuation difference on available-for-sale securities	Deferred gains or losses on hedges	Total valuation and translation adjustments		
<b>As of January 1, 2020</b>	(492,469)	1,403,136	7,283	5,390	12,673	1,556	1,417,365
Changes of items during the period							
Provision of reserve for investment loss on developing new business		—					—
Reversal of reserve for investment loss on developing new business		—					—
Provision of reserve for reduction entry		—					—
Reversal of reserve for reduction entry		—					—
Provision of special account for reduction entry		—					—
Reversal of special account for reduction entry		—					—
Dividends from surplus		(273,200)					(273,200)
Net income		241,752					241,752
Purchase of treasury shares	(1)	(1)					(1)
Disposal of treasury shares	963	813					813
Net changes of items other than shareholders' equity			(3,213)	6,799	3,586	(304)	3,281
Total changes of items during the period	962	(30,635)	(3,213)	6,799	3,586	(304)	(27,354)
<b>As of December 31, 2020</b>	(491,507)	1,372,501	4,069	12,189	16,259	1,252	1,390,011



**Notes to Nonconsolidated Financial Statements**  
**Years ended December 31, 2019 and 2020**

**(Significant Accounting Policies)**

**1. Basis and Method of Valuation for Securities**

(1) Shares of Subsidiaries and Affiliates:

Stated at cost determined by the moving-average method.

(2) Available-for-sale Securities:

A. Securities with a Fair Value:

Stated at fair value based on market prices on the closing date of the accounting period. (Valuation difference is stated as a component of net assets and the cost of securities sold is calculated by applying the moving-average method.)

B. Securities without a Fair Value:

Stated at cost determined by the moving-average method.

**2. Basis and Method of Valuation for Derivatives**

Stated based on the fair value method.

**3. Basis and Method of Valuation for Inventories**

Stated at the lower of cost as determined by the average cost method.

(Balance sheet amounts are measured at the lower of cost or net selling value.)

**4. Depreciation Methods for Depreciable Assets**

(1) Property, Plant and Equipment (Excluding Lease Assets)

The declining-balance method is applied. However, the straight-line method is applied for buildings (excluding accompanying facilities) acquired on or after April 1, 1998 and for accompanying facilities and structures acquired on or after April 1, 2016.

The main useful lives are as follows:

Buildings (excluding accompanying facilities):	38 to 50 years
Machinery and equipment:	10 years

(2) Intangible Assets (Excluding Lease Assets)

The straight-line method is applied.

The main useful lives are as follows:

Patent right:	8 years
Right of trademark:	10 years
Software:	5 years
Goodwill:	10 years

(3) Lease Assets

For finance leases that do not transfer ownership of the leased property to the lessee, depreciation expense is mainly computed by the straight-line method over the lease period as the useful life assuming no residual value.

**5. Policy on Translation of Assets and Liabilities Denominated in Foreign Currency into Japanese Yen**

Receivables and payables denominated in foreign currencies are translated into Japanese yen at the rates prevailing at the closing date of the accounting period with translation differences treated as gains or losses.

## **6. Policy on Accounting of Provisions**

### **(1) Allowance for Doubtful Accounts**

Provided for possible losses from bad debts at an amount determined based on the historical default rate for ordinary receivables and the individual recoverability of specific doubtful receivables from customers experiencing financial difficulties.

### **(2) Provision for Bonuses**

Provided based on the estimated payable amount to provide for the payment of bonuses to employees and directors.

### **(3) Provision for Retirement Benefits**

Provided in preparation for the payment of retirement benefits to employees based on the estimated retirement benefit obligations and fair value of plan assets as of the end of this fiscal year. In calculating retirement benefit obligations, the benefit formula basis is used as the method of attributing expected benefit to periods up to the year ended December 31, 2019.

Past service cost is amortized using the straight-line method over the average remaining years of service of the employees (mainly 10 years).

Actuarial gains and losses are amortized from the year following the year in which the gains or losses are recognized using the straight-line method over the average remaining years of service of the employees (mainly 10 years).

Also included in the provision for retirement benefits is the portion of public pension expenses for mutual assistance association during certain periods in or before June 1956 (prior to the enforcement of the Act on the Mutual Aid Association of Public Corporation Employees).

## **7. Method of Hedge Accounting**

Deferral hedge accounting is applied.

For interest rate and currency swaps, if they satisfy the requirements for treatment that incorporates swaps into underlying accounting items (accounting by applying foreign exchange rate stipulated in the contracts; exceptional treatment), they are accounted for by incorporating swaps into underlying accounting items.

## **8. Other Significant Accounting Policies**

### **(1) Accounting Treatment relating to Retirement Benefits**

With regard to unrecognized actuarial gains and losses and unrecognized past service cost relating to retirement benefits, different accounting treatments have been applied compared to those in the consolidated financial statements.

### **(2) Consumption Taxes**

National consumption tax and local consumption tax are excluded from each amount in the nonconsolidated statement of income.

### **(3) Adoption of Consolidated Taxation System**

The Company applies for the consolidated taxation system.

### **(4) Application of tax effect accounting for the transition from the consolidated taxation system to the group tax sharing system**

Concerning items which transitioned to the group tax sharing system established under the “Act for Partial Amendment of the Income Tax Act and Relevant Acts” (Act No. 8 of 2020) and those for which the non-consolidated tax payment system was reviewed in line with the transition to the group tax sharing system, the Company will not apply the provisions of Paragraph 44 of “Implementation Guidance on Tax Effect Accounting” (Accounting Standards Board of Japan (hereinafter, “ASBJ”) Guidance No.28, February 16, 2018), in accordance with Paragraph 3 of “the Practical Solution on the Treatment of the Tax Effect Accounting from the Consolidated Taxation System to the Group Tax Sharing System” (PITF No.39 March 31, 2020). As a result, the amounts of deferred tax assets and deferred tax liabilities are reported based on the provisions of the tax act before the amendment.

**(Additional Information)**

(Accounting estimates associated with the spread of COVID-19)

Since the same content is described in “4. Significant Accounting Estimates and Judgments” in “Notes to Consolidated Financial Statements”, the description is omitted.

**(Changes in Presentation Methods)**

(Nonconsolidated Statement of Income)

“Gain on sales of investment securities”, which was presented separately for the previous fiscal year, is included in “Other” under “Extraordinary income” for the current fiscal year, due to a decrease in materiality. The financial statements for the previous fiscal year have been reclassified to reflect this change in presentation method.

As a result, ¥22,912 million posted in “Gain on sales of investment securities” has been reclassified into “Other” under “Extraordinary income” in the nonconsolidated statement of income for the previous fiscal year.

**(Accounting Standards Not Yet Adopted)**

- “Accounting Standard for Revenue Recognition” (ASBJ Statement No. 29, March 31, 2020)
- “Implementation Guidance on Accounting Standard for Revenue Recognition” (ASBJ Guidance No. 30, March 31, 2020)

(1) Overview

These are the comprehensive accounting standards for revenue recognition. Revenue is recognized based on the following five-step approach.

Step 1: Identify the contract with a customer

Step 2: Identify the performance obligations in the contract

Step 3: Determine the transaction price

Step 4: Allocate the transaction price to the performance obligations in the contract

Step 5: Recognize revenue when the entity satisfies a performance obligation

(2) Scheduled Date of Adoption

This accounting standard will be applied from the beginning of the fiscal year ending December 31, 2022.

(3) Effect of Adoption

Expenses previously recognized in “Selling, general and administrative expenses” will be partially recognized as a reduction of “Net sales,” for example.

- “Accounting Standard for Disclosure of Accounting Estimates” (ASBJ Statement No.31, March 31, 2020)

(1) Overview

With regard to the disclosure of “Sources of estimation uncertainty” required by Paragraph 125 of International Accounting Standards (IAS) 1 “Presentation of Financial Statements” (hereinafter, “IAS 1”) issued in 2003 by the International Accounting Standards Board (IASB), because this information is of value to users of the financial statements, there were requests to consider disclosing this under Japanese GAAP as information included in explanatory notes, and the ASBJ developed and issued “Accounting Standard for Disclosure of Accounting Estimates” (hereinafter, the “Standard”).

The basic approach taken by the ASBJ in the development of the Standard was, rather than to expand individual notes, to state the general principle (disclosure objectives), and then to allow the company to make a decision on specific content to be disclosed in light of the disclosure objectives. In the development, the ASBJ also made it its policy to make reference to the provisions of Paragraph 125 of IAS 1.

(2) Scheduled Date of Adoption

This accounting standard will be applied at the end of the fiscal year ending December 31, 2021.

- “Accounting Standard for Accounting Policy Disclosures, Accounting Changes and Error Corrections” (ASBJ Statement No.24 March 31, 2020)

(1) Overview

Having been presented with a proposal that consideration should be given to enrich the information in the explanatory notes on “the principles and procedures for accounting treatments adopted in cases where the provisions of relevant

accounting standards and regulations are not clear", the ASBJ performed the necessary revisions to the Standard and issued the revised Standard as "Accounting Standard for Accounting Policy Disclosures, Accounting Changes and Error Corrections".

In addition, when seeking to enrich the information in the explanatory notes on "the principles and procedures for accounting treatments adopted in cases where the provisions of relevant accounting standards and regulations are not clear", in order to avoid affecting practice that has been conducted under conditions where the provisions of relevant accounting standards and regulations are clear, it is assumed to inherit the provisions of the Annotations on the Corporate Accounting Principles (Annotation No. 1-2).

(2) Scheduled Date of Adoption

This accounting standard will be applied at the end of the fiscal year ending December 31, 2021.

**(Notes to Nonconsolidated Balance Sheet)**

\*1. Pursuant to Article 6 of the Japan Tobacco Inc. Act, the Company's assets are pledged as general collateral for corporate bonds issued by the Company. Bondholders have the right to receive payment of their own claims for assets of the Company in preference to other general creditors (with the exception of national taxes, local taxes and other obligations of a public nature).

\*2. Inter-company receivables and payables excluding those separately presented as of December 31 are as follows:

	2019	2020
(Millions of yen)		
Short-term receivables	23,832	14,173
Short-term payables	32,012	26,255
Long-term payables	5,010	3,830

\*3. Repurchase agreement of ¥5,000 million is included in "Other" of Current assets in this year and the fair value of securities received as collateral is ¥5,000 million.

\*4. "Cash management system deposits received" represent the fund entrusted in the cash management system of domestic group companies.

5. Contingent obligations

Guarantees provided for bank loans, bonds and others of subsidiaries and affiliates as of December 31 are as follows:

Bank loans and others							
2019				2020			
(Millions of yen)				(Millions of yen)			
JT International S.A.	68,609	(USD 411 million) (EUR 69 million) (CHF 67 million) others	JT International Company Netherlands B.V.	60,414	(EUR 477 million)		
PT. Karyadibya Mahardhika	54,878	(IDR 6,986,512 million) others	JT International Holding B.V.	34,274	(EUR 270 million)		
JT International Holding B.V.	44,129	(EUR 360 million) others	JT International Hellas A.E.B.E.	27,891	(EUR 220 million)		
JT International Company Netherlands B.V.	37,926	(EUR 310 million)	JT International S.A.	11,001	(CHF 57 million) (EUR 20 million) others		
JTI Ireland Limited	28,772	(EUR 235 million)					
JT International Hellas A.E.B.E.	24,123	(EUR 197 million)					
JT International (Philippines) Inc.	14,768	(PHP 6,850 million)					
LLC Petro	11,838	(RUB 6,689 million)					
JT International Spol s r.o.	10,209	(CZK 2,108 million)					
Other (61 companies)	87,457		Other (54 companies)	126,532			
Total	382,709		Total	260,114			

Bonds

2019				2020			
(Millions of yen)				(Millions of yen)			
JT International		(EUR	1,050 million)	JT International		(EUR	2,050 million)
Financial	298,183	(USD	1,025 million)	Financial	421,878	(USD	1,025 million)
Services B.V.		(GBP	400 million)	Services B.V.		(GBP	400 million)
Total	298,183			Total	421,878		

(Note) Guarantee obligations denominated in foreign currencies were translated into yen amounts using the exchange rate as of the closing date of the accounting period.

**(Notes to Nonconsolidated Statement of Income)**

\*1. Net sales including tobacco excise taxes for each year are as follows:

	(Millions of yen)	
	2019	2020
Net sales including tobacco excise taxes	1,655,611	1,514,560

(Note) Net sales including tobacco excise taxes are net sales plus the amount equivalent to tobacco excise taxes.

\*2. The main components of “Selling, general and administrative expenses” for each year are as follows:

	(Millions of yen)	
	2019	2020
Promotion expenses	40,529	45,198
Compensations, salaries and allowances	30,013	29,735
Provision for bonus	2,870	4,145
Employee benefit expenses	10,528	10,572
Commission	40,431	31,856
Depreciation and amortization	65,129	64,349
Research and development expenses	54,017	57,733
Selling expenses ratio	52%	53%
General and administrative expenses ratio	48%	47%

\*3. The main component of “Gains on sales of noncurrent assets” for each year is as follows:

	(Millions of yen)	
	2019	2020
Land	14,166	4,732

\*4. The main component of “Losses on sales of noncurrent assets” for each year is as follows:

	(Millions of yen)	
	2019	2020
Buildings	15	9
Structures	9	7
Tools, furniture and fixtures	18	249

\*5. The main components of “Losses on disposal of noncurrent assets” for each year are as follows:

	(Millions of yen)	
	2019	2020
Buildings	1,724	1,274
Machinery and equipment	2,485	2,133

\*6. Amounts of transactions with subsidiaries and affiliates for each year are as follows:

	(Millions of yen)	
	2019	2020
Net sales	86,017	51,669
Purchase of goods	62,101	55,995
Selling, general and administrative expenses	58,902	49,949
Dividends income	146,767	142,312
Amount of non-operating transactions	63,542	12,480

\*7. "Gain on sale of the former JT building" is mainly composed of gain and loss on sales of fixed assets, including following major items.

Gain on sale of land	¥	49,655	million
Loss on sale of building	¥	3,680	million



**(Securities)**

Investments in Subsidiaries and Affiliates as of December 31 are as follows:

2019

(Millions of yen)

Type	Balance sheet amount	Fair value	Difference
Investments in subsidiaries	41,580	47,120	5,540
Total	41,580	47,120	5,540

2020

(Millions of yen)

Type	Balance sheet amount	Fair value	Difference
Investments in subsidiaries	41,580	49,584	8,004
Total	41,580	49,584	8,004

(Note) Balance sheet amount of investments in subsidiaries and affiliates whose fair value is deemed extremely difficult to determine as of December 31 is as follows:

(Millions of yen)

Type	2019	2020
Investments in subsidiaries	1,440,350	1,445,883
Investments in affiliates	153	153

The above are not included in “Investments in subsidiaries and affiliates” because their market values are not available and their fair values are deemed extremely difficult to determine.

**(Tax Effect Accounting)****1. Breakdown of deferred tax assets and deferred tax liabilities by major cause****As of December 31, 2019 and 2020**

(Millions of yen)

	2019	2020
Deferred tax assets		
Provision for retirement benefits	28,287	29,375
Obligations pertaining to mutual assistance pension benefits	10,759	9,220
Investments in subsidiaries	12,232	12,232
Other	31,501	31,668
Subtotal	82,779	82,495
Less valuation allowance	(23,301)	(22,950)
Total	59,478	59,545
Deferred tax liabilities		
Reserve for reduction entry	(19,846)	(18,245)
Deferred gains or losses on hedges	(10,962)	(13,661)
Valuation difference on available-for-sale securities	(3,085)	(1,640)
Other	(12,532)	(12,485)
Total	(46,425)	(46,030)
Net deferred tax assets/liabilities	13,053	13,514

**2. Reconciliation between the effective statutory tax rate and the actual effective tax rate after applying tax effect accounting, if there is a significant difference****As of December 31, 2019 and 2020**

(%)

	2019	2020
Effective statutory tax rate	30.43	30.43
(Adjustments)		
Permanent difference arising from non-deductible items including entertainment expenses	0.32	0.22
Permanent difference arising from non-taxable items including dividends income	(14.35)	(14.45)
Tax credit of items including research and development expenses	(2.12)	(1.07)
Taking over tax losses carried forward from liquidation of subsidiaries	(4.97)	-
Loss on liquidation of subsidiaries	2.10	-
Other	(0.12)	(0.05)
Actual effective tax rate after applying tax effect accounting	11.29	15.08

**(Business Combination)**

No items to report.

**(Significant Subsequent Events)**

Since the same content is described in “39. Subsequent Events” of the “(1) Consolidated Financial Statements” in the “1 Consolidated Financial Statements”, the description is omitted. The impact on the nonconsolidated financial statements is expected to be about the same as that on the consolidated financial statements, although there are differences due to initiatives of subsidiaries and accounting standards.

## D. Supplementary Statements

### Detailed Schedule of Property, Plant and Equipment and Others

(Millions of yen)

	Type of assets	As of January 1, 2020	Increase in the year ended December 31, 2020	Decrease in the year ended December 31, 2020	Depreciation during the year ended December 31, 2020	As of December 31, 2020	Accumulated depreciation or accumulated amortization as of December 31, 2020
Property, plant and equipment	Buildings	92,396	8,832	14,495 (883)	6,703	80,030	175,645
	Structures	2,686	167	205 (97)	273	2,375	10,622
	Machinery and equipment	59,262	6,326	2,075 (5)	11,947	51,567	173,702
	Vehicles	1,827	107	110	518	1,307	1,897
	Tools, furniture and fixtures	16,586	5,316	1,239 (11)	6,441	14,221	66,509
	Land	71,279	13	22,384 (2)	—	48,909	—
	Construction in progress	2,503	386	2,444	—	445	—
	Total property, plant and equipment	246,540	21,148	42,952 (999)	25,882	198,854	428,375
Intangible assets	Patent right	224	7	—	76	154	—
	Right of trademark	98,896	3	7	16,772	82,120	—
	Software	19,581	6,005	366	6,921	18,299	—
	Goodwill	214,626	—	—	35,771	178,855	—
	Other	2,705	1,735	1,665 (0)	113	2,662	—
	Total intangible assets	336,031	7,750	2,038 (0)	59,653	282,089	—

(Note 1) The figures in parentheses in the “Decrease in the year ended December 31, 2020” column represent decreases due to impairment loss included in the figures above.

(Note 2) Other includes software in progress.

(Note 3) The major item of “Increase in the year ended December 31, 2020” and “Decrease in the year ended December 31, 2020” is as follows:

Buildings	Decrease	the former JT building	¥13,208 million
Land	Decrease	the former JT building	¥21,488 million

### Detailed Schedule of Reserve Allowances

(Millions of yen)

Category	As of January 1, 2020	Increase in the year ended December 31, 2020	Decrease in the year ended December 31, 2020	As of December 31, 2020
Allowance for doubtful accounts	1,689	2,198	79	3,808
Provision for bonuses	4,726	6,330	4,726	6,330

#### (2) Major Assets and Liabilities

Note is omitted due to the fact that the relevant parts are prepared in the consolidated financial statements.

#### (3) Others

No items to report.

## VI. Outline of Filing Company's Business Concerning Shares

Business year	From January 1 to December 31
Ordinary General Meeting of Shareholders	March
Record date	December 31
Record dates for dividends from surplus	June 30, December 31
Share unit	100 shares
Purchase/sale of shares less than one unit: Office for handling business  Shareholder registry administrator  Forwarding office Handling charge for purchase/sale	(Special account) 4-5, Marunouchi 1-chome, Chiyoda-ku, Tokyo, Japan Mitsubishi UFJ Trust and Banking Corporation, Corporate Agency Division  (Special account) 4-5, Marunouchi 1-chome, Chiyoda-ku, Tokyo, Japan Mitsubishi UFJ Trust and Banking Corporation  — Free
Method of public notice	Electronic public notice will be made. However, if the Company is unable to make electronic public notice due to an accident or any other compelling reason, it will make an alternative public notice on "The Nikkei" newspaper. Electronic public notice will be notified on the Company's website: URL: <a href="https://www.jt.com/">https://www.jt.com/</a>
Special benefits for shareholders	Special benefits for shareholders (1) Scope All shareholders who appear in the shareholder registry as of December 31 each year and hold 100 or more shares (share unit) over a year. (2) Description The Company presents its own products (including products of the group companies) 1) Shareholders with 100 or more than 100 and less than 200 shares ¥2,500 equivalent 2) Shareholders with 200 or more than 200 and less than 1,000 shares ¥4,500 equivalent 3) Shareholders with 1,000 or more than 1,000 and less than 2,000 shares ¥7,000 equivalent 4) Shareholders with 2,000 or more shares ¥13,500 equivalent  * It is possible to choose for a contribution to be made to an organization that carries out social contribution activities in lieu of the presentation of products.

## **VII. Reference Information on Filing Company**

### **1. Information on Filing Company's Parent Company**

The Company does not have a parent company as described by the provisions of Article 24-7, paragraph 1 of the Financial Instruments and Exchange Act.

### **2. Other Reference Information**

From the beginning of this fiscal year until the filing date of this Annual Securities Report, the Company has filed the following documents.

#### **(1) Annual Securities Report and Appendices, and Written Confirmation**

Filed to Director-General of Kanto Local Finance Bureau on March 19, 2020

Business year: 35th term (from January 1, 2019 to December 31, 2019)

#### **(2) Amendment Report of Annual Securities Report and Written Confirmation**

Filed to Director-General of Kanto Local Finance Bureau on April 24, 2020

Business year: 35th term (from January 1, 2019 to December 31, 2019)

#### **(3) Internal Control Report**

Filed to Director-General of Kanto Local Finance Bureau on March 19, 2020

Business year: 35th term (from January 1, 2019 to December 31, 2019)

#### **(4) Quarterly Securities Reports and Written Confirmations**

Filed to Director-General of Kanto Local Finance Bureau on April 30, 2020

First quarter of the 36th term (from January 1, 2020 to March 31, 2020)

Filed to Director-General of Kanto Local Finance Bureau on July 31, 2020

Second quarter of the 36th term (from April 1, 2020 to June 30, 2020)

Filed to Director-General of Kanto Local Finance Bureau on October 30, 2020

Third quarter of the 36th term (from July 1, 2020 to September 30, 2020)

#### **(5) Extraordinary Reports**

Filed to Director-General of Kanto Local Finance Bureau on March 27, 2020

Extraordinary Report based on Article 19, paragraph 2, item (xii) (Event Which May Have Serious Effects on the Financial Position, Operating Results and Cash Flow Status) of the Cabinet Office Ordinance on Disclosure of Corporate Information, etc.

Filed to Director-General of Kanto Local Finance Bureau on August 28, 2020

Extraordinary Report based on Article 19, paragraph 2, item (xii) (Event Which May Have Serious Effects on the Financial Position, Operating Results and Cash Flow Status) of the Cabinet Office Ordinance on Disclosure of Corporate Information, etc.

#### **(6) Shelf Registration Statement and Appendices**

Filed to Director-General of Kanto Local Finance Bureau on August 6, 2020

#### **(7) Amendment to Shelf Registration Statements**

Filed to Director-General of Kanto Local Finance Bureau on August 28, 2020

Amendment to Shelf Registration Statements pertaining to Shelf Registration Statement (bonds) filed on August 6, 2020.

#### **(8) Securities Registration Statement and Appendices**

Filed to Director-General of Kanto Local Finance Bureau on April 30, 2020

**B. Information on Guarantee Companies, etc. of Filing Company**

No items to report

(TRANSLATION)

## INDEPENDENT AUDITOR'S REPORT

March 24, 2021

To the Board of Directors of  
Japan Tobacco Inc.:

Deloitte Touche Tohmatsu LLC  
Tokyo office

Designated Engagement Partner,  
Certified Public Accountant: Yukitaka Maruchi (Seal)

Designated Engagement Partner,  
Certified Public Accountant: Yasuhiko Haga (Seal)

Designated Engagement Partner,  
Certified Public Accountant: Yoichi Matsushita (Seal)

### Audit of Financial Statements

#### *Opinion*

Pursuant to the first paragraph of Article 193-2 of the Financial Instruments and Exchange Act, we have audited the consolidated financial statements of Japan Tobacco Inc. (the "Company") and its consolidated subsidiaries (the "Group") included in the Accounting Section, namely, the consolidated statement of financial position as of December 31, 2020, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the fiscal year from January 1, 2020 to December 31, 2020, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of December 31, 2020, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards pursuant to the provisions of Article 93 of the Ordinance on Terminology, Forms and Preparation Methods of Consolidated Financial Statements.

#### *Basis for Opinion*

We conducted our audit in accordance with auditing standards generally accepted in Japan. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the provisions of the Code of Professional Ethics in Japan, and we have fulfilled our other ethical responsibilities as auditors. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### *Key Audit Matters*

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the fiscal year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.



Contingencies of Smoking and Health Litigation in Canada	
Key Audit Matter Description	How the Key Audit Matter Was Addressed in the Audit
<p>As described in Note 38 to the consolidated financial statements "Contingencies," JTI-Macdonald Corp., the Company's Canadian subsidiary and/or indemnitees are defendants in eight class actions and 10 health-care cost recovery litigation in Canada (collectively, the "Canadian cases"). In two class actions in Quebec (Cecilia Letourneau and Conseil Quebécois sur le tabac et la sante), the Quebec Court of Appeal rendered a judgment ordering JTI-Macdonald Corp. to pay compensation of approximately CAD 1.8 billion (approximately ¥143.4 billion).</p> <p>The judgment of the Quebec Court of Appeal exceeded JTI-Macdonald Corp.'s capacity to pay, and JTI-Macdonald Corp. filed for protection from its creditors under the Companies' Creditors Arrangement Act ("CCAA"), which was approved by the Ontario Superior Court, and is continuing as of the end of this fiscal year. Legal proceedings including the execution of the judgment against JTI-Macdonald Corp. have been stayed by the CCAA proceedings.</p> <p>The amount of compensation ordered by the Quebec Court of Appeal and the amount of compensatory and punitive damages sought by plaintiffs in the other Canadian cases are considered significant for the consolidated financial statements, and the Canadian cases also include some cases for which the amount of damages sought by plaintiffs has not been specified.</p> <p>The management is required to determine whether the recognition of provisions is necessary or not in accordance with the following recognition requirements for provisions defined in International Accounting Standard 37 "Provisions, Contingent Liabilities and Contingent Assets":</p> <ul style="list-style-type: none"> <li>• The company has a present obligation (legal or constructive) as a result of a past event;</li> <li>• The outflow of resources embodying economic benefits is probable (i.e., more likely than not) to settle the obligation; and</li> <li>• A reliable estimate can be made of the amount of the obligation.</li> </ul> <p>Since the determination whether the recognition of provisions is necessary or not involves subjective judgments made by management and uncertainty that is difficult to prove, we have determined this matter regarding the Canadian cases to be a key audit matter.</p>	<p>We developed an audit plan and performed the following audit procedures to address this key audit matter:</p> <ul style="list-style-type: none"> <li>• We inquired of the management and the Legal department of the Company to obtain updates on the statuses of the Canadian cases as of the end of this fiscal year, and assessed the appropriateness of management's judgment whether the recognition requirements for provisions regarding the Canadian cases were met.</li> <li>• We instructed the component auditor to perform the following audit procedures and assessed the appropriateness of component management's judgment on the recognition of provisions based on discussions with the component auditor: <ul style="list-style-type: none"> <li>✓ Evaluating internal controls over the internal approval and examination process to ensure that the judgments on recognizing provisions are appropriately made;</li> <li>✓ Inquiring of component management and inspecting the underlying documents that component management prepared, to assess the appropriateness of the component management's judgments on the recognition requirements for provisions defined in International Accounting Standard 37 "Provisions, Contingent Liabilities and Contingent Assets"; and</li> <li>✓ Sending letters to component legal counsel to confirm the appropriateness of the component management's judgment whether JTI-Macdonald Corp. has a present obligation (legal or constructive) as a result of a past event and whether the outflow of resources embodying economic benefits is probable to settle the obligation among the recognition requirements for provisions.</li> </ul> </li> <li>• We received a third party opinion from an external legal firm to gain assurance that there are no logical contradictions or significant divergences in reasoning to the position adopted by the component's legal counsel.</li> </ul>

Evaluation of Goodwill Allocated to International Tobacco Cash-Generating Unit	
Key Audit Matter Description	How the Key Audit Matter Was Addressed in the Audit
<p>As described in Note 14 to the consolidated financial statements "Goodwill and Intangible Assets," the Group allocates goodwill generated by business combinations to the domestic tobacco cash-generating unit, the international tobacco cash-generating unit and the processed food cash-generating unit.</p> <p>The Group has a goodwill balance of ¥1,618,133 million allocated to the international tobacco cash-generating unit at the end of this fiscal year, that is mainly as results of the acquisitions of RJR Nabisco's non-U.S. tobacco operations in 1999, Gallaher Group Plc in 2007 and Natural American Spirit's non-U.S. tobacco operations in 2016.</p> <p>In accordance with International Accounting Standard 36 "Impairment of Assets," goodwill is required to be tested for impairment annually or whenever there is an indication that the asset may be impaired.</p> <p>The recoverable amount of the international tobacco cash-generating unit is calculated by value in use based on the three-year business plan that was prepared by reflecting past experiences and external information, and approved by management (hereinafter, "the three-year business plan"). After the three-year business plan, the Group sets a growth rate from 4.6% in the fourth year to 2.8% in the ninth year, and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation. As a result of the impairment test, the value in use sufficiently exceeds the carrying amount of the international tobacco cash-generating unit, and the management believes that the value in use will not fall below the carrying amount even if the growth rate used in calculating the value in use fluctuates within a reasonable range.</p> <p>The balance of goodwill allocated to the international tobacco cash-generating unit is material to consolidated financial statements, and the three-year business plan used in the impairment test, and the underlying assumptions for growth rates used to develop the plan for fourth year onwards are greatly affected by management's subjective judgments. In addition, in the international tobacco business, the Group is placed in the environment with the tightening regulations on tobacco products, increased taxes levied on tobacco and a fierce competition with rival companies. These external factors affect to the three-year business plan and the growth rates used to develop the plan for fourth year onwards.</p>	<p>In response to this key audit matter, we developed an audit plan for the impairment test of goodwill allocated to the international tobacco cash-generating unit and performed the following procedures:</p> <ul style="list-style-type: none"> <li>• In order to assess the reasonableness of the three-year business plan and the underlying assumptions for the growth rates developed by component management, we instructed the component auditor to perform the following audit procedures: <ul style="list-style-type: none"> <li>✓ Evaluating internal controls over the approval and examination process to ensure the three-year business plan is appropriately prepared;</li> <li>✓ Considering the achievement of the past three-year business plan retrospectively by comparing the past three-year business plan with actual results during the corresponding period, as well as assessing the feasibility of the current three-year business plan in light of the market conditions and performance of the major markets in which the international tobacco cash-generating unit operates as of the end of this fiscal year; and</li> <li>✓ Inquiring of component management on the background and rationality of data used by component management to determine the growth rates after the current three-year business plan, as well as testing the growth rates based on available external information, with assistance of the valuation specialists in our network firm.</li> </ul> </li> <li>• We discussed with the management the results of the impairment test of goodwill allocated to the international tobacco cash-generating unit and assessed the appropriateness of management's conclusion on the impairment test.</li> </ul>

Since the three-year business plan and the growth rates to develop the plan for fourth year onwards involve uncertainties and require management's judgment, we have determined the evaluation of the goodwill allocated to the international tobacco cash-generating unit to be a key audit matter.	
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*Responsibilities of Management and Audit & Supervisory Board Members and the Audit & Supervisory Board for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern in accordance with International Financial Reporting Standards.

Audit & Supervisory Board members and the Audit & Supervisory Board are responsible for overseeing the Directors' execution of duties relating to the design and operating effectiveness of the controls over the Group's financial reporting process.

*Auditor's Responsibilities for the Audit of the Consolidated Financial Statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with auditing standards generally accepted in Japan, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks. The procedures selected depend on the auditor's judgment. In addition, we obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- Obtain, when performing risk assessment procedures, an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate whether the overall presentation and disclosures of the consolidated financial statements are in accordance with International Financial Reporting Standards, as well as the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with Audit & Supervisory Board members and the Audit & Supervisory Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide Audit & Supervisory Board members and the Audit & Supervisory Board with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with Audit & Supervisory Board members and the Audit & Supervisory Board, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

## **Audit of Internal Control**

### *Opinion*

Pursuant to the second paragraph of Article 193-2 of the Financial Instruments and Exchange Act, we have audited management's report on internal control over financial reporting of Japan Tobacco Inc. as of December 31, 2020.

In our opinion, management's report on internal control over financial reporting referred to above, which represents that the internal control over financial reporting of Japan Tobacco Inc. as of December 31, 2020, is effectively maintained, presents fairly, in all material respects, the results of the assessment of internal control over financial reporting in accordance with assessment standards for internal control over financial reporting generally accepted in Japan.

### *Basis for Opinion*

We conducted our internal control audit in accordance with auditing standards for internal control over financial reporting generally accepted in Japan. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Internal Control Audit section of our report. We are independent of the Group in accordance with the provisions of the Code of Professional Ethics in Japan, and we have fulfilled our other ethical responsibilities as auditors. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### *Responsibility of Management and Audit & Supervisory Board Members and the Audit & Supervisory Board for Report on Internal Control*

Management is responsible for designing and operating effective internal control over financial reporting and for the preparation and fair presentation of its report on internal control in accordance with assessment standards for internal control over financial reporting generally accepted in Japan. Audit & Supervisory Board members and the Audit & Supervisory Board are responsible for overseeing and verifying the design and operating effectiveness of internal control over financial reporting. There is a possibility that misstatements may not be completely prevented or detected by internal control over financial reporting.

### *Auditor's Responsibilities for the Internal Control Audit*

Our objectives are to obtain reasonable assurance about whether management's report on internal control over financial reporting is free from material misstatement and to issue an auditor's report that includes our opinion.

As part of an audit in accordance with auditing standards for internal control over financial reporting generally accepted in Japan, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Perform audit procedures to obtain audit evidence regarding the results of the assessment of internal control over financial reporting in management's report on internal control. The procedures selected depend on the auditor's judgment, including the significance of effects on reliability of financial reporting.
- Examine representations on the scope, procedures and results of the assessment of internal control over financial reporting made by management, as well as evaluating the overall presentation of management's report on internal control.
- Obtain sufficient appropriate audit evidence regarding the results of the assessment of internal control over financial reporting. We are responsible for the direction, supervision and performance of the internal control audit. We remain solely responsible for our audit opinion.

We communicate with Audit & Supervisory Board members and the Audit & Supervisory Board regarding, among other matters, the planned scope and timing of the internal control audit, result of the internal control audit, including any identified material weakness which should be disclosed and the result of remediation.

We also provide Audit & Supervisory Board members and the Audit & Supervisory Board with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

#### **Interest Required to Be Disclosed by the Certified Public Accountants Act of Japan**

Our firm and its designated engagement partners do not have any interest in the Group which is required to be disclosed pursuant to the provisions of the Certified Public Accountants Act of Japan.

#### **Notes to the Readers of Independent Auditor's Report**

This is an English translation of the independent auditor's report as required by the Financial Instruments and Exchange Act of Japan for the conveniences of the reader.

(TRANSLATION)

## INDEPENDENT AUDITOR'S REPORT

March 24, 2021

To the Board of Directors of  
Japan Tobacco Inc.:

Deloitte Touche Tohmatsu LLC  
Tokyo office

Designated Engagement Partner,  
Certified Public Accountant: Yukitaka Maruchi (Seal)

Designated Engagement Partner,  
Certified Public Accountant: Yasuhiko Haga (Seal)

Designated Engagement Partner,  
Certified Public Accountant: Yoichi Matsushita (Seal)

### Opinion

Pursuant to the first paragraph of Article 193-2 of the Financial Instruments and Exchange Act, we have audited the nonconsolidated financial statements of Japan Tobacco Inc. (the "Company") included in the Financial Section, namely, the nonconsolidated balance sheet as of December 31, 2020, and the nonconsolidated statement of income and nonconsolidated statement of changes in net assets for the 36th fiscal year from January 1, 2020 to December 31, 2020, and the significant accounting policies and other related notes and supplemental schedules.

In our opinion, the accompanying nonconsolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020, and its financial performance and for the year then ended in accordance with accounting principles generally accepted in Japan.

### Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in Japan. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Nonconsolidated Financial Statements section of our report. We are independent of the Company in accordance with the provisions of the Code of Professional Ethics in Japan, and we have fulfilled our other ethical responsibilities as auditors. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the nonconsolidated financial statements of the fiscal year. These matters were addressed in the context of our audit of the nonconsolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Evaluation of Shares of Subsidiaries	
Key Audit Matter Description	How the Key Audit Matter Was Addressed in the Audit
<p>On the balance sheet of the Company, Shares of subsidiaries and affiliates was ¥1,487,617 million (approximately 57.3% of Total assets) as of the end of this fiscal year, including shares of JT International Group Holding B.V., one of the subsidiaries, of ¥1,355,146 million.</p> <p>The international tobacco business manufactures and sells tobacco products overseas mainly through JT International S.A., which controls manufacturing and sales operations. The Company invests in JT International Holding B.V., which consolidates the financial results of the international tobacco business, including JT International S.A., through JT International Group Holding B.V.</p> <p>The Company considers whether to recognize impairment of shares of JT International Group Holding B.V. by comparing the carrying amount of JT International Group Holding B.V. shares with the net assets value calculated using the net assets on the balance sheet of JT International Group Holding B.V. In addition, the Company determines whether the net assets value of JT International Group Holding B.V. shares has declined significantly based on the results of the impairment test of goodwill allocated to the international tobacco cash-generating unit.</p> <p>The Company's consolidated financial statements are prepared in accordance with International Financial Reporting Standards, and the Company conducts an impairment test on goodwill allocated to the international tobacco cash-generating unit annually based on International Accounting Standard 36 "Impairment of Assets."</p> <p>The recoverable amount of the international tobacco cash-generating unit is calculated by value in use based on the three-year business plan that was prepared by reflecting past experiences and external information, and approved by management (hereinafter, "the three-year business plan"). After the three-year business plan, the Company sets a growth rate from 4.6% in the fourth year to 2.8% in the ninth year, and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation. As a result of the consideration, the Company concluded that it was not necessary to recognize the impairment on JT International Group Holding B.V. shares.</p>	<p>In response to this key audit matter, we developed the audit plan for the evaluation of JT International Group Holding B.V. shares, obtained and inspected the results of Company's evaluation.</p> <p>In addition, we performed the following procedures in relation to the impairment test of goodwill allocated to the international tobacco cash-generating unit:</p> <ul style="list-style-type: none"> <li>• In order to assess the reasonableness of the three-year business plan and the underlying assumptions for the growth rates developed by component management, we instructed the component auditor to perform the following audit procedures: <ul style="list-style-type: none"> <li>✓ Evaluating internal controls over the approval and examination process to ensure the three-year business plan is appropriately prepared;</li> <li>✓ Considering the achievement of the past three-year business plan retrospectively by comparing the past three-year business plan with actual results during the corresponding period, as well as assessing the feasibility of the current three-year business plan in light of the market conditions and performance of the major markets in which the international tobacco cash-generating unit operates as of the end of this fiscal year; and</li> <li>✓ Inquiring of component management on the background and rationality of data used by component management to determine the growth rates after the current three-year business plan, as well as testing the growth rates based on available external information, with assistance of the valuation specialists in our network firm.</li> </ul> </li> <li>• We discussed with the management the results of the impairment test of goodwill allocated to the international tobacco cash-generating unit and assessed the appropriateness of management's conclusion on the impairment test.</li> </ul>

<p>The three-year business plan used in the evaluation of JT International Group Holding B.V. shares, and the underlying assumptions for growth rates used to develop the plan for fourth year onwards are greatly affected by management's subjective judgements. In addition, in the international tobacco business, the Group is placed in the environment with the tightening regulations on tobacco products, increased taxes levied on tobacco and a fierce competition with rival companies. These external factors affect to the three-year business plan and the growth rates used to develop the plan for fourth year onwards.</p> <p>Since the three-year business plan and the growth rates to develop the plan for fourth year onwards involve uncertainties and require management's judgement, we have determined the evaluation of JT International Group Holding B.V. shares to be a key audit matter.</p>	
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## **Responsibilities of Management and Audit & Supervisory Board Members and the Audit & Supervisory Board for the Nonconsolidated Financial Statements**

Management is responsible for the preparation and fair presentation of the nonconsolidated financial statements in accordance with accounting principles generally accepted in Japan, and for such internal control as management determines is necessary to enable the preparation of nonconsolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the nonconsolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern in accordance with accounting principles generally accepted in Japan.

Audit & Supervisory Board members and the Audit & Supervisory Board are responsible for overseeing the Directors' execution of duties relating to the design and operating effectiveness of the controls over the Company's financial reporting process.

## **Auditor's Responsibilities for the Audit of the Nonconsolidated Financial Statements**

Our objectives are to obtain reasonable assurance about whether the nonconsolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these nonconsolidated financial statements.

As part of an audit in accordance with auditing standards generally accepted in Japan, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the nonconsolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks. The procedures selected depend on the auditor's judgment. In addition, we obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- Obtain, when performing risk assessment procedures, an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.



- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the nonconsolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate whether the overall presentation and disclosures of the nonconsolidated financial statements are in accordance with accounting principles generally accepted in Japan, as well as the overall presentation, structure and content of the nonconsolidated financial statements, including the disclosures, and whether the nonconsolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with Audit & Supervisory Board members and the Audit & Supervisory Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide Audit & Supervisory Board members and the Audit & Supervisory Board with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with Audit & Supervisory Board members and the Audit & Supervisory Board, we determine those matters that were of most significance in the audit of the nonconsolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

### **Interest Required to Be Disclosed by the Certified Public Accountants Act of Japan**

Our firm and its designated engagement partners do not have any interest in the Company which is required to be disclosed pursuant to the provisions of the Certified Public Accountants Act of Japan.

### Notes to the Readers of Independent Auditor's Report

This is an English translation of the independent auditor's report as required by the Financial Instruments and Exchange Act of Japan for the conveniences of the reader.