SUSTAINABILITY ACCOUNTING STANDARD
CONSUMPTION I SECTOR

TOBACCO PRODUCTS
Sustainability Accounting Standard

Sustainable Industry Classification System™ (SICS™) #CN0301
Prepared by the Sustainability Accounting Standards Board®

January 2015
Exposure Draft Standard for Public Comment
TOBACCO PRODUCTS
Sustainability Accounting Standard

About SASB
The Sustainability Accounting Standards Board (SASB) provides sustainability accounting standards for use by publicly listed corporations in the U.S. in disclosing material sustainability information for the benefit of investors and the public. SASB standards are designed for disclosure in mandatory filings to the Securities and Exchange Commission (SEC), such as the Form 10-K and 20-F. SASB is an independent 501(c)3 non-profit organization. Through 2016, SASB is developing standards for more than 80 industries in 10 sectors.

About this Standard
This Standard is an exposure draft presented for public review and comment. This version is not intended for implementation.

The public comment period lasts for 90 days, beginning on Wednesday, January 14th, 2015, and ending on Tuesday, April 14th, 2015. The Standard is subject to change thereafter.

For instructions on providing comments to SASB, please click here.

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INTRODUCTION

Purpose & Structure

This document contains the SASB Sustainability Accounting Standard (SASB Standard) for the Tobacco Products industry.

SASB Standards are comprised of (1) disclosure guidance and (2) accounting standards for sustainability topics for use by U.S. and foreign public companies in their annual filings (Form 10-K or 20-F) with the U.S. Securities and Exchange Commission (SEC). To the extent relevant, SASB Standards may also be applicable to other periodic mandatory filings with the SEC, such as Forms 10-Q, S-1, and 8-K.

SASB’s disclosure guidance identifies sustainability topics at an industry level, which may be material—depending on a company’s specific operating context—to a company within that industry.

Each company is ultimately responsible for determining which information is material and is therefore required to be included in its Form 10-K or 20-F and other periodic SEC filings.

SASB’s accounting standards provide companies with standardized accounting metrics to account for performance on industry-level sustainability topics. When making disclosure on sustainability topics, companies adopting SASB’s accounting standards will help to ensure that disclosure is standardized and therefore useful, relevant, comparable, and auditable.

Industry Description

The Tobacco Products industry is comprised of companies that manufacture tobacco products including cigarettes, cigars, and smokeless tobacco products. Many large tobacco companies operate globally and serve both international and U.S. customers. Companies may obtain or sell exclusive rights to sell certain brands of cigarettes in diverse markets. Most tobacco is grown by independent tobacco farmers, who typically sell their crops to tobacco merchants or to manufacturers under contract. Typically, tobacco products earn fairly robust profit margins due to relatively low material and labor-input costs.
Guidance for Disclosure of Material Sustainability Topics in SEC Filings

1. Industry-level Sustainability Topics

For the Tobacco Products industry, SASB has identified the following sustainability topics:

- Public Health
- Marketing Practices
- Environmental & Social Impacts of Supply Chains

2. Company-level Determination and Disclosure of Material Sustainability Topics

Sustainability disclosures are governed by the same laws and regulations that govern disclosures by securities issuers generally. According to the U.S. Supreme Court, a fact is material if, in the event such fact is omitted from a particular disclosure, there is “a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of the information made available.”\(^1\),\(^2\)

SASB has attempted to identify those sustainability topics that it believes may be material for all companies within each SICS industry. SASB recognizes, however, that each company is ultimately responsible for determining what is material to it.

Regulation S-K, which sets forth certain disclosure requirements associated with Form 10-K and other SEC filings, requires, among other things, that companies describe in the Management’s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) section of Form 10-K “any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations. If the registrant knows of events that will cause a material change in the relationship between costs and revenues (such as known future increases in costs of labor or materials or price increases or inventory adjustments), the change in the relationship shall be disclosed.”\(^2\)

Furthermore, Instructions to Item 303 state that the MD&A “shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition.”\(^2\)

In determining whether a trend or uncertainty should be disclosed, the SEC has stated that management should use a two-part assessment based on probability and magnitude:

- First, a company is not required to make disclosure about a known trend or uncertainty if its management determines that such trend or uncertainty is not reasonably likely to occur.

- Second, if a company’s management cannot make a reasonable determination of the likelihood of an event or uncertainty, then disclosure is required unless management determines that a material effect on the registrant’s financial condition or results of operation is not reasonably likely to occur.

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\(^2\) C.F.R. 229.303(Item 303)(a)(3)(ii)
3. Sustainability Accounting Standard Disclosures in Form 10-K

a. Management's Discussion and Analysis

Companies should consider making disclosure on sustainability topics as a complete set in the MD&A, in a sub-section titled “Sustainability Accounting Standards Disclosures.”

b. Other Relevant Sections of Form 10-K

In addition to the MD&A section, companies should consider disclosing sustainability information in other sections of Form 10-K, as relevant, including:

• **Description of business**—Item 101 of Regulation S-K requires a company to provide a description of its business and its subsidiaries. Item 101(c)(1)(xii) expressly requires disclosure regarding certain costs of complying with environmental laws:

  *Appropriate disclosure also shall be made as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries.*

• **Legal proceedings**—Item 103 of Regulation S-K requires companies to describe briefly any material pending or contemplated legal proceedings. Instructions to Item 103 provide specific disclosure requirements for administrative or judicial proceedings arising from laws and regulations that target discharge of materials into the environment or that are primarily for the purpose of protecting the environment.

• **Risk factors**—Item 503(c) of Regulation S-K requires filing companies to provide a discussion of the most significant factors that make an investment in the registrant speculative or risky, clearly stating the risk and specifying how a particular risk affects the particular filing company.

c. Rule 12b-20

Securities Act Rule 408 and Exchange Act Rule 12b-20 require a registrant to disclose, in addition to the information expressly required by law or regulation, “such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading.”

Guidance on Accounting of Material Sustainability Topics

For sustainability topics in the Tobacco Products industry, SASB identifies accounting metrics.

SASB recommends that each company consider using these sustainability accounting metrics when disclosing its performance with respect to each of the sustainability topics it has identified as material.

As appropriate—and consistent with Rule 12b-2043— for each sustainability topic, companies should consider including a narrative description of any material factors necessary to ensure completeness, accuracy, and comparability of the data reported. Where not addressed by the specific accounting metrics, but relevant, the registrant should discuss the following, related to the topic:

- The registrant’s strategic approach to managing performance on material sustainability issues;
- The registrant’s competitive positioning;
- The degree of control the registrant has;
- Any measures the registrant has undertaken or plans to undertake to improve performance; and
- Data for the registrant’s last three completed fiscal years (when available).

SASB recommends that registrants use SASB Standards specific to their primary industry as identified in the Sustainable Industry Classification System (SICS™). If a registrant generates significant revenue from multiple industries, SASB recommends that it consider the materiality of the sustainability issues that SASB has identified for those industries and disclose the associated SASB accounting metrics.

Users of the SASB Standards

The SASB Standards are intended for companies that engage in public offerings of securities registered under the Securities Act of 1933 (the Securities Act) and those that issue securities registered under the Securities Exchange Act of 1934 (the Exchange Act), for use in SEC filings, including, without limitation, annual reports on Form 10-K (Form 20-F for foreign issuers), quarterly reports on Form 10-Q, current reports on Form 8-K, and registration statements on Forms S-1 and S-3. Nevertheless, disclosure with respect to the SASB Standards is not required or endorsed by the SEC or other entities governing financial reporting, such as FASB, GASB, or IASB.

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3 SEC Rule 12b-20: “In addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.”

4 Registration under the Securities Exchange Act of 1934 is required (1) for securities to be listed on a national securities exchange such as the New York Stock Exchange, the NYSE Amex, and the NASDAQ Stock Market or (2) if (A) the securities are equity securities and are held by more than 2,000 persons (or 500 persons who are not accredited investors) and (B) the company has more than $10 million in assets.
Scope of Disclosure

Unless otherwise specified, SASB recommends:

- That a registrant disclose on sustainability issues and metrics for itself and for entities in which the registrant has a controlling interest and therefore are consolidated for financial reporting purposes (controlling interest is generally defined as ownership of 50% or more of voting shares);\(^5\)

- That for consolidated entities, disclosures be made, and accounting metrics calculated, for the whole entity, regardless of the size of the minority interest; and

- That information from unconsolidated entities not be included in the computation of SASB accounting metrics. A registrant should disclose, however, information about unconsolidated entities to the extent that the registrant considers the information necessary for investors to understand its performance with respect to sustainability issues (typically this disclosure would be limited to risks and opportunities associated with these entities).

Reporting Format

Activity Metrics and Normalization

SASB recognizes that normalizing accounting metrics is important for the analysis of SASB disclosures.

SASB recommends that a registrant disclose any basic business data that may assist in the accurate evaluation and comparability of disclosure, to the extent that the data are not already disclosed in Form 10-K (e.g., revenue, EBITDA, etc.).

Such data—termed “activity metrics”—may include high-level business data such as total number of employees, quantity of products produced or services provided, number of facilities, or number of customers. It may also include industry-specific data such as plant capacity utilization (e.g., for specialty chemical companies), number of transactions (e.g., for Internet media and services companies), hospital bed days (e.g., for health care delivery companies), or proven and probable reserves (e.g., for oil and gas exploration and production companies).

Activity metrics disclosed should:

- Convey contextual information that would not otherwise be apparent from SASB accounting metrics.

- Be deemed generally useful for users of SASB accounting metrics (e.g., investors) in performing their own calculations and creating their own ratios.

- Be explained and consistently disclosed from period to period to the extent they continue to be relevant. However, a decision to make a voluntary disclosure in one period does not obligate a continuation of that disclosure if it is no longer relevant or if a better metric becomes available.

\(^5\) See US GAAP consolidation rules (Section 810).
Where relevant, SASB recommends specific activity metrics that—at a minimum—should accompany SASB accounting metric disclosures.

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**Units of Measure**

Unless specified, disclosures should be reported in International System of Units (SI units).

**Uncertainty**

SASB recognizes that there may be inherent uncertainty when disclosing certain sustainability data and information. This may be related to variables such as the imperfectness of third-party reporting systems or the unpredictable nature of climate events. Where uncertainty around a particular disclosure exists, SASB recommends that the registrant should consider discussing its nature and likelihood.

**Estimates**

SASB recognizes that scientifically based estimates, such as those drawn from certain conversion factors or the exclusion of *de minimis* values, may be necessary for certain quantitative disclosures. Where appropriate, SASB does not discourage the use of such estimates. When using an estimate for a particular disclosure, SASB expects that the registrant discuss its nature and substantiate its basis.

**Timing**

Unless otherwise specified, disclosure shall be for the registrant’s fiscal year.

**Limitations**

There is no guarantee that SASB Standards address all sustainability impacts or opportunities associated with a sector, industry, or company, and therefore, a company must determine for itself the topics—sustainability-related or otherwise—that warrant discussion in its SEC filings.
Disclosure under SASB Standards is voluntary. It is not intended to replace any legal or regulatory requirements that may be applicable to user operations. Where such laws or regulations address legal or regulatory topics, disclosure under SASB Standards is not meant to supersede those requirements. Disclosure according to SASB Standards shall not be construed as demonstration of compliance with any law, regulation, or other requirement.

SASB Standards are intended to be aligned with the principles of materiality enforced by the SEC. However, SASB is not affiliated with or endorsed by the SEC or other entities governing financial reporting, such as FASB, GASB, or IASB.

Forward-looking Statements

Disclosures on sustainability topics can involve discussion of future trends and uncertainties related to the registrant’s operations and financial condition, including those influenced by external variables (e.g., environmental, social, regulatory, and political). Companies making such disclosures should familiarize themselves with the safe harbor provisions of Section 27A of the Securities Act and Section 21E of the Exchange Act, which preclude civil liability for material misstatements or omissions in such statements if the registrant takes certain steps, including, among other things, identifying the disclosure as “forward-looking” and accompanying such disclosure with “meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statements.”

Assurance

In disclosing to SASB Standards, it is expected that registrants disclose with the same level of rigor, accuracy, and responsibility as they apply to all other information contained in their SEC filings.

SASB encourages registrants to use independent assurance (attestation); for example, an Examination Engagement to AT Section 101.

The following sections contain the disclosure guidance associated with each accounting metric, such as guidance on definitions, scope, accounting, compilation, and presentation.

The term “shall” is used throughout this document to indicate those elements that reflect requirements of the Standard. The terms “should” and “may” are used to indicate guidance, which, although not required, provides a recommended means of disclosure.
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⑥ Note to [CN0302-03]—Disclosure shall include a description of fines and settlements and corrective actions implemented in response to events.
Public Health

Description

It is recognized that tobacco products are harmful to both consumers and those around them. Health problems associated with tobacco include lung disease, cancer, and heart disease. Compounding these health risks is the fact that nicotine, found naturally in tobacco leaves, is an addictive substance. Over the past several decades, as scientific studies have linked tobacco use to cancer and other diseases, tobacco product manufacturers have faced class actions and lawsuits from individuals, governments, corporations, and other groups, in some cases resulting in multibillion-dollar settlements. Regulations governing product ingredients and marketing are evolving, and can threaten the industry. In addition, the industry’s health impacts have led some investors to divest from tobacco companies. In an effort to address these risks, tobacco product manufacturers have created an array of reduced-harm products, such as e-cigarettes, aimed at reducing the harmful health impacts of tobacco use.

Accounting Metrics

CN0302-01. Revenue from (1) smokeless tobacco products, (2) non-tobacco nicotine-delivery products, and (3) other “tobacco harm-reduction” products

.01 The registrant shall disclose its revenue, in U.S. dollars, from smokeless tobacco products such as chewing tobacco, moist snuff (i.e., dipping tobacco), dry snuff, and snus.

.02 The registrant shall disclose its revenue, in U.S. dollars, from non-tobacco nicotine-delivery products such as electronic cigarettes, including pharmaceutical nicotine-replacement therapy products (e.g., gums, lozenges, patches, etc.).

.03 The registrant shall disclose its revenue, in U.S. dollars, from other “tobacco harm-reduction” products, such as “heat-not-burn” cigarettes, that are focused on replacing combustible tobacco products.

CN0302-02. Description of the process to assess risks and opportunities associated with “tobacco harm-reduction” products

.04 The registrant shall discuss its process to evaluate risks and opportunities associated with “tobacco harm-reduction” products, where

• “Tobacco harm-reduction” products are non-combustible nicotine-containing products such as smokeless tobacco, nicotine-replacement therapy products, and electronic cigarettes.

.05 The registrant shall discuss the scope, success, and growth plans related to its current “tobacco harm-reduction” product portfolio and, where relevant, its plans to introduce future products and product categories.

.06 The registrant shall discuss risks it faces related to its “tobacco harm-reduction” products, such as technical challenges with bringing the products to market, consumer and public perceptions about the safety of the products, regulatory risks, reputational risks, and other risks.

.07 The registrant shall discuss opportunities presented by “tobacco harm-reduction” products such as the ability to capture new market segments and the ability to contribute to reducing cigarette smoking.
.08 Where relevant, the registrant shall discuss whether risks and opportunities associated with the registrant’s “tobacco harm-reduction” products and strategies pertain differently to different geographic markets.
Marketing Practices

Description

Tobacco product marketing is heavily regulated, both in the U.S. and abroad. The Framework Convention on Tobacco Control has led many countries to introduce new regulatory approaches. Laws aim to prevent people from adopting tobacco use at a young age. Measures include preventing and reducing underage purchases and ensuring transparent advertising to adult consumers. Failure to comply with these regulations could lead to significant regulatory and legal costs, depending on the markets. The industry has faced costly legal battles related to the marketing and advertising of its products, including the Master Settlement Agreement (MSA), which changed the way tobacco products are marketed and mandated substantial annual payments to U.S. states. Tobacco product manufacturers face a dynamic regulatory environment, particularly with the continued introduction of new products. Marketing for new smokeless tobacco products and traditional tobacco products will have to balance regulatory requirements with the need to reach new markets.

Accounting Metrics

CN0302-03. Amount of legal and regulatory fines, settlements, and enforcement actions associated with marketing, labeling, and advertising

09 The registrant shall disclose the amount (excluding legal fees) of all fines or settlements associated with marketing, labeling, and advertising, including, but not limited to, those related to violations of the Tobacco Master Settlement Agreement, the Family Smoking Prevention and Tobacco Control Act, and the European Union Tobacco Advertising Directive.

10 Disclosure shall include civil actions (e.g., civil judgment, settlements, or regulatory penalties) and criminal actions (e.g., criminal judgment, penalties, or restitutions) taken by any entity (government, businesses, or individuals).

Note to CN0302-03

11 The registrant shall briefly describe the nature (e.g., guilty plea, deferred agreement, or non-prosecution agreement) and context (e.g., related to warning labels, advertising bans, promotion, sponsorship, etc.) of fines and settlements.

12 The registrant shall describe any corrective actions it has implemented as a result of each incident. This may include, but is not limited to, specific changes in operations, management, processes, products, business partners, training, or technology.

CN0302-04. Description of alignment of marketing and labeling practices with Articles 11 and 13 of the WHO Framework Convention on Tobacco Control

13 The registrant shall describe the degree to which its marketing and labeling practices are aligned with the following articles of the World Health Organization (WHO) Framework Convention on Tobacco Control (FCTC):

- Article 11 - Packaging and labelling of Tobacco Products
- Article 13 - Tobacco advertising, promotion, and sponsorship
Relevant provisions of Article 11 include:

1 (a) Tobacco product packaging and labelling do not promote a tobacco product by any means that are false, misleading, deceptive or likely to create an erroneous impression about its characteristics, health effects, hazards or emissions, including any term, descriptor, trademark, figurative or any other sign that directly or indirectly creates the false impression that a particular tobacco product is less harmful than other tobacco products. These may include terms such as “low tar”, “light”, “ultra-light”, or “mild”; and

1 (b) each unit packet and package of tobacco products and any outside packaging and labelling of such products also carry health warnings describing the harmful effects of tobacco use, and may include other appropriate messages. These warnings and messages:

(i) shall be approved by the competent national authority
(ii) shall be rotating,
(iii) shall be large, clear, visible and legible,
(iv) should be 50% or more of the principal display areas but shall be no less than 30% of the principal display areas,
(v) may be in the form of or include pictures or pictograms.

2. Each unit packet and package of tobacco products and any outside packaging and labelling of such products shall, in addition to the warnings specified in paragraph 1(b) of this Article, contain information on relevant constituents and emissions of tobacco products as defined by national authorities.

3. Each Party shall require that the warnings and other textual information specified in paragraphs 1(b) and paragraph 2 of this Article will appear on each unit packet and package of tobacco products and any outside packaging and labelling of such products in its principal language or languages.

4. For the purposes of this Article, the term “outside packaging and labelling” in relation to tobacco products applies to any packaging and labelling used in the retail sale of the product.

Relevant provisions of Article 13 include:

1. Parties recognize that a comprehensive ban on advertising, promotion and sponsorship would reduce the consumption of tobacco products.

2. Each Party shall, in accordance with its constitution or constitutional principles, undertake a comprehensive ban of all tobacco advertising, promotion and sponsorship. This shall include, subject to the legal environment and technical means available to that Party, a comprehensive ban on cross-border advertising, promotion and sponsorship originating from its territory. In this respect, within the period of five years after entry into force of this Convention for that Party, each Party shall undertake appropriate legislative, executive, administrative and/or other measures and report accordingly in conformity with Article 21.

3. A Party that is not in a position to undertake a comprehensive ban due to its constitution or constitutional principles shall apply restrictions on all tobacco advertising, promotion and sponsorship. This shall include, subject to the legal environment and technical means available to that Party, restrictions or a comprehensive ban on advertising, promotion and sponsorship originating from its territory.
territory with cross-border effects. In this respect, each Party shall undertake appropriate legislative, executive, administrative and/or other measures and report accordingly in conformity with Article 21.

4. As a minimum, and in accordance with its constitution or constitutional principles, each Party shall:

(a) prohibit all forms of tobacco advertising, promotion and sponsorship that promote a tobacco product by any means that are false, misleading or deceptive or likely to create an erroneous impression about its characteristics, health effects, hazards or emissions;
(b) require that health or other appropriate warnings or messages accompany all tobacco advertising and, as appropriate, promotion and sponsorship;
(c) restrict the use of direct or indirect incentives that encourage the purchase of tobacco products by the public;
(d) require, if it does not have a comprehensive ban, the disclosure to relevant governmental authorities of expenditures by the tobacco industry on advertising, promotion and sponsorship not yet prohibited. Those authorities may decide to make those figures available, subject to national law, to the public and to the Conference of the Parties, pursuant to Article 21;
(e) undertake a comprehensive ban or, in the case of a Party that is not in a position to undertake a comprehensive ban due to its constitution or constitutional principles, restrict tobacco advertising, promotion and sponsorship on radio, television, print media and, as appropriate, other media, such as the internet, within a period of five years; and
(f) prohibit, or in the case of a Party that is not in a position to prohibit due to its constitution or constitutional principles restrict, tobacco sponsorship of international events, activities and/or participants therein.

5. Parties are encouraged to implement measures beyond the obligations set out in paragraph 4.

6. Parties shall cooperate in the development of technologies and other means necessary to facilitate the elimination of cross-border advertising.

7. Parties which have a ban on certain forms of tobacco advertising, promotion and sponsorship have the sovereign right to ban those forms of cross-border tobacco advertising, promotion and sponsorship entering their territory and to impose equal penalties as those applicable to domestic advertising, promotion and sponsorship originating from their territory in accordance with their national law. This paragraph does not endorse or approve of any particular penalty.

8. Parties shall consider the elaboration of a protocol setting out appropriate measures that require international collaboration for a comprehensive ban on cross-border advertising, promotion and sponsorship.

.16 The registrant shall discuss the alignment of its marketing and labeling practices with Articles 11 and 13, regardless of whether it is selling products in countries party to the FCTC, and regardless of whether it is meeting its legal obligations (insofar as they are less strict than the FCTC Articles).

.17 The scope of disclosure shall apply to the registrant’s practices globally.

• If the registrant employs materially different practices in different markets, it should describe those differences.
Environmental & Social Impacts of Supply Chains

Description

Tobacco leaf and wood products used in cigarette filters are the main materials used by tobacco product manufacturers. A stable, low-cost supply of these materials is essential to the profitability of the industry, but there is mounting evidence that environmental and social factors affect the industry’s access to these key inputs. As most large tobacco manufacturers purchase tobacco leaves from tobacco leaf merchants, farmers, farmer co-ops, and wholesalers, managing environmental and social impacts within supply chain farms is critical to securing raw materials and reducing the risk of cost increases. Best practices in supply chain management include ensuring that tobacco is farmed in compliance with social and environmental best practices and audited according to a code of conduct.

Accounting Metrics

CN0302-05. Percentage of tobacco sourced from growers audited to U.S. Tobacco GAP Program guidelines or an equivalent code of conduct

.18 The registrant shall disclose the percentage of tobacco it sourced, in metric tons, from growers that were audited for compliance with the U.S. Tobacco GAP Program guidelines or an equivalent code of conduct, where:

- The percentage shall be calculated as the amount of tobacco, in metric tons, sourced from growers audited for compliance with the U.S. Tobacco GAP Program guidelines divided by total tobacco sourced.
- The amount of tobacco sourced shall be calculated as that which was purchased by the registrant during the fiscal year, adjusted for any changes in inventory of tobacco.
- A code of conduct is considered equivalent if, at a minimum, it has the same as agricultural, social, and environmental criteria as the U.S. Tobacco GAP Program guidelines, addressing the following the following activities:
  - Crop management
  - Environmental management
  - Labor management
  - Record keeping

.19 The scope includes all farmers who have contractual arrangements directly with the registrant, its affiliates, or with third-party leaf suppliers who buy tobacco for the registrant.

- Where applicable, the scope of disclosure additionally includes tobacco cultivated directly by the registrant.
CN0302-06. Suppliers’ social and environmental responsibility audit compliance: (1) priority non-conformance rate and associated corrective action rate, and (2) other non-conformance rate and associated corrective action rate

.20 The registrant shall disclose its tier 1 suppliers’ compliance with the social and environmental responsibility standards based on the number of non-conformances identified.

.21 Tier 1 suppliers are defined as those that transact directly with the registrant for goods and services directly related to manufacturing.

- The registrant may limit its disclosure to those suppliers that, in aggregate, account for greater than, or equal to, 80 percent of its supplier spending directly related to manufacturing.

.22 The registrant shall calculate and disclose the priority non-conformance rate as the total number of priority non-conformances identified in the supply chain divided by the number of facilities audited.

- Priority non-conformances are the highest severity of non-conformance and require escalation by auditors. Depending on the audit program, these non-conformances may also be referred to as “zero tolerance” issues or “core violations.”

- Priority non-conformances typically relate to: confirmed presence of underage child workers (below the legal age for work or apprenticeship), forced labor, health and safety issues that can cause immediate danger to life or serious injury, and environmental practices that can cause serious and immediate harm to the community. Issues representing an immediate danger must be corrected as soon as is practical and not longer than 30 days after discovery.

.23 The registrant shall calculate and disclose the other non-conformance rate as the total number of major and minor non-conformances identified in the supply chain divided by the number of facilities audited.

- A major non-conformance is seen as a significant failure in the management system—one that affects the ability of the system to produce the desired results. It may be caused by failure to implement an established process or procedure or establishing a process or procedure that is ineffective.

- A minor non-conformance by itself doesn’t indicate a systemic problem with the management system. It is typically an isolated or random incident.

.24 A corrective action is defined by the timely completion of a Corrective Action Plan (CAP), which describes how and when the facility will address each of the identified non-conformances, according to the timelines established by the audit program or the following:

- Priority non-conformance: submission of a CAP within one week of discovery and completion of a CAP within 30 days from discovery.

- Major non-conformance: submission of a CAP within two weeks of discovery and completion of a CAP within 90 days from discovery.
• Minor non-conformance: submission of a CAP within two weeks of discovery and completion of a CAP within 270 days from discovery.

.25 The registrant shall calculate and disclose its corrective action rate for priority non-conformances as the number of corrective action plans completed within the timeline established by the audit program (or 30 days) to address priority non-conformances divided by the total number of priority non-conformances that have been identified.

.26 The registrant shall calculate and disclose its corrective action rate for other non-conformances as the number of corrective action plans completed within the timeline established by the audit program (or 90 days) to address major non-conformances plus the number of corrective action plans completed within the timeline established by the audit program (or 270 days) to address minor non-conformances divided by the total number of major and minor non-conformances that have been identified.