ALTRIA GROUP, INC.
Form 10-Q
October 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
(Mark One)

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2012
OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to
Commission File Number 1-08940
Altria Group, Inc.
(Exact name of registrant as specified in its charter)

Virginia	13-3260245
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
6601 West Broad Street, Richmond, Virginia	23230
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (804) 274-2200
Former name, former address and former fiscal year, if changed since last report

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	þ	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No þ

At October 19, 2012, there were 2,025,106,086 shares outstanding of the registrant's common stock, par value $0.33 1/3 per share.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements.
Altria Group, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(in millions of dollars)
(Unaudited)

	September 30, 2012	December 31, 2011
Assets		
Consumer products		
Cash and cash equivalents	$2,186	$3,270
Receivables	196	268
Inventories:		
Leaf tobacco	752	934
Other raw materials	182	170
Work in process	261	316
Finished product	429	359
	1,624	1,779
Deferred income taxes	1,287	1,207
Other current assets	641	607
Total current assets	5,934	7,131
Property, plant and equipment, at cost	4,719	4,728
Less accumulated depreciation	2,608	2,512
	2,111	2,216
Goodwill	5,174	5,174
Other intangible assets, net	12,083	12,098
Investment in SABMiller	6,468	5,509
Other assets	419	1,257
Total consumer products assets	32,189	33,385
Financial services		
Finance assets, net	2,805	3,559
Other assets	44	18
Total financial services assets	2,849	3,577
Total Assets	$35,038	$36,962

See notes to condensed consolidated financial statements.
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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets (Continued)
(in millions of dollars, except share and per share data)
(Unaudited)

	September 30, 2012	December 31, 2011
Liabilities		
Consumer products		
Current portion of long-term debt	$—	$600
Accounts payable	289	503
Accrued liabilities:		
Marketing	526	430
Taxes, except income taxes	65	220
Employment costs	146	225
Settlement charges	3,236	3,513
Other	1,191	1,311
Dividends payable	895	841
Total current liabilities	6,348	7,643
Long-term debt	13,878	13,089
Deferred income taxes	5,095	4,751
Accrued pension costs	1,111	1,662
Accrued postretirement health care costs	2,364	2,359
Other liabilities	560	602
Total consumer products liabilities	29,356	30,106
Financial services		
Deferred income taxes	1,720	2,811
Other liabilities	61	330
Total financial services liabilities	1,781	3,141
Total liabilities	31,137	33,247
Contingencies (Note 11)		
Redeemable noncontrolling interest	33	32
Stockholders' Equity		
Common stock, par value $0.33 1/3 per share (2,805,961,317 shares issued)	935	935
Additional paid-in capital	5,670	5,674
Earnings reinvested in the business	24,098	23,583
Accumulated other comprehensive losses	(1,604)	(1,887)
Cost of repurchased stock (780,829,684 shares in 2012 and 761,542,032 shares in 2011)	(25,233)	(24,625)
Total stockholders’ equity attributable to Altria Group, Inc.	3,866	3,680
Noncontrolling interests	2	3
Total stockholders' equity	3,868	3,683
Total Liabilities and Stockholders' Equity	$35,038	$36,962

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Earnings
(in millions of dollars, except per share data)
(Unaudited)

	For the Nine Months Ended September 30, 2012	2011
Net revenues	$18,376	$17,671
Cost of sales	5,860	5,708
Excise taxes on products	5,336	5,398
Gross profit	7,180	6,565
Marketing, administration and research costs	1,678	1,853
Changes to Mondelēz and PMI tax-related receivables	(48)	(19)
Asset impairment and exit costs	47	3
Amortization of intangibles	15	16
Operating income	5,488	4,712
Interest and other debt expense, net	868	865
Loss on early extinguishment of debt	874	—
Earnings from equity investment in SABMiller	(973)	(552)
Earnings before income taxes	4,719	4,399
Provision for income taxes	1,641	1,843
Net earnings	3,078	2,556
Net earnings attributable to noncontrolling interests	(1)	(2)
Net earnings attributable to Altria Group, Inc.	$3,077	$2,554
Per share data:		
Basic earnings per share attributable to Altria Group, Inc.	$1.51	$1.23
Diluted earnings per share attributable to Altria Group, Inc.	$1.51	$1.23
Dividends declared	$1.26	$1.17

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Earnings
(in millions of dollars, except per share data)
(Unaudited)

	For the Three Months Ended September 30,	
	2012	2011
Net revenues	$6,242	$6,108
Cost of sales	1,982	1,883
Excise taxes on products	1,776	1,780
Gross profit	2,484	2,445
Marketing, administration and research costs	548	581
Changes to Mondelēz and PMI tax-related receivables	(48)	(19)
Asset impairment and exit costs	10	—
Amortization of intangibles	5	5
Operating income	1,969	1,878
Interest and other debt expense, net	282	293
Loss on early extinguishment of debt	874	—
Earnings from equity investment in SABMiller	(230)	(208)
Earnings before income taxes	1,043	1,793
Provision for income taxes	386	619
Net earnings	657	1,174
Net earnings attributable to noncontrolling interests	—	(1)
Net earnings attributable to Altria Group, Inc.	$657	$1,173
Per share data:		
Basic earnings per share attributable to Altria Group, Inc.	$0.32	$0.57
Diluted earnings per share attributable to Altria Group, Inc.	$0.32	$0.57
Dividends declared	$0.44	$0.41

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Earnings
(in millions of dollars)
(Unaudited)

	For the Nine Months Ended September 30,	
	2012	2011
Net earnings	$3,078	$2,556
Other comprehensive earnings, net of deferred income taxes:		
Currency translation adjustments	—	(1)
Benefit plans:		
Amounts reclassified to net earnings	98	100
SABMiller:		
Ownership share of SABMiller's other comprehensive earnings (losses) before reclassifications to net earnings	182	(81)
Amounts reclassified to net earnings	3	5
	185	(76)
Other comprehensive earnings, net of deferred income taxes	283	23
Comprehensive earnings	3,361	2,579
Comprehensive earnings attributable to noncontrolling interests	(1)	(2)
Comprehensive earnings attributable to Altria Group, Inc.	$3,360	$2,577

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Earnings
(in millions of dollars)
(Unaudited)

	For the Three Months Ended September 30,	
	2012	2011
Net earnings	$657	$1,174
Other comprehensive earnings, net of deferred income taxes:		
Currency translation adjustments	—	(2)
Benefit plans:		
Amounts reclassified to net earnings	37	36
SABMiller:		
Ownership share of SABMiller's other comprehensive earnings (losses) before reclassifications to net earnings	28	(216)
Amounts reclassified to net earnings	5	—
	33	(216)
Other comprehensive earnings (losses), net of deferred income taxes	70	(182)
Comprehensive earnings	727	992
Comprehensive earnings attributable to noncontrolling interests	—	(1)
Comprehensive earnings attributable to Altria Group, Inc.	$727	$991

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Stockholders' Equity
for the Year Ended December 31, 2011 and
the Nine Months Ended September 30, 2012
(in millions of dollars, except per share data)
(Unaudited)

	Attributable to Altria Group, Inc.						
	Common Stock	Additional Paid-in Capital	Earnings Reinvested in the Business	Accumulated Other Comprehensive Losses	Cost of Repurchased Stock	Non-controlling Interests	Total Stockholders' Equity
Balances, December 31, 2010	$935	$5,751	$23,459	$ (1,484)	$ (23,469)	$ 3	$ 5,195
Net earnings [1]	—	—	3,390	—	—	1	3,391
Other comprehensive losses, net of deferred income tax benefit	—	—	—	(403)	—	—	(403)
Exercise of stock options and other stock award activity	—	(77)	—	—	171	—	94
Cash dividends declared ($1.58 per share)	—	—	(3,266)	—	—	—	(3,266)
Repurchases of common stock	—	—	—	—	(1,327)	—	(1,327)
Other	—	—	—	—	—	(1)	(1)
Balances, December 31, 2011	935	5,674	23,583	(1,887)	(24,625)	3	3,683
Net earnings [1]	—	—	3,077	—	—	—	3,077
Other comprehensive earnings, net of deferred income taxes	—	—	—	283	—	—	283
Exercise of stock options and other stock award activity	—	(4)	—	—	14	—	10
Cash dividends declared ($1.26 per share)	—	—	(2,562)	—	—	—	(2,562)
Repurchases of common stock	—	—	—	—	(622)	—	(622)
Other	—	—	—	—	—	(1)	(1)
Balances, September 30, 2012	$935	$5,670	$24,098	$ (1,604)	$ (25,233)	$ 2	$ 3,868

(1) Net earnings attributable to noncontrolling interests for the nine months ended September 30, 2012 and for the year ended December 31, 2011 exclude $1 million and $2 million, respectively, due to the redeemable noncontrolling interest related to Stag's Leap Wine Cellars, which is reported in the mezzanine equity section in the condensed consolidated balance sheets at September 30, 2012 and December 31, 2011, respectively. See Note 11.

See notes to condensed consolidated financial statements.

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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(in millions of dollars)
(Unaudited)

	For the Nine Months Ended September 30,	
	2012	2011
Cash Provided by (Used In) Operating Activities		
Net earnings (loss) - Consumer products	$2,915	$3,076
- Financial services	163	(520)
Net earnings	3,078	2,556
Adjustments to reconcile net earnings to operating cash flows:		
Consumer products		
Depreciation and amortization	169	184
Deferred income tax provision	226	190
Earnings from equity investment in SABMiller	(973)	(552)
Dividends from SABMiller	299	264
Asset impairment and exit costs, net of cash paid	(59)	(28)
IRS payment related to LILO and SILO transactions	(456)	—
Loss on early extinguishment of debt	874	—
Cash effects of changes:		
Receivables, net	202	(9)
Inventories	155	178
Accounts payable	(38)	(106)
Income taxes	(559)	215
Accrued liabilities and other current assets	(196)	(208)
Accrued settlement charges	(277)	(394)
Pension plan contributions	(538)	(236)
Pension provisions and postretirement, net	134	182
Other	95	145
Financial services		
Deferred income tax benefit	(1,314)	(639)
PMCC leveraged lease charges	7	490
Decrease to allowance for losses	(10)	(35)
Other liabilities (income taxes)	1,384	373
Other	(83)	(6)
Net cash provided by operating activities	2,120	2,564

See notes to condensed consolidated financial statements.
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Altria Group, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Continued)
(in millions of dollars)
(Unaudited)

	For the Nine Months Ended September 30,			
	2012		2011	
Cash Provided by (Used In) Investing Activities				
Consumer products				
Capital expenditures	$(77	)	$(75	)
Other	(8	)	1	
Financial services				
Proceeds from finance assets	813		248	
Net cash provided by investing activities	728		174	
Cash Provided by (Used In) Financing Activities				
Consumer products				
Long-term debt issued	2,787		1,494	
Long-term debt repaid	(2,600	)	—	
Repurchases of common stock	(595	)	(1,000	)
Dividends paid on common stock	(2,508	)	(2,379	)
Issuances of common stock	—		29	
Financing fees and debt issuance costs	(22	)	(24	)
Tender premiums and fees related to early extinguishment of debt	(864	)	—	
Other	(130	)	(129	)
Net cash used in financing activities	(3,932	)	(2,009	)
Cash and cash equivalents:				
(Decrease) increase	(1,084	)	729	
Balance at beginning of period	3,270		2,314	
Balance at end of period	$2,186		$3,043	

See notes to condensed consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements
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Note 1. Background and Basis of Presentation:

Background

At September 30, 2012, Altria Group, Inc.'s direct and indirect wholly-owned subsidiaries included Philip Morris USA Inc. ("PM USA"), which is engaged in the manufacture and sale of cigarettes and certain smokeless products in the United States; John Middleton Co. ("Middleton"), which is engaged in the manufacture and sale of machine-made large cigars and pipe tobacco, and is a wholly-owned subsidiary of PM USA; and UST LLC ("UST"), which through its direct and indirect wholly-owned subsidiaries, including U.S. Smokeless Tobacco Company LLC ("USSTC") and Ste. Michelle Wine Estates Ltd. ("Ste. Michelle"), is engaged in the manufacture and sale of smokeless products and wine. Philip Morris Capital Corporation ("PMCC"), another wholly-owned subsidiary of Altria Group, Inc., maintains a portfolio of leveraged and direct finance leases. In addition, Altria Group, Inc. held an approximate 27.0% economic and voting interest in SABMiller plc ("SABMiller") at September 30, 2012, which is accounted for under the equity method of accounting. Altria Group, Inc.'s access to the operating cash flows of its wholly-owned subsidiaries consists of cash received from the payment of dividends and distributions, and the payment of interest on intercompany loans by its subsidiaries. In addition, Altria Group, Inc. receives cash dividends on its interest in SABMiller if and when SABMiller pays such dividends. At September 30, 2012, Altria Group, Inc.'s principal wholly-owned subsidiaries were not limited by long-term debt or other agreements in their ability to pay cash dividends or make other distributions with respect to their common stock.

Dividends and Share Repurchases

During the third quarter of 2012, Altria Group, Inc.'s Board of Directors approved a 7.3% increase in the quarterly dividend rate to $0.44 per common share versus the previous rate of $0.41 per common share. The current annualized dividend rate is $1.76 per Altria Group, Inc. common share. Future dividend payments remain subject to the discretion of Altria Group, Inc.'s Board of Directors.

In October 2011, Altria Group, Inc.'s Board of Directors authorized a $1.0 billion share repurchase program. During the nine and three months ended September 30, 2012, Altria Group, Inc. repurchased 19.6 million shares (aggregate cost of approximately $622 million, and $31.76 average price per share) and 7.7 million shares (aggregate cost of approximately $262 million, and $34.25 average price per share), respectively. As of September 30, 2012, Altria Group, Inc. had repurchased a total of 31.4 million shares of its common stock under this program at an aggregate cost of approximately $950 million, and an average price of $30.29 per share.

On October 23, 2012, Altria Group, Inc.'s Board of Directors authorized the expansion of the current share repurchase program from $1.0 billion to $1.5 billion. Upon such authorization, Altria Group, Inc. had approximately $550 million remaining in the expanded program, which Altria Group, Inc. expects to complete by June 30, 2013. The timing of share repurchases under this expanded program depends upon marketplace conditions and other factors, and the program remains subject to the discretion of Altria Group, Inc.'s Board of Directors.

Basis of Presentation

The interim condensed consolidated financial statements of Altria Group, Inc. are unaudited. It is the opinion of Altria Group, Inc.'s management that all adjustments necessary for a fair statement of the interim results presented have been reflected therein. All such adjustments were of a normal recurring nature. Net revenues and net earnings for any interim period are not necessarily indicative of results that may be expected for the entire year.

These statements should be read in conjunction with the consolidated financial statements and related notes, which appear in Altria Group, Inc.'s Annual Report to Shareholders and which are incorporated by reference into Altria Group, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011.

Balance sheet accounts are segregated by two broad types of businesses. Consumer products assets and liabilities are classified as either current or non-current, whereas financial services assets and liabilities are unclassified, in accordance with respective industry practices.

Altria Group, Inc.'s chief operating decision maker has been evaluating the operating results of the former cigarettes and

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cigars segments as a single smokeable products segment since January 1, 2012. The combination of these two formerly separate segments is related to the restructuring associated with the cost reduction program announced in October 2011 (the "2011 Cost Reduction Program"). Also, in connection with the 2011 Cost Reduction Program, effective January 1, 2012, Middleton became a wholly-owned subsidiary of PM USA, reflecting management's goal to achieve efficiencies in the management of these businesses. Effective with the first quarter of 2012, Altria Group, Inc.'s reportable segments are smokeable products, smokeless products, wine and financial services. For further discussion on the 2011 Cost Reduction Program, see Note 2. Asset Impairment, Exit, Implementation and Integration Costs.

Effective January 1, 2012, Altria Group, Inc. adopted new authoritative guidance that eliminated the option of presenting components of other comprehensive earnings as part of the statement of stockholders' equity. With the adoption of this guidance, Altria Group, Inc. is reporting other comprehensive earnings in separate statements immediately following the statements of earnings.

Note 2. Asset Impairment, Exit, Implementation and Integration Costs:

Pre-tax asset impairment, exit and implementation costs for the nine and three months ended September 30, 2012 consisted of the following:

	For the Nine Months Ended September 30, 2012			For the Three Months Ended September 30, 2012		
	Asset Impairment and Exit Costs	Implementation (Gain) Costs	Total	Asset Impairment and Exit Costs	Implementation Costs	Total
	(in millions)					
Smokeable products	$24	$(11)	$13	$1	$1	$2
Smokeless products	22	5	27	8	—	8
General corporate	1	(1)	—	1	—	1
Total	$47	$(7)	$40	$10	$1	$11

The asset impairment, exit and implementation costs shown in the table above are related to the 2011 Cost Reduction Program. The 2011 Cost Reduction Program and related costs are discussed further below.

For the nine months ended September 30, 2011, total pre-tax asset impairment and exit costs were $3 million, all of which were reported in the smokeable products segment. There were no asset impairment and exit costs incurred during the three months ended September 30, 2011. In addition, total pre-tax integration costs of $3 million and $1 million for the nine and three months ended September 30, 2011, respectively, were reported in the smokeless products segment. There were no implementation costs incurred during the nine months ended September 30, 2011. The movement in the severance liability and details of asset impairment and exit costs for Altria Group, Inc. for the nine months ended September 30, 2012 was as follows:

	Severance	Other	Total
	(in millions)		
Severance liability balance, December 31, 2011	$156	$—	$156

Charges	—	47	47
Cash spent	(88)	(18)	(106)
Other	—	(29)	(29)
Severance liability balance, September 30, 2012	$68	$—	$68

2011 Cost Reduction Program: In October 2011, Altria Group, Inc. announced a new cost reduction program for its tobacco and service company subsidiaries, reflecting Altria Group, Inc.'s objective to reduce cigarette-related infrastructure ahead of PM USA's cigarettes volume declines. As a result of this program, Altria Group, Inc. expects to incur total net pre-tax charges

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of approximately $300 million (concluding by the end of 2012). The estimated net charges include employee separation costs of approximately $220 million and other net charges of approximately $80 million. These other net charges include lease termination and asset impairments, partially offset by a curtailment gain related to amendments made to an Altria Group, Inc. postretirement benefit plan. Substantially all of these charges will result in cash expenditures.

Implementation (gain) costs of ($7) million shown in the table above were recorded on Altria Group, Inc.'s condensed consolidated statement of earnings for the nine months ended September 30, 2012, as follows: a net gain of $15 million, which included a $26 million curtailment gain related to amendments made to an Altria Group, Inc. postretirement benefit plan, was included in marketing, administration and research costs; and other costs of $8 million were included in cost of sales. For the three months ended September 30, 2012 implementation costs of $1 million shown in the table above were recorded in marketing, administration and research costs on Altria Group, Inc.'s condensed consolidated statement of earnings.

Total pre-tax charges, net, incurred since the inception of this program through September 30, 2012 were $264 million. Cash payments related to this program of $108 million and $35 million were made during nine and three months ended September 30, 2012, respectively, for total cash payments of $117 million since inception.

In connection with the 2011 Cost Reduction Program, Altria Group, Inc. reorganized two of its tobacco operating companies and revised its reportable segments (see Note 1. Background and Basis of Presentation and Note 7. Segment Reporting).

Note 3. Benefit Plans:

Subsidiaries of Altria Group, Inc. sponsor noncontributory defined benefit pension plans covering the majority of all employees of Altria Group, Inc. However, employees hired on or after a date specific to their employee group are not eligible to participate in these noncontributory defined benefit pension plans but are instead eligible to participate in a defined contribution plan with enhanced benefits. This transition for new hires occurred from October 1, 2006 to January 1, 2008. In addition, effective January 1, 2010, certain employees of UST and Middleton who were participants in noncontributory defined benefit pension plans ceased to earn additional benefit service under those plans and became eligible to participate in a defined contribution plan with enhanced benefits. Altria Group, Inc. and its subsidiaries also provide health care and other benefits to the majority of retired employees.

Pension Plans

Components of Net Periodic Benefit Cost

Net periodic pension cost consisted of the following:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Service cost	$59	$56	$19	$18
Interest cost	258	263	86	88

Expected return on plan assets	(331)	(317)	(110)	(106)
Amortization:				
Net loss	168	129	56	43
Prior service cost	8	10	3	3
Net periodic pension cost	$162	$141	$54	$46

Employer Contributions

Altria Group, Inc. makes contributions to the extent that they are tax deductible and pays benefits that relate to plans for salaried employees that cannot be funded under Internal Revenue Service ("IRS") regulations. On January 3, 2012, Altria Group, Inc. made a voluntary $500 million contribution to its pension plans. Additional employer contributions of $38

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million were made to Altria Group, Inc.'s pension plans during the nine months ended September 30, 2012. Currently, Altria Group, Inc. anticipates making additional employer contributions to its pension plans during the remainder of 2012 of up to approximately $20 million, based on current tax law. However, this estimate is subject to change as a result of changes in tax and other benefit laws, as well as asset performance significantly above or below the assumed long-term rate of return on pension assets, or changes in interest rates.

Postretirement Benefit Plans

Net postretirement health care costs consisted of the following:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Service cost	$16	$25	$5	$8
Interest cost	87	104	27	35
Amortization:				
Net loss	34	30	10	11
Prior service credit	(32)	(16)	(9)	(5)
Curtailment gain	(26)	—	—	—
Net postretirement health care costs	$79	$143	$33	$49

The curtailment gain included in the table above is related to the 2011 Cost Reduction Program. For further information on this program, see Note 2. Asset Impairment, Exit, Implementation and Integration Costs.

Note 4. Earnings from Equity Investment in SABMiller:
Pre-tax earnings from Altria Group, Inc.'s equity investment in SABMiller consisted of the following:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Equity earnings	$942	$534	$216	$201
Gains resulting from issuances of common stock by SABMiller	31	18	14	7
	$973	$552	$230	$208

Altria Group, Inc.'s equity earnings for the nine months ended September 30, 2012 included its share of non-cash gains resulting from SABMiller's strategic alliance transactions with Anadolu Efes and Castel.

Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 5. Earnings Per Share:
Basic and diluted earnings per share ("EPS") were calculated using the following:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Net earnings attributable to Altria Group, Inc.	$3,077	$2,554	$657	$1,173
Less: Distributed and undistributed earnings attributable to unvested restricted and deferred shares	(10)	(10)	(2)	(5)
Earnings for basic and diluted EPS	$3,067	$2,544	$655	$1,168
Weighted-average shares for basic and diluted EPS	2,028	2,071	2,024	2,054

As of February 29, 2012, there were no stock options outstanding. For the nine and three months ended September 30, 2012 and 2011 computations, there were no antidilutive stock options.

Note 6. Other Comprehensive Earnings/Losses:
The following table sets forth the changes in each component of accumulated other comprehensive losses, net of deferred income taxes, attributable to Altria Group, Inc.:

	Currency Translation Adjustments	Benefit Plans	SABMiller	Accumulated Other Comprehensive Losses
	(in millions)			
Balances, December 31, 2010	$4	$(1,811)	$323	$(1,484)
Period change	(2)	(251)	(150)	(403)
Balances, December 31, 2011	2	(2,062)	173	(1,887)
Period change	—	98	185	283
Balances, September 30, 2012	$2	$(1,964)	$358	$(1,604)

The following table sets forth deferred income tax expense (benefit) for the components of other comprehensive earnings (losses) for the nine and three months ended September 30, 2012 and 2011:

	Currency Translation Adjustments	Benefit Plans	SABMiller	Total
	(in millions)			
For the nine months ended September 30, 2012	$—	$64	$99	$163
For the nine months ended September 30, 2011	$—	$63	$(39)	$24
For the three months ended September 30, 2012	$—	$23	$18	$41
For the three months ended September 30, 2011	$—	$21	$(114)	$(93)

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Note 7. Segment Reporting:

The products of Altria Group, Inc.'s consumer products subsidiaries include smokeable products comprised of cigarettes manufactured and sold by PM USA, and machine-made large cigars and pipe tobacco manufactured and sold by Middleton; smokeless products manufactured and sold by or on behalf of USSTC and PM USA; and wine produced and/or distributed by Ste. Michelle. Another subsidiary of Altria Group, Inc., PMCC, maintains a portfolio of leveraged and direct finance leases. The products and services of these subsidiaries constitute Altria Group, Inc.'s reportable segments of smokeable products, smokeless products, wine and financial services.

As discussed in Note 1. Background and Basis of Presentation, beginning with the first quarter of 2012, Altria Group, Inc. revised its reportable segments. Prior-period segment data have been recast to conform with the current-period segment presentation.

Altria Group, Inc.'s chief operating decision maker reviews operating companies income to evaluate the performance of and allocate resources to the segments. Operating companies income for the segments excludes general corporate expenses and amortization of intangibles. Interest and other debt expense, net (consumer products), and provision for income taxes are centrally managed at the corporate level and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by Altria Group, Inc.'s chief operating decision maker.
Segment data were as follows:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Net revenues:				
Smokeable products	$16,616	$16,500	$5,613	$5,499
Smokeless products	1,243	1,209	437	426
Wine	381	349	140	132
Financial services	136	(387)	52	51
Net revenues	$18,376	$17,671	$6,242	$6,108
Earnings before income taxes:				
Operating companies income (loss):				
Smokeable products	$4,716	$4,527	$1,637	$1,575
Smokeless products	678	660	246	245
Wine	63	54	26	23
Financial services	166	(359)	79	83
Amortization of intangibles	(15)	(16)	(5)	(5)
General corporate expenses	(167)	(173)	(61)	(62)
Changes to Mondelēz and PMI tax-related receivables	48	19	48	19
Corporate asset impairment and exit costs	(1)	—	(1)	—
Operating income	5,488	4,712	1,969	1,878
Interest and other debt expense, net	(868)	(865)	(282)	(293)
Loss on early extinguishment of debt	(874)	—	(874)	—
Earnings from equity investment in SABMiller	973	552	230	208
Earnings before income taxes	$4,719	$4,399	$1,043	$1,793

Items affecting the comparability of net revenues and/or operating companies income (loss) for the segments were as follows:

PMCC Leveraged Lease Benefit/Charge - During the second quarter of 2012, Altria Group, Inc. recorded a one-time net earnings benefit of $68 million as a result of the execution of a closing agreement (the "Closing Agreement") with the

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IRS that conclusively resolved the federal income tax treatment for all prior and future tax years of certain leveraged lease transactions entered into by PMCC. Included in this net benefit was a pre-tax charge of $7 million that was recorded as a decrease to PMCC's net revenues and operating companies income. During the second quarter of 2011, Altria Group, Inc. recorded a charge of $627 million related to the federal income tax treatment of these transactions (the "2011 PMCC Leveraged Lease Charge"). Included in this charge was a pre-tax charge of $490 million that was recorded as a decrease to PMCC's net revenues and operating companies income. See Note 8. Finance Assets, net, Note 10. Income Taxes and Note 11. Contingencies for further discussion of this matter.

PMCC Recoveries and Allowance for Losses - During the third quarter of 2012, PMCC recorded pre-tax income of $33 million primarily related to recoveries from the sale of bankruptcy claims on, as well as the sale of aircraft under, its leases to American Airlines, Inc. ("American"). In addition, during the second quarter of 2012 and the third quarter of 2011, PMCC decreased its allowance for losses by $10 million and $35 million, respectively, which was recorded as income during each respective period. See Note 8. Finance Assets, net.

Tobacco and Health Judgments - For the nine and three months ended September 30, 2012 , Altria Group, Inc. recorded pre-tax charges of $4 million and $3 million, respectively, related to certain tobacco and health judgments. For the nine months ended September 30, 2011, Altria Group, Inc. recorded pre-tax charges of $36 million (excluding accrued interest of $5 million), related to certain tobacco and health judgments. These charges are reflected in the smokeable products segment. See Note 11. Contingencies.

Asset Impairment, Exit, Implementation and Integration Costs - See Note 2. Asset Impairment, Exit, Implementation and Integration Costs for a breakdown of these costs by segment.

Note 8. Finance Assets, net:

At September 30, 2012, finance assets, net, of $2,805 million were comprised of investments in finance leases of $2,889 million and an other receivable of $15 million, reduced by the allowance for losses of $99 million. At December 31, 2011, finance assets, net, of $3,559 million were comprised of investments in finance leases of $3,786 million, reduced by the allowance for losses of $227 million.

PMCC assesses the adequacy of its allowance for losses relative to the credit risk of its leasing portfolio on an ongoing basis. During the second quarter of 2012, PMCC determined that its allowance for losses exceeded the amount required based on management's assessment of the credit quality and size of PMCC's leasing portfolio. As a result, PMCC reduced its allowance for losses by $10 million, which was recorded as income during the nine months ended September 30, 2012. During the third quarter of 2011, PMCC determined that its allowance for losses exceeded the amount required based on management's assessment of the credit quality of the leasing portfolio at that time, including reductions in exposure to below investment grade lessees. As a result, PMCC reduced its allowance for losses by $35 million, which was recorded as income during the nine and three months ended September 30, 2011. PMCC believes that, as of September 30, 2012, the allowance for losses of $99 million is adequate. PMCC continues to monitor economic and credit conditions and the individual situations of its lessees and their respective industries, and may have to increase its allowance for losses if such conditions worsen.

The activity in the allowance for losses on finance assets for the nine months ended September 30, 2012, and 2011 was as follows:

	For the Nine Months Ended September 30,	
	2012	2011
	(in millions)	

Balance at beginning of the year	$227	$202
Decrease to allowance	(10)	(35)
Amounts written-off	(118)	—
Balance at September 30	$99	$167

PMCC had 28 aircraft on lease to American on November 29, 2011 when American filed for bankruptcy. As of the date of the bankruptcy filing, PMCC stopped recording income on its $140 million investment in finance leases from American. In the first quarter of 2012, American filed a motion to reject the leases for nine of the 28 aircraft under lease, which resulted in

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a $23 million write off of the related investment in finance lease balance against PMCC's allowance for losses. The debtholders subsequently foreclosed upon PMCC's interest in these nine aircraft. During the second quarter of 2012, as a result of the early termination of an additional American aircraft lease, PMCC wrote off $6 million against its allowance for losses. During the third quarter of 2012: (i) the bankruptcy court approved an agreement for American to purchase 10 aircraft, resulting in a $60 million write off against PMCC's allowance for losses; (ii) the bankruptcy court approved an agreement between PMCC and American to amend the eight remaining leases at reduced rent levels, resulting in a write off of $29 million against PMCC's allowance for losses; and (iii) PMCC sold the 10 aircraft, and bankruptcy claims related to these aircraft and to the eight remaining leases. As a result of the above activities, during the third quarter of 2012, deferred taxes of $22 million were accelerated and PMCC recorded $33 million of pre-tax income primarily related to recoveries from the sale of bankruptcy claims on, as well as the sale of aircraft under, its leases to American. The remaining investment in finance lease balance with American was $7 million at September 30, 2012.

All PMCC lessees, including American under its restructured leases, were current on their lease payment obligations as of September 30, 2012.
The credit quality of PMCC’s investments in finance assets as assigned by Standard & Poor’s Ratings Services ("Standard & Poor’s") and Moody’s Investors Service, Inc. ("Moody’s") at September 30, 2012 and December 31, 2011 was as follows:

	September 30, 2012	December 31, 2011
	(in millions)	
Credit Rating by Standard & Poor’s/Moody’s:		
“AAA/Aaa” to “A-/A3”	$1,137	$1,570
“BBB+/Baa1” to “BBB-/Baa3”	978	1,080
“BB+/Ba1” and Lower	789	1,136
Total	$2,904	$3,786

During the second quarter of 2012, Altria Group, Inc. entered into the Closing Agreement with the IRS that conclusively resolved the federal income tax treatment for all prior and future tax years of certain leveraged lease transactions entered into by PMCC. As a result of the Closing Agreement, Altria Group, Inc. recorded a one-time net earnings benefit of $68 million during the second quarter of 2012 due primarily to lower than estimated interest on tax underpayments.

During the second quarter of 2011, Altria Group, Inc. recorded the 2011 PMCC Leveraged Lease Charge. Approximately 50% of the charge ($315 million) represented a reduction in cumulative lease earnings recorded to date that will be recaptured over the remainder of the terms of the affected leases. The remaining portion of the charge ($312 million) primarily represented a permanent charge for interest on tax underpayments.

For the nine months ended, September 30, 2012 and 2011, the benefit/charge associated with PMCC's leveraged lease transactions was recorded in Altria Group, Inc.'s condensed consolidated statements of earnings as follows:

	For the Nine Months Ended September 30, 2012			For the Nine Months Ended September 30, 2011		
	Net Revenues	Benefit for Income Taxes	Total	Net Revenues	(Benefit) Provision for Income Taxes	Total

(in millions)						
Reduction to cumulative lease earnings	$7	$(2)	$5	$490	$(175)	$315
Interest on tax underpayments	—	(73)	(73)	—	312	312
Total	$7	$(75)	$(68)	$490	$137	$627

See Note 10. Income Taxes and Note 11. Contingencies for a further discussion of the Closing Agreement and the PMCC leveraged lease benefit/charge.

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Note 9. Debt:

At September 30, 2012 and December 31, 2011, Altria Group, Inc. had no short-term borrowings.

Long-term Debt

On August 9, 2012, Altria Group, Inc. issued $1.9 billion aggregate principal amount of 2.850% senior unsecured long-term notes due 2022 and $0.9 billion aggregate principal amount of 4.250% senior unsecured long-term notes due 2042. Interest on these notes is payable semi-annually. The net proceeds from the issuances of these senior unsecured notes were added to Altria Group, Inc.'s general funds and were used to repurchase certain of its senior unsecured notes in connection with the tender offer described below, and other general corporate purposes.

The notes are Altria Group, Inc.'s senior unsecured obligations and rank equally in right of payment with all of Altria Group, Inc.'s existing and future senior unsecured indebtedness. Upon the occurrence of both (i) a change of control of Altria Group, Inc. and (ii) the notes ceasing to be rated investment grade by each of Moody's, Standard & Poor's and Fitch Ratings Ltd. within a specified time period, Altria Group, Inc. will be required to make an offer to purchase the notes at a price equal to 101% of the aggregate principal amount of such notes, plus accrued and unpaid interest to the date of repurchase as and to the extent set forth in the terms of the notes.

The obligations of Altria Group, Inc. under the notes are guaranteed by PM USA (see Note 12. Condensed Consolidating Financial Information).

In July 2012, senior unsecured notes issued by UST in the aggregate principal amount of $600 million matured and were repaid in full.

Altria Group, Inc.'s estimate of the fair value of its debt is based on observable market information derived from a third party pricing source and is classified in level 2 of the fair value hierarchy. The aggregate fair value of Altria Group, Inc.'s total long-term debt at September 30, 2012 and December 31, 2011, was $18.0 billion and $17.7 billion, respectively, as compared with its carrying value of $13.9 billion and $13.7 billion, respectively for each period.

Tender Offer for Altria Group, Inc. Notes

During the third quarter of 2012, Altria Group, Inc. completed a tender offer to purchase for cash $2.0 billion aggregate principal amount of certain of its senior unsecured notes. Altria Group, Inc. repurchased $1,151 million aggregate principal amount of its 9.700% notes due 2018, and $849 million aggregate principal amount of its 9.250% notes due 2019. As a result of the tender offer, during the third quarter of 2012, Altria Group, Inc. recorded a pre-tax loss on early extinguishment of debt of $874 million, which included debt tender premiums and fees of $864 million, and the write off of related unamortized debt discounts and debt issuance costs of $10 million.

Note 10. Income Taxes:

The income tax rate of 34.8% for the nine months ended September 30, 2012 decreased 7.1 percentage points from 41.9% for the nine months ended September 30, 2011. The decrease in the income tax rate was due primarily to a $312 million charge that primarily represents interest on tax underpayments associated with the 2011 PMCC Leveraged Lease Charge that was recorded during the second quarter of 2011, and a $73 million interest benefit, recorded during the second quarter of 2012, resulting primarily from lower than estimated interest on tax underpayments related to the Closing Agreement with the IRS. The effect of these items on the nine-month income tax rate was partially offset by a reduction in certain consolidated tax benefits resulting from the third quarter of 2012 debt tender offer (see Note 9. Debt). The income tax rate of 37.0% for the three months ended September 30, 2012 increased 2.5 percentage points from 34.5% for the three months ended September 30, 2011 due primarily to the reduction in certain consolidated tax benefits resulting from the third quarter of 2012 debt tender offer. In addition, the income tax rate comparisons for the nine and three months were further impacted by: (i) the reversal of tax reserves and associated interest of $53 million due primarily to the closure in August 2012 of the IRS audit of Altria Group, Inc. and its consolidated subsidiaries' 2004 - 2006 tax years ("IRS 2004 - 2006 Audit"); (ii) the resolution of various Kraft Foods Inc., now known as Mondelēz International, Inc. ("Mondelēz"), and Philip Morris International Inc. ("PMI") tax matters in the third quarters of 2012 and 2011 as discussed further below; and (iii) the reversal of tax accruals no longer required and the expiration of statutes of limitations of $24 million during the third quarter of 2011.

As a result of the Closing Agreement, during the second quarter of 2012, Altria Group, Inc. paid $456 million in federal income taxes and related estimated interest on tax underpayments. Altria Group, Inc. also expects to pay approximately $50 million in state taxes and related estimated interest. The tax component of these payments represents an acceleration of federal and state income taxes that Altria Group, Inc. would have otherwise paid over the lease terms of these transactions. See Note 8. Finance Assets, net and Note 11. Contingencies for further discussion of the Closing Agreement and the PMCC leveraged lease benefit/charge.

Under tax sharing agreements entered into in connection with the 2007 and 2008 spin-offs between Altria Group, Inc. and its former subsidiaries Mondelēz and PMI, respectively, Mondelēz and PMI are responsible for their respective pre-spin-off tax obligations. Altria Group, Inc., however, remains severally liable for Mondelēz's and PMI's pre-spin-off federal tax obligations pursuant to regulations governing federal consolidated income tax returns, and continues to include the pre-spin-off federal income tax reserves of Mondelēz and PMI in its liability for uncertain tax positions. Altria Group, Inc. also includes corresponding receivables from Mondelēz and PMI in its assets. An additional third quarter of 2012 tax provision of $48 million for Mondelēz and PMI tax matters, resulting from the closure of the IRS 2004 - 2006 Audit, was offset by an increase to the corresponding receivables from Mondelēz and PMI, which was recorded as an increase to operating income on Altria Group, Inc.'s condensed consolidated statements of earnings for the nine and three months ended September 30, 2012. An additional third quarter of 2011 tax provision of $19 million related to various Mondelēz tax matters was offset by an increase to the corresponding receivable from Mondelēz, which was recorded as an increase to operating income on Altria Group, Inc.'s condensed consolidated statements of earnings for the nine and three months ended September 30, 2011. As a result, the Mondelēz and PMI tax matters discussed above had no impact on Altria Group, Inc.'s net earnings for the nine and three months ended September 30, 2012 and 2011.

Altria Group, Inc. is subject to income taxation in many jurisdictions. Uncertain tax positions reflect the difference between tax positions taken or expected to be taken on income tax returns and the amounts recognized in the financial statements. Resolution of the related tax positions with the relevant tax authorities may take many years to complete, since such timing is not entirely within the control of Altria Group, Inc. It is reasonably possible that within the next 12 months certain tax examinations will be resolved, which could result in a decrease in unrecognized tax benefits of approximately $90 million, the majority of which would relate to the unrecognized tax benefits of Mondelēz and PMI, for which Altria Group, Inc. is indemnified.

Note 11. Contingencies:

Legal proceedings covering a wide range of matters are pending or threatened in various United States and foreign jurisdictions against Altria Group, Inc. and its subsidiaries, including PM USA and UST and its subsidiaries, as well as their respective indemnitees. Various types of claims may be raised in these proceedings, including product liability, consumer protection, antitrust, tax, contraband shipments, patent infringement, employment matters, claims for contribution and claims of distributors.

Litigation is subject to uncertainty and it is possible that there could be adverse developments in pending or future cases. An unfavorable outcome or settlement of pending tobacco-related or other litigation could encourage the commencement of additional litigation. Damages claimed in some tobacco-related and other litigation are or can be significant and, in certain cases, range in the billions of dollars. The variability in pleadings in multiple jurisdictions, together with the actual experience of management in litigating claims, demonstrate that the monetary relief that may be specified in a lawsuit bears little relevance to the ultimate outcome. In certain cases, plaintiffs claim that defendants' liability is joint and several. In such cases, Altria Group, Inc. or its subsidiaries may face the risk that one or more co-defendants decline or otherwise fail to participate in the bonding required for an appeal or to pay their proportionate or jury-allocated share of a judgment. As a result, Altria Group, Inc. or its subsidiaries under certain circumstances may have to pay more than their proportionate share of any bonding- or judgment-related amounts.

Although PM USA has historically been able to obtain required bonds or relief from bonding requirements in order to prevent plaintiffs from seeking to collect judgments while adverse verdicts have been appealed, there remains a risk that such relief may not be obtainable in all cases. This risk has been substantially reduced given that 44 states and Puerto Rico now limit the dollar amount of bonds or require no bond at all. As discussed below, however, tobacco litigation plaintiffs

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have challenged the constitutionality of Florida's bond cap statute in several cases and plaintiffs may challenge state bond cap statutes in other jurisdictions as well. Such challenges may include the applicability of state bond caps in federal court. Although we cannot predict the outcome of such challenges, it is possible that the consolidated results of operations, cash flows or financial position of Altria Group, Inc., or one or more of its subsidiaries, could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome of one or more such challenges.

Altria Group, Inc. and its subsidiaries record provisions in the condensed consolidated financial statements for pending litigation when they determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, while it is reasonably possible that an unfavorable outcome in a case may occur, except as discussed elsewhere in this Note 11. Contingencies: (i) management has concluded that it is not probable that a loss has been incurred in any of the pending tobacco-related cases; (ii) management is unable to estimate the possible loss or range of loss that could result from an unfavorable outcome in any of the pending tobacco-related cases; and (iii) accordingly, management has not provided any amounts in the condensed consolidated financial statements for unfavorable outcomes, if any. Legal defense costs are expensed as incurred.

Altria Group, Inc. and its subsidiaries have achieved substantial success in managing litigation. Nevertheless, litigation is subject to uncertainty and significant challenges remain. It is possible that the consolidated results of operations, cash flows or financial position of Altria Group, Inc., or one or more of its subsidiaries, could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Altria Group, Inc. and each of its subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that it has valid defenses to the litigation pending against it, as well as valid bases for appeal of adverse verdicts. Each of the companies has defended, and will continue to defend, vigorously against litigation challenges. However, Altria Group, Inc. and its subsidiaries may enter into settlement discussions in particular cases if they believe it is in the best interests of Altria Group, Inc. to do so.

Overview of Altria Group, Inc. and/or PM USA Tobacco-Related Litigation
Types and Number of Cases
Claims related to tobacco products generally fall within the following categories: (i) smoking and health cases alleging personal injury brought on behalf of individual plaintiffs; (ii) smoking and health cases primarily alleging personal injury or seeking court-supervised programs for ongoing medical monitoring and purporting to be brought on behalf of a class of individual plaintiffs, including cases in which the aggregated claims of a number of individual plaintiffs are to be tried in a single proceeding; (iii) health care cost recovery cases brought by governmental (both domestic and foreign) plaintiffs seeking reimbursement for health care expenditures allegedly caused by cigarette smoking and/or disgorgement of profits; (iv) class action suits alleging that the uses of the terms "Lights" and "Ultra Lights" constitute deceptive and unfair trade practices, common law fraud or violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"); and (v) other tobacco-related litigation described below. Plaintiffs' theories of recovery and the defenses raised in pending smoking and health, health care cost recovery and "Lights/Ultra Lights" cases are discussed below.
The table below lists the number of certain tobacco-related cases pending in the United States against PM USA and, in some instances, Altria Group, Inc. as of October 25, 2012, October 24, 2011 and October 25, 2010.

Type of Case	Number of Cases Pending as of October 25, 2012	Number of Cases Pending as of October 24, 2011	Number of Cases Pending as of October 25, 2010
Individual Smoking and Health Cases [1]	77	79	85

Smoking and Health Class Actions and Aggregated Claims Litigation [2]	7	7	9
Health Care Cost Recovery Actions	1	2	3
"Lights/Ultra Lights" Class Actions	14	18	29
Tobacco Price Cases	1	1	1

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(1) Does not include 2,574 cases brought by flight attendants seeking compensatory damages for personal injuries allegedly caused by exposure to environmental tobacco smoke ("ETS"). The flight attendants allege that they are members of an ETS smoking and health class action in Florida, which was settled in 1997 (Broin). The terms of the court-approved settlement in that case allow class members to file individual lawsuits seeking compensatory damages, but prohibit them from seeking punitive damages. Also, does not include individual smoking and health cases brought by or on behalf of plaintiffs in Florida state and federal courts following the decertification of the Engle case (discussed below in Smoking and Health Litigation - Engle Class Action).

(2) Includes as one case the 600 civil actions (of which 346 are actions against PM USA) that are to be tried in a single proceeding in West Virginia (In re: Tobacco Litigation). The West Virginia Supreme Court of Appeals has ruled that the United States Constitution does not preclude a trial in two phases in this case. Under the current trial plan, issues related to defendants' conduct and whether punitive damages are permissible will be tried in the first phase. The second phase would consist of individual trials to determine liability, if any, as well as compensatory and punitive damages, if any. Trial in the case began in October 2011, but ended in a mistrial in November 2011. The court has scheduled trial for April 15, 2013.

International Tobacco-Related Cases

As of October 25, 2012, PM USA is a named defendant in Israel in one "Lights" class action. PM USA is a named defendant in eight health care cost recovery actions in Canada, six of which also name Altria Group, Inc. as a defendant. PM USA and Altria Group, Inc. are also named defendants in six smoking and health class actions filed in various Canadian provinces. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement between Altria Group, Inc. and PMI that provides for indemnities for certain liabilities concerning tobacco products.

Pending and Upcoming Tobacco-Related Trials

As of October 25, 2012, one Engle progeny case and one individual smoking and health case against PM USA are set for trial for the remainder of 2012. Cases against other companies in the tobacco industry are also scheduled for trial in 2012. Trial dates are subject to change.

Trial Results

Since January 1999, excluding the Engle progeny cases (separately discussed below), verdicts have been returned in 51 smoking and health, "Lights/Ultra Lights" and health care cost recovery cases in which PM USA was a defendant. Verdicts in favor of PM USA and other defendants were returned in 34 of the 51 cases. These 34 cases were tried in Alaska (1), California (5), Florida (9), Louisiana (1), Massachusetts (1), Mississippi (1), Missouri (3), New Hampshire (1), New Jersey (1), New York (4), Ohio (2), Pennsylvania (1), Rhode Island (1), Tennessee (2), and West Virginia (1). A motion for a new trial was granted in one of the cases in Florida.

Of the 17 non-Engle progeny cases in which verdicts were returned in favor of plaintiffs, 15 have reached final resolution. A verdict against defendants in one health care cost recovery case (Blue Cross/Blue Shield) was reversed and all claims were dismissed with prejudice. In addition, a verdict against defendants in a purported "Lights" class action in Illinois (Price) was reversed and the case was dismissed with prejudice in December 2006. In December 2008, the plaintiff in Price filed a motion with the state trial court to vacate the judgment dismissing this case in light of the United States Supreme Court's decision in Good (see below for a discussion of developments in Good and Price).

As of October 25, 2012, 33 Engle progeny cases involving PM USA have resulted in verdicts since the Florida Supreme Court's Engle decision. Sixteen verdicts were returned in favor of plaintiffs and 17 verdicts were returned in favor of PM USA. See Smoking and Health Litigation - Engle Progeny Trial Results below for a discussion of these verdicts.

After exhausting all appeals in those cases resulting in adverse verdicts (Engle progeny and non-Engle progeny), PM USA has paid judgments (and related costs and fees) totaling approximately $242 million and interest totaling approximately $139 million as of October 25, 2012.

Security for Judgments

To obtain stays of judgments pending current appeals, as of September 30, 2012, PM USA has posted various forms of security totaling approximately $37 million, the majority of which has been collateralized with cash deposits that are included in other assets on the condensed consolidated balance sheets.

Smoking and Health Litigation

Overview

Plaintiffs' allegations of liability in smoking and health cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, nuisance, breach of express and implied warranties, breach of special duty, conspiracy, concert of action, violations of deceptive trade practice laws and consumer protection statutes, and claims under the federal and state anti-racketeering statutes. Plaintiffs in the smoking and health actions seek various forms of relief, including compensatory and punitive damages, treble/multiple damages and other statutory damages and penalties, creation of medical monitoring and smoking cessation funds, disgorgement of profits, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, assumption of the risk, comparative fault and/or contributory negligence, statutes of limitations and preemption by the Federal Cigarette Labeling and Advertising Act.

Non-Engle Progeny Trial Results

Summarized below are the non-Engle progeny smoking and health cases that were pending during 2012 in which verdicts were returned in favor of plaintiffs. A chart listing the verdicts for plaintiffs in the Engle progeny cases can be found in Smoking and Health Litigation - Engle Progeny Trial Results below.

D. Boeken: In August 2011, a California jury returned a verdict in favor of plaintiff, awarding $12.8 million in compensatory damages against PM USA. PM USA's motions for judgment notwithstanding the verdict and for a new trial were denied in October 2011. PM USA appealed and posted a bond in the amount of $12.8 million in November 2011.

Bullock: This litigation has concluded. In the fourth quarter of 2011, PM USA recorded a pre-tax provision of $14 million related to damages and costs and $3 million related to interest and in March 2012, paid an amount of approximately $19.1 million in satisfaction of the judgment and associated costs and interest.

Schwarz: In March 2002, an Oregon jury awarded against PM USA $168,500 in compensatory damages and $150 million in punitive damages. In May 2002, the trial court reduced the punitive damages award to $100 million. In May 2006, the Oregon Court of Appeals affirmed the compensatory damages verdict, reversed the award of punitive damages and remanded the case to the trial court for a second trial to determine the amount of punitive damages, if any. In June 2006, plaintiff petitioned the Oregon Supreme Court to review the portion of the court of appeals' decision reversing and remanding the case for a new trial on punitive damages. In June 2010, the Oregon Supreme Court affirmed the court of appeals' decision and remanded the case to the trial court for a new trial limited to the question of punitive damages. In December 2010, the Oregon Supreme Court reaffirmed its earlier ruling and awarded PM USA approximately $500,000 in costs. In March 2011, PM USA filed a claim against the plaintiff for its costs and disbursements on appeal, plus interest. Trial on the amount of punitive damages began in January 2012. In February 2012, the jury awarded plaintiff $25 million in punitive damages. In March 2012, PM USA filed motions to set aside the verdict, for a new trial or, in the alternative, for a remittitur. The trial court denied these motions in May 2012. On September 4, 2012, PM USA filed a notice of appeal from the trial court's judgment with the Oregon Court of Appeals.

Williams: This litigation has concluded. In the fourth quarter of 2011, PM USA recorded a provision of approximately $48 million related to damages and costs and $54 million related to interest and in January 2012 paid an amount of approximately $102 million in satisfaction of the judgment and associated costs and interest.

See Scott Class Action below for a discussion of the verdict and post-trial developments in the Scott class action and Federal Government Lawsuit below for a discussion of the verdict and post-trial developments in the United States of America healthcare cost recovery case.

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Engle Class Action

In July 2000, in the second phase of the Engle smoking and health class action in Florida, a jury returned a verdict assessing punitive damages totaling approximately $145 billion against various defendants, including $74 billion against PM USA. Following entry of judgment, PM USA appealed.

In May 2001, the trial court approved a stipulation providing that execution of the punitive damages component of the Engle judgment will remain stayed against PM USA and the other participating defendants through the completion of all judicial review. As a result of the stipulation, PM USA placed $500 million into an interest-bearing escrow account that, regardless of the outcome of the judicial review, was to be paid to the court and the court was to determine how to allocate or distribute it consistent with Florida Rules of Civil Procedure. In May 2003, the Florida Third District Court of Appeal reversed the judgment entered by the trial court and instructed the trial court to order the decertification of the class. Plaintiffs petitioned the Florida Supreme Court for further review.

In July 2006, the Florida Supreme Court ordered that the punitive damages award be vacated, that the class approved by the trial court be decertified, and that members of the decertified class could file individual actions against defendants within one year of issuance of the mandate. The court further declared the following Phase I findings are entitled to res judicata effect in such individual actions brought within one year of the issuance of the mandate: (i) that smoking causes various diseases; (ii) that nicotine in cigarettes is addictive; (iii) that defendants' cigarettes were defective and unreasonably dangerous; (iv) that defendants concealed or omitted material information not otherwise known or available knowing that the material was false or misleading or failed to disclose a material fact concerning the health effects or addictive nature of smoking; (v) that defendants agreed to misrepresent information regarding the health effects or addictive nature of cigarettes with the intention of causing the public to rely on this information to their detriment; (vi) that defendants agreed to conceal or omit information regarding the health effects of cigarettes or their addictive nature with the intention that smokers would rely on the information to their detriment; (vii) that all defendants sold or supplied cigarettes that were defective; and (viii) that defendants were negligent. The court also reinstated compensatory damages awards totaling approximately $6.9 million to two individual plaintiffs and found that a third plaintiff's claim was barred by the statute of limitations. In February 2008, PM USA paid approximately $3 million, representing its share of compensatory damages and interest, to the two individual plaintiffs identified in the Florida Supreme Court's order.

In August 2006, PM USA sought rehearing from the Florida Supreme Court on parts of its July 2006 opinion, including the ruling (described above) that certain jury findings have res judicata effect in subsequent individual trials timely brought by Engle class members. The rehearing motion also asked, among other things, that legal errors that were raised but not expressly ruled upon in the Third District Court of Appeal or in the Florida Supreme Court now be addressed. Plaintiffs also filed a motion for rehearing in August 2006 seeking clarification of the applicability of the statute of limitations to non-members of the decertified class. In December 2006, the Florida Supreme Court refused to revise its July 2006 ruling, except that it revised the set of Phase I findings entitled to res judicata effect by excluding finding (v) listed above (relating to agreement to misrepresent information), and added the finding that defendants sold or supplied cigarettes that, at the time of sale or supply, did not conform to the representations of fact made by defendants. In January 2007, the Florida Supreme Court issued the mandate from its revised opinion. Defendants then filed a motion with the Florida Third District Court of Appeal requesting that the court address legal errors that were previously raised by defendants but have not yet been addressed either by the Third District Court of Appeal or by the Florida Supreme Court. In February 2007, the Third District Court of Appeal denied defendants' motion. In May 2007, defendants' motion for a partial stay of the mandate pending the completion of appellate review was denied by the Third District Court of Appeal. In May 2007, defendants filed a petition for writ of certiorari with the United States Supreme Court. In October 2007, the United States Supreme Court denied defendants' petition. In November 2007, the United States Supreme Court denied defendants' petition for rehearing from the denial of their petition for writ of certiorari.

In February 2008, the trial court decertified the class except for purposes of the May 2001 bond stipulation, and formally vacated the punitive damages award pursuant to the Florida Supreme Court's mandate. In April 2008, the trial court ruled that certain defendants, including PM USA, lacked standing with respect to allocation of the funds escrowed under the May 2001 bond stipulation and will receive no credit at this time from the $500 million paid by PM USA against any future punitive damages awards in cases brought by former Engle class members.

In May 2008, the trial court, among other things, decertified the limited class maintained for purposes of the May 2001 bond stipulation and, in July 2008, severed the remaining plaintiffs' claims except for those of Howard Engle. The only remaining plaintiff in the Engle case, Howard Engle, voluntarily dismissed his claims with prejudice.

The deadline for filing Engle progeny cases, as required by the Florida Supreme Court's decision, expired in January 2008. As of October 25, 2012, approximately 3,300 state court cases were pending against PM USA or Altria Group, Inc. asserting individual claims by or on behalf of approximately 4,400 state court plaintiffs. Furthermore, as of October 25, 2012, approximately 2,000 federal court cases were pending against PM USA or Altria Group, Inc asserting individual claims by or on behalf of a similar number of federal court plaintiffs. Because of a number of factors including but not limited to docketing delays, duplicated filings, and overlapping dismissal orders, these numbers are estimates.

Federal Engle Progeny Cases

Three federal district courts (in the Merlob, B. Brown and Burr cases) ruled in 2008 that the findings in the first phase of the Engle proceedings cannot be used to satisfy elements of plaintiffs' claims, and two of those rulings (B. Brown and Burr) were certified by the trial court for interlocutory review. The certification in both cases was granted by the United States Court of Appeals for the Eleventh Circuit and the appeals were consolidated. In February 2009, the appeal in Burr was dismissed for lack of prosecution and, on September 28, 2012, the district court dismissed the case on statute of limitations grounds. In July 2010, the Eleventh Circuit ruled in B. Brown that, as a matter of Florida law, plaintiffs do not have an unlimited right to use the findings from the original Engle trial to meet their burden of establishing the elements of their claims at trial. The Eleventh Circuit did not reach the issue of whether the use of the Engle findings violates the defendants' due process rights. Rather, plaintiffs may only use the findings to establish those specific facts, if any, that they demonstrate with a reasonable degree of certainty were actually decided by the original Engle jury. The Eleventh Circuit remanded the case to the district court to determine what specific factual findings the Engle jury actually made.

After the remand of B. Brown, the Eleventh Circuit's ruling on Florida state law was superseded by state appellate rulings (discussed below), which include Martin, an Engle progeny case against R.J. Reynolds Tobacco Company ("R.J. Reynolds") in Escambia County, and J. Brown, an Engle progeny case against R.J. Reynolds in Broward County. Martin and J. Brown are discussed in more detail in Appeals of Engle Progeny Verdicts below.

Following Martin and J. Brown, in the Waggoner case, the United States District Court for the Middle District of Florida (Jacksonville) ruled in December 2011 that application of the Engle findings to establish the wrongful conduct elements of plaintiffs' claims consistent with Martin or J. Brown did not violate defendants' due process rights. The court ruled, however, that plaintiffs must establish legal causation to establish liability. PM USA and the other defendants sought appellate review of the due process ruling. In February 2012, the district court denied the motion for interlocutory appeal, but did apply the ruling to all active pending federal Engle progeny cases. As a result, the ruling can be appealed after an adverse verdict or in a cross-appeal. The ruling has been appealed by R.J. Reynolds in the Walker and Duke cases pending before the Eleventh Circuit.

On August 1, 2012, in PM USA's third federal case to go to trial (Denton), the jury returned a defense verdict.

Engle progeny cases pending against PM USA or Altria Group, Inc. in the federal district courts in the Middle District of Florida asserting individual claims by or on behalf of approximately 2,000 plaintiffs remain stayed. There are currently 19 active cases pending in federal court.

Florida Bond Cap Statute

In June 2009, Florida amended its existing bond cap statute by adding a $200 million bond cap that applies to all state Engle progeny lawsuits in the aggregate and establishes individual bond caps for individual Engle progeny cases in amounts that vary depending on the number of judgments in effect at a given time. Plaintiffs in three Engle progeny cases against R.J. Reynolds in Alachua County, Florida (Alexander, Townsend and Hall) and one case in Escambia County (Clay) challenged the constitutionality of the bond cap statute. The Florida Attorney General intervened in these cases in defense of the constitutionality of the statute.

Trial court rulings were rendered in Clay, Alexander, Townsend and Hall rejecting the plaintiffs' bond cap statute challenges in those cases. The plaintiffs unsuccessfully appealed these rulings. In Alexander, Clay and Hall, the District Court of Appeal for the First District of Florida affirmed the trial court decisions and certified the decision in Hall for appeal to the Florida Supreme Court, but declined to certify the question of the constitutionality of the bond cap statute in Clay and

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Alexander. The Florida Supreme Court granted review of the Hall decision, but, on September 4, 2012, the court dismissed the appeal as moot. On October 12, 2012, the Florida Supreme Court denied the plaintiffs' rehearing petition.

No federal court has yet to address the constitutionality of the bond cap statute or the applicability of the bond cap to Engle progeny cases tried in federal court.

Engle Progeny Trial Results

As of October 25, 2012, 33 federal and state Engle progeny cases involving PM USA have resulted in verdicts since the Florida Supreme Court Engle decision. Sixteen verdicts were returned in favor of plaintiffs. For a further discussion of these cases, see the verdict chart below.

Seventeen verdicts were returned in favor of PM USA (Gelep, Kalyvas, Gil de Rubio, Warrick, Willis, Russo (formerly Frazier), C. Campbell, Rohr, Espinosa, Oliva, Weingart, Junious, Szymanski, Gollihue, McCray, Denton and Hancock). While the juries in the Weingart and Hancock cases returned verdicts against PM USA awarding no damages, the trial court in each case granted an additur. In the Russo case (formerly Frazier), the Florida Third District Court of Appeal reversed the judgment in defendants' favor in April 2012 and remanded the case for a new trial. Defendants are seeking review of the case in the Florida Supreme Court. In addition, there have been a number of mistrials, only some of which have resulted in new trials as of October 25, 2012.

In Lukacs, a case that was tried to verdict before the Florida Supreme Court Engle decision, the Florida Third District Court of Appeal in March 2010 affirmed per curiam the trial court decision without issuing an opinion. Under Florida procedure, further review of a per curiam affirmance without opinion by the Florida Supreme Court is generally prohibited. Subsequently in 2010, after defendants' petition for rehearing with the Court of Appeal was denied, defendants paid the judgment.

The chart below lists the verdicts and post-trial developments in the Engle progeny cases that were pending during 2012 in which verdicts were returned in favor of plaintiffs.

Date	Plaintiff	Verdict	Post-Trial Developments
October 2012	Lock	On October 25, 2012, a Pinellas County jury returned a verdict in favor of plaintiff and against PM USA and R.J. Reynolds. The jury awarded $1,150,000 in compensatory damages and allocated 9% of the fault to each of the defendants (an amount of $103,500).	
August 2012	Hancock	On August 10, 2012, a Broward County jury returned a verdict in the amount of zero damages and allocated 5% of the fault to each of the defendants (PM USA and R.J. Reynolds). The trial court granted an additur of $110,000, which is subject to the jury's comparative fault finding.	On August 20, 2012, the defendants moved to set aside the verdict and to enter judgment in accordance with their motion for directed verdict. The defendants also moved to reduce damages, which motion the court granted on August 31, 2012. The trial court granted defendants'

motion to set off the damages award by the amount of economic damages paid by third parties, which will reduce further any final award. On October 16, 2012, the trial court entered final judgment. PM USA's portion of the damages was approximately $700.

Date	Plaintiff	Verdict	Post-Trial Developments
May 2012	Calloway	A Broward County jury returned a verdict in favor of plaintiff and against PM USA, R.J. Reynolds, Lorillard Tobacco Company and Liggett Group. The jury awarded approximately $21 million in compensatory damages and allocated 25% of the fault against PM USA but the trial court ruled that it will not apply the comparative fault allocations because the jury found against each defendant on the intentional tort claims. The jury also awarded approximately $17 million in punitive damages against PM USA, approximately $17 million in punitive damages against R.J. Reynolds, approximately $13 million in punitive damages against Lorillard Tobacco Company and approximately $8 million in punitive damages against Liggett Group.	In May and June, 2012, the defendants filed motions to set aside the verdict and for a new trial. On August 20, 2012, the trial court denied the remaining post-trial motions and entered final judgment, reducing the total compensatory damages award to $16.1 million but leaving undisturbed the separate punitive damages awards. On September 11, 2012, PM USA posted a bond in an amount of $1.5 million and on September 12, 2012, the defendants filed a notice of appeal to the Florida Fourth District Court of Appeal.
January 2012	Hallgren	A Highland County jury returned a verdict in favor of plaintiff and against PM USA and R.J. Reynolds. The jury awarded approximately $2 million in compensatory damages and allocated 25% of the fault to PM USA (an amount of approximately $500,000). The jury also awarded $750,000 in punitive damages against each of the defendants.	The trial court entered final judgment in March 2012. In April 2012, PM USA posted a bond in an amount of approximately $1.25 million. In May 2012, the defendants filed a notice of appeal to the Florida Second District Court of Appeal.
July 2011	Weingart	A Palm Beach County jury returned a verdict in the amount of zero damages and allocated 3% of the fault to each of the defendants (PM USA, R.J. Reynolds and Lorillard Tobacco Company).	In September 2011, the trial court granted plaintiff's motion for additur or a new trial, concluding that an additur of $150,000 is required for plaintiff's pain and suffering. The trial court entered final judgment and, since PM USA was allocated 3% of the fault, its portion of the damages was $4,500. In October 2011, PM USA filed its notice of appeal and, in November 2011, posted bonds in an aggregate amount of $48,000.

April 2011	Allen	A Duval County jury returned a verdict in favor of plaintiffs and against PM USA and R.J. Reynolds. The jury awarded a total of $6 million in compensatory damages and allocated 15% of the fault to PM USA (an amount of $900,000). The jury also awarded $17 million in punitive damages against each of the defendants.	In May 2011, the trial court entered final judgment. In October 2011, the trial court granted the defendants' motion for remittitur, reducing the punitive damages award against PM USA to $2.7 million, and denied defendants' remaining post-trial motions. PM USA filed a notice of appeal and posted a bond in the amount of $1.25 million in November 2011.

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Date	Plaintiff	Verdict	Post-Trial Developments
April 2011	Tullo	A Palm Beach County jury returned a verdict in favor of plaintiff and against PM USA, Lorillard Tobacco Company and Liggett Group. The jury awarded a total of $4.5 million in compensatory damages and allocated 45% of the fault to PM USA (an amount of $2,025,000).	In April 2011, the trial court entered final judgment. In July 2011, PM USA filed its notice of appeal and posted a $2 million bond.
February 2011	Huish	An Alachua County jury returned a verdict in favor of plaintiff and against PM USA. The jury awarded $750,000 in compensatory damages and allocated 25% of the fault to PM USA (an amount of $187,500). The jury also awarded $1.5 million in punitive damages against PM USA.	In March 2012, the Florida First District Court of Appeal affirmed per curiam the trial court's decision without issuing an opinion. In the second quarter of 2012, PM USA recorded a provision on its condensed consolidated balance sheet of approximately $2.5 million. In July 2012, PM USA paid an amount of $2.5 million in satisfaction of the judgment and associated costs. PM USA's $1.7 million appeal bond was released on August 29, 2012. This litigation has concluded.
February 2011	Hatziyannakis	A Broward County jury returned a verdict in favor of plaintiff and against PM USA. The jury awarded approximately $270,000 in compensatory damages and allocated 32% of the fault to PM USA (an amount of approximately $86,000).	In April 2011, the trial court denied PM USA's post-trial motions for a new trial and to set aside the verdict. In June 2011, PM USA filed its notice of appeal and posted an $86,000 appeal bond.

Date	Plaintiff	Verdict	Post-Trial Developments
August 2010	Piendle	A Palm Beach County jury returned a verdict in favor of plaintiff and against PM USA and R.J. Reynolds. The jury awarded $4 million in compensatory damages and allocated 27.5% of the fault to PM USA (an amount of approximately $1.1 million). The jury also awarded $90,000 in punitive damages against PM USA.	In September 2010, the trial court entered final judgment. PM USA filed its notice of appeal and posted a $1.2 million appeal bond. In June 2012, the Florida Fourth District Court of Appeal affirmed per curiam the trial court's decision without issuing an opinion. In July 2012, the defendants filed a motion requesting that the court add a citation to its per curiam affirmance so that defendants could seek review of the decision in the Florida Supreme Court. Alternatively, the motion requested that the court stay the proceeding pending the Florida Supreme Court's disposition of Douglas. The court denied both motions on July 27, 2012. In the third quarter of 2012, PM USA recorded a provision on its condensed consolidated balance sheet of approximately $2.7 million for the judgment and associated costs. On September 12, 2012, the United States Supreme Court granted defendants an extension to November 17, 2012 to file a petition for writ of certiorari.
July 2010	Kayton (formerly Tate)	A Broward County jury returned a verdict in favor of the plaintiff and against PM USA. The jury awarded $8 million in compensatory damages and allocated 64% of the fault to PM USA (an amount of approximately $5.1 million). The jury also awarded approximately $16.2 million in punitive damages against PM USA.	In August 2010, the trial court entered final judgment, and PM USA filed its notice of appeal and posted a $5 million appeal bond. Argument on the merits of the appeal was heard in June 2012.
April 2010	Putney	A Broward County jury returned a verdict in favor of the plaintiff and against PM USA, R.J. Reynolds and Liggett Group. The jury awarded approximately $15.1 million in	In August 2010, the trial court entered final judgment. PM USA filed its notice of appeal and posted a $1.6 million appeal bond. Argument on the merits of the

compensatory damages and allocated 15% of the fault to PM USA (an amount of approximately $2.3 million). The jury also awarded $2.5 million in punitive damages against PM USA.	appeal occurred on September 27, 2012.

Date	Plaintiff	Verdict	Post-Trial Developments
March 2010	R. Cohen	A Broward County jury returned a verdict in favor of the plaintiff and against PM USA and R.J. Reynolds. The jury awarded $10 million in compensatory damages and allocated 33 1/3% of the fault to PM USA (an amount of approximately $3.3 million). The jury also awarded a total of $20 million in punitive damages, assessing separate $10 million awards against each defendant.	In July 2010, the trial court entered final judgment and, in August 2010, PM USA filed its notice of appeal. In October 2010, PM USA posted a $2.5 million appeal bond. On September 12, 2012, the Florida Fourth District Court of Appeal affirmed the compensatory damages award but reversed and remanded the punitive damages verdict. The Fourth District returned the case to the trial court for a new jury to determine whether the statute of repose barred the concealment claim, which was the only basis for the punitive damages award. If the jury finds in plaintiff's favor on that claim, the $10 million punitive damages award will be reinstated. On October 8, 2012, both plaintiff and defendants filed petitions for rehearing.
March 2010	Douglas	A Hillsborough County jury returned a verdict in favor of the plaintiff and against PM USA, R.J. Reynolds and Liggett Group. The jury awarded $5 million in compensatory damages. Punitive damages were dismissed prior to trial. The jury allocated 18% of the fault to PM USA, resulting in an award of $900,000.	In June 2010, PM USA filed its notice of appeal and posted a $900,000 appeal bond. In March 2012, the Florida Second District Court of Appeal issued a decision affirming the judgment and upholding the use of the Engle jury findings but certified to the Florida Supreme Court the question of whether granting res judicata effect to the Engle jury findings violates defendants' federal due process rights. In April 2012, the defendants filed a notice to invoke discretionary jurisdiction with the Florida Supreme Court. In May 2012, the Florida Supreme Court accepted jurisdiction of the case. Argument occurred on September 6, 2012.

Date	Plaintiff	Verdict	Post-Trial Developments
November 2009	Naugle	A Broward County jury returned a verdict in favor of the plaintiff and against PM USA. The jury awarded approximately $56.6 million in compensatory damages and $244 million in punitive damages. The jury allocated 90% of the fault to PM USA.	In March 2010, the trial court entered final judgment reflecting a reduced award of approximately $13 million in compensatory damages and $26 million in punitive damages. In April 2010, PM USA filed its notice of appeal and posted a $5 million appeal bond. In August 2010, upon the motion of PM USA, the trial court entered an amended final judgment of approximately $12.3 million in compensatory damages and approximately $24.5 million in punitive damages to correct a clerical error. In June 2012, the Fourth District Court of Appeal affirmed the amended final judgment. In July 2012, PM USA filed a motion for rehearing.
August 2009	F. Campbell	An Escambia County jury returned a verdict in favor of the plaintiff and against R.J. Reynolds, PM USA and Liggett Group. The jury awarded $7.8 million in compensatory damages. In September 2009, the trial court entered final judgment and awarded the plaintiff $156,000 in damages against PM USA due to the jury allocating only 2% of the fault to PM USA.	In March 2011, the Florida First District Court of Appeal affirmed per curiam the trial court's decision without issuing an opinion. In May 2012, PM USA paid an amount of approximately $262,000 in satisfaction of the judgment and associated costs and interest. This litigation has concluded.
August 2009	Barbanell	A Broward County jury returned a verdict in favor of the plaintiff, awarding $5.3 million in compensatory damages. The judge had previously dismissed the punitive damages claim. In September 2009, the trial court entered final judgment and awarded the plaintiff $1.95 million in actual damages. The judgment reduced the jury's $5.3 million award of compensatory damages due to the jury allocating 36.5% of the fault to PM USA.	A notice of appeal was filed by PM USA in September 2009, and PM USA posted a $1.95 million appeal bond. In February 2012, the Florida Fourth District Court of Appeal reversed the judgment, holding that the statute of limitations barred the plaintiff's claims. On October 17, 2012, on motion for rehearing, the Fourth District withdrew its prior decision and affirmed the trial court's judgment.

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February 2009	Hess	A Broward County jury found in favor of plaintiffs and against PM USA. The jury awarded $3 million in compensatory damages and $5 million in punitive damages. In June 2009, the trial court entered final judgment and awarded plaintiffs $1.26 million in actual damages and $5 million in punitive damages. The judgment reduced the jury's $3 million award of compensatory damages due to the jury allocating 42% of the fault to PM USA.	PM USA noticed an appeal to the Fourth District Court of Appeal in July 2009. In April 2012, PM USA filed a motion to stay the appeal pending the decision of the Florida Supreme Court on whether to review the Douglas case. In May 2012, the Fourth District denied PM USA's motion to stay the appeal. The Fourth District also reversed and vacated the punitive damages award and affirmed the judgment in all other respects, upholding the compensatory damages award of $1.26 million. In June 2012, both parties filed rehearing motions with the Fourth District, which were denied on September 14, 2012. On October 15, 2012, PM USA and plaintiffs filed notices to invoke the Florida Supreme Court's discretionary jurisdiction.

Appeals of Engle Progeny Verdicts

Plaintiffs in various Engle progeny cases have appealed adverse rulings or verdicts, and in some cases, PM USA has cross-appealed. PM USA's appeals of adverse verdicts are discussed in the chart above.

Since the remand of B. Brown (discussed above under the heading Federal Engle Progeny Cases), several state appellate rulings have superseded the Eleventh Circuit's ruling on Florida state law. These include Martin, an Engle progeny case against R.J. Reynolds in Escambia County, J. Brown, an Engle progeny case against R.J. Reynolds in Broward County, and Douglas, an Engle progeny case against PM USA, R.J. Reynolds and Liggett Group in Hillsborough County. In Martin, the Florida First District Court of Appeal rejected the B. Brown ruling as a matter of state law and upheld the use of the Engle findings to relax plaintiffs' burden of proof. R.J. Reynolds had sought Florida Supreme Court review in that case but, in July 2011, the Florida Supreme Court declined to hear the appeal. In December 2011, petitions for certiorari were filed with the United States Supreme Court by R.J. Reynolds in Campbell, Martin, Gray and Hall and by PM USA and Liggett Group in Campbell. The Supreme Court denied the defendants' certiorari petitions in March 2012.

In J. Brown, the Florida Fourth District Court of Appeal also rejected the B. Brown ruling as a matter of state law and upheld the use of the Engle findings to relax plaintiffs' burden of proof. However, the Fourth District expressly disagreed with the First District's Martin decision by ruling that Engle progeny plaintiffs must prove legal causation on their claims. In addition, the J. Brown court expressed concerns that using the Engle findings to reduce plaintiffs' burden may violate defendants' due process rights. In October 2011, the Fourth District denied R.J. Reynolds' motion to certify J. Brown to the Florida Supreme Court for review. R.J. Reynolds is seeking review of the case by the Florida

Supreme Court.

In Douglas, in March 2012, the Florida Second District Court of Appeal issued a decision affirming the judgment of the trial court in favor of the plaintiff and upholding the use of the Engle jury findings but certified to the Florida Supreme Court the question of whether granting res judicata effect to the Engle jury findings violates defendants' federal due process rights. In April 2012, the defendants in Douglas filed a notice to invoke discretionary jurisdiction with the Florida Supreme Court. In May 2012, the Florida Supreme Court accepted jurisdiction of the case. Argument occurred on September 6, 2012.

As noted above in Federal Engle Progeny Cases, there has been no federal appellate review of the federal due process issues raised by the use of findings from the original Engle trial in Engle progeny cases, although several appeals brought by other cigarette manufacturers are pending.

Because of the substantial period of time required for the federal and state appellate processes, it is possible that PM USA may have to pay additional outstanding judgments in the Engle progeny cases before the final adjudication of these issues by the Florida Supreme Court or the United States Supreme Court.

Other Smoking and Health Class Actions

Since the dismissal in May 1996 of a purported nationwide class action brought on behalf of allegedly addicted smokers, plaintiffs have filed numerous putative smoking and health class action suits in various state and federal courts. In general, these cases purport to be brought on behalf of residents of a particular state or states (although a few cases purport to be nationwide in scope) and raise addiction claims and, in many cases, claims of physical injury as well.

Class certification has been denied or reversed by courts in 59 smoking and health class actions involving PM USA in Arkansas (1), California (1), the District of Columbia (2), Florida (2), Illinois (3), Iowa (1), Kansas (1), Louisiana (1), Maryland (1), Michigan (1), Minnesota (1), Nevada (29), New Jersey (6), New York (2), Ohio (1), Oklahoma (1), Pennsylvania (1), Puerto Rico (1), South Carolina (1), Texas (1) and Wisconsin (1).

PM USA and Altria Group, Inc. are named as defendants, along with other cigarette manufacturers, in six actions filed in the Canadian provinces of Alberta, Manitoba, Nova Scotia, Saskatchewan and British Columbia. In Saskatchewan and British Columbia, plaintiffs seek class certification on behalf of individuals who suffer or have suffered from various diseases, including chronic obstructive pulmonary disease, emphysema, heart disease or cancer, after smoking defendants' cigarettes. In the actions filed in Alberta, Manitoba and Nova Scotia, plaintiffs seek certification of classes of all individuals who smoked defendants' cigarettes. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement between Altria Group, Inc. and PMI that provides for indemnities for certain liabilities concerning tobacco products.

Scott Class Action

Following a 2004 verdict that awarded plaintiffs approximately $590 million to fund a 10-year smoking cessation program and a series of appeals and other post-trial motions, PM USA recorded in the second quarter of 2011 a provision on its condensed consolidated balance sheet of approximately $36 million related to the judgment and approximately $5 million related to interest, which was in addition to a previously recorded provision of approximately $30 million. In August 2011, PM USA paid its share of the judgment and interest in an amount of approximately $70 million. The defendants' payments have been deposited into a court-supervised fund that is intended to pay for smoking cessation programs.

In October 2011, plaintiffs' counsel filed a motion for an award of attorneys' fees and costs. Plaintiffs' counsel sought additional fees from defendants of up to $673 million. Additionally, plaintiffs' counsel requested an award of approximately $13 million in costs. In March 2012, the trial court denied defendants' motion challenging plaintiffs' counsel's request that defendants pay their attorneys' fees directly, as opposed to out of the court-supervised fund. Defendants subsequently filed a petition for a supervisory writ challenging the decision to the Louisiana Fourth Circuit Court of Appeal.

In May 2012, the parties reached a settlement on the amount of fees and costs to be awarded to plaintiffs' counsel. Plaintiffs agreed that any recovery of fees and costs would come from the court-supervised fund, not the defendants, and indicated they would seek approximately $114 million from the fund. In exchange, defendants agreed to waive 50% of their right to a refund of any unspent money in the fund after the 10-year program is completed. The agreement is not contingent on the trial court's granting plaintiffs' request for additional costs and fees. The trustee of the fund intervened to challenge whether the plaintiffs' lawyers should get any money from the fund or, alternatively, the amount they would recover from the fund. Plaintiffs and defendants are challenging the standing of the trustee. Argument was scheduled for August 22, 2012, but the matter was removed from the docket.

Other Medical Monitoring Class Actions

In addition to the Scott class action discussed above, two purported medical monitoring class actions are pending against PM USA. These two cases were brought in New York (Caronia, filed in January 2006 in the United States District Court for the Eastern District of New York) and Massachusetts (Donovan, filed in December 2006 in the United States District Court for the District of Massachusetts) on behalf of each state's respective residents who: are age 50 or older; have smoked the Marlboro brand for 20 pack-years or more; and have neither been diagnosed with lung cancer nor are under investigation by a physician for suspected lung cancer. Plaintiffs in these cases seek to impose liability under various product-based causes of action and the creation of a court-supervised program providing members of the purported class Low Dose CT Scanning in order to identify and diagnose lung cancer. Plaintiffs in these cases do not seek punitive damages. A case brought in California (Xavier) was dismissed in July 2011, and a case brought in Florida (Gargano) was voluntarily dismissed with prejudice in August 2011.

In Caronia, in February 2010, the district court granted in part PM USA's summary judgment motion, dismissing plaintiffs' strict liability and negligence claims and certain other claims, granted plaintiffs leave to amend their complaint to allege a medical monitoring cause of action and requested further briefing on PM USA's summary judgment motion as to plaintiffs' implied warranty claim and, if plaintiffs amend their complaint, their medical monitoring claim. In March 2010, plaintiffs filed their amended complaint and PM USA moved to dismiss the implied warranty and medical monitoring claims. In January 2011, the district court granted PM USA's motion, dismissed plaintiffs' claims and declared plaintiffs' motion for class certification moot in light of the dismissal of the case. The plaintiffs have appealed that decision to the United States Court of Appeals for the Second Circuit. Argument before the Second Circuit was heard in March 2012.

In Donovan, the Supreme Judicial Court of Massachusetts, in answering questions certified to it by the district court, held in October 2009 that under certain circumstances state law recognizes a claim by individual smokers for medical monitoring despite the absence of an actual injury. The court also ruled that whether or not the case is barred by the applicable statute of limitations is a factual issue to be determined by the trial court. The case was remanded to federal court for further proceedings. In June 2010, the district court granted in part the plaintiffs' motion for class certification, certifying the class as to plaintiffs' claims for breach of implied warranty and violation of the Massachusetts Consumer Protection Act, but denying certification as to plaintiffs' negligence claim. In July 2010, PM USA petitioned the United States Court of Appeals for the First Circuit for appellate review of the class certification decision. The petition was denied in September 2010. As a remedy, plaintiffs have proposed a 28-year medical monitoring program with an approximate cost of $190 million. In April 2011, plaintiffs moved to amend their class certification to extend the cut-off date for individuals to satisfy the class membership criteria from December 14, 2006 to August 1, 2011. The district court granted this motion in May 2011. In June 2011, plaintiffs filed various motions for summary judgment and to strike affirmative defenses, which the district court denied in March 2012. In October 2011, PM USA filed a motion for class decertification, which motion was denied in March 2012. A trial date has not been set.

Evolving medical standards and practices could have an impact on the defense of medical monitoring claims. For example, the first publication of the findings of the National Cancer Institute's National Lung Screening Trial (NLST) in June 2011 reported a 20% reduction in lung cancer deaths among certain long-term smokers receiving Low Dose CT Scanning for lung cancer. Since then, various public health organizations have begun to develop new lung cancer screening guidelines. Also, a number of hospitals have advertised the availability of screening programs. Other studies in this area are ongoing.

Health Care Cost Recovery Litigation

Overview

In the health care cost recovery litigation, governmental entities seek reimbursement of health care cost expenditures allegedly caused by tobacco products and, in some cases, of future expenditures and damages as well. Relief sought by some but not all plaintiffs includes punitive damages, multiple damages and other statutory damages and penalties, injunctions prohibiting alleged marketing and sales to minors, disclosure of research, disgorgement of profits, funding of anti-smoking programs, additional disclosure of nicotine yields, and payment of attorney and expert witness fees.

The claims asserted include the claim that cigarette manufacturers were "unjustly enriched" by plaintiffs' payment of health care costs allegedly attributable to smoking, as well as claims of indemnity, negligence, strict liability, breach of express and implied warranty, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, claims under federal and state statutes governing consumer fraud, antitrust, deceptive trade practices and false advertising, and claims under federal and state anti-racketeering statutes.

Defenses raised include lack of proximate cause, remoteness of injury, failure to state a valid claim, lack of benefit, adequate remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), lack of antitrust standing and injury, federal preemption, lack of statutory authority to bring suit, and statutes of limitations. In addition, defendants argue that they should be entitled to "set off" any alleged damages to the extent the plaintiffs benefit economically from the sale of cigarettes through the receipt of excise taxes or otherwise. Defendants also argue that these cases are improper because plaintiffs must proceed under principles of subrogation and assignment. Under traditional theories of recovery, a payor of medical costs (such as an insurer) can seek recovery of health care costs from a third party solely by "standing in the shoes" of the injured party. Defendants argue that plaintiffs should be required to bring any actions as subrogees of individual health care recipients and should be subject to all defenses available against the injured party.

Although there have been some decisions to the contrary, most judicial decisions in the United States have dismissed all or most health care cost recovery claims against cigarette manufacturers. Nine federal circuit courts of appeals and eight state appellate courts, relying primarily on grounds that plaintiffs' claims were too remote, have ordered or affirmed dismissals of health care cost recovery actions. The United States Supreme Court has refused to consider plaintiffs' appeals from the cases decided by five circuit courts of appeals. In 2011, in the health care cost recovery case brought against PM USA and other defendants by the City of St. Louis, Missouri and approximately 40 Missouri hospitals, a verdict was returned in favor of the defendants.

Individuals and associations have also sued in purported class actions or as private attorneys general under the Medicare as Secondary Payer ("MSP") provisions of the Social Security Act to recover from defendants Medicare expenditures allegedly incurred for the treatment of smoking-related diseases. Cases were brought in New York (2), Florida (2) and Massachusetts (1). All were dismissed by federal courts.

In addition to the cases brought in the United States, health care cost recovery actions have also been brought against tobacco industry participants, including PM USA and Altria Group, Inc., in Israel (dismissed), the Marshall Islands (dismissed), and Canada (8), and other entities have stated that they are considering filing such actions.

In September 2005, in the first of several health care cost recovery cases filed in Canada, the Canadian Supreme Court ruled that legislation passed in British Columbia permitting the lawsuit is constitutional, and, as a result, the case, which had previously been dismissed by the trial court, was permitted to proceed. PM USA's and other defendants' challenge to the British Columbia court's exercise of jurisdiction was rejected by the Court of Appeals of British Columbia and, in April 2007, the Supreme Court of Canada denied review of that decision. In December 2009, the Court of Appeals of British Columbia ruled that certain defendants can proceed against the Federal Government of Canada as third parties on the theory that the Federal Government of Canada negligently misrepresented to defendants the efficacy of a low tar tobacco variety that the Federal Government of Canada developed and licensed to defendants. In May 2010, the Supreme Court of Canada granted leave to the Federal Government of Canada to appeal this decision and leave to defendants to cross-appeal the Court of Appeals' decision to dismiss claims against the Federal Government of Canada based on other theories of liability. In July 2011, the Supreme Court of Canada dismissed the third-party claims against the Federal Government of Canada.

Since the beginning of 2008, the Canadian Provinces of New Brunswick, Ontario, Newfoundland and Labrador, Quebec, Alberta, Manitoba and Saskatchewan have all brought health care reimbursement claims against cigarette manufacturers. PM USA is named as a defendant in the British Columbia and Quebec cases, while both Altria Group, Inc. and PM USA are named as defendants in the New Brunswick, Ontario, Newfoundland and Labrador, Quebec, Alberta, Manitoba and Saskatchewan cases. Several other provinces and territories in Canada have enacted similar legislation or are in the process of enacting similar legislation. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement between Altria Group, Inc. and PMI that provides for indemnities for certain liabilities concerning tobacco products.

Settlements of Health Care Cost Recovery Litigation

In November 1998, PM USA and certain other United States tobacco product manufacturers entered into the Master Settlement Agreement (the "MSA") with 46 states, the District of Columbia, Puerto Rico, Guam, the United States Virgin Islands, American Samoa and the Northern Marianas to settle asserted and unasserted health care cost recovery and other claims. PM USA and certain other United States tobacco product manufacturers had previously settled similar claims brought by Mississippi, Florida, Texas and Minnesota (together with the MSA, the "State Settlement Agreements"). The State Settlement Agreements require that the original participating manufacturers make substantial annual payments of approximately $9.4 billion, subject to adjustments for several factors, including inflation, market share and industry volume. In addition, the original participating manufacturers are required to pay settling plaintiffs' attorneys' fees, subject to an annual cap of $500 million. For the three months ended September 30, 2012 and September 30, 2011, the aggregate amount recorded in cost of sales with respect to the State Settlement Agreements and the Fair and Equitable Tobacco Reform Act of 2004 ("FETRA") was approximately $1.2 billion for each period. For the nine months ended September 30, 2012 and September 30, 2011, the aggregate amount recorded in cost of sales with respect to the State Settlement Agreements and FETRA was approximately $3.6 billion for each period.

The State Settlement Agreements also include provisions relating to advertising and marketing restrictions, public disclosure of certain industry documents, limitations on challenges to certain tobacco control and underage use laws, restrictions on lobbying activities and other provisions.

Possible Adjustments in MSA Payments for 2003 to 2011

Pursuant to the provisions of the MSA, domestic tobacco product manufacturers, including PM USA, who are original signatories to the MSA (the "Original Participating Manufacturers" or "OPMs") are participating in proceedings that may result in downward adjustments to the amounts paid by the OPMs and the other MSA-participating manufacturers to the states and territories that are parties to the MSA for each of the years 2003 to 2011. The proceedings relate to an MSA payment adjustment (the "NPM Adjustment") based on the collective loss of market share for the relevant year by all participating manufacturers who are subject to the payment obligations and marketing restrictions of the MSA to non-participating manufacturers ("NPMs") who are not subject to such obligations and restrictions.

As part of these proceedings, an independent economic consulting firm jointly selected by the MSA parties or otherwise selected pursuant to the MSA's provisions is required to determine whether the disadvantages of the MSA were a "significant factor" contributing to the participating manufacturers' collective loss of market share for the year in question. If the firm determines that the disadvantages of the MSA were such a "significant factor," each state may avoid a downward adjustment to its share of the participating manufacturers' annual payments for that year by establishing that it diligently enforced a qualifying escrow statute during the entirety of that year. Any potential downward adjustment would then be reallocated to any states that do not establish such diligent enforcement. PM USA believes that the MSA's arbitration clause requires a state to submit its claim to have diligently enforced a qualifying escrow statute to binding arbitration before a panel of three former federal judges in the manner provided for in the MSA. A number of states have taken the position that this claim should be decided in state court on a state-by-state basis.

An independent economic consulting firm, jointly selected by the MSA parties, determined that the disadvantages of the MSA were a significant factor contributing to the participating manufacturers' collective loss of market share for each of the years 2003 – 2005. A different independent economic consulting firm, jointly selected by the MSA parties, determined that the disadvantages of the MSA were a significant factor contributing to the participating manufacturers' collective loss of market share for the year 2006. Following the firm's determination for 2006, the OPMs and the states agreed that the states would not contest that the disadvantages of the MSA were a significant factor contributing to the participating manufacturers' collective loss of market share for the years 2007, 2008 and 2009. Accordingly, the OPMs and the states have agreed that no "significant factor" determination by an independent economic consulting firm will be necessary with respect to the participating manufacturers' collective loss of market share for the years 2007, 2008 and 2009 (the "significant factor agreement"). This agreement became effective for 2007, 2008 and 2009 on February 1, 2010, 2011 and 2012, respectively. The OPMs and the states have agreed to extend the significant factor agreement to apply to the participating manufacturers' collective loss of market share for 2010 and 2011, as well as to any collective loss of market share that the participating manufacturers experience for 2012. This agreement will become effective for 2010 on February 1, 2013 and for 2011 on February 1, 2014. If the MSA's Independent Auditor determines that the participating manufacturers collectively lost market share for 2012, this agreement will become effective for 2012 on February 1, 2015.

Following the "significant factor" determination with respect to 2003, 38 states filed declaratory judgment actions in state courts seeking a declaration that the state diligently enforced its escrow statute during 2003. The OPMs and other MSA-participating manufacturers responded to these actions by filing motions to compel arbitration in accordance with the terms of the MSA, including filing motions to compel arbitration in 11 MSA states and territories that did not file declaratory judgment actions. Courts in all but one of the 46 MSA states and the District of Columbia and Puerto Rico have ruled that the question of whether a state diligently enforced its escrow statute during 2003 is subject to arbitration. Several of these rulings may be subject to further review. The Montana state courts have ruled that the diligent enforcement claims of that state may be litigated in state court, rather than in arbitration. In June 2012, following the denial of the OPMs' petition to the United States Supreme Court for a writ of certiorari, the participating manufacturers and Montana entered into a consent decree pursuant to which Montana will not be subject to the 2003 NPM Adjustment.

PM USA, the other OPMs and approximately 25 other MSA-participating manufacturers have entered into an agreement regarding arbitration with 45 MSA states and territories concerning the 2003 NPM Adjustment, including the states' claims of diligent enforcement for 2003. The agreement further provides for a partial liability reduction for the 2003 NPM Adjustment for states that entered into the agreement by January 30, 2009 and are determined in the arbitration not to have diligently enforced a qualifying escrow statute during 2003. Based on the number of states that entered into the agreement by January 30, 2009 (45), the partial liability reduction for those states is 20%. The partial liability reduction would reduce the amount of PM USA's 2003 NPM Adjustment by up to a corresponding percentage. The selection of the arbitration panel for the 2003 NPM Adjustment was completed in July 2010, and the arbitration is currently ongoing. Following the completion of discovery, the participating manufacturers determined to continue to contest the 2003 diligent enforcement claims of 33 states, the District of Columbia and Puerto Rico and to no longer contest such claims by 12 states and four U.S. territories (the "non-contested states"). As a result, the non-contested states will not be subject to the 2003 NPM Adjustment, and their share of any such NPM Adjustment, along with the shares of any states found by the arbitration panel to have diligently enforced during 2003, will be reallocated in accordance with the MSA to those states, if any, found by the panel not to have diligently enforced during 2003. Proceedings to determine state diligent enforcement claims for the years 2004 through 2011 have not yet been scheduled.

Once a significant factor determination in favor of the participating manufacturers for a particular year has been made by an economic consulting firm, or the states' agreement not to contest significant factor for a particular year has become effective, PM USA has the right under the MSA to pay the disputed amount of the NPM Adjustment for that year into a disputed payments account or withhold it altogether. PM USA has made its full MSA payment due in each year from 2006 - 2010 to the states (subject to a right to recoup the NPM Adjustment amount in the form of a credit against future MSA payments), even though it had the right to deduct the disputed amounts of the 2003 - 2007 NPM Adjustments, as described above, from such MSA payments. PM USA paid its share of the amount of the disputed 2008 and 2009 NPM Adjustments shown below into the MSA's disputed payments account in connection with its MSA payments due in 2011 and 2012, respectively. The approximate maximum principal amounts of PM USA's share of the disputed NPM Adjustment for the years 2003 through 2011, as currently calculated by the MSA's Independent Auditor, are as follows (the amounts shown below do not include the interest or earnings thereon to which PM USA believes it would be entitled in the manner provided in the MSA and do not reflect the partial liability reduction for the 2003 NPM Adjustment pursuant to the arbitration agreement described above):

Year for which NPM Adjustment calculated	2003	2004	2005	2006	2007	2008	2009	2010	2011
Year in which deduction for NPM Adjustment may be taken	2006	2007	2008	2009	2010	2011	2012	2013	2014
PM USA's Approximate Share of Disputed NPM Adjustment (in millions)	$337	$388	$181	$154	$185	$252	$206	$208	$137

The foregoing amounts may be recalculated by the MSA's Independent Auditor if it receives information that is different from or in addition to the information on which it based these calculations, including, among other things, if it receives revised sales volumes from any participating manufacturer. Disputes among the manufacturers could also reduce the foregoing amounts. The availability and the precise amount of any NPM Adjustment for 2003 - 2011 will not be finally determined until 2013 or thereafter. There is no certainty that the OPMs and other MSA-participating manufacturers will ultimately receive any adjustment as a result of these proceedings, and the amount of any adjustment received for a year could be less than the amount for that year listed above. If the OPMs do receive such an adjustment through these proceedings, the adjustment would be allocated among the OPMs pursuant to the MSA's provisions. It is expected that PM USA would receive its share of any adjustments for 2003 - 2007 in the form of a credit against future MSA payments and its share of any adjustment for 2008 or 2009 in the form of a withdrawal from the disputed payments account.

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PM USA intends to pursue vigorously the disputed NPM Adjustments for 2003 - 2011 through the proceedings described above. PM USA would be willing, however, to enter into a settlement of those disputed NPM Adjustments if it determined that such a settlement were in its best interests.

Other Disputes Related to MSA Payments

In addition to the disputed NPM Adjustments described above, MSA states and participating manufacturers, including PM USA, are conducting another arbitration to resolve certain other disputes related to the calculation of the participating manufacturers' payments under the MSA. PM USA disputes the method by which ounces of "roll your own" tobacco have been converted to cigarettes for purposes of calculating the downward volume adjustments to its MSA payments. PM USA believes that, for the years 2004 – 2012, the use of an incorrect conversion method resulted in excess MSA payments by PM USA in those years of approximately $92 million in the aggregate. If PM USA prevails on this issue, it would be entitled to a credit against future MSA payments in that amount, plus interest. In addition, PM USA seeks application of what it believes to be the correct method for payments to be made in years subsequent to 2012.

This arbitration will also resolve a dispute concerning whether the total domestic cigarette market and certain other calculations related to the participating manufacturers' MSA payments should be determined based on the "net" number of cigarettes on which federal excise tax is paid, as is currently the case, or whether the "adjusted gross" number of cigarettes on which federal excise tax is paid is the correct methodology. PM USA does not have sufficient information at this time to determine the aggregate impact on its MSA payments that would result from a change from the "net" to the "adjusted gross" methodology.

PM USA anticipates that this arbitration will not be concluded until 2013. No assurance can be given that PM USA will prevail in this arbitration.

Other MSA-Related Litigation

Without naming PM USA or any other private party as a defendant, NPMs and/or their distributors or customers have filed several legal challenges to the MSA and related legislation. New York state officials and the Attorneys General of a number of other states were defendants in a lawsuit (King, formerly Pryor) filed in the United States District Court for the Southern District of New York in which plaintiffs alleged that the MSA and/or related legislation violated federal antitrust laws and the Commerce Clause of the United States Constitution. In March 2011, the trial court granted summary judgment on all claims for the New York state officials. Plaintiffs appealed to the United States Court of Appeals for the Second Circuit. In June 2012, the Second Circuit dismissed that appeal pursuant to a stipulation of the parties, concluding the litigation.

In addition to the King decision above, the United States Courts of Appeals for the Second, Fifth, Sixth, Eighth, Ninth and Tenth Circuits have affirmed dismissals or grants of summary judgment in favor of state officials in seven other cases asserting antitrust and constitutional challenges to the allocable share amendment legislation in those states.

In January 2011, an international arbitration tribunal rejected claims brought against the United States challenging MSA-related legislation in various states under the North American Free Trade Agreement.

Federal Government's Lawsuit

In 1999, the United States government filed a lawsuit in the United States District Court for the District of Columbia against various cigarette manufacturers, including PM USA, and others, including Altria Group, Inc., asserting claims under three federal statutes, namely the Medical Care Recovery Act ("MCRA"), the MSP provisions of the Social Security Act and the civil provisions of RICO. Trial of the case ended in June 2005. The lawsuit sought to recover an unspecified amount of health care costs for tobacco-related illnesses allegedly caused by defendants' fraudulent and tortious conduct and paid for by the government under various federal health care programs, including Medicare, military and veterans' health benefits programs, and the Federal Employees Health Benefits Program. The complaint alleged that such costs total more than $20 billion annually. It also sought what it alleged to be equitable and declaratory relief, including disgorgement of profits which arose from defendants' allegedly tortious conduct, an injunction prohibiting certain actions by the defendants, and a declaration that the defendants are liable for the federal government's future costs of providing health care resulting from defendants' alleged past tortious and wrongful conduct. In September 2000, the trial court dismissed the government's

MCRA and MSP claims, but permitted discovery to proceed on the government's claims for relief under the civil provisions of RICO.

The government alleged that disgorgement by defendants of approximately $280 billion is an appropriate remedy. In May 2004, the trial court issued an order denying defendants' motion for partial summary judgment limiting the disgorgement remedy. In February 2005, a panel of the United States Court of Appeals for the District of Columbia Circuit held that disgorgement is not a remedy available to the government under the civil provisions of RICO and entered summary judgment in favor of defendants with respect to the disgorgement claim. In July 2005, the government petitioned the United States Supreme Court for further review of the Court of Appeals' ruling that disgorgement is not an available remedy, and in October 2005, the Supreme Court denied the petition.

In June 2005, the government filed with the trial court its proposed final judgment seeking remedies of approximately $14 billion, including $10 billion over a five-year period to fund a national smoking cessation program and $4 billion over a ten-year period to fund a public education and counter-marketing campaign. Further, the government's proposed remedy would have required defendants to pay additional monies to these programs if targeted reductions in the smoking rate of those under 21 are not achieved according to a prescribed timetable. The government's proposed remedies also included a series of measures and restrictions applicable to cigarette business operations, including, but not limited to, restrictions on advertising and marketing, potential measures with respect to certain price promotional activities and research and development, disclosure requirements for certain confidential data and implementation of a monitoring system with potential broad powers over cigarette operations.

In August 2006, the federal trial court entered judgment in favor of the government. The court held that certain defendants, including Altria Group, Inc. and PM USA, violated RICO and engaged in 7 of the 8 "sub-schemes" to defraud that the government had alleged. Specifically, the court found that:

- defendants falsely denied, distorted and minimized the significant adverse health consequences of smoking;

- defendants hid from the public that cigarette smoking and nicotine are addictive;

- defendants falsely denied that they control the level of nicotine delivered to create and sustain addiction;

- defendants falsely marketed and promoted "low tar/light" cigarettes as less harmful than full-flavor cigarettes;

- defendants falsely denied that they intentionally marketed to youth;

- defendants publicly and falsely denied that ETS is hazardous to non-smokers; and

- defendants suppressed scientific research.

The court did not impose monetary penalties on the defendants, but ordered the following relief: (i) an injunction against "committing any act of racketeering" relating to the manufacturing, marketing, promotion, health consequences or sale of cigarettes in the United States; (ii) an injunction against participating directly or indirectly in the management or control of the Council for Tobacco Research, the Tobacco Institute, or the Center for Indoor Air Research, or any successor or affiliated entities of each; (iii) an injunction against "making, or causing to be made in any way, any material false, misleading, or deceptive statement or representation or engaging in any public relations or marketing endeavor that is disseminated to the United States public and that misrepresents or suppresses information concerning cigarettes"; (iv) an injunction against conveying any express or implied health message through use of descriptors on cigarette packaging or in cigarette advertising or promotional material, including "lights," "ultra lights" and "low tar," which the court found could cause consumers to believe one cigarette brand is less hazardous than another brand; (v) the issuance of "corrective statements" in various media regarding the adverse health effects of smoking, the addictiveness of smoking and nicotine, the lack of any significant health benefit from smoking "low tar" or "light" cigarettes, defendants' manipulation of cigarette design to ensure optimum nicotine delivery and the adverse health effects of exposure to environmental tobacco smoke; (vi) the disclosure on defendants' public document websites and in the Minnesota document repository of all documents produced to the government in the lawsuit or produced in any future court or administrative action concerning smoking and health until 2021, with certain additional requirements as to documents withheld from production under a claim of privilege or confidentiality; (vii) the disclosure of disaggregated marketing data to the government in the same form and on the same schedule as defendants now follow in disclosing such data to the Federal Trade Commission (“FTC”) for a period of ten years; (viii) certain restrictions on the sale or transfer by defendants of any cigarette brands, brand names, formulas or cigarette businesses within the United States; and (ix) payment of the government's costs in bringing the action.

The defendants appealed and, in May 2009, a three judge panel of the Court of Appeals for the District of Columbia Circuit issued a per curiam decision largely affirming the trial court's judgment against defendants and in favor of the government. Although the panel largely affirmed the remedial order that was issued by the trial court, it vacated the following aspects of the order:

- its application to defendants' subsidiaries;
- the prohibition on the use of express or implied health messages or health descriptors, but only to the extent of extraterritorial application;
- its point-of-sale display provisions; and
- its application to Brown & Williamson Holdings.

The Court of Appeals panel remanded the case for the trial court to reconsider these four aspects of the injunction and to reformulate its remedial order accordingly.

Furthermore, the Court of Appeals panel rejected all of the government's and intervenors' cross appeal arguments and refused to broaden the remedial order entered by the trial court. The Court of Appeals panel also left undisturbed its prior holding that the government cannot obtain disgorgement as a permissible remedy under RICO.

In July 2009, defendants filed petitions for a rehearing before the panel and for a rehearing by the entire Court of Appeals. Defendants also filed a motion to vacate portions of the trial court's judgment on the grounds of mootness because of the passage of the Family Smoking Prevention and Tobacco Control Act ("FSPTCA"), granting the United States Food and Drug Administration (the "FDA") broad authority over the regulation of tobacco products. In September 2009, the Court of Appeals entered three per curiam rulings. Two of them denied defendants' petitions for panel rehearing or for rehearing en banc. In the third per curiam decision, the Court of Appeals denied defendants' suggestion of mootness and motion for partial vacatur. In February 2010, PM USA and Altria Group, Inc. filed their certiorari petitions with the United States Supreme Court. In addition, the federal government and the intervenors filed their own certiorari petitions, asking the court to reverse an earlier Court of Appeals decision and hold that civil RICO allows the trial court to order disgorgement as well as other equitable relief, such as smoking cessation remedies, designed to redress continuing consequences of prior RICO violations. In June 2010, the United States Supreme Court denied all of the parties' petitions. In July 2010, the Court of Appeals issued its mandate lifting the stay of the trial court's judgment and remanding the case to the trial court. As a result of the mandate, except for those matters remanded to the trial court for further proceedings, defendants are now subject to the injunction discussed above and the other elements of the trial court's judgment.

In February 2011, the government submitted its proposed corrective statements and the trial court referred issues relating to a document repository to a special master. The defendants filed a response to the government's proposed corrective statements and filed a motion to vacate the trial court's injunction in light of the FSPTCA, which motion was denied in June 2011. The defendants appealed the trial court's ruling to the United States Court of Appeals for the District of Columbia Circuit. On July 27, 2012, the Court of Appeals affirmed the district court's denial of the defendants' motion to vacate the district court's injunction.

Remaining issues pending before the district court include: (i) the substance of the court-ordered corrective statements and (ii) the requirements related to point-of-sale signage. In November 2011, the district court ordered the parties to submit their views on whether the district court should delay its order on these issues while other courts decide more recent cases challenging the FDA's new rules imposing certain tobacco marketing restrictions and graphic warnings. The parties complied with the district court's requests, and defendants asked the court to defer resolution of these issues until these other cases are fully resolved. In January 2012, the district court ruled that it would not delay its decision until after the resolution of the cases challenging the FDA's new rules. Proceedings continue related to the content of the corrective communications and the requirements related to point-of-sale signage and argument on the matter occurred on October 15, 2012.

In December 2011, the parties to the lawsuit entered into an agreement as to the issues concerning the document repository. Pursuant to this agreement, PM USA agreed to deposit an amount of approximately $3.1 million into the district court in installments over a five-year period.

"Lights/Ultra Lights" Cases

Overview

Plaintiffs in certain pending matters seek certification of their cases as class actions and allege, among other things, that the uses of the terms "Lights" and/or "Ultra Lights" constitute deceptive and unfair trade practices, common law fraud, or RICO violations, and seek injunctive and equitable relief, including restitution and, in certain cases, punitive damages. These class actions have been brought against PM USA and, in certain instances, Altria Group, Inc. or its subsidiaries, on behalf of individuals who purchased and consumed various brands of cigarettes, including Marlboro Lights, Marlboro Ultra Lights, Virginia Slims Lights and Superslims, Merit Lights and Cambridge Lights. Defenses raised in these cases include lack of misrepresentation, lack of causation, injury and damages, the statute of limitations, non-liability under state statutory provisions exempting conduct that complies with federal regulatory directives, and the First Amendment. As of October 25, 2012, a total of 14 such cases were pending in the United States. Three of these cases were pending in U.S. federal courts as discussed below. The other cases were pending in various U.S. state courts. In addition, a purported "Lights" class action is pending against PM USA in Israel.

In the one "Lights" case pending in Israel (El-Roy), hearings on plaintiffs' motion for class certification were held in November and December 2008, and an additional hearing on class certification was held in November 2011. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement between Altria Group, Inc. and PMI that provides for indemnities for certain liabilities concerning tobacco products.

The Good Case

In May 2006, a federal trial court in Maine granted PM USA's motion for summary judgment in Good, a purported "Lights" class action, on the grounds that plaintiffs' claims are preempted by the Federal Cigarette Labeling and Advertising Act ("FCLAA") and dismissed the case. In December 2008, the United States Supreme Court ruled that plaintiffs' claims are not barred by federal preemption. Although the Court rejected the argument that the FTC's actions were so extensive with respect to the descriptors that the state law claims were barred as a matter of federal law, the Court's decision was limited: it did not address the ultimate merits of plaintiffs' claim, the viability of the action as a class action, or other state law issues. The case was returned to the federal court in Maine and consolidated with other federal cases in the multidistrict litigation proceeding discussed below. In June 2011, the plaintiffs voluntarily dismissed the case without prejudice after the district court denied plaintiffs' motion for class certification, concluding the litigation.

Federal Multidistrict Proceeding and Subsequent Developments

Since the December 2008 United States Supreme Court decision in Good, and through October 25, 2012, 24 purported "Lights" class actions were served upon PM USA and, in certain cases, Altria Group, Inc. These cases were filed in 14 states, the U.S. Virgin Islands and the District of Columbia. All of these cases either were filed in federal court or were removed to federal court by PM USA and were transferred and consolidated by the Judicial Panel on Multidistrict Litigation ("JPMDL") before the United States District Court for the District of Maine for pretrial proceedings ("MDL proceeding").

In November 2010, the district court in the MDL proceeding denied plaintiffs' motion for class certification in four cases, covering the jurisdictions of California, the District of Columbia, Illinois and Maine. These jurisdictions were selected by the parties as sample cases, with two selected by plaintiffs and two selected by defendants. Plaintiffs sought appellate review of this decision but, in February 2011, the United States Court of Appeals for the First Circuit denied plaintiffs' petition for leave to appeal. Later that year, plaintiffs in 13 cases voluntarily dismissed without prejudice their cases. In April 2012, the JPMDL remanded the remaining four cases (Phillips, Tang, Wyatt and Cabbat) back to the federal district courts in which the suits originated.

In Phillips, which is now pending in the United States District Court for the Northern District of Ohio, defendants filed in

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June 2012 a motion for partial judgment on the pleadings on plaintiffs' class action consumer sales practices claims and a motion for judgment on the pleadings on plaintiffs' state deceptive trade practices claims. A hearing on plaintiff's motion for class certification is currently set for August 30, 2013.

In Tang, which was pending in the United States District Court for the Eastern District of New York, the plaintiffs voluntarily dismissed the case without prejudice on July 30, 2012, concluding the litigation.

In Cabbat, which is pending in the United States District Court for the District of Hawaii, plaintiffs on July 30, 2012 amended their complaint, adding a claim for unjust enrichment and dropping their claims for breach of express and implied warranty.

"Lights" Cases Dismissed, Not Certified or Ordered De-Certified

To date, in addition to the district court in the MDL proceeding, 16 courts in 17 "Lights" cases have refused to certify class actions, dismissed class action allegations, reversed prior class certification decisions or have entered judgment in favor of PM USA.

Trial courts in Arizona, Illinois, Kansas, New Jersey, New Mexico, Oregon, Tennessee and Washington have refused to grant class certification or have dismissed plaintiffs' class action allegations. Plaintiffs voluntarily dismissed a case in Michigan after a trial court dismissed the claims plaintiffs asserted under the Michigan Unfair Trade and Consumer Protection Act.

Several appellate courts have issued rulings that either affirmed rulings in favor of Altria Group, Inc. and/or PM USA or reversed rulings entered in favor of plaintiffs. In Florida, an intermediate appellate court overturned an order by a trial court that granted class certification in Hines. The Florida Supreme Court denied review in January 2008. The Supreme Court of Illinois has overturned a judgment that awarded damages to a certified class in the Price case. See The Price Case below for further discussion. In Louisiana, the United States Court of Appeals for the Fifth Circuit dismissed a purported "Lights" class action brought in Louisiana federal court (Sullivan) on the grounds that plaintiffs' claims were preempted by the FCLAA. In New York, the United States Court of Appeals for the Second Circuit overturned a decision by a New York trial court in Schwab that denied defendants' summary judgment motions and granted plaintiffs' motion for certification of a nationwide class of all United States residents that purchased cigarettes in the United States that were labeled "Light" or "Lights." In July 2010, plaintiffs in Schwab voluntarily dismissed the case with prejudice. In Ohio, the Ohio Supreme Court overturned class certifications in the Marrone and Phillips cases. Plaintiffs voluntarily dismissed without prejudice both cases in August 2009, but refiled in federal court (discussed above). The Supreme Court of Washington denied a motion for interlocutory review filed by the plaintiffs in the Davies case that sought review of an order by the trial court that refused to certify a class. Plaintiffs subsequently voluntarily dismissed the Davies case with prejudice. In August 2011, the United States Court of Appeals for the Seventh Circuit affirmed the Illinois federal district court's dismissal of "Lights" claims brought against PM USA in the Cleary case. In Curtis, a certified class action, in May 2012, the Minnesota Supreme Court affirmed the trial court's entry of summary judgment in favor of PM USA, concluding this litigation.

In Lawrence, on August 21, 2012, the New Hampshire Supreme Court reversed the trial court's order to certify a class and subsequently denied plaintiffs' rehearing petition. On October 26, 2012, the case was dismissed after plaintiffs filed a motion to dismiss the case with prejudice, concluding this litigation. See State Trial Court Class Certifications below for a discussion of this case.

In Oregon (Pearson), a state court denied plaintiff's motion for interlocutory review of the trial court's refusal to certify a class. In February 2007, PM USA filed a motion for summary judgment based on federal preemption and the Oregon statutory exemption. In September 2007, the district court granted PM USA's motion based on express preemption under the FCLAA, and plaintiffs appealed this dismissal and the class certification denial to the Oregon Court of Appeals. Argument was held in April 2010.

Other Developments

In December 2009, the state trial court in the Carroll (formerly known as Holmes) case (pending in Delaware) denied PM USA's motion for summary judgment based on an exemption provision in the Delaware Consumer Fraud Act. In January 2011, the trial court allowed the plaintiffs to file an amended complaint substituting class representatives and naming Altria

Group, Inc. and PMI as additional defendants. In July 2011, the parties stipulated to the dismissal without prejudice of Altria Group, Inc. and PMI. The stipulation is signed by the parties but not yet approved by the trial court. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement between Altria Group, Inc. and PMI that provides for indemnities for certain liabilities concerning tobacco products.

In June 2007, the United States Supreme Court reversed the lower court rulings in the Miner (formerly known as Watson) case that denied plaintiffs' motion to have the case heard in a state, as opposed to federal, trial court. The Supreme Court rejected defendants' contention that the case must be tried in federal court under the "federal officer" statute. The case was removed to federal court in Arkansas and the case was transferred to the MDL proceeding discussed above. In November 2010, the district court in the MDL proceeding remanded the case to Arkansas state court. In December 2011, the plaintiffs voluntarily dismissed their claims against Altria Group, Inc. without prejudice.

The Price Case

Trial in the Price case commenced in state court in Illinois in January 2003, and in March 2003, the judge found in favor of the plaintiff class and awarded $7.1 billion in compensatory damages and $3 billion in punitive damages against PM USA. In December 2005, the Illinois Supreme Court reversed the trial court's judgment in favor of the plaintiffs. In November 2006, the United States Supreme Court denied plaintiffs' petition for writ of certiorari and, in December 2006, the Circuit Court of Madison County enforced the Illinois Supreme Court's mandate and dismissed the case with prejudice.

In December 2008, plaintiffs filed with the trial court a petition for relief from the final judgment that was entered in favor of PM USA. Specifically, plaintiffs sought to vacate the judgment entered by the trial court on remand from the 2005 Illinois Supreme Court decision overturning the verdict on the ground that the United States Supreme Court's December 2008 decision in Good demonstrated that the Illinois Supreme Court's decision was "inaccurate." PM USA filed a motion to dismiss plaintiffs' petition and, in February 2009, the trial court granted PM USA's motion on the basis that the petition was not timely filed. In March 2009, the Price plaintiffs filed a notice of appeal with the Fifth Judicial District of the Appellate Court of Illinois. In February 2011, the intermediate appellate court ruled that the petition was timely filed and reversed the trial court's dismissal of the plaintiffs' petition and, in September 2011, the Illinois Supreme Court declined PM USA's petition for review. As a result, the case has returned to the trial court for proceedings on whether the court should grant the plaintiffs' petition to reopen the prior judgment. In February 2012, plaintiffs filed an amended petition, which PM USA opposed. Subsequently, in responding to PM USA's opposition to the amended petition, plaintiffs asked the trial court to reinstate the original judgment. A hearing on PM USA's opposition to plaintiffs' amended petition was held on August 21, 2012.

In June 2009, the plaintiff in an individual smoker lawsuit (Kelly) brought on behalf of an alleged smoker of "Lights" cigarettes in Madison County, Illinois state court filed a motion seeking a declaration that his claims under the Illinois Consumer Fraud Act are not (i) barred by the exemption in that statute based on his assertion that the Illinois Supreme Court's decision in Price is no longer good law in light of the decisions by the United States Supreme Court in Good and Watson, and (ii) preempted in light of the United States Supreme Court's decision in Good. In September 2009, the court granted plaintiff's motion as to federal preemption, but denied it with respect to the state statutory exemption.

State Trial Court Class Certifications

State trial courts have certified classes against PM USA in several jurisdictions. Over time, several such cases have been dismissed by the courts at the summary judgment stage. Certified class actions remain pending in California

(Brown, discussed below in Certain Other Tobacco-Related Litigation), Massachusetts (Aspinall), and Missouri (Larsen) and one was recently dismissed in New Hampshire (Lawrence). Significant developments in these cases include:

- Aspinall: In August 2004, the Massachusetts Supreme Judicial Court affirmed the class certification order. In August 2006, the trial court denied PM USA's motion for summary judgment and granted plaintiffs' motion for summary judgment on the defenses of federal preemption and a state law exemption to Massachusetts' consumer protection statute. On motion of the parties, the trial court subsequently reported its decision to deny summary judgment to the appeals court for review and stayed further proceedings pending completion of the appellate review. In December 2008, subsequent to the United States Supreme Court's decision in Good, the Massachusetts Supreme Judicial Court issued an order requesting that the parties advise the court within 30 days whether the Good decision is dispositive of federal preemption issues pending on appeal. In January 2009, PM USA notified

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the Massachusetts Supreme Judicial Court that Good is dispositive of the federal preemption issues on appeal, but requested further briefing on the state law statutory exemption issue. In March 2009, the Massachusetts Supreme Judicial Court affirmed the order denying summary judgment to PM USA and granting the plaintiffs' cross-motion. In January 2010, plaintiffs moved for partial summary judgment as to liability claiming collateral estoppel from the findings in the case brought by the Department of Justice (see Federal Government's Lawsuit described above). In March 2012, the trial court denied plaintiffs' motion.

- Larsen: In August 2005, a Missouri Court of Appeals affirmed the class certification order. In December 2009, the trial court denied plaintiffs' motion for reconsideration of the period during which potential class members can qualify to become part of the class. The class period remains 1995 through 2003. In June 2010, PM USA's motion for partial summary judgment regarding plaintiffs' request for punitive damages was denied. In April 2010, plaintiffs moved for partial summary judgment as to an element of liability in the case, claiming collateral estoppel from the findings in the case brought by the Department of Justice (see Federal Government's Lawsuit described above). The plaintiffs' motion was denied in December 2010. In June 2011, PM USA filed various summary judgment motions challenging the plaintiffs' claims. In August 2011, the trial court granted PM USA's motion for partial summary judgment, ruling that plaintiffs could not present a damages claim based on allegations that Marlboro Lights are more dangerous than Marlboro Reds. The trial court denied PM USA's remaining summary judgment motions. Trial in the case began in September 2011 and, in October 2011 the court declared a mistrial after the jury failed to reach a verdict. The court has continued the new trial through January 2014, with an exact date to be determined.

- Lawrence: In November 2010, the trial court certified a class consisting of all persons who purchased Marlboro Lights cigarettes in the state of New Hampshire at any time from the date the brand was introduced into commerce until the date trial in the case begins. PM USA's motion for reconsideration of this decision was denied in January 2011. In September 2011, the New Hampshire Supreme Court accepted review of the class certification decision. On August 21, 2012, the New Hampshire Supreme Court reversed the trial court decision, holding that the trial court abused its discretion in certifying the class. Plaintiffs' motion for reconsideration with the New Hampshire Supreme Court was denied on October 1, 2012. On October 26, 2012, the case was dismissed after plaintiffs filed a motion to dismiss the case with prejudice. This litigation has concluded.

Certain Other Tobacco-Related Litigation

Tobacco Price Case: One case remains pending in Kansas (Smith) in which plaintiffs allege that defendants, including PM USA and Altria Group, Inc., conspired to fix cigarette prices in violation of antitrust laws. Plaintiffs' motion for class certification was granted. In March 2012, the trial court granted defendants' motions for summary judgment. Plaintiffs sought the trial court's reconsideration of its decision, but in June 2012, the trial court denied plaintiffs' motion for reconsideration. Plaintiffs have appealed the decision, and the defendants have appealed the trial court's class certification decision, to the Court of Appeals of Kansas.

Case Under the California Business and Professions Code: In June 1997, a lawsuit (Brown) was filed in California state court alleging that domestic cigarette manufacturers, including PM USA and others, violated California Business and Professions Code Sections 17200 and 17500 regarding unfair, unlawful and fraudulent business practices. Class certification was granted as to plaintiffs' claims that class members are entitled to reimbursement of the costs of cigarettes purchased during the class periods and injunctive relief. In September 2004, the trial court granted defendants' motion for summary judgment as to plaintiffs' claims attacking defendants' cigarette advertising and promotion and denied defendants' motion for summary judgment on plaintiffs' claims based on allegedly false affirmative statements. In March 2005, the court granted defendants' motion to decertify the class based on a

California law, which, among other things, limits the ability to bring a lawsuit to only those plaintiffs who have "suffered injury in fact" and "lost money or property" as a result of defendants' alleged statutory violations ("Proposition 64").

In September 2006, an intermediate appellate court affirmed the trial court's order decertifying the class. In May 2009, the California Supreme Court reversed the trial court decision that was affirmed by the appellate court and remanded the case to the trial court. In March 2010, the trial court granted reconsideration of its September 2004 order granting partial summary judgment to defendants with respect to plaintiffs' "Lights" claims on the basis of judicial decisions issued since its order was issued, including the United States Supreme Court's ruling in Good, thereby reinstating plaintiffs' "Lights" claims. Since the trial court's prior ruling decertifying the class was reversed on appeal by the California Supreme Court, the parties and the court are treating all claims currently being asserted by the plaintiffs as certified, subject, however, to defendants' challenge to the class representatives' standing to assert their claims. The class is defined as people who, at the time they were residents of California, smoked in California one or more cigarettes between June 10, 1993 and April 23, 2001, and who were exposed to defendants' marketing and advertising activities in California.

In July 2010, plaintiffs filed a motion seeking collateral estoppel effect from the findings in the case brought by the Department of Justice (see Federal Government's Lawsuit described above). In September 2010, plaintiffs filed a motion for preliminary resolution of legal issues regarding restitutionary relief. The trial court denied both of plaintiffs' motions in November 2010. In November 2010, defendants filed a motion seeking a determination that Brown class members who were also part of the class in Daniels (a previously disclosed consumer fraud case in which the California Supreme Court affirmed summary judgment in PM USA's favor based on preemption and First Amendment grounds) are precluded by the Daniels judgment from recovering in Brown. This motion was denied in December 2010. Defendants sought review of this decision before the Fourth District Court of Appeal but were denied review in March 2011. In January 2012, defendants filed motions for a determination that the class representatives lack standing and are not typical or adequate to represent the class and to decertify the class. In May 2012, the trial court decertified the class as to plaintiffs' claims alleging that the defendants falsely denied nicotine manipulation and that they concealed the dangers and addictiveness of smoking, finding that none of the named representatives could adequately represent the class on these issues. The trial court denied defendants' decertification motion as to the claim regarding "Lights" cigarettes and found that only one of the four named class representatives may assert this claim. As a result, the case is proceeding as a "Lights"-only class action brought by the sole remaining class representative. In future reports, Altria Group, Inc. will report on this case in the discussion above on "Lights/Ultra Lights" Cases. The trial court also continued the trial date from October 5, 2012 to April 19, 2013. In July 2012, defendants filed a petition in the Court of Appeal asking the court to issue a writ of mandate ordering the trial court to vacate its denial of defendants' motion to decertify and instead to decertify the class. On September 26, 2012, at the plaintiffs' request, the trial court dismissed all defendants except PM USA from the lawsuit. On October 18, 2012, the Court of Appeal denied the defendants' petition to issue a writ of mandate.

Ignition Propensity Cases: PM USA is currently facing litigation alleging that a fire caused by cigarettes led to individuals' deaths. In a Kentucky case (Walker), the federal district court denied plaintiffs' motion to remand the case to state court and dismissed plaintiffs' claims in February 2009. Plaintiffs subsequently filed a notice of appeal. In October 2011, the United States Court of Appeals for the Sixth Circuit reversed the portion of the district court decision that denied remand of the case to Kentucky state court and remanded the case to Kentucky state court. The Sixth Circuit did not address the merits of the district court's dismissal order. Defendants' petition for rehearing with the Sixth Circuit was denied in December 2011.

False Claims Act Case: PM USA is a defendant in a qui tam action filed in the United States District Court for the District of Columbia (United States ex rel. Anthony Oliver) alleging violation of the False Claims Act in connection with sales of cigarettes to the U.S. military. The relator contends that PM USA violated "most favored customer" provisions in government contracts and regulations by selling cigarettes to non-military customers in overseas markets at more favorable prices than it sold to the U.S. military exchange services for resale on overseas military bases in those same markets. The relator has dropped Altria Group, Inc. as a defendant and has dropped claims related to post-MSA price increases on cigarettes sold to the U.S. military. On July 27, 2012, PM USA filed a motion to dismiss.

Argentine Grower Cases: PM USA and Altria Group, Inc. are defendants in two cases (Hupan) and (Chalanuk) filed in Delaware state court against multiple defendants by the parents of minor Argentine children born with alleged birth defects. Plaintiffs in these cases allege that they grew tobacco in Argentina under contract with Tabacos Norte S.A., an alleged subsidiary of PMI, and that they and their infant children were exposed directly and in utero to hazardous herbicides and pesticides used in the production and cultivation of tobacco. Plaintiffs seek compensatory and punitive damages against all defendants under U.S. and Argentine law. Altria Group, Inc. and PM USA are in discussions with PMI regarding indemnification for these cases pursuant to the Distribution Agreement between Altria Group, Inc. and PMI. See Guarantees and Other Similar Matters below for a discussion of the Distribution Agreement.

UST Litigation

Claims related to smokeless tobacco products generally fall within the following categories:

First, UST and/or its tobacco subsidiaries has been named in certain actions in West Virginia (See In re: Tobacco Litigation above) brought by or on behalf of individual plaintiffs against cigarette manufacturers, smokeless tobacco manufacturers, and other organizations seeking damages and other relief in connection with injuries allegedly sustained as a result of tobacco usage, including smokeless tobacco products. Included among the plaintiffs are five individuals alleging use of USSTC's smokeless tobacco products and alleging the types of injuries claimed to be associated with the use of smokeless tobacco products. USSTC, along with other non-cigarette manufacturers, has remained severed from such proceedings since December 2001.

Second, UST and/or its tobacco subsidiaries has been named in a number of other individual tobacco and health suits over time. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, such as negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of implied warranty, addiction, and breach of consumer protection statutes. Plaintiffs seek various forms of relief, including compensatory and punitive damages, and certain equitable relief, including but not limited to disgorgement. Defenses raised in these cases include lack of causation, assumption of the risk, comparative fault and/or contributory negligence, and statutes of limitations. USSTC is currently named in one such action in Florida (Vassallo).

Certain Other Actions

IRS Challenges to PMCC Leases

As discussed in Note 7. Segment Reporting, Note 8. Finance Assets, net and Note 10. Income Taxes above, Altria Group, Inc. entered into the Closing Agreement with the IRS in May 2012 that conclusively resolved the federal income tax treatment for all prior and future tax years of certain leveraged lease transactions (referred to by the IRS as lease-in/lease-out ("LILO") and sale-in/lease-out ("SILO") transactions) entered into by PMCC.

Pursuant to the Closing Agreement, Altria Group, Inc. paid $456 million in federal income taxes and related estimated interest with respect to the 2000 through 2010 tax years in June 2012. This payment is net of federal income taxes that Altria Group, Inc. paid on gains associated with sales of assets leased in the LILO and SILO transactions from January 1, 2008 through December 31, 2011. In addition, Altria Group, Inc. expects to pay approximately $50 million in state taxes and related estimated interest for the 2000 through 2010 tax years. The tax component of these payments represents an acceleration of federal and state income taxes that Altria Group, Inc. would have otherwise paid over the lease terms of the LILO and SILO transactions.

As described in previous reports, the IRS disallowed the tax benefits pertaining to PMCC's LILO and SILO transactions for the 1996 through 2003 tax years and was expected to disallow such benefits for the 2004 through 2009 tax years. Pursuant to the Closing Agreement, the IRS will not assess against Altria Group, Inc. any additional taxes or any penalties in any open tax year through the 2010 tax year related to the LILO and SILO transactions; nor will the IRS impose penalties with respect to any prior tax years. Altria Group, Inc. did not claim tax benefits pertaining to the LILO and SILO transactions in the 2010 and 2011 tax years and, under the terms of the Closing Agreement, will not claim such benefits in future tax years.

As previously reported in June 2011, Altria Group, Inc. recorded a one-time charge of $627 million against its reported earnings related to the tax treatment of the LILO and SILO transactions. In quantifying this charge, Altria Group, Inc. was required to make assumptions regarding the timing and terms of a potential settlement of this matter with the IRS. As a result of differences between those assumptions and the terms of the Closing Agreement, Altria Group, Inc. recorded a one-time net earnings benefit of $68 million during the second quarter of 2012 due primarily to lower than estimated interest expense on tax underpayments.

Pursuant to the Closing Agreement, Altria Group, Inc. also agreed to dismiss, with prejudice, the litigation in federal court related to the tax treatment of the LILO and SILO transactions and to relinquish its right to seek refunds for federal taxes and interest previously paid. The court entered the order of dismissal in May 2012 and Altria Group, Inc. reduced both Other assets and tax liabilities on its condensed consolidated balance sheet by approximately $750 million, which represents the remaining amount of federal taxes and interest that Altria Group, Inc. previously paid and accounted for as deposits pending the outcome of the LILO and SILO dispute.

Kraft Thrift Plan Cases: Four participants in the Kraft Foods Global, Inc. Thrift Plan ("Kraft Thrift Plan"), a defined contribution plan, filed a class action complaint (George II) on behalf of all participants and beneficiaries of the Kraft Thrift Plan in July 2008 in the United States District Court for the Northern District of Illinois alleging breach of fiduciary duty under the Employee Retirement Income Security Act ("ERISA"). Named defendants in this action included Altria

Corporate Services, Inc. (now Altria Client Services Inc.) and certain company committees that allegedly had a relationship to the Kraft Thrift Plan. Plaintiffs requested, among other remedies, that defendants restore to the Kraft Thrift Plan all losses improperly incurred.
In August 2011, Altria Client Services Inc. and a company committee that allegedly had a relationship to the Kraft Thrift Plan were added as defendants in another class action previously brought by the same plaintiffs in 2006 (George I), in which plaintiffs allege defendants breached their fiduciary duties under ERISA by offering company stock funds in a unitized format and by allegedly overpaying for recordkeeping services.
The parties have reached a court-approved class-wide settlement for George I and George II that does not require any payment by the Altria Group, Inc. defendants. In June 2012, the class-wide settlement for both cases was approved and a final order and judgment was issued, concluding this litigation.

Environmental Regulation

Altria Group, Inc. and its subsidiaries (and former subsidiaries) are subject to various federal, state and local laws and regulations concerning the discharge of materials into the environment, or otherwise related to environmental protection, including, in the United States: The Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act and the Comprehensive Environmental Response, Compensation and Liability Act (commonly known as "Superfund"), which can impose joint and several liability on each responsible party. Subsidiaries (and former subsidiaries) of Altria Group, Inc. are involved in several matters subjecting them to potential costs of remediation and natural resource damages under Superfund or other laws and regulations. Altria Group, Inc.'s subsidiaries expect to continue to make capital and other expenditures in connection with environmental laws and regulations.

Altria Group, Inc. provides for expenses associated with environmental remediation obligations on an undiscounted basis when such amounts are probable and can be reasonably estimated. Such accruals are adjusted as new information develops or circumstances change. Other than those amounts, it is not possible to reasonably estimate the cost of any environmental remediation and compliance efforts that subsidiaries of Altria Group, Inc. may undertake in the future. In the opinion of management, however, compliance with environmental laws and regulations, including the payment of any remediation costs or damages and the making of related expenditures, has not had, and is not expected to have, a material adverse effect on Altria Group, Inc.'s consolidated results of operations, capital expenditures, financial position or cash flows.

Guarantees and Other Similar Matters

In the ordinary course of business, certain subsidiaries of Altria Group, Inc. have agreed to indemnify a limited number of third parties in the event of future litigation. At September 30, 2012, subsidiaries of Altria Group, Inc. were also contingently liable for $32 million of guarantees related to their own performance, consisting primarily of surety bonds. In addition, from time to time, subsidiaries of Altria Group, Inc. issue lines of credit to affiliated entities. These items have not had, and are not expected to have, a significant impact on Altria Group, Inc.'s liquidity.

Under the terms of a distribution agreement between Altria Group, Inc. and PMI (the "Distribution Agreement"), entered into as a result of Altria Group, Inc.'s 2008 spin-off of its former subsidiary PMI, liabilities concerning tobacco products will be allocated based in substantial part on the manufacturer. PMI will indemnify Altria Group, Inc. and PM USA for liabilities related to tobacco products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for liabilities related to tobacco products manufactured by PM USA, excluding tobacco products contract manufactured for PMI. Altria Group, Inc. does not have a related liability recorded on its condensed consolidated balance sheet at September 30, 2012 as the fair value of this indemnification is insignificant.

As more fully discussed in Note 12. Condensed Consolidating Financial Information, PM USA has issued guarantees relating to Altria Group, Inc.'s obligations under its outstanding debt securities, borrowings under its senior unsecured 5-year revolving credit agreement (the "Credit Agreement") and amounts outstanding under its commercial paper program.

Redeemable Noncontrolling Interest

In September 2007, Ste. Michelle completed the acquisition of Stag's Leap Wine Cellars through one of its consolidated subsidiaries, Michelle-Antinori, LLC ("Michelle-Antinori"), in which Ste. Michelle holds an 85% ownership interest with a

15% noncontrolling interest held by Antinori California ("Antinori"). In connection with the acquisition of Stag's Leap Wine Cellars, Ste. Michelle entered into a put arrangement with Antinori. The put arrangement, as later amended, provides Antinori with the right to require Ste. Michelle to purchase its 15% ownership interest in Michelle-Antinori at a price equal to Antinori's initial investment of $27 million. The put arrangement became exercisable on September 11, 2010 and has no expiration date. As of September 30, 2012, the redemption value of the put arrangement did not exceed the noncontrolling interest balance. Therefore, no adjustment to the value of the redeemable noncontrolling interest was recognized on the condensed consolidated balance sheet for the put arrangement.

The noncontrolling interest put arrangement is accounted for as mandatorily redeemable securities because redemption is outside of the control of Ste. Michelle. As such, the redeemable noncontrolling interest is reported in the mezzanine equity section on the condensed consolidated balance sheets at September 30, 2012 and December 31, 2011.

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Note 12. Condensed Consolidating Financial Information:

PM USA, which is a wholly-owned subsidiary of Altria Group, Inc., has issued guarantees relating to Altria Group, Inc.'s obligations under its outstanding debt securities, borrowings under its Credit Agreement and amounts outstanding under its commercial paper program (the “Guarantees”). Pursuant to the Guarantees, PM USA fully and unconditionally guarantees, as primary obligor, the payment and performance of Altria Group, Inc.'s obligations under the guaranteed debt instruments (the “Obligations”), subject to release under certain customary circumstances as noted below.

The Guarantees provide that PM USA guarantees the punctual payment when due, whether at stated maturity, by acceleration or otherwise, of the Obligations. The liability of PM USA under the Guarantees is absolute and unconditional irrespective of: any lack of validity, enforceability or genuineness of any provision of any agreement or instrument relating thereto; any change in the time, manner or place of payment of, or in any other term of, all or any of the Obligations, or any other amendment or waiver of or any consent to departure from any agreement or instrument relating thereto; any exchange, release or non-perfection of any collateral, or any release or amendment or waiver of or consent to departure from any other guarantee, for all or any of the Obligations; or any other circumstance that might otherwise constitute a defense available to, or a discharge of, Altria Group, Inc. or PM USA.

The obligations of PM USA under the Guarantees are limited to the maximum amount as will, after giving effect to such maximum amount and all other contingent and fixed liabilities of PM USA that are relevant under Bankruptcy Law, the Uniform Fraudulent Conveyance Act, the Uniform Fraudulent Transfer Act or any similar federal or state law to the extent applicable to the Guarantees, result in PM USA's obligations under the Guarantees not constituting a fraudulent transfer or conveyance. For this purpose, “Bankruptcy Law” means Title 11, U.S. Code, or any similar federal or state law for the relief of debtors.

PM USA will be unconditionally released and discharged from its obligations under each of the Guarantees upon the earliest to occur of:

- the date, if any, on which PM USA consolidates with or merges into Altria Group, Inc. or any successor;
- the date, if any, on which Altria Group, Inc. or any successor consolidates with or merges into PM USA;
- the payment in full of the Obligations pertaining to such Guarantees; and
- the rating of Altria Group, Inc.'s long-term senior unsecured debt by Standard & Poor's of A or higher.

At September 30, 2012, the respective principal wholly-owned subsidiaries of Altria Group, Inc. and PM USA were not limited by long-term debt or other agreements in their ability to pay cash dividends or make other distributions with respect to their common stock.

The following sets forth the condensed consolidating balance sheets as of September 30, 2012 and December 31, 2011, condensed consolidating statements of earnings and comprehensive earnings for the nine and three months ended September 30, 2012 and 2011, and condensed consolidating statements of cash flows for the nine months ended September 30, 2012 and 2011 for Altria Group, Inc., PM USA and Altria Group, Inc.'s other subsidiaries that are not guarantors of Altria Group, Inc.’s debt instruments (the “Non-Guarantor Subsidiaries”). The financial information is based on Altria Group, Inc.'s understanding of the Securities and Exchange Commission ("SEC") interpretation and application of Rule 3-10 of SEC Regulation S-X.

The financial information may not necessarily be indicative of results of operations or financial position had PM USA and the Non-Guarantor Subsidiaries operated as independent entities. Altria Group, Inc. and PM USA account for investments in their subsidiaries under the equity method of accounting.

Certain prior-period amounts have been recast to conform with the current-period presentation, due to Middleton becoming a wholly-owned subsidiary of PM USA effective January 1, 2012.

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Beginning in the second quarter of 2012, Altria Group, Inc. revised the classification of cash dividends received from subsidiaries on its condensed consolidating statements of cash flows to present them as cash flows from operating activities. These amounts were previously classified as cash flows from financing activities. As other prior period financial information is presented, Altria Group, Inc. will similarly revise the condensed consolidating statements of cash flows in its future filings. The impact of this revision, which Altria Group, Inc. determined is not material to the related financial statements, is to increase cash inflows from operating activities (and decrease cash inflows from financing activities) for Altria Group, Inc. and PM USA as follows:

	Altria Group, Inc.	PM USA
	(in millions)	
For the years ended:		
December 31, 2011	$3,666	$213
December 31, 2010	$3,438	$179
December 31, 2009	$3,711	$136
For the:		
Three months ended March 31, 2012	$923	$59
Nine months ended September 30, 2011	$2,702	$110
Three months ended March 31, 2011	$890	$26

There was no impact on Altria Group, Inc.'s consolidated statements of cash flows.

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Condensed Consolidating Balance Sheets
September 30, 2012
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Assets					
Consumer products					
Cash and cash equivalents	$2,153	$—	$33	$—	$2,186
Receivables	97	11	88	—	196
Inventories:					
Leaf tobacco	—	416	336	—	752
Other raw materials	—	133	49	—	182
Work in process	—	8	253	—	261
Finished product	—	162	267	—	429
	—	719	905	—	1,624
Due from Altria Group, Inc. and subsidiaries	1,108	2,851	881	(4,840)	—
Deferred income taxes	9	1,245	33	—	1,287
Other current assets	270	341	30	—	641
Total current assets	3,637	5,167	1,970	(4,840)	5,934
Property, plant and equipment, at cost	2	3,243	1,474	—	4,719
Less accumulated depreciation	2	2,047	559	—	2,608
	—	1,196	915	—	2,111
Goodwill	—	—	5,174	—	5,174
Other intangible assets, net	—	2	12,081	—	12,083
Investment in SABMiller	6,468	—	—	—	6,468
Investment in consolidated subsidiaries	9,723	3,017	—	(12,740)	—
Due from Altria Group, Inc. and subsidiaries	4,500	—	—	(4,500)	—
Other assets	138	505	111	(335)	419
Total consumer products assets	24,466	9,887	20,251	(22,415)	32,189
Financial services					
Finance assets, net	—	—	2,805	—	2,805
Other assets	—	—	44	—	44
Total financial services assets	—	—	2,849	—	2,849
Total Assets	$24,466	$9,887	$23,100	$(22,415)	$35,038

Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
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Condensed Consolidating Balance Sheets (Continued)
September 30, 2012
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Liabilities					
Consumer products					
Accounts payable	$3	$122	$164	$—	$289
Accrued liabilities:					
Marketing	—	512	14	—	526
Taxes, except income taxes	—	57	8	—	65
Employment costs	25	9	112	—	146
Settlement charges	—	3,230	6	—	3,236
Other	342	533	316	—	1,191
Dividends payable	895	—	—	—	895
Due to Altria Group, Inc. and subsidiaries	3,279	355	1,030	(4,664)	—
Total current liabilities	4,544	4,818	1,650	(4,664)	6,348
Long-term debt	13,579	—	299	—	13,878
Deferred income taxes	2,038	—	3,392	(335)	5,095
Accrued pension costs	220	—	891	—	1,111
Accrued postretirement health care costs	—	1,553	811	—	2,364
Due to Altria Group, Inc. and subsidiaries	—	—	4,500	(4,500)	—
Other liabilities	219	190	151	—	560
Total consumer products liabilities	20,600	6,561	11,694	(9,499)	29,356
Financial services					
Deferred income taxes	—	—	1,720	—	1,720
Due to Altria Group, Inc. and subsidiaries	—	—	176	(176)	—
Other liabilities	—	—	61	—	61
Total financial services liabilities	—	—	1,957	(176)	1,781
Total liabilities	20,600	6,561	13,651	(9,675)	31,137
Contingencies					
Redeemable noncontrolling interest	—	—	33	—	33
Stockholders' Equity					
Common stock	935	—	9	(9)	935
Additional paid-in capital	5,670	3,321	10,220	(13,541)	5,670
Earnings reinvested in the business	24,098	308	751	(1,059)	24,098
Accumulated other comprehensive losses	(1,604)	(303)	(1,566)	1,869	(1,604)
Cost of repurchased stock	(25,233)	—	—	—	(25,233)
Total stockholders' equity attributable to Altria Group, Inc.	3,866	3,326	9,414	(12,740)	3,866
Noncontrolling interests	—	—	2	—	2
Total stockholders' equity	3,866	3,326	9,416	(12,740)	3,868
Total Liabilities and Stockholders' Equity	$24,466	$9,887	$23,100	$(22,415)	$35,038

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Balance Sheets
December 31, 2011
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Assets					
Consumer products					
Cash and cash equivalents	$3,245	$—	$25	$—	$3,270
Receivables	174	16	78	—	268
Inventories:					
Leaf tobacco	—	565	369	—	934
Other raw materials	—	128	42	—	170
Work in process	—	4	312	—	316
Finished product	—	126	233	—	359
	—	823	956	—	1,779
Due from Altria Group, Inc. and subsidiaries	403	3,007	1,765	(5,175)	—
Deferred income taxes	9	1,157	41	—	1,207
Other current assets	6	430	247	(76)	607
Total current assets	3,837	5,433	3,112	(5,251)	7,131
Property, plant and equipment, at cost	2	3,280	1,446	—	4,728
Less accumulated depreciation	2	2,005	505	—	2,512
	—	1,275	941	—	2,216
Goodwill	—	—	5,174	—	5,174
Other intangible assets, net	—	2	12,096	—	12,098
Investment in SABMiller	5,509	—	—	—	5,509
Investment in consolidated subsidiaries	7,009	3,035	—	(10,044)	—
Due from Altria Group, Inc. and subsidiaries	6,500	—	—	(6,500)	—
Other assets	941	586	111	(381)	1,257
Total consumer products assets	23,796	10,331	21,434	(22,176)	33,385
Financial services					
Finance assets, net	—	—	3,559	—	3,559
Due from Altria Group, Inc. and subsidiaries	—	—	292	(292)	—
Other assets	—	—	18	—	18
Total financial services assets	—	—	3,869	(292)	3,577
Total Assets	$23,796	$10,331	$25,303	$ (22,468)	$36,962

Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Balance Sheets (Continued)
December 31, 2011
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Liabilities					
Consumer products					
Current portion of long-term debt	$—	$—	$600	$—	$600
Accounts payable	69	159	275	—	503
Accrued liabilities:					
Marketing	—	390	40	—	430
Taxes, except income taxes	—	209	11	—	220
Employment costs	29	12	184	—	225
Settlement charges	—	3,508	5	—	3,513
Other	384	620	383	(76)	1,311
Dividends payable	841	—	—	—	841
Due to Altria Group, Inc. and subsidiaries	3,792	474	1,201	(5,467)	—
Total current liabilities	5,115	5,372	2,699	(5,543)	7,643
Long-term debt	12,790	—	299	—	13,089
Deferred income taxes	1,787	—	3,345	(381)	4,751
Accrued pension costs	236	—	1,426	—	1,662
Accrued postretirement health care costs	—	1,562	797	—	2,359
Due to Altria Group, Inc. and subsidiaries	—	—	6,500	(6,500)	—
Other liabilities	188	216	198	—	602
Total consumer products liabilities	20,116	7,150	15,264	(12,424)	30,106
Financial services					
Deferred income taxes	—	—	2,811	—	2,811
Other liabilities	—	—	330	—	330
Total financial services liabilities	—	—	3,141	—	3,141
Total liabilities	20,116	7,150	18,405	(12,424)	33,247
Contingencies					
Redeemable noncontrolling interest	—	—	32	—	32
Stockholders' Equity					
Common stock	935	—	9	(9)	935
Additional paid-in capital	5,674	3,283	8,238	(11,521)	5,674
Earnings reinvested in the business	23,583	210	265	(475)	23,583
Accumulated other comprehensive losses	(1,887)	(312)	(1,649)	1,961	(1,887)
Cost of repurchased stock	(24,625)	—	—	—	(24,625)
Total stockholders' equity attributable to Altria Group, Inc.	3,680	3,181	6,863	(10,044)	3,680
Noncontrolling interests	—	—	3	—	3
Total stockholders' equity	3,680	3,181	6,866	(10,044)	3,683
Total Liabilities and Stockholders' Equity	$23,796	$10,331	$25,303	$(22,468)	$36,962

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Earnings and Comprehensive Earnings
For the Nine Months Ended September 30, 2012
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Net revenues	$—	$16,090	$2,304	$(18)	$18,376
Cost of sales	—	5,238	640	(18)	5,860
Excise taxes on products	—	5,117	219	—	5,336
Gross profit	—	5,735	1,445	—	7,180
Marketing, administration and research costs	148	1,382	148	—	1,678
Changes to Mondelēz and PMI tax-related receivables	(48)	—	—	—	(48)
Asset impairment and exit costs	1	45	1	—	47
Amortization of intangibles	—	—	15	—	15
Operating (expense) income	(101)	4,308	1,281	—	5,488
Interest and other debt expense (income), net	548	(2)	322	—	868
Loss on early extinguishment of debt	874	—	—	—	874
Earnings from equity investment in SABMiller	(973)	—	—	—	(973)
(Loss) earnings before income taxes and equity earnings of subsidiaries	(550)	4,310	959	—	4,719
(Benefit) provision for income taxes	(240)	1,567	314	—	1,641
Equity earnings of subsidiaries	3,387	163	—	(3,550)	—
Net earnings	3,077	2,906	645	(3,550)	3,078
Net earnings attributable to noncontrolling interests	—	—	(1)	—	(1)
Net earnings attributable to Altria Group, Inc.	$3,077	$2,906	$644	$(3,550)	$3,077
Net earnings	$3,077	$2,906	$645	$(3,550)	$3,078
Other comprehensive earnings, net of deferred income taxes	283	10	82	(92)	283
Comprehensive earnings	3,360	2,916	727	(3,642)	3,361
Comprehensive earnings attributable to noncontrolling interests	—	—	(1)	—	(1)
Comprehensive earnings attributable to Altria Group, Inc.	$3,360	$2,916	$726	$(3,642)	$3,360

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Earnings and Comprehensive Earnings
For The Nine Months Ended September 30, 2011
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Net revenues	$—	$16,009	$1,681	$(19)	$17,671
Cost of sales	—	5,139	588	(19)	5,708
Excise taxes on products	—	5,139	259	—	5,398
Gross profit	—	5,731	834	—	6,565
Marketing, administration and research costs	133	1,551	169	—	1,853
Changes to Mondelēz and PMI tax-related receivables	(19)	—	—	—	(19)
Asset impairment and exit costs	—	3	—	—	3
Amortization of intangibles	—	—	16	—	16
Operating (expense) income	(114)	4,177	649	—	4,712
Interest and other debt expense, net	517	5	343	—	865
Earnings from equity investment in SABMiller	(552)	—	—	—	(552)
(Loss) earnings before income taxes and equity earnings of subsidiaries	(79)	4,172	306	—	4,399
(Benefit) provision for income taxes	(122)	1,569	396	—	1,843
Equity earnings of subsidiaries	2,511	116	—	(2,627)	—
Net earnings (loss)	2,554	2,719	(90)	(2,627)	2,556
Net earnings attributable to noncontrolling interests	—	—	(2)	—	(2)
Net earnings (loss) attributable to Altria Group, Inc.	$2,554	$2,719	$(92)	$(2,627)	$2,554
Net earnings (loss)	$2,554	$2,719	$(90)	$(2,627)	$2,556
Other comprehensive earnings, net of deferred income taxes	23	12	80	(92)	23
Comprehensive earnings (losses)	2,577	2,731	(10)	(2,719)	2,579
Comprehensive earnings attributable to noncontrolling interests	—	—	(2)	—	(2)
Comprehensive earnings (losses) attributable to Altria Group, Inc.	$2,577	$2,731	$(12)	$(2,719)	$2,577

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Earnings and Comprehensive Earnings
For the Three Months Ended September 30, 2012
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Net revenues	$—	$5,444	$804	$(6)	$6,242
Cost of sales	—	1,763	225	(6)	1,982
Excise taxes on products	—	1,706	70	—	1,776
Gross profit	—	1,975	509	—	2,484
Marketing, administration and research costs	61	464	23	—	548
Changes to Mondelēz and PMI tax-related receivables	(48)	—	—	—	(48)
Asset impairment and exit costs	1	9	—	—	10
Amortization of intangibles	—	—	5	—	5
Operating (expense) income	(14)	1,502	481	—	1,969
Interest and other debt expense (income), net	181	(1)	102	—	282
Loss on early extinguishment of debt	874	—	—	—	874
Earnings from equity investment in SABMiller	(230)	—	—	—	(230)
(Loss) earnings before income taxes and equity earnings of subsidiaries	(839)	1,503	379	—	1,043
(Benefit) provision for income taxes	(295)	527	154	—	386
Equity earnings of subsidiaries	1,201	56	—	(1,257)	—
Net earnings	657	1,032	225	(1,257)	657
Net earnings attributable to noncontrolling interests	—	—	—	—	—
Net earnings attributable to Altria Group, Inc.	$657	$1,032	$225	$(1,257)	$657
Net earnings	$657	$1,032	$225	$(1,257)	$657
Other comprehensive earnings, net of deferred income taxes	70	4	31	(35)	70
Comprehensive earnings	727	1,036	256	(1,292)	727
Comprehensive earnings attributable to noncontrolling interests	—	—	—	—	—
Comprehensive earnings attributable to Altria Group, Inc.	$727	$1,036	$256	$(1,292)	$727

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Earnings and Comprehensive Earnings
For The Three Months Ended September 30, 2011
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Net revenues	$—	$5,311	$804	$(7)	$6,108
Cost of sales	—	1,684	206	(7)	1,883
Excise taxes on products	—	1,687	93	—	1,780
Gross profit	—	1,940	505	—	2,445
Marketing, administration and research costs	49	499	33	—	581
Changes to Mondelēz and PMI tax-related receivables	(19)	—	—	—	(19)
Amortization of intangibles	—	—	5	—	5
Operating (expense) income	(30)	1,441	467	—	1,878
Interest and other debt expense, net	177	1	115	—	293
Earnings from equity investment in SABMiller	(208)	—	—	—	(208)
Earnings before income taxes and equity earnings of subsidiaries	1	1,440	352	—	1,793
(Benefit) provision for income taxes	(51)	553	117	—	619
Equity earnings of subsidiaries	1,121	49	—	(1,170)	—
Net earnings	1,173	936	235	(1,170)	1,174
Net earnings attributable to noncontrolling interests	—	—	(1)	—	(1)
Net earnings attributable to Altria Group, Inc.	$1,173	$936	$234	$(1,170)	$1,173
Net earnings	$1,173	$936	$235	$(1,170)	$1,174
Other comprehensive (losses) earnings, net of deferred income taxes	(182)	5	27	(32)	(182)
Comprehensive earnings	991	941	262	(1,202)	992
Comprehensive earnings attributable to noncontrolling interests	—	—	(1)	—	(1)
Comprehensive earnings attributable to Altria Group, Inc.	$991	$941	$261	$(1,202)	$991

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Cash Flows
For the Nine Months Ended September 30, 2012
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Cash Provided by Operating Activities					
Net cash provided by operating activities	$1,883	$2,814	$382	$(2,959)	$2,120
Cash Provided by (Used In) Investing Activities					
Consumer products					
Capital expenditures	—	(18)	(59)	—	(77)
Other	—	—	(8)	—	(8)
Financial services					
Proceeds from finance assets	—	—	813	—	813
Net cash (used in) provided by investing activities	—	(18)	746	—	728
Cash Provided by (Used In) Financing Activities					
Consumer products					
Long-term debt issued	2,787	—	—	—	2,787
Long-term debt repaid	(2,000)	—	(600)	—	(2,600)
Repurchases of common stock	(595)	—	—	—	(595)
Dividends paid on common stock	(2,508)	—	—	—	(2,508)
Issuances of common stock	—	—	—	—	—
Changes in amounts due to/from Altria Group, Inc. and subsidiaries	220	17	(237)	—	—
Financing fees and debt issuance costs	(22)	—	—	—	(22)
Tender premiums and fees related to early extinguishment of debt	(864)	—	—	—	(864)
Cash dividends paid to parent	—	(2,774)	(185)	2,959	—
Other	7	(39)	(98)	—	(130)
Net cash used in financing activities	(2,975)	(2,796)	(1,120)	2,959	(3,932)
Cash and cash equivalents:					
(Decrease) increase	(1,092)	—	8	—	(1,084)
Balance at beginning of period	3,245	—	25	—	3,270
Balance at end of period	$2,153	$—	$33	$—	$2,186

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Altria Group, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Condensed Consolidating Statements of Cash Flows
For The Nine Months Ended September 30, 2011
(in millions of dollars)

	Altria Group, Inc.	PM USA	Non-Guarantor Subsidiaries	Total Consolidating Adjustments	Consolidated
Cash Provided by Operating Activities					
Net cash provided by operating activities	$2,596	$2,663	$117	$(2,812)	$2,564
Cash Provided by (Used In) Investing Activities					
Consumer products					
Capital expenditures	—	(16)	(59)	—	(75)
Other	—	1	—	—	1
Financial services					
Proceeds from finance assets	—	—	248	—	248
Net cash (used in) provided by investing activities	—	(15)	189	—	174
Cash Provided by (Used In) Financing Activities					
Consumer products					
Long-term debt issued	1,494	—	—	—	1,494
Repurchases of common stock	(1,000)	—	—	—	(1,000)
Dividends paid on common stock	(2,379)	—	—	—	(2,379)
Issuances of common stock	29	—	—	—	29
Changes in amounts due to/from Altria Group, Inc. and subsidiaries	(34)	150	(116)	—	—
Financing fees and debt issuance costs	(24)	—	—	—	(24)
Cash dividends paid to parent	—	(2,702)	(110)	2,812	—
Other	35	(96)	(68)	—	(129)
Net cash used in financing activities	(1,879)	(2,648)	(294)	2,812	(2,009)
Cash and cash equivalents:					
Increase	717	—	12	—	729
Balance at beginning of period	2,298	—	16	—	2,314
Balance at end of period	$3,015	$—	$28	$—	$3,043

Note 13. Recent Accounting Guidance Not Yet Adopted:

In July 2012, the Financial Accounting Standards Board ("FASB") issued authoritative guidance with an option that simplifies how entities test indefinite-lived intangible assets for impairment. The guidance permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform the currently required quantitative impairment test. The new guidance is effective for interim and annual impairment tests performed for fiscal years beginning after September 15, 2012; however, early adoption is permitted. Altria Group, Inc. intends to perform the quantitative impairment test under existing guidance for the 2012 annual indefinite-lived intangible asset impairment test and will evaluate the impact of performing a qualitative assessment in 2013.

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Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Description of the Company

At September 30, 2012, Altria Group, Inc.'s direct and indirect wholly-owned subsidiaries included Philip Morris USA Inc. ("PM USA"), which is engaged in the manufacture and sale of cigarettes and certain smokeless products in the United States; John Middleton Co. ("Middleton"), which is engaged in the manufacture and sale of machine-made large cigars and pipe tobacco, and is a wholly-owned subsidiary of PM USA; and UST LLC ("UST"), which through its direct and indirect wholly-owned subsidiaries, including U.S. Smokeless Tobacco Company LLC ("USSTC") and Ste. Michelle Wine Estates Ltd. ("Ste. Michelle"), is engaged in the manufacture and sale of smokeless products and wine. Philip Morris Capital Corporation ("PMCC"), another wholly-owned subsidiary of Altria Group, Inc., maintains a portfolio of leveraged and direct finance leases. In addition, Altria Group, Inc. held an approximate 27.0% economic and voting interest in SABMiller plc ("SABMiller") at September 30, 2012, which is accounted for under the equity method of accounting. Altria Group, Inc.'s access to the operating cash flows of its wholly-owned subsidiaries consists of cash received from the payment of dividends and distributions, and the payment of interest on intercompany loans by its subsidiaries. In addition, Altria Group, Inc. receives cash dividends on its interest in SABMiller if and when SABMiller pays such dividends. At September 30, 2012, Altria Group, Inc.'s principal wholly-owned subsidiaries were not limited by long-term debt or other agreements in their ability to pay cash dividends or make other distributions with respect to their common stock.

Altria Group, Inc.'s chief operating decision maker has been evaluating the operating results of the former cigarettes and cigars segments as a single smokeable products segment since January 1, 2012. The combination of these two formerly separate segments is related to the restructuring associated with a cost reduction program announced in October 2011 (the "2011 Cost Reduction Program"). Also, in connection with the 2011 Cost Reduction Program, effective January 1, 2012, Middleton became a wholly-owned subsidiary of PM USA, reflecting management's goal to achieve efficiencies in the management of these businesses. Effective with the first quarter of 2012, Altria Group, Inc.'s reportable segments are smokeable products, smokeless products, wine and financial services. As a result of the revised reportable segments and Middleton becoming a wholly-owned subsidiary of PM USA, certain prior period amounts have been recast to conform with the current-period presentation. For further discussion on the 2011 Cost Reduction Program, see Note 2. Asset Impairment, Exit, Implementation and Integration Costs to the condensed consolidated financial statements ("Note 2").

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Executive Summary

The following executive summary is intended to provide significant highlights of the Discussion and Analysis that follows.

Consolidated Results of Operations for the Nine Months Ended September 30, 2012: The changes in Altria Group, Inc.'s net earnings and diluted earnings per share ("EPS") attributable to Altria Group, Inc. for the nine months ended September 30, 2012, from the nine months ended September 30, 2011, were due primarily to the following:

	Net Earnings	Diluted EPS
	(in millions, except per share data)	
For the nine months ended September 30, 2011	$2,554	$1.23
2011 Asset impairment, exit and integration costs	4	—
2011 SABMiller special items	24	0.01
2011 PMCC leveraged lease charge	627	0.30
2011 Tobacco and health judgments	24	0.01
2011 UST acquisition-related costs	4	—
2011 Tax items (*)	(24)	(0.01)
Subtotal 2011 special items	659	0.31
2012 Asset impairment, exit and implementation costs	(25)	(0.01)
2012 SABMiller special items	172	0.08
2012 PMCC leveraged lease benefit	68	0.03
2012 Tobacco and health judgments	(3)	—
2012 Loss on early extinguishment of debt	(559)	(0.28)
2012 Tax items (*)	51	0.03
Subtotal 2012 special items	(296)	(0.15)
Fewer shares outstanding	—	0.04
Change in tax rate	(84)	(0.04)
Operations	244	0.12
For the nine months ended September 30, 2012	$3,077	$1.51

(*) Excludes the tax impact included in the PMCC leveraged lease benefit/charge.
See discussion of events affecting the comparability of statement of earnings amounts in the Consolidated Operating Results section of the following Discussion and Analysis.

Fewer Shares Outstanding: Fewer shares outstanding during the nine months ended September 30, 2012 compared with the prior-year period were due primarily to shares repurchased by Altria Group, Inc. under its share repurchase programs.

Change in Tax Rate: The change in tax rate was due primarily to a reduction in certain consolidated tax benefits resulting from the third quarter of 2012 debt tender offer.

Operations: The increase of $244 million shown in the table above was due primarily to the following:

- higher income from the smokeable products, financial services and smokeless products segments; and

- higher equity earnings from SABMiller.

For further details, see the Consolidated Operating Results and Operating Results by Business Segment sections of the following Discussion and Analysis.

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Consolidated Results of Operations for the Three Months Ended September 30, 2012: The changes in Altria Group, Inc.'s net earnings and diluted EPS attributable to Altria Group, Inc. for the three months ended September 30, 2012, from the three months ended September 30, 2011, were due primarily to the following:

	Net Earnings	Diluted EPS
	(in millions, except per share data)	
For the three months ended September 30, 2011	$1,173	$0.57
2011 Integration costs	1	—
2011 SABMiller special items	8	—
2011 UST acquisition-related costs	1	—
2011 Tax items	(24)	(0.01)
Subtotal 2011 special items	(14)	(0.01)
2012 Asset impairment, exit and implementation costs	(7)	—
2012 SABMiller special items	(12)	(0.01)
2012 Tobacco and health judgments	(2)	—
2012 Loss on early extinguishment of debt	(559)	(0.28)
2012 Tax items	62	0.03
Subtotal 2012 special items	(518)	(0.26)
Fewer shares outstanding	—	0.01
Change in tax rate	(60)	(0.03)
Operations	76	0.04
For the three months ended September 30, 2012	$657	$0.32

See discussion of events affecting the comparability of statement of earnings amounts in the Consolidated Operating Results section of the following Discussion and Analysis.

Fewer Shares Outstanding: Fewer shares outstanding during the three months ended September 30, 2012 compared with the prior-year period were due primarily to shares repurchased by Altria Group, Inc. under its share repurchase programs.

Change in Tax Rate: The change in tax rate was due primarily to a reduction in certain consolidated tax benefits resulting from the third quarter of 2012 debt tender offer.

Operations: The increase of $76 million shown in the table above was due primarily to the following:

- higher income from the smokeable products and smokeless products segments;
- higher equity earnings from SABMiller; and
- lower interest and other debt expense, net.

For further details, see the Consolidated Operating Results and Operating Results by Business Segment sections of the following Discussion and Analysis.

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2012 Forecasted Results: In August 2012, Altria Group, Inc. revised its 2012 full-year reported diluted EPS forecast to a range of $2.01 to $2.05 from a range of $2.29 to $2.33, reflecting the loss on early extinguishment of debt related to a debt tender offer completed during the third quarter of 2012. In September 2012, Altria Group, Inc. revised its 2012 full-year reported diluted EPS forecast to a range of $2.03 to $2.07, reflecting an income tax benefit primarily attributable to the reversal of tax reserves and associated interest related to the closure of the Internal Revenue Service ("IRS") audit of the 2004-2006 tax years. In October 2012, Altria Group, Inc. reaffirmed its 2012 full-year reported diluted EPS forecast. The 2012 full-year reported diluted EPS forecast includes total estimated net expenses of $0.16 per share as detailed in the table below, as compared with 2011 full-year reported diluted EPS of $1.64, which included $0.41 per share of net expenses as detailed in the table below. In addition, in October 2012, Altria Group, Inc. reaffirmed its 2012 full-year forecast for adjusted diluted EPS, which excludes the net expenses in the table below, representing a growth rate of 7% to 9% over 2011 full-year adjusted diluted EPS.

The factors described in the Cautionary Factors That May Affect Future Results section of the following Discussion and Analysis represent continuing risks to this forecast.

(Income) Expense, Net, Included in Reported Diluted EPS

	2012		2011	
Loss on early extinguishment of debt	$0.28		$—	
Asset impairment, exit, implementation and integration costs	0.02		0.07	
SABMiller special items	(0.08	)	0.03	
PMCC leveraged lease (benefit) charge	(0.03	)	0.30	
Tobacco and health judgments	—		0.05	
Tax items*	(0.03	)	(0.04	)
	$0.16		$0.41	

* Excludes the tax impact included in the PMCC leveraged lease (benefit) charge.

Adjusted diluted EPS is a financial measure that is not consistent with accounting principles generally accepted in the United States of America ("U.S. GAAP"). Altria Group, Inc.'s management reviews diluted EPS on an adjusted basis, which excludes certain income and expense items that management believes are not part of underlying operations. These items include loss on early extinguishment of debt, restructuring charges, SABMiller special items, certain PMCC leveraged lease items, certain tax items and tobacco and health judgments. Altria Group, Inc.'s management does not view any of these special items to be part of its sustainable results as they may be highly variable and difficult to predict and can distort underlying business trends and results. Altria Group, Inc.'s management believes it is appropriate to disclose this non-GAAP financial measure to provide useful insight into underlying business trends and results, and to provide a more meaningful comparison of year-over-year results. Adjusted measures are used by management and regularly provided to Altria Group, Inc.'s chief operating decision maker for planning, forecasting and evaluating the performances of Altria Group, Inc.'s businesses, including allocating resources and evaluating results relative to employee compensation targets. This information should be considered as supplemental in nature and not considered in isolation or as a substitute for the related financial information prepared in accordance with U.S. GAAP.

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Discussion and Analysis

Consolidated Operating Results

See pages 98-101 for a discussion of Cautionary Factors That May Affect Future Results.

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2012	2011	2012	2011
	(in millions)			
Net revenues:				
Smokeable products	$16,616	$16,500	$5,613	$5,499
Smokeless products	1,243	1,209	437	426
Wine	381	349	140	132
Financial services	136	(387)	52	51
Net revenues	$18,376	$17,671	$6,242	$6,108
Excise taxes on products:				
Smokeable products	$5,239	$5,304	$1,742	$1,747
Smokeless products	83	81	29	28
Wine	14	13	5	5
Excise taxes on products	$5,336	$5,398	$1,776	$1,780
Operating income:				
Operating companies income (loss):				
Smokeable products	$4,716	$4,527	$1,637	$1,575
Smokeless products	678	660	246	245
Wine	63	54	26	23
Financial services	166	(359)	79	83
Amortization of intangibles	(15)	(16)	(5)	(5)
General corporate expenses	(167)	(173)	(61)	(62)
Changes to Mondelēz and PMI tax-related receivables	48	19	48	19
Corporate asset impairment and exit costs	(1)	—	(1)	—
Operating income	$5,488	$4,712	$1,969	$1,878

As discussed further in Note 7. Segment Reporting to the condensed consolidated financial statements, Altria Group, Inc.'s chief operating decision maker reviews operating companies income to evaluate the performance of and allocate resources to the segments. Operating companies income for the segments is defined as operating income before amortization of intangibles and general corporate expenses. Management believes it is appropriate to disclose this measure to help investors analyze business performance and trends of the various business segments.

The following events that occurred during the nine and three months ended September 30, 2012 and 2011 affected the comparability of statement of earnings amounts.

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- Asset Impairment, Exit, Implementation and Integration Costs: For the nine and three months ended September 30, 2012, pre-tax asset impairment, exit and implementation costs consisted of the following:

	For the Nine Months Ended September 30, 2012			For the Three Months Ended September 30, 2012		
	Asset Impairment and Exit Costs	Implementation (Gain) Costs	Total	Asset Impairment and Exit Costs	Implementation Costs	Total
	(in millions)					
Smokeable products	$24	$(11)	$13	$1	$1	$2
Smokeless products	22	5	27	8	—	8
General corporate	1	(1)	—	1	—	1
Total	$47	$(7)	$40	$10	$	