Notes to Consolidated Financial Statements

Note 1.

Background and Basis of Presentation:

Background

Philip Morris International Inc. is a holding company incorporated in Virginia, U.S.A., whose subsidiaries and affiliates and their licensees are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products, in markets outside of the United States of America. In addition, PMI ships a version of its Platform 1 device and its consumables authorized by the U.S. Food and Drug Administration ("FDA") to Altria Group, Inc., for sale in the United States under license. Throughout these financial statements, the term "PMI" refers to Philip Morris International Inc. and its subsidiaries.

Reduced-risk products ("RRPs") is the term PMI uses to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continuing smoking. PMI has a range of RRPs in various stages of development, scientific assessment and commercialization.

"Platform 1" is the term PMI uses to refer to PMI's reduced-risk product that uses a precisely controlled heating device incorporating our *IQOS HeatControl* technology, into which a specially designed and proprietary tobacco unit is inserted and heated to generate an aerosol.

Basis of presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of net revenues and expenses during the reporting periods. Significant estimates and assumptions include, among other things: pension and benefit plan assumptions; useful lives and valuation assumptions of goodwill and other intangible assets; valuation assumptions for non-marketable equity securities; marketing programs, and income taxes. Actual results could differ from those estimates.

The consolidated financial statements include PMI, as well as its wholly owned and majority-owned subsidiaries. Investments in which PMI exercises significant influence (generally 20%-50% ownership interest) are accounted for under the equity method of accounting. Investments not accounted for under the equity method of accounting are measured at fair value, if it is readily determinable, with changes in fair value recognized in net income. Investments without readily determinable fair values, non-marketable equity securities, are measured and recorded using a measurement alternative that values the security at cost minus any impairment. All intercompany transactions and balances have been eliminated.

As of March 22, 2019, PMI deconsolidated the financial results of its Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH") from PMI's financial statements. For further details, see Note 22. *Deconsolidation of RBH*.

Note 2.

Summary of Significant Accounting Policies:

Cash and cash equivalents

Cash equivalents include demand deposits with banks and all highly liquid investments with original maturities of three months or less.

Depreciation

Property, plant and equipment are stated at historical cost and depreciated by the straight-line method over the estimated useful lives of the assets. Machinery and equipment are depreciated over periods ranging from 3 to 15 years, and buildings and building improvements over periods up to 40 years.

Employee benefit plans

PMI provides a range of benefits to its employees and retired employees, including pensions, postretirement health care and postemployment benefits (primarily severance). PMI records annual amounts relating to these plans based on calculations specified under U.S. GAAP. PMI recognizes the funded status of its defined pension and postretirement plans on the consolidated balance sheets. The funded status is measured as the difference between the fair value of the plans assets and the benefit obligation. PMI measures the plan assets and liabilities at the end of the fiscal year. For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For the postretirement health care plans, the benefit obligation is the accumulated postretirement benefit obligation. Any plan with an overfunded status is recognized as an asset, and any plan with an underfunded status is recognized as a liability. Any gains or losses and prior service costs or credits that have not been recognized as a component of net periodic benefit costs are recorded as a component of other comprehensive earnings (losses), net of deferred taxes. PMI elects to recognize actuarial gains/(losses) using the corridor approach.

Foreign currency translation

PMI translates the results of operations of its subsidiaries and affiliates using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Currency translation adjustments are recorded as a component of stockholders' (deficit) equity. In addition, some of PMI's subsidiaries have assets and liabilities denominated in currencies other than their functional currencies, and to the extent those are not designated as net investment hedges, these assets and liabilities generate transaction gains and losses when translated into their respective functional currencies.

Goodwill and non-amortizable intangible assets valuation

PMI tests goodwill and non-amortizable intangible assets for impairment annually or more frequently if events occur that would warrant such review. PMI performs its annual impairment analysis in the second quarter of each year. The impairment analysis involves comparing the fair value of each reporting unit or non-amortizable intangible asset to the carrying value. If the carrying value exceeds the fair value, goodwill or a non-amortizable intangible asset is considered impaired.

Hedging instruments

Derivative financial instruments are recorded at fair value on the consolidated balance sheets as either assets or liabilities. Changes in the fair value of derivatives are recorded each period either in accumulated other comprehensive losses on the consolidated balance sheet or in earnings, depending on whether a derivative is designated and effective as part of a hedge transaction and, if it is, the type of hedge transaction. Gains and losses on derivative instruments reported in accumulated other comprehensive losses are reclassified to the consolidated statements of earnings, into the same line item as the impact of the underlying transaction, in the periods in which operating results are affected by the hedged item. Cash flows from hedging instruments are classified in the same manner as the affected hedged item in the consolidated statements of cash flows.

Impairment of long-lived assets

PMI reviews long-lived assets, including amortizable intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. PMI performs undiscounted operating cash flow analyses to determine if an impairment exists. For purposes of recognition and measurement of an impairment for assets held for use, PMI groups assets and liabilities at the lowest level for which cash flows are separately identifiable. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal.

Impairment of investment in non-marketable equity securities

Non-marketable equity securities are subject to periodic impairment reviews during which PMI considers both qualitative and quantitative factors that may have a significant impact on the investees' fair value. Upon determining that an impairment may exist, the security's fair value is calculated and compared to its carrying value, and an impairment is recognized immediately if the carrying value exceeds the fair value. For further details see Note 22. *Deconsolidation of RBH*.

Impairment of investments in unconsolidated subsidiaries

Investments in unconsolidated subsidiaries are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the investments may not be recoverable. An impairment loss would be recorded whenever a decline in value of an equity investment below its carrying amount is determined to be other than temporary. PMI determines whether a loss is other than temporary by considering the length of time and extent to which the fair value of the equity investment has been less than the carrying amount, the financial condition of the equity investment, and the intent to retain the investment for a period of time is sufficient to allow for any anticipated recovery in market value.

Income taxes

Income taxes are provided on all earnings for jurisdictions outside the United States. These provisions, as well as state and local income tax provisions, are determined on a separate company basis, and the related assets and liabilities are recorded in PMI's consolidated balance sheets. Significant judgment is required in determining income tax provisions and in evaluating tax positions. PMI recognizes accrued interest and penalties associated with uncertain tax positions as part of the provision for income taxes on the consolidated statements of earnings. PMI recognizes income taxes associated with Global Intangible Low-Taxed Income ("GILTI") taxes as current period expense rather than including these amounts in the measurement of deferred taxes.

Inventories

Inventories are stated at the lower of cost or market. The first-in, first-out and average cost methods are used to cost substantially all inventories. It is a generally recognized industry practice to classify leaf tobacco inventory as a current asset, although part of such inventory, because of the duration of the aging process, ordinarily would not be utilized within one year.

Leases

PMI determines that a contract contains a lease if the contract conveys a right to control the use of the identified asset for a period of time in exchange for consideration. Lease expense is recognized on a straight-line basis over the lease term. At lease commencement, PMI recognizes lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases. The recognition of the right-of-use asset and lease liability includes renewal options when it is reasonably certain that they will be exercised. Certain of PMI's leases include payments that are based on changes to an index or on actual usage. These lease payments are adjusted periodically and are included within variable lease costs. PMI accounts for lease and nonlease components as a single-lease component with the exception of its vehicle leases, of which PMI accounts for the lease components separately from the nonlease components. Additionally, leases with an initial term of 12 months or less are not included in the right-of-use asset or lease liability on the consolidated statement of financial position.

Marketing costs

PMI supports its products with advertising, adult consumer engagement and trade promotions. Such programs include, but are not limited to, discounts, rebates, in-store display incentives, e-commerce, mobile and other digital platforms, adult consumer activation and promotion activities, as well as costs associated with adult consumer experience outlets and other adult consumer touchpoints and volume-based incentives. Advertising, as well as certain consumer engagement and trade activities costs, are expensed as incurred. Trade promotions are recorded as a reduction of revenues based on amounts estimated as being due to customers at the end of a period, based principally on historical utilization. For interim reporting purposes, advertising and certain consumer engagement expenses are charged to earnings based on estimated sales and related expenses for the full year.

Revenue recognition

PMI recognizes revenue primarily through the manufacture and sale of cigarettes and other nicotine-containing products, including reduced-risk products. The majority of PMI revenues are generated by sales through direct and indirect distribution networks with short-term payment conditions and where control is typically transferred to the customer either upon shipment or delivery of goods. PMI evaluates the transfer of control through evidence of the customer's receipt and acceptance, transfer of title, PMI's right to payment for those products and the customer's ability to direct the use of those products upon receipt. Typically, PMI's performance obligations are satisfied and revenue is recognized either upon shipment or delivery of goods.

In certain instances, PMI facilitates shipping and handling activities after control has transferred to the customer. PMI has elected to record all shipping and handling activities as costs to fulfill a contract. The shipping and handling costs that have not been incurred at the time revenue is recognized are accrued. The transaction price is typically based on the amount billed to the customer and includes estimated variable consideration, where applicable. Such variable consideration is typically not constrained and is estimated based on the most likely amount that PMI expects to be entitled to under the terms of the contracts with customers, historical experience of discount or rebate redemption, where relevant, and the terms of any underlying discount or rebate programs, which may change from time to time as the business and product categories evolve. PMI has elected to exclude excise taxes collected from customers from the measurement of the transaction price, thereby presenting revenues net of excise taxes. Estimated costs associated with warranty programs are generally provided for in cost of sales in the period the related revenues are recognized.

Stock-based compensation

PMI measures compensation cost for all stock-based awards at fair value on date of grant and recognizes the compensation costs over the service periods for awards expected to vest. PMI's accounting policy is to estimate the number of awards expected to be forfeited and adjust the expense when it is no longer probable that the employee will fulfill the service condition. For further details, see Note 9. *Stock Plans*.

Note 3.

Goodwill and Other Intangible Assets, net:

The movements in goodwill were as follows:

(in millions)	European Union	Eastern Europe	Middle East & Africa	South & Southeast Asia	East Asia & Australia	Latin America & Canada	Total
Balance at January 1, 2018	$ 1,419	$ 321	$ 102	$ 3,010	$ 567	$ 2,247	$ 7,666
Changes due to:							
Currency	(62)	(18)	(15)	(215)	(31)	(136)	(477)
Balances, December 31, 2018	1,357	303	87	2,795	536	2,111	7,189
Changes due to:							
Currency	**(19)**	**(3)**	**2**	**103**	**15**	**34**	**132**
Deconsolidation of RBH						**(1,463)**	**(1,463)**
Balances, December 31, 2019	**$ 1,338**	**$ 300**	**$ 89**	**$ 2,898**	**$ 551**	**$ 682**	**$ 5,858**

At December 31, 2019, goodwill primarily reflects PMI's acquisitions in Colombia, Greece, Indonesia, Mexico, Pakistan and Serbia, as well as the business combination in the Philippines.

For details on the deconsolidation of RBH, see Note 22. *Deconsolidation of RBH.*

Details of other intangible assets were as follows:

		December 31, 2019			December 31, 2018		
(in millions)	Weighted-Average Remaining Useful Life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Non-amortizable intangible assets		**$ 1,319**		**$ 1,319**	$ 1,269		$ 1,269
Amortizable intangible assets:							
Trademarks	**14 years**	**1,217**	**$ 526**	**691**	1,488	$ 608	880
Distribution networks	**8 years**	**113**	**72**	**41**	141	82	59
Other*	**9 years**	**106**	**44**	**62**	107	37	70
Total other intangible assets		**$ 2,755**	**$ 642**	**$ 2,113**	$ 3,005	$ 727	$ 2,278

* Includes farmer contracts and intellectual property rights

Non-amortizable intangible assets substantially consist of trademarks from PMI’s acquisitions in Indonesia and Mexico. The increase since December 31, 2018, was due to currency movements of $50 million.

The decrease in the gross carrying amount of amortizable intangible assets from December 31, 2018, was mainly due to the deconsolidation of RBH's trademarks of ($275 million) and distribution network of ($29 million), partially offset by currency movements of $6 million.

The change in the accumulated amortization from December 31, 2018 was mainly due to the deconsolidation of RBH's trademarks of ($133 million) and distribution network of ($18 million), partially offset by the 2019 amortization of $66 million and by currency movements of $2 million.

Amortization expense for each of the next five years is estimated to be $73 million or less, assuming no additional transactions occur that require the amortization of intangible assets.

During the second quarter of 2019, PMI completed its annual review of goodwill and non-amortizable intangible assets for potential impairment, and no impairment charges were required as a result of this review.

Note 4.

Related Parties - Investments in Unconsolidated Subsidiaries, Equity Securities and Other:

Investments in unconsolidated subsidiaries:

At December 31, 2019 and 2018, PMI had total investments in unconsolidated subsidiaries of $1,053 million and $981 million, respectively, which were accounted for under the equity method of accounting. Equity method investments are initially recorded at cost. Under the equity method of accounting, the investment is adjusted for PMI's proportionate share of earnings or losses, dividends, capital contributions, changes in ownership interests and movements in currency translation adjustments. The carrying value of our equity method investments at December 31, 2019 and 2018, exceeded our share of the unconsolidated subsidiaries' book value by $901 million and $835 million, respectively. The difference between the investment carrying value and the amount of underlying equity in net assets, excluding $863 million and $793 million attributable to goodwill as of December 31, 2019 and 2018, respectively, is being amortized on a straight-line basis over the underlying assets' estimated useful lives of 10 to 20 years. At December 31, 2019 and 2018, PMI received year-to-date dividends from unconsolidated subsidiaries of $100 million and $118 million, respectively.

PMI holds a 23% equity interest in Megapolis Distribution BV, the holding company of CJSC TK Megapolis, PMI's distributor in Russia (Eastern Europe segment).

PMI holds a 49% equity interest in United Arab Emirates-based Emirati Investors-TA (FZC) (“EITA”). PMI holds an approximate 25% economic interest in Société des Tabacs Algéro-Emiratie (“STAEM”), an Algerian joint venture that is 51% owned by EITA and 49% by the Algerian state-owned enterprise Management et Développement des Actifs et des Ressources Holding ("MADAR Holding"), which is part of the Middle East & Africa segment, manufactures and distributes under license some of PMI’s brands.

The initial investments in Megapolis Distribution BV and EITA were recorded at cost and are included in investments in unconsolidated subsidiaries and equity securities on the consolidated balance sheets.

Equity securities:

Following the deconsolidation of RBH, PMI recorded the continuing investment in RBH, PMI's wholly owned subsidiary, at fair value of $3,280 million at the date of deconsolidation, within investments in unconsolidated subsidiaries and equity securities. For further details, see Note 22. *Deconsolidation of RBH*. Transactions between PMI and RBH are considered to be related-party transactions from the date of deconsolidation and are included in the tables below.

Other related parties:

United Arab Emirates-based Trans-Emirates Trading and Investments (FZC) ("TTI") holds a 33% non-controlling interest in Philip Morris Misr LLC ("PMM"), an entity incorporated in Egypt which is consolidated in PMI’s financial statements in the Middle East & Africa segment. PMM sells, under license, PMI brands in Egypt through an exclusive distribution agreement with a local entity that is also controlled by TTI.

IPM India, PMI's consolidated subsidiary in the South & Southeast Asia segment, has a non-controlling interest of 43.7% held by Godfrey Phillips India Ltd, who also acts as contract manufacturer and distributor for IPM. Amounts in the tables below include transactions between these related parties, beginning in 2019. Prior periods do not include these transactions as they were not material.

Financial activity with the above related parties:

PMI’s net revenues and expenses with the above related parties were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net revenues			
Megapolis Group	**$ 2,236**	$ 1,994	$ 1,874
Other	**1,015**	720	647
Net revenues [a]	**$ 3,251**	$ 2,714	$ 2,521
Expenses:			
Other	**$ 63**	$ 21	$ 23
Expenses	**$ 63**	$ 21	$ 23

[a] Net revenues exclude excise taxes and VAT billed to customers. Prior year's amounts have been reclassified to conform with the current year's presentation.

PMI’s balance sheet activity with the above related parties was as follows:

	At December 31,	
(in millions)	**2019**	**2018**
Receivables:		
Megapolis Group	**$ 375**	$ 172
Other	**148**	136
Receivables	**$ 523**	$ 308
Payables:		
Other	**$ 20**	$ 8
Payables	**$ 20**	$ 8

The activities with the above related parties are in the ordinary course of business, and are primarily for distribution, service fees, contract manufacturing and license agreements. PMI eliminated its respective share of all significant intercompany transactions with the equity method investees.

Note 5.

Product Warranty:

PMI's *IQOS* devices are subject to standard product warranties generally for a period of 12 months from the date of purchase or such other periods as required by law. PMI generally provides in cost of sales for the estimated cost of warranty in the period the related revenue is recognized. PMI assesses the adequacy of its accrued product warranties and adjusts the amounts as necessary based on actual experience and changes in future estimates. Factors that affect product warranties may vary across markets but typically include device version mix, product failure rates, logistics and service delivery costs, and warranty policies. PMI accounts for its product warranties within other accrued liabilities. At December 31, 2019 and December 31, 2018, these amounts were as follows:

	At December 31,	
(in millions)	**2019**	**2018**
Balance at beginning of period	**$ 67**	$ 71
Changes due to:		
Warranties issued	**303**	179
Settlements	**(230)**	(183)
Currency	**—**	—
Balance at end of period	**$ 140**	$ 67

Note 6.

Acquisitions:

On March 21, 2018, PMI acquired the remaining 49% interest in Tabacalera Costarricense, S.A. and Mendiola y Compañía, S.A. for a net purchase price of $95 million, which includes $2 million of contingent consideration. As a result, PMI now owns 100% of these Costa Rican affiliates. The purchase of the remaining 49% interest resulted in a decrease to PMI's additional paid-in capital of $86 million.

Note 7.

Indebtedness:

Short-Term Borrowings

At December 31, 2019 and 2018, PMI's short-term borrowings and related average interest rates consisted of the following:

	December 31, 2019		December 31, 2018	
(in millions)	**Amount Outstanding**	**Average Year-End Rate**	**Amount Outstanding**	**Average Year-End Rate**
Commercial paper	**$ —**	**—%**	$ —	—%
Bank loans	**338**	**5.5**	730	5.8
	$ 338		$ 730	

Given the mix of subsidiaries and their respective local economic environments, the average interest rate for bank loans above can vary significantly from day to day and country to country.

The fair values of PMI's short-term borrowings at December 31, 2019 and 2018, based upon current market interest rates, approximate the amounts disclosed above.

Long-Term Debt

At December 31, 2019 and 2018, PMI's long-term debt consisted of the following:

(in millions)	December 31, 2019	December 31, 2018
U.S. dollar notes, 1.875% to 6.375% (average interest rate 3.516%), due through 2044	**$ 19,783**	$ 20,819
Foreign currency obligations:		
Euro notes, 0.125% to 3.125% (average interest rate 1.950%), due through 2039	**9,822**	8,656
Swiss franc notes, 1.000% to 2.000% (average interest rate 1.521%), due through 2024	**899**	1,374
Other (average interest rate 3.125%), due through 2025	**203**	180
	30,707	31,029
Less current portion of long-term debt	**4,051**	4,054
	$ 26,656	$ 26,975

Other debt:

Other foreign currency debt above includes mortgage debt in Switzerland and finance lease obligations at December 31, 2019 and December 31, 2018.

Debt Issuances Outstanding:

PMI's debt issuances outstanding at December 31, 2019, were as follows:

(in millions)

Type		Face Value	Interest Rate	Issuance	Maturity
U.S. dollar notes		**$300**	**Floating**	February 2017	February 2020
U.S. dollar notes		**$1,000**	**2.000%**	February 2017	February 2020
U.S. dollar notes		**$1,000**	**4.500%**	March 2010	March 2020
U.S. dollar notes		**$750**	**1.875%**	February 2016	February 2021
U.S. dollar notes		**$350**	**4.125%**	May 2011	May 2021
U.S. dollar notes		**$750**	**2.900%**	November 2011	November 2021
U.S. dollar notes		**$500**	**2.625%**	February 2017	February 2022
U.S. dollar notes		**$750**	**2.375%**	August 2017	August 2022
U.S. dollar notes		**$750**	**2.500%**	August 2012	August 2022
U.S. dollar notes		**$750**	**2.500%**	November 2017	November 2022
U.S. dollar notes		**$600**	**2.625%**	March 2013	March 2023
U.S. dollar notes		**$500**	**2.125%**	May 2016	May 2023
U.S. dollar notes		**$500**	**3.600%**	November 2013	November 2023
U.S. dollar notes		**$900**	**2.875%**	May 2019	May 2024
U.S. dollar notes		**$750**	**3.250%**	November 2014	November 2024
U.S. dollar notes		**$750**	**3.375%**	August 2015	August 2025
U.S. dollar notes		**$750**	**2.750%**	February 2016	February 2026
U.S. dollar notes		**$500**	**3.125%**	August 2017	August 2027
U.S. dollar notes		**$500**	**3.125%**	November 2017	March 2028
U.S. dollar notes		**$750**	**3.375%**	May 2019	August 2029
U.S. dollar notes		**$1,500**	**6.375%**	May 2008	May 2038
U.S. dollar notes		**$750**	**4.375%**	November 2011	November 2041
U.S. dollar notes		**$700**	**4.500%**	March 2012	March 2042
U.S. dollar notes		**$750**	**3.875%**	August 2012	August 2042
U.S. dollar notes		**$850**	**4.125%**	March 2013	March 2043
U.S. dollar notes		**$750**	**4.875%**	November 2013	November 2043
U.S. dollar notes		**$750**	**4.250%**	November 2014	November 2044
U.S. dollar notes	(a)	**$500**	**4.250%**	May 2016	November 2044
EURO notes	(b)	**€1,250 (approximately $1,621)**	**1.750%**	March 2013	March 2020
EURO notes	(b)	**€750 (approximately $1,029)**	**1.875%**	March 2014	March 2021
EURO notes	(b)	**€600 (approximately $761)**	**2.875%**	May 2012	May 2024
EURO notes	(b)	**€500 (approximately $582)**	**0.625%**	November 2017	November 2024
EURO notes	(b)	**€750 (approximately $972)**	**2.750%**	March 2013	March 2025
EURO notes	(b)	**€1,000 (approximately $1,372)**	**2.875%**	March 2014	March 2026
EURO notes	(b)	**€500 (approximately $557)**	**0.125%**	August 2019	August 2026
EURO notes	(b)	**€500 (approximately $697)**	**2.875%**	May 2014	May 2029
EURO notes	(b)	**€750 (approximately $835)**	**0.800%**	August 2019	August 2031
EURO notes	(b)	**€500 (approximately $648)**	**3.125%**	June 2013	June 2033
EURO notes	(b)	**€500 (approximately $578)**	**2.000%**	May 2016	May 2036
EURO notes	(b)	**€500 (approximately $582)**	**1.875%**	November 2017	November 2037
Euro notes	(b)	**€750 (approximately $835)**	**1.450%**	August 2019	August 2039
Swiss franc notes	(b)	**CHF325 (approximately $334)**	**1.000%**	September 2012	September 2020
Swiss franc notes	(b)	**CHF300 (approximately $335)**	**2.000%**	December 2011	December 2021
Swiss franc notes	(b)	**CHF250 (approximately $283)**	**1.625%**	May 2014	May 2024

[a] These notes are a further issuance of the 4.250% notes issued by PMI in November 2014.
[b] USD equivalents for foreign currency notes were calculated based on exchange rates on the date of issuance.

The net proceeds from the sale of the securities listed in the table above were used for general corporate purposes, including working capital requirements and repurchase of PMI's common stock until 2015.

Aggregate maturities:

Aggregate maturities of long-term debt are as follows:

(in millions)		
2020	$	4,051
2021		3,015
2022		2,764
2023		1,607
2024		3,283
2025-2029		6,332
2030-2034		1,400
Thereafter		8,510
		30,962
Debt discounts		(255)
Total long-term debt	$	30,707

See Note 16. *Fair Value Measurements* for additional disclosures related to the fair value of PMI’s debt.

Credit Facilities

On January 28, 2019, PMI entered into an agreement to extend the term of its $2.0 billion 364-day revolving credit facility from February 5, 2019, to February 4, 2020.

At December 31, 2019, PMI’s total committed credit facilities and commercial paper outstanding were as follows:

Type (in billions of dollars)	Committed Credit Facilities	Commercial Paper
364-day revolving credit, expiring February 4, 2020	**$ 2.0**	
Multi-year revolving credit, expiring February 28, 2021	**2.5**	
Multi-year revolving credit, expiring October 1, 2022	**3.5**	
Total facilities	**$ 8.0**	
Commercial paper outstanding		**$ —**

At December 31, 2019, there were no borrowings under these committed credit facilities, and the entire committed amounts were available for borrowing.

Each of these facilities requires PMI to maintain a ratio of consolidated earnings before interest, taxes, depreciation and amortization (“consolidated EBITDA”) to consolidated interest expense of not less than 3.5 to 1.0 on a rolling four-quarter basis. At December 31, 2019, PMI’s ratio calculated in accordance with the agreements was 11.2 to 1.0. These facilities do not include any credit rating triggers, material adverse change clauses or any provisions that could require PMI to post collateral. The terms “consolidated EBITDA” and “consolidated interest expense,” both of which include certain adjustments, are defined in the facility agreements previously filed with the Securities and Exchange Commission.

On January 31, 2020, PMI entered into an agreement to amend and extend the term of its $2 billion 364-day revolving credit facility from February 4, 2020, to February 2, 2021.

In addition to the committed credit facilities discussed above, certain subsidiaries maintain short-term credit arrangements to meet their respective working capital needs. These credit arrangements, which amounted to approximately $2.7 billion at December 31, 2019, and $3.3 billion at December 31, 2018, are for the sole use of the subsidiaries. Borrowings under these arrangements amounted to $338 million at December 31, 2019, and $730 million at December 31, 2018.

Note 8.

Capital Stock:

Shares of authorized common stock are 6.0 billion; issued, repurchased and outstanding shares were as follows:

	Shares Issued	Shares Repurchased	Shares Outstanding
Balances, January 1, 2017	2,109,316,331	(557,930,784)	1,551,385,547
Issuance of stock awards		1,832,215	1,832,215
Balances, December 31, 2017	2,109,316,331	(556,098,569)	1,553,217,762
Issuance of stock awards		1,361,959	1,361,959
Balances, December 31, 2018	2,109,316,331	(554,736,610)	1,554,579,721
Issuance of stock awards		**1,314,942**	**1,314,942**
Balances, December 31, 2019	**2,109,316,331**	**(553,421,668)**	**1,555,894,663**

At December 31, 2019, 27,371,404 shares of common stock were reserved for stock awards under PMI's stock plans, and 250 million shares of preferred stock, without par value, were authorized but unissued. PMI currently has no plans to issue any shares of preferred stock.

Note 9.

Stock Plans:

In May 2017, PMI's shareholders approved the Philip Morris International Inc. 2017 Performance Incentive Plan (the "2017 Plan"). Under the 2017 Plan, PMI may grant to eligible employees restricted shares and restricted share units, performance-based cash incentive awards and performance-based equity awards. Up to 25 million shares of PMI's common stock may be issued under the 2017 Plan. At December 31, 2019, shares available for grant under the 2017 Plan were 20,127,360.

In May 2017, PMI's shareholders also approved the Philip Morris International Inc. 2017 Stock Compensation Plan for Non-Employee Directors (the "2017 Non-Employee Directors Plan"). A non-employee director is defined as a member of the PMI Board of Directors who is not a full-time employee of PMI or of any corporation in which PMI owns, directly or indirectly, stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote in the election of directors in such corporation. Up to 1 million shares of PMI common stock may be awarded under the 2017 Non-Employee Directors Plan. At December 31, 2019, shares available for grant under the plan were 954,084.

Restricted share unit (RSU) awards

PMI may grant RSU awards to eligible employees; recipients may not sell, assign, pledge or otherwise encumber such awards. Such awards are subject to forfeiture if certain employment conditions are not met. RSU awards generally vest on the third anniversary of the grant date. RSU awards do not carry voting rights, although they do earn dividend equivalents.

During 2019, the activity for RSU awards was as follows:

	Number of Shares		Weighted-Average Grant Date Fair Value Per Share
Balance at January 1, 2019	**3,318,795**	**$**	**96.26**
Granted	**1,726,760**		**77.28**
Vested	**(1,126,057)**		**89.56**
Forfeited	**(193,628)**		**89.36**
Balance at December 31, 2019	**3,725,870**	**$**	**89.85**

During the years ended December 31, 2019, 2018 and 2017, the weighted-average grant date fair value of the RSU awards granted to PMI employees and the recorded compensation expense related to RSU awards were as follows:

(in millions, except per RSU award granted)		Total Weighted-Average Grant Date Fair Value of RSU Awards Granted		Weighted-Average Grant Date Fair Value Per RSU Award Granted		Compensation Expense related to RSU Awards
2019	**$**	**133**	**$**	**77.28**	**$**	**118**
2018	$	129	$	100.19	$	114
2017	$	119	$	98.59	$	111

The fair value of the RSU awards at the date of grant is amortized to expense over the restriction period, typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2019, PMI had $124 million of total unrecognized compensation costs related to non-vested RSU awards. These costs are expected to be recognized over a weighted-average period of approximately two years, or upon death, disability or reaching the age of 58.

During the years ended December 31, 2019, 2018 and 2017, share and fair value information for PMI RSU awards that vested were as follows:

(dollars in millions)	Shares of RSU Awards that Vested		Grant Date Fair Value of Vested Shares of RSU Awards		Total Fair Value of RSU Awards that Vested
2019	**1,126,057**	**$**	**101**	**$**	**95**
2018	1,451,876	$	121	$	149
2017	2,022,856	$	158	$	208

Performance share unit (PSU) awards

PMI may grant PSU awards to certain executives; recipients may not sell, assign, pledge or otherwise encumber such awards. The PSU awards require the achievement of certain performance factors, which are predetermined at the time of grant, typically over a three-year performance cycle with performance metrics for such PSUs consisting of PMI's Total Shareholder Return (TSR) relative to a predetermined peer group and on an absolute basis (50% weight), PMI's currency-neutral compound annual adjusted operating income growth rate, excluding acquisitions (30% weight), and PMI's performance against specific measures of PMI's transformation (20% weight). The aggregate of the weighted performance factors for the three metrics determines the percentage of PSUs that will vest at the end of the three-year performance cycle. The minimum percentage of such PSUs that can vest is zero, with a target percentage of 100 and a maximum percentage of 200. Each such vested PSU entitles the participant to one share of common stock. An aggregate weighted PSU performance factor of 100 will result in the targeted number of PSUs being vested. At the end of the performance cycle, participants are entitled to an amount equivalent to the accumulated dividends paid on common stock during the performance cycle for the number of shares earned. PSU awards do not carry voting rights.

During 2019, the activity for PSU awards was as follows:

	Number of Shares	Grant Date Fair Value Subject to Other Performance Factors Per Share	Grant Date Fair Value Subject to TSR Performance Factor Per Share
Balance at January 1, 2019	**1,194,970**	**$ 95.85**	**$ 117.09**
Granted	**647,700**	**77.23**	**83.59**
Vested	**(330,616)**	**89.02**	**104.60**
Forfeited	**(164,594)**	**90.28**	**107.09**
Balance at December 31, 2019	**1,347,460**	**$ 88.19**	**$ 107.61**

During the years ended December 31, 2019, 2018 and 2017, the grant date fair value of the PSU awards granted to PMI employees and the recorded compensation expense related to PSU awards were as follows:

(in millions, except per PSU award granted)	PSU Grant Date Fair Value Subject to Other Performance Factors		PSU Grant Date Fair Value Subject to TSR Performance Factor		Compensation Expense related to PSU Awards
	Total	Per PSU Award	Total	Per PSU Award	Total
2019	**$ 30**	**$ 77.23**	**$ 21**	**$ 83.59**	**$ 54**
2018	$ 20	$ 100.69	$ 24	$ 118.98	$ 24
2017	$ 19	$ 98.29	$ 25	$ 128.72	$ 37

The grant date fair value of the PSU awards subject to the other performance factors was determined by using the average of the high and low market price of PMI's stock at the date of the grant. The grant date fair value of the PSU market-based awards subject to the TSR performance factor was determined by using the Monte Carlo simulation model. The following assumptions were used to determine the grant date fair value of the PSU awards subject to the TSR performance factor for the years ended December 31, 2019, 2018 and 2017:

	For the Years Ended December 31,		
	2019	2018	2017
Risk-free interest rate [a]	**2.4%**	2.3%	1.5%
Expected volatility	**21.4%** [b]	19.6% [c]	15.8% [c]

[a] Based on the U.S. Treasury yield curve.
[b] Determined using the observed historical volatility.
[c] Determined using a weighted-average of historical and implied volatility.

The fair value of the PSU award at the date of grant is amortized to expense over the performance period, which is typically three years after the date of the award, or upon death, disability or reaching the age of 58. As of December 31, 2019, PMI had $33 million of total unrecognized compensation cost related to non-vested PSU awards. This cost is recognized over a weighted-average performance cycle period of approximately two years, or upon death, disability or reaching the age of 58.

During the year ended December 31, 2019, share and fair value information for PMI PSU awards that vested were as follows:

(dollars in millions)	Shares of PSU Awards that Vested	Grant Date Fair Value of Vested Shares of PSU Awards	Total Fair Value of PSU Awards that Vested
2019	**330,616**	**$ 32**	**$ 28**

During the years ended December 31, 2018 and 2017, there were no PSU awards that vested.

Note 10.

Earnings per Share:

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and therefore are included in PMI's earnings per share calculation pursuant to the two-class method.

Basic and diluted earnings per share ("EPS") were calculated using the following:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net earnings attributable to PMI	**$ 7,185**	$ 7,911	$ 6,035
Less distributed and undistributed earnings attributable to share-based payment awards	**17**	16	14
Net earnings for basic and diluted EPS	**$ 7,168**	$ 7,895	$ 6,021
Weighted-average shares for basic EPS	**1,555**	1,555	1,552
Plus contingently issuable performance stock units (PSUs)	**1**	—	1
Weighted-average shares for diluted EPS	**1,556**	1,555	1,553

For the 2019, 2018 and 2017 computations, there were no antidilutive stock options.

Note 11.

Income Taxes:

Earnings before income taxes and provision for income taxes consisted of the following for the years ended December 31, 2019, 2018 and 2017:

(in millions)	**2019**	**2018**	**2017**
Earnings before income taxes	**$ 9,872**	$ 10,671	$ 10,589
Provision for income taxes:			
United States federal and state:			
Current	**$ 17**	$ 120	$ 1,662
Deferred	**24**	(113)	(384)
Total United States	**41**	7	1,278
Outside United States:			
Current	**2,417**	2,425	3,146
Deferred	**(165)**	13	(117)
Total outside United States	**2,252**	2,438	3,029
Total provision for income taxes	**$ 2,293**	$ 2,445	$ 4,307

In December 2017, the Tax Cuts and Jobs Act was signed into law. Accordingly, PMI recorded a provisional charge of $1.6 billion in its 2017 income tax provision, including a charge for the transition tax on accumulated foreign earnings of $1.4 billion (which represented the transition tax of $2.2 billion, net of a reversal of $0.7 billion of previously recorded deferred tax liabilities on part of its accumulated foreign earnings and other items of $0.1 billion) and $0.2 billion due to the re-measurement of U.S. deferred tax assets and liabilities applying the U.S. federal corporate tax rate of 21%.

PMI completed its analysis of the Tax Cuts and Jobs Act during 2018 and adjusted the 2017 provisional estimates to the final amounts based on its 2017 U.S. federal income tax return as filed. Accordingly, PMI recorded in its income tax provision a charge of $31 million representing a current income tax charge of $185 million, primarily due to an increase in its aggregate foreign cash position used to determine PMI's final 2017 transition tax liability, mostly offset by a deferred income tax benefit of $154 million primarily due to the recognition of deferred tax assets for net operating losses in the state of New York. Updates to the provisional estimates have been recorded in accordance with Staff Accounting Bulletin No. 118 ("SAB 118").

At December 31, 2017, PMI recorded an income tax payable of $1.7 billion attributable to the Tax Cuts and Jobs Act, of which $1.6 billion was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet. The income tax payable of $1.7 billion represented the transition tax of $2.2 billion, partially offset by foreign tax credits related to foreign withholding taxes previously paid of $0.5 billion. The income tax payable is due over an eight-year period beginning in 2018. In December 2018, PMI recorded an increase to income tax payable of $0.1 billion related to PMI's transition tax liability, in accordance with SAB 118. At December 31, 2019 and December 31, 2018, $1.2 billion and $1.5 billion of PMI's remaining transition tax liability, respectively, was recorded in "income taxes and other liabilities" on PMI's consolidated balance sheet.

At December 31, 2019 and December 31, 2018, U.S. federal and foreign deferred income taxes have been provided on all accumulated earnings of PMI's foreign subsidiaries.

In accordance with the alternatives provided by ASU 2018-02 "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," PMI has elected not to reclassify the income tax effects of the Tax Cuts and Jobs Act from accumulated other comprehensive losses to retained earnings.

PMI is regularly examined by tax authorities around the world and is currently under examination in a number of jurisdictions. The U.S. federal statute of limitations remains open for the years 2015 and onward. Foreign and U.S. state jurisdictions have statutes of limitations generally ranging from three to five years. Years still open to examination by foreign tax authorities in major jurisdictions include Germany (2015 onward), Indonesia (2014 onward), Russia (2017 onward), Switzerland (2017 onward), and Turkey (2014 onward).

It is reasonably possible that within the next 12 months certain tax examinations will close, which could result in a change in unrecognized tax benefits, along with related interest and penalties. An estimate of any possible change cannot be made at this time.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

(in millions)	**2019**	**2018**	**2017**
Balance at January 1,	**$ 56**	$ 145	$ 79
Additions based on tax positions related to the current year	**10**	10	71
Additions for tax positions of previous years	**1**	15	5
Reductions for tax positions of prior years	**(2)**	(94)	—
Reductions due to lapse of statute of limitations	**(1)**	(3)	(7)
Settlements	**—**	(19)	(4)
Other	**(1)**	2	1
Balance at December 31,	**$ 63**	$ 56	$ 145

Unrecognized tax benefits and PMI's liability for contingent income taxes, interest and penalties were as follows:

(in millions)	**December 31, 2019**	**December 31, 2018**	**December 31, 2017**
Unrecognized tax benefits	**$ 63**	$ 56	$ 145
Accrued interest and penalties	**16**	12	23
Tax credits and other indirect benefits	**(12)**	(14)	(35)
Liability for tax contingencies	**$ 67**	$ 54	$ 133

The amount of unrecognized tax benefits that, if recognized, would impact the effective tax rate was $50 million at December 31, 2019. The remainder, if recognized, would principally affect deferred taxes.

For the years ended December 31, 2019, 2018 and 2017, PMI recognized income (expense) in its consolidated statements of earnings of $(4) million, $4 million and $(11) million, respectively, related to interest and penalties associated with uncertain tax positions.

The effective income tax rate on pre-tax earnings differed from the U.S. federal statutory rate for the following reasons for the years ended December 31, 2019, 2018 and 2017:

	2019	2018	2017
U.S. federal statutory rate	**21.0%**	21.0%	35.0%
Increase (decrease) resulting from:			
Foreign rate differences	**1.8**	1.3	(12.2)
Dividend repatriation cost	**(0.5)**	2.5	16.4
Global intangible low-taxed income	**1.4**	1.2	
U.S. state taxes	**0.7**	(1.1)	
Foreign derived intangible income	**(1.2)**	(1.1)	
Other	**—**	(0.9)	1.5
Effective tax rate	**23.2%**	22.9%	40.7%

The 2019 effective tax rate increased 0.3 percentage points to 23.2%. The change in the effective tax rate for 2019, as compared to 2018, was unfavorably impacted by changes in earnings mix by taxing jurisdiction and U.S. state deferred income tax expense, partially offset by the reversal of a deferred tax liability on the unremitted earnings of PMI's Canadian subsidiary, RBH ($49 million), a reduction in estimated U.S. federal income tax on dividend repatriation for the years 2015-2018 ($67 million), and other repatriation cost differences.

The 2018 effective tax rate decreased 17.8 percentage points to 22.9%. The change in the effective tax rate for 2018, as compared to 2017, was primarily due to the Tax Cuts and Jobs Act, which reduced the U.S. federal income tax rate from 35% to 21%, in addition to repatriation cost differences and earnings mix by taxing jurisdiction.

The 2017 effective tax rate increased 12.8 percentage points to 40.7%. The change in the effective tax rate for 2017, as compared to 2016, was primarily due to the Tax Cuts and Jobs Act. In addition to the transition tax, which resulted in a net tax charge of $1.4 billion, the Tax Cuts and Jobs Act also included a reduction in the U.S. income tax rate from 35% to 21%, as of January 1, 2018. This change in income tax rate required a re-measurement of PMI's U.S. deferred tax assets and liabilities at December 31, 2017, resulting in a tax charge of $0.2 billion.

The tax effects of temporary differences that gave rise to deferred income tax assets and liabilities consisted of the following:

	At December 31,	
(in millions)	**2019**	**2018**
Deferred income tax assets:		
Accrued postretirement and postemployment benefits	**$ 184**	$ 193
Accrued pension costs	**620**	390
Inventory	**176**	136
Accrued liabilities	**130**	138
Net operating loss carryforwards and tax credits	**486**	452
Other	**101**	37
Total deferred income tax assets	**1,697**	1,346
Less: valuation allowance	**(304)**	(257)
Deferred income tax assets, net of valuation allowance	**1,393**	1,089
Deferred income tax liabilities:		
Trade names	**(469)**	(508)
Property, plant and equipment	**(180)**	(222)
Unremitted earnings	**(243)**	(123)
Foreign exchange	**(256)**	(157)
Total deferred income tax liabilities	**(1,148)**	(1,010)
Net deferred income tax assets	**$ 245**	$ 79

At December 31, 2019, PMI recorded deferred tax assets for net operating loss carryforwards and tax credits of $486 million, with varying dates of expiration, primarily after 2024, including $98 million with an unlimited carryforward period. At December 31, 2019, PMI has recorded a valuation allowance of $304 million against deferred tax assets that do not meet the more-likely-than not recognition threshold.

At December 31, 2018, PMI recorded deferred tax assets for net operating loss carryforwards of $452 million, with varying dates of expiration, primarily after 2023, including $87 million with an unlimited carryforward period. At December 31, 2018, PMI has recorded a valuation allowance of $257 million against deferred tax assets that do not meet the more-likely-than-not recognition threshold. The increases in deferred tax assets for net operating loss carryforwards and the valuation allowance during 2018 are primarily due to law changes associated with the Tax Cuts and Jobs Act, as discussed above.

Note 12.

Segment Reporting:

PMI's subsidiaries and affiliates are engaged in the manufacture and sale of cigarettes and other nicotine-containing products, including RRPs, in markets outside of the United States of America. In addition, PMI ships a version of its Platform 1 device and its consumables authorized by the FDA to Altria Group, Inc. for sale in the United States under license. Operating segments for PMI are organized by geographic region and managed by segment managers who are responsible for the operating and financial results of the regions inclusive of all product categories sold in the region. PMI's operating segments are the European Union; Eastern Europe; Middle East & Africa; South & Southeast Asia; East Asia & Australia; and Latin America & Canada. PMI records net revenues and operating income to its segments based upon the geographic area in which the customer resides. Revenues from shipments of Platform 1 devices, heated tobacco units and accessories to Altria Group, Inc. for sale under license in the United States are included in Net Revenues of the Latin America & Canada segment.

PMI's chief operating decision maker evaluates segment performance and allocates resources based on regional operating income, which includes results from all product categories sold in each region. Interest expense, net, and provision for income taxes are centrally managed and, accordingly, such items are not presented by segment since they are excluded from the measure of segment profitability reviewed by management. Information about total assets by segment is not disclosed because such information is not reported to or used by PMI's chief operating decision maker. Segment goodwill and other intangible assets, net, are disclosed in Note 3. *Goodwill and Other Intangible Assets, net.* The accounting policies of the segments are the same as those described in Note 2. *Summary of Significant Accounting Policies.*

PMI disaggregates its net revenue from contracts with customers by both geographic location and product category for each of PMI's six operating segments, as PMI believes this best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows are affected by economic factors.

Net revenues by segment were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Net revenues:			
European Union	**$ 9,817**	$ 9,298	$ 8,318
Eastern Europe	**3,282**	2,921	2,711
Middle East & Africa	**4,042**	4,114	3,988
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**5,364**	5,580	6,373
Latin America & Canada	**2,206**	3,056	2,941
Net revenues	**$ 29,805**	$ 29,625	$ 28,748

Total net revenues attributable to customers located in Japan, PMI's largest market in terms of net revenues, were $3.9 billion, $3.8 billion and $4.7 billion in 2019, 2018 and 2017, respectively. Total net revenues attributable to customers located in Indonesia were $3.1 billion, $3.1 billion and $3.2 billion in 2019, 2018 and 2017, respectively. PMI had one customer in the East Asia & Australia segment that accounted for 13%, 13% and 16% of PMI's consolidated net revenues, and one customer in the European Union segment that accounted for 10%, 10% and 10% of PMI's consolidated net revenues in 2019, 2018 and 2017, respectively.

PMI's net revenues by product category were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Combustible products:			
European Union	**$ 8,093**	$ 8,433	$ 8,048
Eastern Europe	**2,438**	2,597	2,657
Middle East & Africa	**3,721**	3,732	3,893
South & Southeast Asia	**5,094**	4,656	4,417
East Asia & Australia	**2,693**	3,074	3,156
Latin America & Canada	**2,179**	3,037	2,937
Total combustible products	**$ 24,218**	$ 25,529	$ 25,107
Reduced-risk products:			
European Union	**$ 1,724**	$ 865	$ 269
Eastern Europe	**844**	324	55
Middle East & Africa	**321**	382	94
South & Southeast Asia	**—**	—	—
East Asia & Australia	**2,671**	2,506	3,218
Latin America & Canada	**27**	19	4
Total reduced-risk products	**$ 5,587**	$ 4,096	$ 3,640
Total PMI net revenues	**$ 29,805**	$ 29,625	$ 28,748

Note: Sum of product categories or Regions might not foot to total PMI due to roundings.

Net revenues related to combustible products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's cigarettes and other tobacco products combined. Other tobacco products primarily include roll-your-own and make-your-own cigarettes, pipe tobacco, cigars and cigarillos and do not include reduced-risk products.

Net revenues related to reduced-risk products refer to the operating revenues generated from the sale of these products, including shipping and handling charges billed to customers, net of sales and promotion incentives, and excise taxes. These net revenue amounts consist of the sale of PMI's heated tobacco units, *IQOS* devices and related accessories, and other nicotine-containing products, which primarily include PMI's e-vapor products.

PMI recognizes revenue, when control is transferred to the customer, typically either upon shipment or delivery of goods.

Operating income by segment were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Operating income:			
European Union	**$ 3,970**	$ 4,105	$ 3,691
Eastern Europe	**547**	902	887
Middle East & Africa	**1,684**	1,627	1,884
South & Southeast Asia	**2,163**	1,747	1,514
East Asia & Australia	**1,932**	1,851	2,608
Latin America & Canada	**235**	1,145	997
Operating income	**$ 10,531**	$ 11,377	$ 11,581

Items affecting the comparability of results from operations were as follows:

- **Russia excise and VAT audit charge** - See Note 18. *Contingencies* for details of the $374 million pre-tax charge included in the Eastern Europe segment for the year ended December 31, 2019.
- **Asset impairment and exit costs** - See Note 21. *Asset Impairment and Exit Costs* for details of the $422 million pre-tax charge for the year ended December 31, 2019, as well as a breakdown of these costs by segment.
- **Canadian tobacco litigation-related expense** - See Note 18. *Contingencies* and Note 22. *Deconsolidation of RBH* for details of the $194 million pre-tax charge included in the Latin America & Canada segment for the year ended December 31, 2019.
- **Loss on deconsolidation of RBH** - See Note 22. *Deconsolidation of RBH* for details of the $239 million loss included in the Latin America & Canada segment for the year ended December 31, 2019.

Other segment data were as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Depreciation expense:			
European Union	**$ 254**	$ 269	$ 213
Eastern Europe	**147**	101	76
Middle East & Africa	**90**	105	88
South & Southeast Asia	**142**	154	153
East Asia & Australia	**185**	173	160
Latin America & Canada	**69**	94	85
	887	896	775
Other	**11**	11	12
Total depreciation expense	**$ 898**	$ 907	$ 787

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Capital expenditures:			
European Union	**$ 466**	$ 813	$ 956
Eastern Europe	**132**	136	97
Middle East & Africa	**35**	65	85
South & Southeast Asia	**100**	129	140
East Asia & Australia	**67**	215	87
Latin America & Canada	**52**	74	175
	852	1,432	1,540
Other	**—**	4	8
Total capital expenditures	**$ 852**	$ 1,436	$ 1,548

(in millions)	At December 31, 2019	2018	2017
Long-lived assets:			
European Union	**$ 4,275**	$ 4,216	$ 4,130
Eastern Europe	**774**	547	546
Middle East & Africa	**369**	362	430
South & Southeast Asia	**1,361**	1,297	1,419
East Asia & Australia	**829**	781	659
Latin America & Canada	**478**	779	885
Total long-lived assets	**8,086**	7,982	8,069
Other	**516**	664	1,126
Total property, plant and equipment, net and Other assets	**$ 8,602**	$ 8,646	$ 9,195

Long-lived assets consist of non-current assets other than goodwill; other intangible assets, net; deferred tax assets, investments in unconsolidated subsidiaries and equity securities, and financial instruments. PMI's largest markets in terms of long-lived assets are Italy, Switzerland and Indonesia. Total long-lived assets located in Italy, which is reflected in the European Union segment above, were $1.1 billion, $1.1 billion and $1.2 billion at December 31, 2019, 2018 and 2017, respectively. Total long-lived assets located in Switzerland, which is reflected in the European Union segment above, were $1.1 billion, $1.0 billion and $0.9 billion at December 31, 2019, 2018 and 2017, respectively. Total long-lived assets located in Indonesia, which is reflected in the South & Southeast Asia segment above, were $0.8 billion, $0.7 billion and $0.8 billion at December 31, 2019, 2018 and 2017, respectively.

Note 13.

Benefit Plans:

Pension coverage for employees of PMI's subsidiaries is provided, to the extent deemed appropriate, through separate plans, many of which are governed by local statutory requirements. In addition, PMI provides health care and other benefits to substantially all U.S. retired employees and certain non-U.S. retired employees. In general, health care benefits for non-U.S. retired employees are covered through local government plans.

Pension and other employee benefit costs per the consolidated statements of earnings consisted of the following for December 31, 2019, 2018 and 2017:

(in millions)	2019	2018	2017
Net pension costs (income)	**$ (18)**	$ (51)	$ (20)
Net postemployment costs	**100**	80	85
Net postretirement costs	**7**	12	13
Total pension and other employee benefit costs	**$ 89**	$ 41	$ 78

Pension and Postretirement Benefit Plans

Obligations and Funded Status

The postretirement health care plans are not funded. The projected benefit obligations, plan assets and funded status of PMI's pension plans, and the accumulated benefit obligation and net amount accrued for PMI's postretirement health care plans, at December 31, 2019 and 2018, were as follows:

	Pension[(1)]		**Postretirement**	
(in millions)	**2019**	**2018**	**2019**	**2018**
Benefit obligation at January 1	**$ 9,152**	$ 9,028	**$ 209**	$ 248
Service cost	**214**	210	**2**	4
Interest cost	**118**	109	**7**	9
Net benefits paid	**(250)**	(218)	**(8)**	(8)
Settlement and curtailment	**50**	1		—
Actuarial losses (gains)	**1,430**	210	**27**	(34)
Currency	**29**	(196)	**—**	(9)
Deconsolidation of RBH	**(166)**	—	**(42)**	—
Other	**35**	8	**(5)**	(1)
Benefit obligation at December 31,	**10,612**	9,152	**190**	209
Fair value of plan assets at January 1,	**6,888**	7,598		
Actual return on plan assets	**1,211**	(447)		
Employer contributions	**200**	110		
Standard employee contributions	**44**	24		
Net benefits paid	**(250)**	(218)		
Settlement and curtailment	**—**	—		
Currency	**7**	(179)		
Deconsolidation of RBH	**(172)**	—		
Fair value of plan assets at December 31,	**7,928**	6,888		
Net pension and postretirement liability recognized at December 31,	**$ (2,684)**	$ (2,264)	**$ (190)**	$ (209)

(1) Primarily non-U.S. based defined benefit retirement plans.

At December 31, 2019, actuarial losses (gains) consisted primarily of losses for assumption changes related to lower discount rate for Swiss, German and Dutch plans. At December 31, 2018, actuarial losses (gains) consisted of losses for experience differences related to the change in population profile, coupled with updated mortality table assumptions for the Swiss plan.

At December 31, 2019 and 2018, the Swiss pension plan represented 62% and 60% of the benefit obligation, respectively, and approximately 59% and 57% of the fair value of plan assets at December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, the U.S. pension plan represented 4% and 4% of the benefit obligation, respectively, and approximately 4% and 4% of the fair value of plan assets at December 31, 2019 and 2018, respectively.

At December 31, 2019 and 2018, the amounts recognized on PMI's consolidated balance sheets for the pension and postretirement plans were as follows:

	Pension		Postretirement	
(in millions)	**2019**	**2018**	**2019**	**2018**
Other assets	**$ 43**	$ 37		
Accrued liabilities — employment costs	**(23)**	(20)	**$ (8)**	$ (10)
Long-term employment costs	**(2,704)**	(2,281)	**(182)**	(199)
	$ (2,684)	$ (2,264)	**$ (190)**	$ (209)

The accumulated benefit obligation, which represents benefits earned to date, for the pension plans was $9,969 million and $8,557 million at December 31, 2019 and 2018, respectively.

For pension plans with accumulated benefit obligations in excess of plan assets, the accumulated benefit obligation and fair value of plan assets were $8,962 million and $6,825 million, respectively, as of December 31, 2019. The accumulated benefit obligation and fair value of plan assets were $7,641 million and $5,866 million, respectively, as of December 31, 2018.

For pension plans with projected benefit obligations in excess of plan assets, the projected benefit obligation and fair value of plan assets were $10,364 million and $7,654 million, respectively, as of December 31, 2019. The projected benefit obligation and fair value of plan assets were $8,807 million and $6,504 million, respectively, as of December 31, 2018.

The following weighted-average assumptions were used to determine PMI’s pension and postretirement benefit obligations at December 31:

	Pension		Postretirement	
	2019	**2018**	**2019**	**2018**
Discount rate	**0.83%**	1.61%	**3.28%**	3.97%
Rate of compensation increase	**1.82**	1.86		
Interest crediting rate	**3.20**	3.40		
Health care cost trend rate assumed for next year			**6.21**	6.17
Ultimate trend rate			**5.09**	4.59
Year that rate reaches the ultimate trend rate			**2023**	2040

The discount rate for the largest pension plans is based on a yield curve constructed from a portfolio of high quality corporate bonds that produces a cash flow pattern equivalent to each plan’s expected benefit payments. The discount rate for the remaining plans is developed from local bond indices that match local benefit obligations as closely as possible.

Components of Net Periodic Benefit Cost

Net periodic pension and postretirement health care costs consisted of the following for the years ended December 31, 2019, 2018 and 2017:

	Pension			Postretirement		
(in millions)	**2019**	**2018**	**2017**	**2019**	**2018**	**2017**
Service cost	**$ 214**	$ 210	$ 208	**$ 2**	$ 4	$ 4
Interest cost	**118**	109	108	**7**	9	8
Expected return on plan assets	**(328)**	(349)	(326)	**—**	—	—
Amortization:						
Net losses	**189**	172	186	**—**	4	5
Prior service cost	**(1)**	2	6	**—**	(1)	—
Settlement and curtailment	**4**	15	6	**—**	—	—
Net periodic pension and postretirement costs	**$ 196**	$ 159	$ 188	**$ 9**	$ 16	$ 17

Settlement and curtailment charges were due primarily to employee severance and early retirement programs.

The following weighted-average assumptions were used to determine PMI's net pension and postretirement health care costs:

	Pension			Postretirement		
	2019	**2018**	**2017**	**2019**	**2018**	**2017**
Discount rate - service cost	**2.14%**	1.92%	1.68%	**3.97%**	3.79%	3.68%
Discount rate - interest cost	**1.35**	1.25	1.27	**3.97**	3.79	3.68
Expected rate of return on plan assets	**4.70**	4.76	4.80			
Rate of compensation increase	**1.86**	1.65	1.68			
Interest crediting rate	**3.40**	3.40	3.40			
Health care cost trend rate				**6.17**	6.17	7.15

PMI's expected rate of return on pension plan assets is determined by the plan assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

PMI and certain of its subsidiaries sponsor defined contribution plans. Amounts charged to expense for defined contribution plans totaled \$63 million, \$66 million and \$58 million for the years ended December 31, 2019, 2018 and 2017, respectively.

Plan Assets

PMI's investment strategy for pension plans is based on an expectation that equity securities will outperform debt securities over the long term. Accordingly, the target allocation of PMI's plan assets is broadly characterized as approximately 60% in equity securities and approximately 40% in debt securities and other assets. The strategy primarily utilizes indexed U.S. equity securities, international equity securities and investment-grade debt securities. PMI's plans have no investments in hedge funds, private equity or derivatives. PMI attempts to mitigate investment risk by rebalancing between equity and debt asset classes once a year or as PMI's contributions and benefit payments are made.

The fair value of PMI's pension plan assets at December 31, 2019 and 2018, by asset category was as follows:

Asset Category (in millions)	At December 31, 2019	Quoted Prices In Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	**$ 276**	**$ 276**		
Equity securities:				
U.S. securities	**170**	**170**		
International securities	**563**	**563**		
Investment funds[(a)]	**6,125**	**4,625**	**$ 1,500**	
International government bonds	**197**	**137**	**60**	
Corporate bonds	**282**	**282**		
Other	**6**	**6**		
Total assets in the fair value hierarchy	**$ 7,619**	**$ 6,059**	**$ 1,560**	**$ —**
Investment funds measured at net asset value[(b)]	**309**			
Total assets	**$ 7,928**			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and JP Morgan EMBI for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 63% are invested in U.S. and international equities; 16% are invested in U.S. and international government bonds; 12% are invested in real estate and other money markets, and 9% are invested in corporate bonds.

[(b)] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Asset Category (in millions)	At December 31, 2018	Quoted Prices In Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	$ 84	$ 84		
Equity securities:				
U.S. securities	139	139		
International securities	442	442		
Investment funds[(a)]	5,508	3,595	$ 1,913	
International government bonds	176	120	56	
Corporate bonds	232	232		
Other	19	19		
Total assets in the fair value hierarchy	$ 6,600	$ 4,631	$ 1,969	$ —
Investment funds measured at net asset value[(b)]	288			
Total assets	$ 6,888			

[(a)] Investment funds whose objective seeks to replicate the returns and characteristics of specified market indices (primarily MSCI — Europe, Switzerland, North America, Asia Pacific, Japan; Russell 3000; S&P 500 for equities, and Citigroup EMU and Barclays Capital U.S. for bonds), primarily consist of mutual funds, common trust funds and commingled funds. Of these funds, 57% were invested in U.S. and international equities; 20% were invested in U.S. and international government bonds; 12% were invested in real estate and other money markets, and 11% were invested in corporate bonds.

[b] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

See Note 16. *Fair Value Measurements* for a discussion of the fair value of pension plan assets.

PMI makes, and plans to make, contributions to the extent that they are tax deductible and to meet specific funding requirements of its funded pension plans. Currently, PMI anticipates making contributions of approximately $77 million in 2020 to its pension plans, based on current tax and benefit laws. 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 and currency rates.

The estimated future benefit payments from PMI pension plans at December 31, 2019, are as follows:

(in millions)		
2020	$	317
2021		340
2022		341
2023		351
2024		361
2025 - 2029		2,008

PMI's expected future annual benefit payments for its postretirement health care plans are estimated to be not material through 2029.

Postemployment Benefit Plans

PMI and certain of its subsidiaries sponsor postemployment benefit plans covering substantially all salaried and certain hourly employees. The cost of these plans is charged to expense over the working life of the covered employees. Net postemployment costs were $171 million, $158 million and $144 million for the years ended December 31, 2019, 2018 and 2017, respectively.

The amounts recognized in accrued postemployment costs on PMI's consolidated balance sheets at December 31, 2019 and 2018, were $751 million and $708 million, respectively. The change in the liability is primarily due to actuarial losses of $152 million in 2019 resulting from increased employee severance rate primarily in countries in the European Union segment, coupled with the periodic expense, partially offset by cash payments.

The accrued postemployment costs were determined using a weighted-average discount rate of 3.0% and 3.1% in 2019 and 2018, respectively; an assumed ultimate annual weighted-average turnover rate of 3.0% and 3.2% in 2019 and 2018, respectively; assumed compensation cost increases of 2.6% in 2019 and 2.6% in 2018, and assumed benefits as defined in the respective plans. In accordance with local regulations, certain postemployment plans are funded. As a result, the accrued postemployment costs disclosed above are presented net of the related assets of $40 million and $38 million at December 31, 2019 and 2018, respectively. Postemployment costs arising from actions that offer employees benefits in excess of those specified in the respective plans are charged to expense when incurred.

Comprehensive Earnings (Losses)

The amounts recorded in accumulated other comprehensive losses at December 31, 2019, consisted of the following:

(in millions)		**Pension**		**Post-retirement**		**Post-employment**		**Total**
Net losses	**$**	**(3,718)**	**$**	**(63)**	**$**	**(775)**	**$**	**(4,556)**
Prior service cost		**3**		**2**		**—**		**5**
Net transition obligation		**(4)**		**—**		**—**		**(4)**
Deferred income taxes		**520**		**24**		**182**		**726**
Losses to be amortized	**$**	**(3,199)**	**$**	**(37)**	**$**	**(593)**	**$**	**(3,829)**

The amounts recorded in accumulated other comprehensive losses at December 31, 2018, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (3,438)	$ (41)	$ (702)	$ (4,181)
Prior service cost	(27)	3	—	(24)
Net transition obligation	(4)	—	—	(4)
Deferred income taxes	379	20	164	563
Losses to be amortized	$ (3,090)	$ (18)	$ (538)	$ (3,646)

The amounts recorded in accumulated other comprehensive losses at December 31, 2017, consisted of the following:

(in millions)	Pension	Post-retirement	Post-employment	Total
Net losses	$ (2,624)	$ (80)	$ (617)	$ (3,321)
Prior service cost	(35)	4	—	(31)
Net transition obligation	(5)	—	—	(5)
Deferred income taxes	327	28	186	541
Losses to be amortized	$ (2,337)	$ (48)	$ (431)	$ (2,816)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2019, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	**$ 198**	**$ 3**	**$ 77**	**$ 278**
Prior service cost	**32**	**(1)**	**—**	**31**
Other income/expense:				
Net losses	**3**	**—**	**—**	**3**
Deferred income taxes	**(51)**	**(1)**	**(17)**	**(69)**
	182	**1**	**60**	**243**
Other movements during the year:				
Net losses	**(521)**	**(27)**	**(150)**	**(698)**
Prior service cost	**(2)**	**—**	**—**	**(2)**
Deconsolidation of RBH (net of deferred income taxes)	**26**	**1**		**27**
Deferred income taxes	**206**	**6**	**35**	**247**
	(291)	**(20)**	**(115)**	**(426)**
Total movements in other comprehensive earnings (losses)	**$ (109)**	**$ (19)**	**$ (55)**	**$ (183)**

The movements in other comprehensive earnings (losses) during the year ended December 31, 2018, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 180	$ 5	$ 62	$ 247
Prior service cost	—	(1)	—	(1)
Net transition obligation	1	—	—	1
Other income/expense:				
Net losses	14	—	—	14
Deferred income taxes	(28)	(1)	(14)	(43)
	167	3	48	218
Other movements during the year:				
Net losses	(1,008)	34	(147)	(1,121)
Prior service cost	8	—	—	8
Deferred income taxes	80	(7)	(8)	65
	(920)	27	(155)	(1,048)
Total movements in other comprehensive earnings (losses)	$ (753)	$ 30	$ (107)	$ (830)

The movements in other comprehensive earnings (losses) during the year ended December 31, 2017, were as follows:

(in millions)	Pension	Post-retirement	Post-employment	Total
Amounts transferred to earnings as components of net periodic benefit cost:				
Amortization:				
Net losses	$ 175	$ 5	$ 68	$ 248
Prior service cost	5	—	—	5
Other income/expense:				
Net losses	6	—	—	6
Deferred income taxes	(10)	(1)	(20)	(31)
	176	4	48	228
Other movements during the year:				
Net losses	509	(12)	28	525
Prior service cost	13	—	—	13
Deferred income taxes	(13)	5	(9)	(17)
	509	(7)	19	521
Total movements in other comprehensive earnings (losses)	$ 685	$ (3)	$ 67	$ 749

Note 14.

Additional Information:

(in millions)	For the Years Ended December 31, 2019	2018	2017
Research and development expense	**$ 465**	$ 383	$ 453
Advertising expense	**$ 730**	$ 896	$ 830
Foreign currency net transaction (gains)/losses	**$ (95)**	$ 21	$ 49
Interest expense	**$ 796**	$ 855	$ 1,096
Interest income	**(226)**	(190)	(182)
Interest expense, net	**$ 570**	$ 665	$ 914
Total lease cost	**$ 332** [1]	$ 312	$ 313

[1] For additional information on total lease costs, see Note 23. *Leases.*

Note 15.

Financial Instruments:

Overview

PMI operates in markets outside of the United States of America, with manufacturing and sales facilities in various locations around the world. PMI utilizes certain financial instruments to manage foreign currency and interest rate exposure. Derivative financial instruments are used by PMI principally to reduce exposures to market risks resulting from fluctuations in foreign currency exchange and interest rates by creating offsetting exposures. PMI is not a party to leveraged derivatives and, by policy, does not use derivative financial instruments for speculative purposes. Financial instruments qualifying for hedge accounting must maintain a specified level of effectiveness between the hedging instrument and the item being hedged, both at inception and throughout the hedged period. PMI formally documents the nature and relationships between the hedging instruments and hedged items, as well as its risk-management objectives, strategies for undertaking the various hedge transactions and method of assessing hedge effectiveness. Additionally, for hedges of forecasted transactions, the significant characteristics and expected terms of the forecasted transaction must be specifically identified, and it must be probable that each forecasted transaction will occur. If it were deemed probable that the forecasted transaction would not occur, the gain or loss would be recognized in earnings.

PMI uses deliverable and non-deliverable forward foreign exchange contracts, foreign currency swaps and foreign currency options, collectively referred to as foreign exchange contracts ("foreign exchange contracts"), and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Both foreign exchange contracts and interest rate contracts are collectively referred to as derivative contracts ("derivative contracts"). The primary currencies to which PMI is exposed include the Euro, Indonesian rupiah, Japanese yen, Mexican peso, Philippine peso, Russian ruble and Swiss franc. At December 31, 2019 and 2018, PMI had contracts with aggregate notional amounts of $24.1 billion and $27.4 billion, respectively. Of the $24.1 billion aggregate notional amount at December 31, 2019, $2.8 billion related to cash flow hedges, $9.9 billion related to hedges of net investments in foreign operations and $11.4 billion related to other derivatives that primarily offset currency exposures on intercompany financing. Of the $27.4 billion aggregate notional amount at December 31, 2018, $3.2 billion related to cash flow hedges, $10.1 billion related to hedges of net investments in foreign operations and $14.1 billion related to other derivatives that primarily offset currency exposures on intercompany financing.

The fair value of PMI's derivative exchange contracts included in the consolidated balance sheet as of December 31, 2019 and 2018, were as follows:

	Derivative Assets			Derivative Liabilities		
		Fair Value			Fair Value	
(in millions)	**Balance Sheet Classification**	**2019**	**2018**	**Balance Sheet Classification**	**2019**	**2018**
Derivative contracts designated as hedging instruments	Other current assets	**$ 319**	$ 54	Other accrued liabilities	**$ 23**	$ 47
	Other assets	**21**	99	Income taxes and other liabilities	**301**	525
Derivative contracts not designated as hedging instruments	Other current assets	**50**	67	Other accrued liabilities	**70**	46
	Other assets	**—**	—	Income taxes and other liabilities	**25**	13
Total derivatives		**$ 390**	$ 220		**$ 419**	$ 631

For the years ended December 31, 2019, 2018 and 2017, PMI's cash flow and net investment hedging instruments impacted the consolidated statements of earnings and comprehensive earnings as follows:

(pre-tax, in millions)	**For the Year Ended December 31,**						
	Amount of Gain/(Loss) Recognized in Other Comprehensive Earnings/(Losses) on Derivatives			**Statement of Earnings Classification of Gain/(Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings**	**Amount of Gain/(Loss) Reclassified from Other Comprehensive Earnings/(Losses) into Earnings**		
	2019	**2018**	**2017**		**2019**	**2018**	**2017**
Derivatives in Cash Flow Hedging Relationship							
Derivative contracts	**$ (20)**	$ 28	$ (52)				
				Net revenues	**$ 22**	$ 18	$ 60
				Cost of sales	**1**	—	1
				Marketing, administration and research costs	**2**	6	(7)
				Interest expense, net	**(8)**	(1)	(41)
Derivatives in Net Investment Hedging Relationship							
Derivative contracts	**369**	324	(1,644)				
Total	**$ 349**	$ 352	$ (1,696)		**$ 17**	$ 23	$ 13

Cash Flow Hedges

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to certain forecasted transactions. Gains and losses associated with qualifying cash flow hedge contracts are deferred as components of accumulated other comprehensive losses until the underlying hedged transactions are reported in PMI's consolidated statements of earnings. As of December 31, 2019, PMI has hedged forecasted transactions for periods not exceeding the next twelve months, with the exception of one derivative contract that expires in May 2024. The impact of these hedges is primarily included in operating cash flows on PMI's consolidated statements of cash flows.

Hedges of Net Investments in Foreign Operations

PMI designates certain foreign currency denominated debt and derivative contracts as net investment hedges, primarily of its Euro net assets. For the years ended December 31, 2019, 2018 and 2017, these hedges of net investments resulted in gains (losses), net of income taxes, of $470 million, $521 million and $(1,725) million, respectively, principally related to changes in the exchange rates between the Euro and U.S. dollar. These gains (losses) were reported as a component of accumulated other comprehensive losses within currency translation adjustments and were substantially offset by the losses and gains generated on the underlying assets. For the years ended December 31, 2019 and 2018, the gains for amounts excluded from the effectiveness testing recognized in earnings were $230 million and $260 million, respectively. These gains were accounted for in interest expense, net, on the consolidated statement of earnings. The premiums paid for, and settlements of, net investment hedges are included in investing cash flows on PMI's consolidated statements of cash flows.

Other Derivatives

PMI has entered into derivative contracts to hedge the foreign currency exchange and interest rate risks related to intercompany loans between certain subsidiaries, and third-party loans. While effective as economic hedges, no hedge accounting is applied for these contracts; therefore, the unrealized gains (losses) relating to these contracts are reported in marketing, administration and research costs in PMI's consolidated statements of earnings. For the years ended December 31, 2019, 2018 and 2017, the gains (losses) from contracts for which PMI did not apply hedge accounting were $(57) million, $405 million and $382 million, respectively. The gains (losses) from these contracts substantially offset the losses and gains generated by the underlying intercompany and third-party loans being hedged.

As a result, for the years ended December 31, 2019, 2018 and 2017, these items impacted the consolidated statement of earnings as follows:

(pre-tax, in millions)

Derivatives not Designated as Hedging Instruments	**Statement of Earnings Classification of Gain/(Loss)**	**Amount of Gain/(Loss) Recognized in Earnings**		
		2019	**2018**	**2017**
Derivative contracts				
	Interest expense, net	**$ 94**	$ 62	$ (60)
Total		**$ 94**	$ 62	$ (60)

Qualifying Hedging Activities Reported in Accumulated Other Comprehensive Losses

Derivative gains or losses reported in accumulated other comprehensive losses are a result of qualifying hedging activity. Transfers of these gains or losses to earnings are offset by the corresponding gains or losses on the underlying hedged item. Hedging activity affected accumulated other comprehensive losses, net of income taxes, as follows:

	For the Years Ended December 31,		
(in millions)	**2019**	**2018**	**2017**
Gain as of January 1,	**$ 35**	$ 42	$ 97
Derivative (gains)/losses transferred to earnings	**(14)**	(31)	(11)
Change in fair value	**(18)**	24	(44)
Gain as of December 31,	**$ 3**	$ 35	$ 42

At December 31, 2019, PMI expects $22 million of derivative gains that are included in accumulated other comprehensive losses to be reclassified to the consolidated statement of earnings within the next 12 months. These gains are expected to be substantially offset by the statement of earnings impact of the respective hedged transactions.

Contingent Features

PMI's derivative instruments do not contain contingent features.

Credit Exposure and Credit Risk

PMI is exposed to credit loss in the event of non-performance by counterparties. While PMI does not anticipate non-performance, its risk is limited to the fair value of the financial instruments less any cash collateral received or pledged. PMI actively monitors its exposure to credit risk through the use of credit approvals and credit limits and by selecting and continuously monitoring a diverse group of major international banks and financial institutions as counterparties.

Fair Value

See Note 16. *Fair Value Measurements* and Note 19. *Balance Sheet Offsetting* for additional discussion of derivative financial instruments.

Note 16.

Fair Value Measurements:

The authoritative guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of input that may be used to measure fair value, which are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities;

Level 2 — Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Equity Securities

The fair value of PMI's equity securities, which are determined by using quoted prices in active markets, have been classified within Level 1.

Derivative Financial Instruments

PMI assesses the fair value of its foreign exchange contracts and interest rate contracts using standard valuation models that use, as their basis, readily observable market inputs. The fair value of PMI's foreign exchange forward contracts is determined by using the prevailing foreign exchange spot rates and interest rate differentials, and the respective maturity dates of the instruments. The fair value of PMI's currency options is determined by using a Black-Scholes methodology based on foreign exchange spot rates and interest rate differentials, currency volatilities and maturity dates. PMI's derivative financial instruments have been classified within Level 2 at December 31, 2019 and 2018. See Note 15. *Financial Instruments* for additional discussion of derivative financial instruments.

Pension Plan Assets

The fair value of pension plan assets, determined by using readily available quoted market prices in active markets, has been classified within Level 1 of the fair value hierarchy at December 31, 2019 and 2018. The fair value of pension plan assets, determined by using quoted prices in markets that are not active, has been classified within Level 2 at December 31, 2019 and 2018. See Note 13. *Benefit Plans* for additional discussion of pension plan assets.

Debt

The fair value of PMI's outstanding debt, which is utilized solely for disclosure purposes, is determined using quotes and market interest rates currently available to PMI for issuances of debt with similar terms and remaining maturities. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $56 million of finance leases, was $30,651 million at December 31, 2019. The aggregate carrying value of PMI's debt, excluding short-term borrowings and $33 million of finance leases, was $30,996 million at December 31,

2018. The fair value of PMI's outstanding debt, excluding the aforementioned short-term borrowings and finance leases, was classified within Level 1 and Level 2 at December 31, 2019 and 2018.

The aggregate fair values of PMI's investments in equity securities, derivative financial instruments, pension plan assets and PMI's debt as of December 31, 2019, were as follows:

(in millions)	Fair Value at December 31, 2019	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Equity securities [1]	$ 332	$ 332	$ —	$ —
Derivative contracts	390	$ —	390	—
Pension plan assets	7,619	6,059	1,560	—
Total assets in fair value hierarchy	$ 8,341	$ 6,391	$ 1,950	$ —
Pension plan assets measured at net asset value [2]	309			
Total assets	$ 8,650			
Liabilities:				
Debt	$ 32,988	$ 32,821	$ 167	$ —
Derivative contracts	419	—	419	—
Total liabilities	$ 33,407	$ 32,821	$ 586	$ —

[1] Unrealized pre-tax gain of $44 million ($35 million net of tax) on equity securities was recorded in the consolidated statement of earnings for the year ended December 31, 2019.

[2] In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

The aggregate fair values of PMI's investments in equity securities, derivative financial instruments, pension plan assets and PMI's debt as of December 31, 2018 , were as follows:

(in millions)		Fair Value at December 31, 2018		Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)
Assets:								
Equity securities	$	288	$	288	$	—	$	—
Derivative contracts		220		—		220		—
Pension plan assets		6,600		4,631		1,969		—
Total assets in fair value hierarchy	$	7,108	$	4,919	$	2,189	$	—
Pension plan assets measured at net asset value [(1)]		288						
Total assets	$	7,396						
Liabilities:								
Debt	$	31,162	$	30,997	$	165	$	—
Derivative contracts		631		—		631		—
Total liabilities	$	31,793	$	30,997	$	796	$	—

(1) In accordance with FASB ASC Subtopic 820-10, certain investments measured at fair value using the net asset value per share practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in these tables are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

Note 17.

Accumulated Other Comprehensive Losses:

PMI's accumulated other comprehensive losses, net of taxes, consisted of the following:

(Losses) Earnings	At December 31,					
(in millions)		2019		2018		2017
Currency translation adjustments	**$**	**(5,537)**	$	(6,500)	$	(5,761)
Pension and other benefits		**(3,829)**		(3,646)		(2,816)
Derivatives accounted for as hedges		**3**		35		42
Total accumulated other comprehensive losses	**$**	**(9,363)**	$	(10,111)	$	(8,535)

Reclassifications from Other Comprehensive Earnings

The movements in accumulated other comprehensive losses and the related tax impact, for each of the components above, that are due to current period activity and reclassifications to the income statement, including those related to the deconsolidation of RBH, are shown on the consolidated statements of comprehensive earnings for the years ended December 31, 2019, 2018, and 2017. For the year ended 2017, $2 million of net currency translation adjustment gains/(losses) were transferred from other comprehensive earnings to marketing, administration and research costs in the consolidated statements of earnings, respectively, upon liquidation of subsidiaries. For additional information, see Note 13. *Benefit Plans* for disclosures related to PMI's pension and other benefits, Note 15. *Financial Instruments* for disclosures related to derivative financial instruments and Note 22. *Deconsolidation of RBH* for disclosures related to the deconsolidation of RBH.

Note 18.

Contingencies:

Tobacco-Related Litigation

Legal proceedings covering a wide range of matters are pending or threatened against us, and/or our subsidiaries, and/or our indemnitees in various jurisdictions. Our indemnitees include distributors, licensees, and others that have been named as parties in certain cases and that we have agreed to defend, as well as to pay costs and some or all of judgments, if any, that may be entered against them. Pursuant to the terms of the Distribution Agreement between Altria Group, Inc. ("Altria") and PMI, PMI will indemnify Altria and Philip Morris USA Inc. ("PM USA"), a U.S. tobacco subsidiary of Altria, for tobacco product claims based in substantial part on products manufactured by PMI or contract manufactured for PMI by PM USA, and PM USA will indemnify PMI for tobacco product claims based in substantial part on products manufactured by PM USA, excluding tobacco products contract manufactured for PMI.

It is possible that there could be adverse developments in pending cases against us and our subsidiaries. An unfavorable outcome or settlement of pending tobacco-related litigation could encourage the commencement of additional litigation.

Damages claimed in some of the tobacco-related litigation are significant and, in certain cases in Brazil, Canada and Nigeria, range into the billions of U.S. 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. Much of the tobacco-related litigation is in its early stages, and litigation is subject to uncertainty. However, as discussed below, we have to date been largely successful in defending tobacco-related litigation.

We and our subsidiaries record provisions in the consolidated financial statements for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. At the present time, except as stated otherwise in this Note 18. *Contingencies,* while it is reasonably possible that an unfavorable outcome in a case may occur, after assessing the information available to it (i) management has not concluded that it is 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 for any of the pending tobacco-related cases; and (iii) accordingly, no estimated loss has been accrued in the consolidated financial statements for unfavorable outcomes in these cases, if any. Legal defense costs are expensed as incurred.

It is possible that our consolidated results of operations, cash flows or financial position could be materially affected in a particular fiscal quarter or fiscal year by an unfavorable outcome or settlement of certain pending litigation. Nevertheless, although litigation is subject to uncertainty, we and each of our subsidiaries named as a defendant believe, and each has been so advised by counsel handling the respective cases, that we have valid defenses to the litigation pending against us, as well as valid bases for appeal of adverse verdicts. All such cases are, and will continue to be, vigorously defended. However, we and our subsidiaries may enter into settlement discussions in particular cases if we believe it is in our best interests to do so.

CCAA Proceedings and Stay of Tobacco-Related Cases Pending in Canada

As a result of the Court of Appeal of Quebec's decision in both the *Létourneau* and *Blais* cases described below, our subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), and the other defendants, JTI Macdonald Corp., and Imperial Tobacco Canada Limited, sought protection in the Ontario Superior Court of Justice under the Companies' Creditors Arrangement Act ("CCAA") on March 22, March 8, and March 12, respectively. CCAA is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course. The initial CCAA order made by the Ontario Superior Court on March 22, 2019 authorizes RBH to pay all expenses incurred in carrying on its business in the ordinary course after the CCAA filing, including obligations to employees, vendors, and suppliers. As further described in Note 22. *Deconsolidation of RBH*, RBH is now deconsolidated from our consolidated financial statements. As part of the CCAA proceedings, there is currently a comprehensive stay up to and including March 12, 2020 of all tobacco-related litigation pending in Canada against RBH and the other defendants, including PMI and our indemnitees (PM USA and Altria), namely, the smoking and health class actions filed in various Canadian provinces and health care cost recovery actions. These proceedings are presented below under the caption "*Stayed Litigation — Canada*." Ernst & Young Inc. has been appointed as monitor of RBH in the CCAA proceedings. In accordance with the CCAA process, as the parties work towards a plan of arrangement or compromise in a confidential mediation, it is anticipated that the court will set additional hearings and further extend the stay of proceedings. On April 17, 2019, the Ontario Superior Court ruled that RBH and the other defendants will not be allowed to file an application to the Supreme Court of Canada for leave to appeal the Court of Appeal's decision in the *Létourneau* and the *Blais* cases so long as the comprehensive stay of all tobacco-related litigation in Canada remains in effect and that the time period to file the application would be extended by the stay period. While RBH believes that the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect, the CCAA proceedings will provide a forum for RBH to seek resolution through a plan of arrangement or compromise of all tobacco-related litigation pending in Canada. It is not possible to predict the resolution of the underlying legal proceedings or the length of the CCAA process.

Stayed Litigation — Canada

Smoking and Health Litigation — Canada

In the first class action pending in Canada, *Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada*, filed in November 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiffs, an anti-smoking organization and an individual smoker, sought compensatory and punitive damages for each member of the class who allegedly suffers from certain smoking-related diseases. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and found that the class members' compensatory damages totaled approximately CAD 15.5 billion, including pre-judgment interest (approximately $11.7 billion). The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion, including pre-judgment interest (approximately $2.34 billion)). In addition, the trial court awarded CAD 90,000 (approximately $67,980) in punitive damages, allocating CAD 30,000 (approximately $22,660) to RBH. The trial court estimated the disease class at 99,957 members. RBH appealed to the Court of Appeal of Quebec. In October 2015, the Court of Appeal ordered RBH to furnish security totaling CAD 226 million (approximately $170.7 million) to cover both the *Létourneau* and *Blais* cases, which RBH has paid in installments through March 2017. The Court of Appeal ordered Imperial Tobacco Canada Ltd. to furnish security totaling CAD 758 million (approximately $573 million) in installments through June 2017. JTI Macdonald Corp. was not required to furnish security in accordance with plaintiffs' motion. The Court of Appeal ordered that the security is payable upon a final judgment of the Court of Appeal affirming the trial court's judgment or upon further order of the Court of Appeal. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the compensatory and punitive damages award while reducing the total amount of compensatory damages to approximately CAD 13.5 billion including interest (approximately $10.2 billion) due to the trial court's error in the calculation of interest. The compensatory damages award is on a joint and several basis with an allocation of 20% to RBH (approximately CAD 2.7 billion, including pre-judgment interest (approximately $2.04 billion)). The Court of Appeal upheld the trial court's findings that defendants violated the Civil Code of Quebec, the Quebec Charter of Human Rights and Freedoms, and the Quebec Consumer Protection Act by failing to warn adequately of the dangers of smoking and by conspiring to prevent consumers from learning of the dangers of smoking. The Court of Appeal further held that the plaintiffs either need not prove, or had adequately proven, that these faults were a cause of the class members' injuries. In accordance with the judgment, defendants are required to deposit their respective portions of the damages awarded in both the *Létourneau* case described below and the *Blais* case, approximately CAD 1.1 billion (approximately $831 million), into trust accounts within 60 days. RBH's share of the deposit is approximately CAD 257 million (approximately $194.1 million). PMI recorded a pre-tax charge of $194 million in its consolidated results, representing $142 million net of tax, as tobacco litigation-related expense, in the first quarter of 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment.

In the second class action pending in Canada, *Cecilia Létourneau v. Imperial Tobacco Ltd., Rothmans, Benson & Hedges Inc. and JTI-Macdonald Corp., Quebec Superior Court, Canada,* filed in September 1998, RBH and other Canadian manufacturers (Imperial Tobacco Canada Ltd. and JTI-Macdonald Corp.) are defendants. The plaintiff, an individual smoker, sought compensatory and punitive damages for each member of the class who is deemed addicted to smoking. The class was certified in 2005. The trial court issued its judgment on May 27, 2015. The trial court found RBH and two other Canadian manufacturers liable and awarded a total of CAD 131 million (approximately $99 million) in punitive damages, allocating CAD 46 million (approximately $34.7 million) to RBH. The trial court estimated the size of the addiction class at 918,000 members but declined to award compensatory damages to the addiction class because the evidence did not establish the claims with sufficient accuracy. The trial court found that a claims process to allocate the awarded punitive damages to individual class members would be too expensive and difficult to administer. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's findings of liability and the total amount of punitive damages awarded allocating CAD 57 million including interest (approximately $43.1 million) to RBH. See the *Blais* description above and Note 22. *Deconsolidation of RBH* below for further detail concerning the security order pertaining to both *Létourneau* and *Blais* cases and the impact of the decision on PMI's financial statements.

RBH and PMI believe the findings of liability and damages in both *Létourneau* and the *Blais* cases were incorrect and in contravention of applicable law on several grounds including the following: (i) defendants had no obligation to warn class members who knew, or should have known, of the risks of smoking; (ii) defendants cannot be liable to class members who would have smoked regardless of what warnings were given; and (iii) defendants cannot be liable to all class members given the individual differences between class members.

In the third class action pending in Canada, *Kunta v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Winnipeg, Canada*, filed June 12, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic obstructive pulmonary disease ("COPD"), severe asthma, and mild reversible lung disease resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the fourth class action pending in Canada, *Adams v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Saskatchewan, Canada*, filed July 10, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, emphysema, heart disease, or cancer, as well as restitution of profits.

In the fifth class action pending in Canada, *Semple v. Canadian Tobacco Manufacturers' Council, et al., The Supreme Court (trial court), Nova Scotia, Canada*, filed June 18, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and COPD resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, as well as restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products.

In the sixth class action pending in Canada, *Dorion v. Canadian Tobacco Manufacturers' Council, et al., The Queen's Bench, Alberta, Canada,* filed June 15, 2009, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and chronic bronchitis and severe sinus infections resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers, their estates, dependents and family members, restitution of profits, and reimbursement of government health care costs allegedly caused by tobacco products. To date, we, our subsidiaries, and our indemnitees have not been properly served with the complaint.

In the seventh class action pending in Canada, *McDermid v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges his own addiction to tobacco products and heart disease resulting from the use of tobacco products. He is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from heart disease allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed.

In the eighth class action pending in Canada, *Bourassa v. Imperial Tobacco Canada Limited, et al., Supreme Court, British Columbia, Canada*, filed June 25, 2010, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, the heir to a deceased smoker, alleges that the decedent was addicted to tobacco products and suffered from emphysema resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who were alive on June 12, 2007, and who suffered from chronic respiratory diseases allegedly caused by smoking, their estates, dependents and family members, plus disgorgement of revenues earned by the defendants from January 1, 1954, to the date the claim was filed. In December 2014, plaintiff filed an amended statement of claim.

In the ninth class action pending in Canada, *Suzanne Jacklin v. Canadian Tobacco Manufacturers' Council, et al., Ontario Superior Court of Justice,* filed June 20, 2012, we, RBH, and our indemnitees (PM USA and Altria), and other members of the industry are defendants. The plaintiff, an individual smoker, alleges her own addiction to tobacco products and COPD resulting from the use of tobacco products. She is seeking compensatory and punitive damages on behalf of a proposed class comprised of all smokers who have smoked a minimum of 25,000 cigarettes and have allegedly suffered, or suffer, from COPD, heart disease, or cancer, as well as restitution of profits.

Health Care Cost Recovery Litigation — Canada

In the first health care cost recovery case pending in Canada, *Her Majesty the Queen in Right of British Columbia v. Imperial Tobacco Limited, et al., Supreme Court, British Columbia, Vancouver Registry, Canada,* filed January 24, 2001, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The plaintiff, the government of the province of British Columbia, brought a claim based upon legislation enacted by the province authorizing the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, resulting from a “tobacco related wrong.”

In the second health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of New Brunswick v. Rothmans Inc., et al., Court of Queen's Bench of New Brunswick, Trial Court, New Brunswick, Fredericton, Canada,* filed March 13, 2008, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of New Brunswick based on legislation enacted in the province. This legislation is similar to the law introduced in British Columbia that authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a “tobacco related wrong.”

In the third health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of Ontario v. Rothmans Inc., et al., Ontario Superior Court of Justice, Toronto, Canada*, filed September 29, 2009, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Ontario based on legislation enacted in the province. This legislation is similar to the laws introduced in British Columbia and New Brunswick that authorize the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fourth health care cost recovery case filed in Canada, *Attorney General of Newfoundland and Labrador v. Rothmans Inc., et al., Supreme Court of Newfoundland and Labrador, St. Johns, Canada*, filed February 8, 2011, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Newfoundland and Labrador based on legislation enacted in the province that is similar to the laws introduced in British Columbia, New Brunswick and Ontario. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the fifth health care cost recovery case filed in Canada, *Attorney General of Quebec v. Imperial Tobacco Limited, et al., Superior Court of Quebec, Canada*, filed June 8, 2012, we, RBH, our indemnitee (PM USA), and other members of the industry are defendants. The claim was filed by the government of the province of Quebec based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the sixth health care cost recovery case filed in Canada, *Her Majesty in Right of Alberta v. Altria Group, Inc., et al., Supreme Court of Queen's Bench Alberta, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Alberta based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the seventh health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Manitoba v. Rothmans, Benson & Hedges, Inc., et al., The Queen's Bench, Winnipeg Judicial Centre, Canada*, filed May 31, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Manitoba based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the eighth health care cost recovery case filed in Canada, *The Government of Saskatchewan v. Rothmans, Benson & Hedges Inc., et al., Queen's Bench, Judicial Centre of Saskatchewan, Canada*, filed June 8, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Saskatchewan based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the ninth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Prince Edward Island v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Prince Edward Island (General Section), Canada*, filed September 10, 2012, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Prince Edward Island based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

In the tenth health care cost recovery case filed in Canada, *Her Majesty the Queen in Right of the Province of Nova Scotia v. Rothmans, Benson & Hedges Inc., et al., Supreme Court of Nova Scotia, Canada*, filed January 2, 2015, we, RBH, our indemnitees (PM USA and Altria), and other members of the industry are defendants. The claim was filed by the government of the province of Nova Scotia based on legislation enacted in the province that is similar to the laws enacted in several other Canadian provinces. The legislation authorizes the government to file a direct action against cigarette manufacturers to recover the health care costs it has incurred, and will incur, as a result of a "tobacco related wrong."

The table below lists the number of tobacco-related cases pertaining to combustible products pending against us and/or our subsidiaries or indemnitees as of February 3, 2020, February 4, 2019 and February 9, 2018:[1]

Type of Case	Number of Cases Pending as of February 3, 2020	Number of Cases Pending as of February 4, 2019	Number of Cases Pending as of February 9, 2018
Individual Smoking and Health Cases	50	55	57
Smoking and Health Class Actions	10	10	11
Health Care Cost Recovery Actions	17	16	16
Label-Related Class Actions	—	1	1
Individual Label-Related Cases	5	7	1
Public Civil Actions	2	2	2

Since 1995, when the first tobacco-related litigation was filed against a PMI entity, 501 Smoking and Health, Label-Related, Health Care Cost Recovery, and Public Civil Actions in which we and/or one of our subsidiaries and/or indemnitees were a defendant have been terminated in our favor. Thirteen cases have had decisions in favor of plaintiffs. Nine of these cases have subsequently reached final resolution in our favor and four remain on appeal.

The table below lists the verdict and significant post-trial developments in the four pending cases where a verdict was returned in favor of the plaintiff:

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
February 2004	Brazil/The Smoker Health Defense Association	Class Action	The Civil Court of São Paulo found defendants liable without hearing evidence. In April 2004, the court awarded "moral damages" of R$1,000 (approximately $233) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not assess actual damages, which were to be assessed in a second phase of the case. The size of the class was not defined in the ruling.	Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

[1] Includes cases pending in Canada.

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Conseil Québécois Sur Le Tabac Et La Santé and Jean-Yves Blais	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Blais* class on liability and found the class members' compensatory damages totaled approximately CAD 15.5 billion (approximately $11.7 billion), including pre-judgment interest. The trial court awarded compensatory damages on a joint and several liability basis, allocating 20% to our subsidiary (approximately CAD 3.1 billion including pre-judgment interest (approximately $2.34 billion)). The trial court awarded CAD 90,000 (approximately $67,980) in punitive damages, allocating CAD 30,000 (approximately $22,660) to our subsidiary. The trial court ordered defendants to pay CAD 1 billion (approximately $755.3 million) of the compensatory damage award, CAD 200 million (approximately $151.1 million) of which is our subsidiary's portion, into a trust within 60 days.	In June 2015, RBH commenced the appellate process with the Court of Appeal of Quebec. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's decision. (See "*Stayed Litigation — Canada*" for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
May 27, 2015	Canada/Cecilia Létourneau	Class Action	On May 27, 2015, the Superior Court of the District of Montreal, Province of Quebec ruled in favor of the *Létourneau* class on liability and awarded a total of CAD 131 million (approximately $99 million) in punitive damages, allocating CAD 46 million (approximately $34.7 million) to RBH. The trial court ordered defendants to pay the full punitive damage award into a trust within 60 days. The court did not order the payment of compensatory damages.	In June 2015, RBH commenced the appellate process with the Court of Appeal of Quebec. On March 1, 2019, the Court of Appeal issued a decision largely affirming the trial court's decision. (See "*Stayed Litigation — Canada*" for further detail.)

Date	Location of Court/Name of Plaintiff	Type of Case	Verdict	Post-Trial Developments
August 5, 2016	Argentina/Hugo Lespada	Individual Action	On August 5, 2016, the Civil Court No. 14 - Mar del Plata, issued a verdict in favor of plaintiff, an individual smoker, and awarded him ARS 110,000 (approximately $1,825), plus interest, in compensatory and moral damages. The trial court found that our subsidiary failed to warn plaintiff of the risk of becoming addicted to cigarettes.	On August 23, 2016, our subsidiary filed its notice of appeal. On October 31, 2017, the Civil and Commercial Court of Appeals of Mar del Plata ruled that plaintiff's claim was barred by the statute of limitations and it reversed the trial court's decision. On November 28, 2017, plaintiff filed an extraordinary appeal of the reversal of the trial court's decision to the Supreme Court of the Province of Buenos Aires.

Pending claims related to tobacco products generally fall within the following categories:

Smoking and Health Litigation: These cases primarily allege personal injury and are brought by individual plaintiffs or on behalf of a class or purported class of individual plaintiffs. Plaintiffs' allegations of liability in these cases are based on various theories of recovery, including negligence, gross negligence, strict liability, fraud, misrepresentation, design defect, failure to warn, breach of express and implied warranties, violations of deceptive trade practice laws and consumer protection statutes. Plaintiffs in these cases seek various forms of relief, including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include licit activity, failure to state a claim, lack of defect, lack of proximate cause, assumption of the risk, contributory negligence, and statute of limitations.

As of February 3, 2020, there were a number of smoking and health cases pending against us, our subsidiaries or indemnitees, as follows:

- 50 cases brought by individual plaintiffs in Argentina (31), Brazil (5), Canada (2), Chile (5), Costa Rica (1), Italy (1), the Philippines (1), Poland (2), Turkey (1) and Scotland (1), compared with 55 such cases on February 4, 2019, and 57 cases on February 9, 2018; and
- 10 cases brought on behalf of classes of individual plaintiffs in Brazil (1) and Canada (9), compared with 10 such cases on February 4, 2019 and 11 such cases on February 9, 2018.

The class actions pending in Canada are described above under the caption "*Smoking and Health Litigation — Canada.*"

In the class action pending in Brazil, *The Smoker Health Defense Association (ADESF) v. Souza Cruz, S.A. and Philip Morris Marketing, S.A., Nineteenth Lower Civil Court of the Central Courts of the Judiciary District of São Paulo, Brazil*, filed July 25, 1995, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer organization, is seeking damages for all addicted smokers and former smokers, and injunctive relief. In 2004, the trial court found defendants liable without hearing evidence and awarded "moral damages" of R$1,000 (approximately $233) per smoker per full year of smoking plus interest at the rate of 1% per month, as of the date of the ruling. The court did not award actual damages, which were to be assessed in the second phase of the case. The size of the class was not estimated. Defendants appealed to the São Paulo Court of Appeals, which annulled the ruling in November 2008, finding that the trial court had inappropriately ruled without hearing evidence and returned the case to the trial court for further proceedings. In May 2011, the trial court dismissed the claim. In February 2015, the appellate court unanimously dismissed plaintiff's appeal. In September 2015, plaintiff appealed to the Superior Court of Justice. In February 2017, the Chief Justice of the Superior Court of Justice denied plaintiff's appeal. In March 2017, plaintiff filed an *en banc* appeal to the Superior Court of Justice. In addition, the defendants filed a constitutional appeal to the Federal Supreme Tribunal on the basis that plaintiff did not have standing to bring the lawsuit. Both appeals are still pending.

Health Care Cost Recovery Litigation: These cases, brought by governmental and non-governmental plaintiffs, seek reimbursement of health care cost expenditures allegedly caused by tobacco products. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including unjust enrichment, negligence, negligent design, strict liability, breach of express and implied warranties, violation of a voluntary undertaking or special duty, fraud, negligent misrepresentation, conspiracy, public nuisance, defective product, failure to warn, sale of cigarettes to minors, and claims under statutes governing competition and deceptive trade practices. Plaintiffs in these cases seek various forms of relief including compensatory and other damages, and injunctive and equitable relief. Defenses raised in these cases include lack of proximate cause, remoteness of injury, failure to state a claim, adequate remedy at law, "unclean hands" (namely, that plaintiffs cannot obtain equitable relief because they participated in, and benefited from, the sale of cigarettes), and statute of limitations.

As of February 3, 2020, there were 17 health care cost recovery cases pending against us, our subsidiaries or indemnitees in Brazil (1), Canada (10), Korea (1) and Nigeria (5), compared with 16 such cases on February 4, 2019 and 16 such cases on February 9, 2018.

The health care cost recovery actions pending in Canada are described above under the caption "*Health Care Cost Recovery Litigation — Canada.*"

In the health care cost recovery case in Brazil, *The Attorney General of Brazil v. Souza Cruz Ltda., et al., Federal Trial Court, Porto Alegre, Rio Grande do Sul, Brazil*, filed May 21, 2019, we, our subsidiaries, and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past five years, payment of anticipated costs of treating future alleged smoking-related diseases, and moral damages. Our subsidiaries were served with the complaint. A challenge to the service of PMI as improper is pending.

In the first health care cost recovery case in Nigeria, *The Attorney General of Lagos State v. British American Tobacco (Nigeria) Limited, et al., High Court of Lagos State, Lagos, Nigeria,* filed March 13, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the second health care cost recovery case in Nigeria, *The Attorney General of Kano State v. British American Tobacco (Nigeria) Limited, et al., High Court of Kano State, Kano, Nigeria,* filed May 9, 2007, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We are in the process of making challenges to service and the court's jurisdiction. Currently, the case is stayed in the trial court pending the appeals of certain co-defendants relating to service objections.

In the third health care cost recovery case in Nigeria, *The Attorney General of Gombe State v. British American Tobacco (Nigeria) Limited, et al., High Court of Gombe State, Gombe, Nigeria,* filed October 17, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In February 2011, the court ruled that the plaintiff had not complied with the procedural steps necessary to serve us. As a result of this ruling, plaintiff must re-serve its claim. We have not yet been re-served.

In the fourth health care cost recovery case in Nigeria, *The Attorney General of Oyo State, et al., v. British American Tobacco (Nigeria) Limited, et al., High Court of Oyo State, Ibadan, Nigeria,* filed May 25, 2007, we and other members of the industry are defendants. Plaintiffs seek reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. We challenged service as improper. In June 2010, the court ruled that plaintiffs did not have leave to serve the writ of summons on the defendants and that they must re-serve the writ. We have not yet been re-served.

In the fifth health care cost recovery case in Nigeria, *The Attorney General of Ogun State v. British American Tobacco (Nigeria) Limited, et al., High Court of Ogun State, Abeokuta, Nigeria*, filed February 26, 2008, we and other members of the industry are defendants. Plaintiff seeks reimbursement for the cost of treating alleged smoking-related diseases for the past 20 years, payment of anticipated costs of treating alleged smoking-related diseases for the next 20 years, various forms of injunctive relief, plus punitive damages. In May 2010, the trial court rejected our service objections. We have appealed.

In the health care cost recovery case in Korea, the *National Health Insurance Service v. KT&G, et. al.,* filed April 14, 2014, our subsidiary and other Korean manufacturers are defendants. Plaintiff alleges that defendants concealed the health hazards of smoking, marketed to youth, added ingredients to make their products more harmful and addictive, and misled consumers into believing that *Lights* cigarettes are safer than regular cigarettes. The National Health Insurance Service seeks to recover damages allegedly incurred in treating 3,484 patients with small cell lung cancer, squamous cell lung cancer, and squamous cell laryngeal cancer from 2003 to 2012. The case is now in the evidentiary phase.

Label-Related Cases: These cases, brought by individual plaintiffs, or on behalf of a class or purported class of individual plaintiffs, allege that the use of the descriptor "Lights" or other alleged misrepresentations or omissions of labeling information constitute fraudulent and misleading conduct. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including misrepresentation, deception, and breach of consumer protection laws. Plaintiffs seek various forms of relief including restitution, injunctive relief, and compensatory and other damages. Defenses raised include lack of causation, lack of reliance, assumption of the risk, and statute of limitations.

As of February 3, 2020, there were 5 label-related cases brought by individual plaintiffs in Italy (1) and Chile (4) pending against our subsidiaries, compared with 7 such case on February 4, 2019, and 1 such case on February 9, 2018.

An individual plaintiff filed a purported class action certification motion, *Aharon Ringer v. Philip Morris Ltd. and Globrands Ltd.,* on July 18, 2017, in the Central District Court of Israel. Our Israeli affiliate and an Israeli importer and distributor for other multinational tobacco companies were defendants. Plaintiff sought to represent a class of smokers in Israel who have purchased cigarettes imported by defendants since July 18, 2010. Plaintiff estimated the class size to be 7,000,000 smokers. Plaintiff alleged that defendants misled consumers by not disclosing sufficient information about carbon monoxide, tar, and nicotine yields of, and tobacco contained in, the imported cigarettes. Plaintiff sought various forms of relief, including an order for defendants to label cigarette packs in accordance with plaintiff's demands, and damages for misleading consumers, breach of autonomy and unjust enrichment. In September 2019, plaintiff voluntarily withdrew the class certification motion, and the trial court dismissed the case with prejudice.

Public Civil Actions: Claims have been filed either by an individual, or a public or private entity, seeking to protect collective or individual rights, such as the right to health, the right to information or the right to safety. Plaintiffs' allegations of liability in these cases are based on various theories of recovery including product defect, concealment, and misrepresentation. Plaintiffs in these cases seek various forms of relief including injunctive relief such as banning cigarettes, descriptors, smoking in certain places and advertising, as well as implementing communication campaigns and reimbursement of medical expenses incurred by public or private institutions.

As of February 3, 2020, there were 2 public civil actions pending against our subsidiaries in Argentina (1) and Venezuela (1), compared with 2 such cases on February 4, 2019, and 2 such cases on February 9, 2018.

In the public civil action in Argentina, *Asociación Argentina de Derecho de Danos v. Massalin Particulares S.A., et al., Civil Court of Buenos Aires, Argentina,* filed February 26, 2007, our subsidiary and another member of the industry are defendants. The plaintiff, a consumer association, seeks the establishment of a relief fund for reimbursement of medical costs associated with diseases allegedly caused by smoking. Our subsidiary filed its answer in September 2007. In March 2010, the case file was transferred to the Federal Court on Administrative Matters after the Civil Court granted plaintiff's request to add the national government as a co-plaintiff in the case. The case is currently awaiting a court decision on the merits.

In the public civil action in Venezuela, *Federation of Consumers and Users Associations ("FEVACU"), et al. v. National Assembly of Venezuela and the Venezuelan Ministry of Health, Constitutional Chamber of the Venezuelan Supreme Court*, filed April 29, 2008, we were not named as a defendant, but the plaintiffs published a notice pursuant to court order, notifying all interested parties to appear in the case. In January 2009, our subsidiary appeared in the case in response to this notice. The plaintiffs purport to represent the right to health of the citizens of Venezuela and claim that the government failed to protect adequately its citizens' right to health. The claim asks the court to order the government to enact stricter regulations on the manufacture and sale of tobacco products. In addition, the plaintiffs ask the court to order companies involved in the tobacco industry to allocate a percentage of their "sales or benefits" to establish a fund to pay for the health care costs of treating smoking-related diseases. In October 2008, the court ruled that plaintiffs have standing to file the claim and that the claim meets the threshold admissibility requirements. In December 2012, the court admitted our subsidiary and BAT's subsidiary as interested third parties. In February 2013, our subsidiary answered the complaint.

Reduced-Risk Products

In Colombia, an individual filed a purported class action, *Ana Ferrero Rebolledo vs. Philip Morris Colombia S.A., et al.*, in April 2019 against our subsidiaries with the Civil Court of Bogota related to the marketing of our Platform 1 product. Plaintiff alleges that our subsidiaries advertise the product in contravention of law and in a manner that misleads consumers by portraying the product in a positive light, and further asserts that the Platform 1 vapor contains many toxic compounds, creates a high level of dependence, and has damaging second-hand effects. Plaintiff seeks injunctive relief and damages on her behalf and on a behalf of two classes (class 1 - all Platform 1 consumers in Colombia who seek damages for the purchase price of the product and personal injuries related to the alleged addiction, and class 2 - all residents of the neighborhood where the advertising allegedly took place who seek damages for exposure to the alleged illegal advertising). Our subsidiaries answered the complaint in January 2020.

Other Litigation

The Department of Special Investigations of the government of Thailand ("DSI") conducted an investigation into alleged underpayment by our subsidiary, Philip Morris (Thailand) Limited ("PM Thailand"), of customs duties and excise taxes relating to imports from the Philippines covering the period 2003-2007. On January 18, 2016, the Public Prosecutor filed charges against our subsidiary and seven former and current employees in the Bangkok Criminal Court alleging that PM Thailand and the individual defendants jointly and with the intention to defraud the Thai government, under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries of cigarettes from the Philippines during the period of July 2003 to June 2006. The government is seeking a fine of approximately THB 80.8 billion (approximately $2.58 billion). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and other Thai governmental agencies. Trial in the case began in November 2017 and concluded in September 2019. In November 2019, the trial court found our subsidiary guilty of under-declaration of the prices and imposed a fine of approximately THB 1.2 billion (approximately $38.4 million). The trial court dismissed all charges against the individual defendants. In December 2019, as required by the Thai law, our subsidiary paid the fine. This payment is included in other assets on the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. Our subsidiary will appeal the trial court's decision. If our subsidiary ultimately prevails on appeal, then Thailand will be required to return this payment to our subsidiary.

The DSI also conducted an investigation into alleged underpayment by PM Thailand of customs duties and excise taxes relating to imports from Indonesia covering the period 2000-2003. On January 26, 2017, the Public Prosecutor filed charges against PM Thailand and its former Thai employee in the Bangkok Criminal Court alleging that PM Thailand and its former employee jointly and with the intention to defraud the Thai government under-declared import prices of cigarettes to avoid full payment of taxes and duties in connection with import entries during the period from January 2002 to July 2003. The government is seeking a fine of approximately THB 19.8 billion (approximately $633 million). In May 2017, Thailand enacted a new customs act. The new act, which took effect in November 2017, substantially limits the amount of fines that Thailand could seek in these proceedings. PM Thailand believes that its declared import prices are in compliance with the Customs Valuation Agreement of the World Trade Organization and Thai law, and that the allegations of the Public Prosecutor are inconsistent with several decisions already taken by Thai Customs and a Thai court. Trial in the case began in November 2018 and concluded in December 2019. The case is awaiting a court decision in March 2020.

The South Korean Board of Audit and Inspection ("BAI") conducted an audit of certain Korean government agencies and the tobacco industry into whether inventory movements ahead of the January 1, 2015 increase of cigarette-related taxes by tobacco companies, including Philip Morris Korea Inc. ("PM Korea"), our South Korean affiliate, were in compliance with South Korean tax laws. In November 2016, the tax authorities completed their audit and assessed allegedly underpaid taxes and penalties. In order to avoid nonpayment financial costs, PM Korea paid approximately KRW 272 billion (approximately $227 million), of which KRW 100 billion (approximately $83.5 million) was paid in 2016 and KRW 172 billion (approximately $143.7 million) was paid in the first quarter of 2017. These amounts are included in other assets in the consolidated balance sheets and in cash used in operating activities in the consolidated statements of cash flows. PM Korea appealed the assessments. In January 2020, a trial court ruled that PM Korea did not underpay the approximately KRW 218 billion (approximately $182 million) in taxes that were subject to its jurisdiction. The tax authorities have appealed this decision. If the tax authorities ultimately lose, then they would be required to return the paid amounts to PM Korea. PM Korea's appeal of approximately KRW 54 billion of alleged underpayments (approximately $45 million) is pending at another court. The tax authorities have also referred the matter to the Public Prosecutor. On June 19, 2018, the Public Prosecutor decided not to file criminal charges against PM Korea and/or other alleged co-offenders. The Public Prosecutor also decided not to prosecute PM Korea and its managing director in connection with a criminal complaint against them that had been filed by the South Korean Ministry of Strategy and Finance ("MOSF"). In the criminal complaint, the MOSF alleged that PM Korea exceeded the monthly product withdrawal limits that the MOSF had set in its notice. In March 2019, the Supreme Prosecutor's Office dismissed both the tax authorities' and the MOSF's appeals on the decisions of the Public Prosecutor, concluding the criminal investigations in these matters.

The Moscow Tax Inspectorate for Major Taxpayers ("MTI") conducted an audit of AO Philip Morris Izhora ("PM Izhora"), our Russian affiliate, for the 2015-2017 financial years. On July 26, 2019, MTI issued its initial assessment, claiming that intercompany sales of cigarettes between PM Izhora and another Russian affiliate prior to excise tax increases and submission by PM Izhora of the maximum retail sales price notifications for cigarettes to the tax authorities were improper under Russian tax laws and resulted in underpayment of excise taxes and VAT. In August 2019, PM Izhora submitted its objections disagreeing with MTI's allegations set forth in the initial assessment and MTI's methodology for calculating the alleged underpayments. MTI accepted some of PM Izhora's arguments and in September 2019, issued the final tax assessment claiming an underpayment of RUB 24.3 billion (approximately $374 million), including penalties and interest. In accordance with Russian tax laws, PM Izhora paid the entire amount of MTI's final assessment. This amount was neither imposed on, nor concurrent with, the specific revenue-producing transaction, nor was it collected from customers of our Russian affiliates. PMI believes that the loss of $374 million in this matter is probable and estimable. Consequently, in the third quarter of 2019, PMI recorded a pre-tax charge of $374 million, in marketing, administration and research costs in the consolidated statements of earnings, representing $315 million net of income tax. Under the Russian law, PM Izhora has until mid-September 2020 to challenge the final tax assessment to the Federal Tax Service and is considering whether to pursue such challenge.

A putative shareholder class action lawsuit, *In re Philip Morris International Inc. Securities Litigation*, is pending in the United States District Court for the Southern District of New York, purportedly on behalf of purchasers of Philip Morris International Inc. stock between July 26, 2016 and April 18, 2018. The lawsuit names Philip Morris International Inc. and certain officers and employees as defendants and includes allegations that the defendants made false and/or misleading statements and/or failed to disclose information about PMI's business, operations, financial condition, and prospects, related to product sales of, and alleged irregularities in clinical studies of, PMI's Platform 1 product. The lawsuit seeks various forms of relief, including damages. In November 2018, the court consolidated three putative shareholder class action lawsuits with similar allegations previously filed in the Southern District of New York (namely, *City of Westland Police and Fire Retirement System v. Philip Morris International Inc., et al, Greater Pennsylvania Carpenters' Pension Fund v. Philip Morris International Inc., et al., and Gilchrist v. Philip Morris International Inc., et al.*) into these proceedings. A putative shareholder class action lawsuit, *Rubenstahl v. Philip Morris International Inc., et al.*, that had been previously filed in December 2017 in the United States District Court for the District of New Jersey, was voluntarily dismissed by the plaintiff due to similar allegations in these proceedings. On February 4, 2020, the court granted defendants' motion in its entirety, dismissing all but one of the plaintiffs' claims with prejudice. The court noted that one of plaintiffs' claims (allegations relating to four non-clinical studies of PMI's Platform 1 product) did not state a viable claim but allowed plaintiffs to replead that claim by March 3, 2020. We believe that this lawsuit is without merit and, in the event that plaintiffs take further action, will continue to defend it vigorously.

We are also involved in additional litigation arising in the ordinary course of our business. While the outcomes of these proceedings are uncertain, management does not expect that the ultimate outcomes of other litigation, including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our consolidated results of operations, cash flows or financial position.

Note 19.

Balance Sheet Offsetting:

Derivative Financial Instruments

PMI uses foreign exchange contracts and interest rate contracts to mitigate its exposure to changes in exchange and interest rates from third-party and intercompany actual and forecasted transactions. Substantially all of PMI's derivative financial instruments are subject to master netting arrangements, whereby the right to offset occurs in the event of default by a participating party. While these contracts contain the enforceable right to offset through close-out netting rights, PMI elects to present them on a gross basis in the consolidated balance sheets. Collateral associated with these arrangements is in the form of cash and is unrestricted. See Note 15. *Financial Instruments* for disclosures related to PMI's derivative financial instruments.

The effects of these derivative financial instrument assets and liabilities on PMI's consolidated balance sheets were as follows:

(in millions)	Gross Amounts Recognized	Gross Amount Offset in the Consolidated Balance Sheet	Net Amounts Presented in the Consolidated Balance Sheet	Gross Amounts Not Offset in the Consolidated Balance Sheet: Financial Instruments	Gross Amounts Not Offset in the Consolidated Balance Sheet: Cash Collateral Received/ Pledged	Net Amount
At December 31, 2019						
Assets						
Derivative contracts	**$ 390**	**$ —**	**$ 390**	**$ (297)**	**$ (91)**	**$ 2**
Liabilities						
Derivative contracts	**$ 419**	**$ —**	**$ 419**	**$ (297)**	**$ (59)**	**$ 63**
At December 31, 2018						
Assets						
Derivative contracts	$ 220	$ —	$ 220	$ (124)	$ (80)	$ 16
Liabilities						
Derivative contracts	$ 631	$ —	$ 631	$ (124)	$ (427)	$ 80

Note 20.

Sale of Accounts Receivable:

To mitigate risk and enhance cash and liquidity management PMI sells trade receivables to unaffiliated financial institutions. These arrangements allow PMI to sell, on an ongoing basis, certain trade receivables without recourse. The trade receivables sold are generally short-term in nature and are removed from the consolidated balance sheets. PMI sells trade receivables under two types of arrangements, servicing and non-servicing. For servicing arrangements, PMI continues to service the sold trade receivables on an administrative basis and does not act on behalf of the unaffiliated financial institutions. When applicable, a servicing liability is recorded for the estimated fair value of the servicing. The amounts associated with the servicing liability were not material for the years ended December 31, 2019 and 2018. Under the non-servicing arrangements, PMI does not provide any administrative support or servicing after the trade receivables have been sold to the unaffiliated financial institutions.

Cumulative trade receivables sold, including excise taxes, for the years ended December 31, 2019 and 2018, were $10.7 billion and $11.0 billion, respectively. PMI’s operating cash flows were positively impacted by the amount of the trade receivables sold and derecognized from the consolidated balance sheets, which remained outstanding with the unaffiliated financial institutions. The trade receivables sold that remained outstanding under these arrangements as of December 31, 2019, 2018 and 2017, were $0.9 billion, $1.0 billion and $1.1 billion, respectively. The net proceeds received are included in cash provided by operating activities in the consolidated statements of cash flows. The difference between the carrying amount of the trade receivables sold and the sum of the cash received is recorded as a loss on sale of trade receivables within marketing, administration and research costs in the consolidated statements of earnings. For the years ended December 31, 2019, 2018 and 2017 the loss on sale of trade receivables was immaterial.

Note 21.

Asset Impairment and Exit Costs:

Global Manufacturing Infrastructure Optimization

In light of declining PMI cigarette volumes resulting from lower total industry volumes and the shift to smoke-free alternatives, PMI continues to optimize its global manufacturing infrastructure.

Germany

On November 4, 2019, PMI announced that, as part of its global manufacturing infrastructure optimization, its German affiliate, Philip Morris Manufacturing GmbH ("PMMG"), reached an agreement with employee representatives to end cigarette production in its factory in Berlin, Germany, by January 1, 2020. As a result of this agreement, during 2019, PMI recorded pre-tax asset impairment and exit costs of $342 million in the European Union segment. This amount included pension and employee separation costs of $251 million, which will be paid in cash, and asset impairment costs of $91 million, primarily related to machinery and equipment, which are non-cash charges.

Other

During 2019, PMI also recorded pre-tax asset impairment and exit costs of $80 million as part of its global manufacturing infrastructure optimization. These costs were related to a cigarette plant closure in Argentina ($15 million), Colombia ($45 million) and Pakistan ($20 million). The charges were reflected in the Latin America & Canada segment (Argentina and Colombia) and the South & Southeast Asia segment (Pakistan).

Asset Impairment and Exit Costs by Segment

During 2019, pre-tax asset impairment and exit costs consisted of the following:

(in millions)		**2019**
Separation programs:		
European Union	$	251
South & Southeast Asia		3
Latin America & Canada		49
Total separation programs		303
Asset impairment charges		
European Union		91
South & Southeast Asia		17
Latin America & Canada		11
Total asset impairment charges		119
Asset impairment and exit costs	$	422

The total pre-tax asset impairment and exit costs above were included in marketing, administration and research costs on the consolidated statements of earnings. During 2018 and 2017, PMI did not incur asset impairment and exit costs.

Movement in Exit Cost Liabilities

The movement in exit cost liabilities for the year ended December 31, 2019 was as follows:

(in millions)		
Liability balance, January 1, 2019	$	—
Charges, net		303
Cash spent		(49)
Currency/other[a]		(63)
Liability balance, December 31, 2019	$	191

[a] Relates primarily to the reclassification of pension amounts.

Future cash payments for exit costs incurred to date are anticipated to be substantially paid by the end of 2021, with approximately $115 million expected to be paid in 2020.

Note 22.

Deconsolidation of RBH:

As discussed in Note 18. *Contingencies,* following the March 1, 2019, judgment of the Court of Appeal of Québec in two class action lawsuits against PMI's Canadian subsidiary, Rothmans, Benson & Hedges Inc. ("RBH"), PMI recorded in its consolidated results a pre-tax charge of $194 million, representing $142 million net of tax, in the first quarter of 2019. This pre-tax Canadian tobacco litigation-related expense was included in marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. The charge reflects PMI's assessment of the portion of the judgment that represents probable and estimable loss prior to the deconsolidation of RBH and corresponds to the trust account deposit required by the judgment. RBH's share of the deposit is approximately CAD 257 million.

On March 22, 2019, RBH obtained an initial order from the Ontario Superior Court of Justice granting it protection under the Companies' Creditors Arrangement Act ("CCAA"), which is a Canadian federal law that permits a Canadian business to restructure its affairs while carrying on its business in the ordinary course with minimal disruption to its customers, suppliers and employees.

The administration of the CCAA process, principally relating to the powers provided to the court and the court appointed monitor, removes certain elements of control of the business from both PMI and RBH. As a result, PMI has determined that it no longer has a controlling financial interest over RBH as defined in ASC 810 (Consolidation), and PMI deconsolidated RBH as of the date of the CCAA filing. PMI has also determined that it does not exert "significant influence" over RBH as that term is defined in ASC 323 (Investments-Equity Method and Joint Ventures). Therefore, as of March 22, 2019, PMI accounted for its continuing investment in RBH in accordance with ASC 321 (Investments-Equity Securities) as an equity security, without readily determinable fair value.

Following the deconsolidation, the carrying value of assets and liabilities of RBH was removed from the consolidated balance sheet of PMI, and the continuing investment in RBH was recorded at fair value at the date of deconsolidation. The total amount deconsolidated from PMI's balance sheet was $3,519 million, including $1,323 million of cash, $1,463 million of goodwill, $529 million of accumulated other comprehensive earnings, primarily related to historical currency translation and $204 million of other assets and liabilities, net. While PMI is accounting for its investment in RBH as an equity security, PMI would recognize dividends as income upon receipt. However, while it remains under creditor protection, RBH does not anticipate paying dividends.

The fair value of PMI's continuing investment in RBH of $3,280 million was determined at the date of deconsolidation, recorded within Investments in unconsolidated subsidiaries and equity securities and is assessed for impairment on an ongoing basis. The estimated fair value of the underlying business was determined based on an income approach using a discounted cash flow analysis, as well as a market approach for certain contingent liabilities. The information used in the estimate includes observable inputs, primarily a discount rate of 8%, a terminal growth rate of 2.5% and information about total tobacco market size in Canada and RBH's share of the market, as well as unobservable inputs such as operating budgets and strategic plans, various inflation scenarios, estimated shipment volumes, and expected product pricing and projected margins.

The difference between the carrying value of the assets and liabilities of RBH that were deconsolidated and the fair value of the continuing investment, as determined at the date of deconsolidation, was $239 million, before tax, and this loss on deconsolidation is reflected within marketing, administration and research costs on PMI's consolidated statement of earnings for the year ended December 31, 2019. PMI also recorded a tax benefit of $49 million within the provision for income taxes for the year ended December 31, 2019, related to the reversal of a deferred tax liability on unremitted earnings of RBH.

RBH is party to transactions with PMI and its consolidated subsidiaries entered into in the normal course of business; these transactions include royalty payments and recharge of various corporate expenses for services benefiting RBH. Up to the date of CCAA filing, these transactions were eliminated on consolidation and had no impact on PMI's consolidated statement of earnings. After deconsolidating RBH, these transactions are treated as third-party transactions in PMI's financial statements. The amount of these related-party transactions is included within Note 4. *Related Parties - Investments in Unconsolidated Subsidiaries, Equity Securities and Other.*

Developments in the CCAA process, including resolution through a plan of arrangement or compromise of all pending tobacco-related litigation currently stayed in Canada, as discussed in Note 18. *Contingencies*, could result in a material change in the fair value of PMI's continuing investment in RBH.

Note 23.

Leases:

PMI's operating leases are principally for real estate (office space, warehouses and retail store space) and vehicles. Lease terms range from 1 year to 74 years, some of which include options to renew, which are reasonably certain to be renewed. Lease terms may also include options to terminate the lease. The exercise of a lease renewal or termination option is at PMI's discretion.
PMI's operating leases at December 31, 2019, were as follows:

(in millions)		December 31, 2019
Assets:		
Other assets	$	766
Liabilities:		
Current		
Accrued liabilities - Other	$	194
Noncurrent		
Income taxes and other liabilities		569
Total lease liabilities	$	763

For information regarding PMI's immaterial finance leases, see Note 16. *Fair Value Measurements*.

The components of PMI's lease cost were as follows for the year ended December 31, 2019:

(in millions)		December 31, 2019
Operating lease cost	$	242
Short-term lease cost		61
Variable lease cost		29
Total lease cost	$	332

For the year ended December 31, 2019, lease cost of $79 million was recorded in cost of sales and $253 million was recorded in marketing, administration and research cost.

Maturity of PMI's operating lease liabilities, on an undiscounted basis, as of December 31, 2019, was as follows (as calculated under the new guidance ASC 842 (Leases)):

(in millions)		Total
2020	$	222
2021		162
2022		124
2023		92
2024		66
Thereafter		283
Total lease payments		949
Less: Interest		186
Present value of lease liabilities	$	763

Minimum rental commitments under non-cancelable operating leases in effect at December 31, 2018, were as follows (as calculated under legacy guidance ASC 840 (Leases)):

(in millions)		Total
2019	$	147
2020		103
2021		73
2022		52
2023		43
Thereafter		354
	$	772

Other information related to PMI's operating leases was as follows for the year ended December 31, 2019:

(in millions)		December 31, 2019
Cash paid for amounts included in the measurement of lease liabilities in Operating cash flows	**$**	**240**
Leased assets obtained in exchange for new operating lease liabilities	**$**	**221**
Weighted-average remaining lease term (years)		**9.6**
Weighted-average discount rate[1]		**4.4%**

[1] PMI's weighted-average discount rate is based on its estimated pre-tax cost of debt adjusted for country-specific risk.

For further details, see Note 24. *New Accounting Standards*.

Note 24.

New Accounting Standards:

Recently adopted

On February 25, 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ASU 2016-02, "Leases" ("ASU 2016-02"). ASU 2016-02 requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Additionally, ASU 2016-02 modifies current guidance for lessors' accounting. ASU 2016-02 is effective for interim and annual reporting periods beginning on or after January 1, 2019, with early adoption permitted. PMI has identified its lease management system and has identified and evaluated the applicable leases. In addition to the guidance in ASU 2016-02, PMI has evaluated ASU 2018-11, which was issued in July 2018 and provides an optional transitional method. As a result of this evaluation, PMI elected to use the optional transition method, which allows companies to use the effective date as the date of initial application on transition and not adjust comparative period financial information or make the new required disclosures for periods prior to the effective date. Additionally, PMI elected to use the hindsight practical expedient, as well as the package of practical expedients permitted under the transition guidance within the new standard. Upon adoption, PMI recognized lease liabilities and the corresponding right-of-use assets (at the present value of future payments) for predominately all of its operating leases in place at that time. At January 1, 2019, PMI's adoption of ASU 2016-02 resulted in an increase of approximately $0.7 billion on its assets and liabilities in its statement of financial position. ASU 2016-02 did not have a material impact on its results of operations or cash flows. For further details, see Note 23. *Leases*.

On January 1, 2019, PMI elected to early adopt ASU 2018-15 "Intangibles - Goodwill and Other - Internal - Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract." The adoption of ASU 2018-15 did not have a material impact on PMI's consolidated financial position or results of operations.

Note 25.

Quarterly Financial Data (Unaudited):

(in millions, except per share data)	2019 Quarters 1st	2nd	3rd	4th
Net revenues	**$ 6,751**	**$ 7,699**	**$ 7,642**	**$ 7,713**
Gross profit	**$ 4,286**	**$ 5,034**	**$ 5,037**	**$ 4,935**
Net earnings attributable to PMI	**$ 1,354**	**$ 2,319**	**$ 1,896**	**$ 1,616**
Per share data:				
Basic EPS	**$ 0.87**	**$ 1.49**	**$ 1.22**	**$ 1.04**
Diluted EPS	**$ 0.87**	**$ 1.49**	**$ 1.22**	**$ 1.04**
Dividends declared	**$ 1.14**	**$ 1.14**	**$ 1.17**	**$ 1.17**

(in millions, except per share data)	2018 Quarters 1st	2nd	3rd	4th
Net revenues	$ 6,896	$ 7,726	$ 7,504	$ 7,499
Gross profit	$ 4,281	$ 4,982	$ 4,886	$ 4,718
Net earnings attributable to PMI	$ 1,556	$ 2,198	$ 2,247	$ 1,910
Per share data:				
Basic EPS	$ 1.00	$ 1.41	$ 1.44	$ 1.23
Diluted EPS	$ 1.00	$ 1.41	$ 1.44	$ 1.23
Dividends declared	$ 1.07	$ 1.14	$ 1.14	$ 1.14

Basic and diluted EPS are computed independently for each of the periods presented. Accordingly, the sum of the quarterly EPS amounts may not agree to the total for the year.