RBH
Rothmans, Benson & Hedges Inc.
1500 DON MILLS ROAD, NORTH YORK, ONTARIO M3B 3L1
TELEPHONE (416) 449-5525

APR 22 1993

Orig. letter to DEAD
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JOE HEFFERNAN
PRESIDENT AND
CHIEF EXECUTIVE OFFICER
DIRECT LINE 442-3856

April 19, 1993

DDa ret.
Lee Pollak
Tom Kearns

Could you pls. work up effect upon us of such a change. 4/22

Mr. William I. Campbell
President & C.E.O.
Philip Morris U.S.A.
120 Park Avenue
New York, N.Y.
10017

Dear Bill:

As a result of political pressure from anti-tobacco forces in Canada, there is renewed governmental interest in applying an export tax to Canadian manufactured cigarettes. While Finance Department officials understand the consequences of such a tax, and are opposed to it, they acknowledge that political pressures may be strong enough to cause Cabinet to reimpose the tax. The bill authorizing an export tax at Ministerial discretion (Bill C-102) is in the final stages of working its way through the House of Commons, and is expected to become law within the next two weeks.

RBH has been working for several months on a contingency plan to ensure continued supply to Philip Morris U.S.A. and T.E.I. should manufacturing in Canada become prohibitively expensive. We have now managed to reach a general understanding with Rothmans International Tobacco Limited regarding manufacture of all brands in the U.K. and Republic of Ireland (see attached letter).

We are now therefore in a position to propose a contingency plan to you, the broad terms of which would be as follows:

- All products currently manufactured by RBH for the U.S. domestic and duty free markets would be manufactured by RITL, as agent for RBH, at its factories in the U.K. and Republic of Ireland. These products would be manufactured to RBH specifications, on RBH owned equipment. RBH would supply all materials, cut rag and/or strips and stem. Conversion costs charged to RBH would be average factory costs, in the order of £1.70 per M, which is roughly equivalent to RBH's conversion cost in Quebec. RBH would take title to the product immediately following manufacture.

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- RITL advise us that they would be in a position to secure the necessary trademark permissions to manufacture the Rothmans, Craven "A", Number 7, Benson & Hedges and Belvedere trademarks. For Mark Ten and Viscount, RITL would require permission from Philip Morris. No trademark licensing fees would be paid by RBH for these permissions.

- All additional costs associated with this situation, including extra freight costs, would be absorbed by RBH, at no additional cost to Philip Morris U.S.A.,

- Import duty, currently paid by Philip Morris U.S.A. and T.E.I. on all domestic volume, would increase due to higher duty rates from the U.K. and Ireland than from Canada. RBH proposes that this difference in duty be absorbed by RBH, as a credit on our invoice, or a price adjustment. For duty free markets, no duty is payable, although there may be an issue with respect to P.M. U.S.A. customers who purchase on a duty free basis from P.M., and subsequently pay import duties if and when product is transferred to the domestic market. We would expect that this cost would continue to be passed along to the customer, albeit at a higher level.

While final understandings with respect to this matter would need to be developed in the form of written contracts, we would appreciate an indication from you that this approach is generally acceptable to P.M. U.S.A. Following a positive response from Philip Morris, RBH would be in a position to move quickly to deal with machinery and logistical issues, while the details of formal agreements were being negotiated.

The contingency plan outlined above, while perhaps the most viable short-term alternative, will to a certain extent lead to reduced profitability for RBH. RBH will be preparing a separate communication for all RBH directors. Messrs. Dangoor and Pollak, as members of the RBH Board of Directors, will be fully apprised of these issues and the associated profitability effect on RBH.

Yours truly,

Joe Heffernan

cc: D. Dangoor
L. Pollak

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