

**Lotte Confectionery Co., Ltd.  
and Subsidiaries**

Consolidated Financial Statements  
December 31, 2011 and 2010

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Index**  
**December 31, 2011 and 2010**

---

	<b>Page(s)</b>
<b>Report of Independent Auditors .....</b>	<b>1 - 2</b>
<b>Consolidated Financial Statements</b>	
Consolidated Statements of Financial Position .....	3
Consolidated Statements of Comprehensive Income .....	4
Consolidated Statements of Changes in Equity .....	5
Consolidated Statements of Cash Flows .....	6 - 7
Notes to the Consolidated Financial Statements .....	8 - 69

## Report of Independent Auditors

To the Board of Directors and Shareholders of  
Lotte Confectionery Co., Ltd.

We have audited the accompanying consolidated statements of financial position of Lotte Confectionery Co., Ltd. and its subsidiaries (collectively the "Company") as of December 31, 2011 and 2010, and the related consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended, expressed in Korean won. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of consolidated subsidiaries, whose financial statements represent 15% of the Company's consolidated total assets as of December 31, 2011, and 17% of the Company's consolidated income before income taxes for the year then ended. These financial statements were audited by other auditors whose audit reports have been furnished for us and our opinion, insofar as it relates to the amounts included for consolidated subsidiaries, is based solely on the reports of the other auditors.

We conducted our audits in conformity with auditing standards generally accepted in the Republic of Korea. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lotte Confectionery Co., Ltd. and its subsidiaries as of December 31, 2011 and 2010, the financial performance and its cash flows for the years then ended in conformity with International Financial Reporting Standards as adopted by the Republic of Korea ("Korean IFRS").

### Samil PricewaterhouseCoopers

LS Yongsan Tower, 191, Hangeungno 2-ga, Yongsan-gu, Seoul 140-702, Korea (Yongsan P. O. Box 266, 140-600) [www.samill.com](http://www.samill.com)

Samil PricewaterhouseCoopers is the Korean network firm of PricewaterhouseCoopers International Limited ("PwCIL"), "PricewaterhouseCoopers" and "PwC" refer to the network of member firms of PwCIL. Each member firm is a separate legal entity and does not act as an agent of PwCIL or any other member firm.

Auditing standards and their application in practice vary among countries. The procedures and practices used in the Republic of Korea to audit such consolidated financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report is for use by those who are informed about Korean auditing standards and their application in practice.

*Samil PricewaterhouseCoopers*

Seoul, Korea

March 15, 2012

This report is effective as of March 15, 2011, the audit report date. Certain subsequent events or circumstances, which may occur between the audit report date and the time of reading this report, could have a material impact on the accompanying consolidated financial statements and notes thereto. Accordingly, the readers of the audit report should understand that there is a possibility that the above audit report may have to be revised to reflect the impact of such subsequent events or circumstances, if any.

**Lotte Confectionery and Subsidiaries**  
**Consolidated Statements of Financial Position**  
**December 31, 2011 and 2010, and January 1, 2010**

<i>(in millions of Korean won)</i>	Notes	December 31, 2011	December 31, 2010	January 1, 2010
<b>Assets</b>				
<b>Current assets</b>				
Cash and cash equivalents	3,6,7	182,610	192,539	89,408
Trade and other receivables	6,9,36	247,449	219,965	191,879
Other financial assets	6,8,10	104,491	115,190	177,381
Inventories	11	181,245	142,242	132,192
Other current assets		25,089	14,531	28,014
		<u>740,884</u>	<u>684,467</u>	<u>618,874</u>
<b>Non-current assets</b>				
Investments in associate	12	231,153	235,548	230,578
Other financial assets	6,10	1,537,064	1,709,234	1,324,482
Property, plant and equipment	5,13	1,231,626	1,204,025	1,177,658
Intangible assets	5,14	75,125	74,547	83,255
Investment property	5,16	78,064	80,006	61,347
Deferred tax assets	20	4,576	1,216	-
Other non-current assets		2,773	2,837	5,955
		<u>3,160,381</u>	<u>3,307,413</u>	<u>2,883,275</u>
<b>Total assets</b>		<u>3,901,265</u>	<u>3,991,880</u>	<u>3,502,149</u>
<b>Liabilities</b>				
<b>Current liabilities</b>				
Trade and other payables	3,6,17,36	259,904	231,277	240,101
Borrowings	3,6,18	6,509	20,959	9,667
Debtentures	3,6,18	289,358	153,568	-
Other financial liabilities	3,6,10	48,647	49,862	65,949
Income taxes payable		22,463	25,024	14,870
Deferred revenue		1,751	2,328	2,979
Provisions	21	23,891	22,852	15,622
Other current liabilities		19,329	20,153	19,570
		<u>671,852</u>	<u>526,023</u>	<u>368,758</u>
<b>Non-current liabilities</b>				
Borrowings	3,6,18	10,994	2,714	4,494
Debtentures	3,6,18	99,605	271,888	384,164
Other financial liabilities	3,6,10	22,109	22,836	21,780
Defined benefit liabilities	19	7,648	10,915	5,053
Provisions	21	38	-	-
Deferred income tax liabilities	20	455,443	444,299	363,734
Deferred revenue		9,560	10,700	118
Other non-current liabilities		9,036	10,565	9,531
		<u>614,423</u>	<u>773,917</u>	<u>788,874</u>
<b>Total liabilities</b>		<u>1,286,275</u>	<u>1,299,940</u>	<u>1,157,632</u>
<b>Equity attributable to owners of the parent</b>				
Capital stock	22	7,107	7,107	7,107
Capital surplus		12,998	12,998	12,998
Other components of equity	22	(15,034)	(15,034)	(12,401)
Accumulated other comprehensive income	23	988,526	1,167,082	894,211
Retained earnings	24	1,537,107	1,444,939	1,361,452
		<u>2,530,704</u>	<u>2,617,092</u>	<u>2,263,367</u>
<b>Non-controlling interest</b>		<u>84,286</u>	<u>74,848</u>	<u>81,150</u>
<b>Total equity</b>		<u>2,614,990</u>	<u>2,691,940</u>	<u>2,344,517</u>
<b>Total liabilities and equity</b>		<u>3,901,265</u>	<u>3,991,880</u>	<u>3,502,149</u>

The accompanying notes are an integral part of these consolidated financial statements.

**Lotte Confectionery and Subsidiaries**  
**Consolidated Statements of Comprehensive Income**  
**Years Ended December 31, 2011 and 2010**

<i>(in millions of Korean won)</i>	<b>Notes</b>	<b>2011</b>	<b>2010</b>
Revenue	5,36	1,854,158	1,650,681
Cost of sales	29	1,139,791	978,502
Gross profit	30	714,367	672,179
Selling and administrative expenses		541,151	503,544
Other operating income		19,432	13,625
Other operating expenses		28,29,30	11,005
Operating profit		179,259	171,255
Finance income	31	49,979	55,436
Finance costs	32	43,102	64,240
Share of (loss)/profit of associates		(28,535)	(31,726)
<b>Profit before income tax</b>		<b>157,601</b>	<b>130,725</b>
Income tax expense	33	57,240	36,651
<b>Profit for the year</b>		<b>100,361</b>	<b>94,074</b>
Attributable to:			
Owners of the parent		97,676	93,537
Non-controlling interest		2,685	537
<b>Other comprehensive income</b>			
Change in value of available-for-sale financial assets		(181,673)	363,469
Cash flow hedge		4,990	(2,729)
Exchange differences on translating foreign operations		(16,161)	(13,368)
Share of other comprehensive income of associate		3,593	(1,895)
Actuarial gain (loss) on defined benefit liabilities	19	(29)	(6,568)
Income tax effect relating to components of other comprehensive income		9,752	(77,918)
<b>Other comprehensive income for the year, net of tax</b>		<b>(179,528)</b>	<b>260,991</b>
<b>Total comprehensive income(loss) for the year</b>		<b>(79,167)</b>	<b>355,065</b>
Attributable to:			
Owners of the parent		(80,757)	361,284
Non-controlling interests		1,590	(6,219)
<b>Earnings per share for profit attributable to owners of the parent (in Korean won)</b>			
Basic and diluted earnings per share	34	69,402	66,461

The accompanying notes are an integral part of these consolidated financial statements.

Lotte Confectionery and Subsidiaries  
Consolidated Statements of Changes in Equity  
Years Ended December 31, 2011 and 2010

	Attributable to equity holders of the Parent Company							
	Capital Stock	Capital Surplus	Other Components of Equity	Accumulated Other Components of Equity	Retained earnings	Total	Non-controlling Interest	Total Equity
<b>Balance as of January 1, 2010</b>	7,107	12,998	(12,401)	894,211	1,381,452	2,283,367	81,150	2,344,517
Comprehensive Income	-	-	-	-	93,537	93,537	537	94,074
Profit for the year	-	-	-	-	(5,123)	(5,123)	-	(5,123)
Actuarial gain(loss) on defined benefit liabilities	-	-	-	283,505	-	283,505	-	283,505
Valuation of available-for-sale financial assets	-	-	-	(2,128)	-	(2,128)	-	(2,128)
Cash flow hedge	-	-	-	(6,612)	-	(6,612)	(6,756)	(13,368)
Currency translation differences	-	-	-	(1,884)	-	(1,884)	-	(1,884)
Share of other comprehensive income of associate	-	-	-	272,871	88,414	361,285	(6,219)	355,066
Total comprehensive income for the year	-	-	-	-	88,414	361,285	-	361,285
Transactions with equity holders of the Company:	-	-	-	-	(4,926)	(4,926)	-	(4,926)
Dividends	-	-	(2,633)	-	-	(2,633)	(64)	(2,697)
Consolidated equity transaction	-	-	(2,633)	-	-	(2,633)	-	-
Total transactions with equity holders of the Company	-	-	(2,633)	-	(4,926)	(7,559)	(64)	(7,623)
Balance as of December 31, 2010	7,107	12,998	(15,034)	1,167,082	1,444,939	2,617,092	74,945	2,691,940
Other	-	-	(15,034)	-	(1)	(1)	(19)	(20)
Balance as of January 1, 2011	7,107	12,998	(15,034)	1,167,082	1,444,939	2,617,092	74,945	2,691,940
Comprehensive Income	-	-	-	-	97,676	97,676	2,885	100,561
Profit for the year	-	-	-	-	122	122	-	122
Actuarial gain(loss) on defined benefit liabilities	-	-	-	(171,023)	-	(171,023)	-	(171,023)
Change in value of available-for-sale financial assets	-	-	-	3,939	-	3,939	-	3,939
Cash flow hedge	-	-	-	(15,065)	-	(15,065)	(1,094)	(16,159)
Exchange differences on translating foreign operations	-	-	-	3,593	-	3,593	-	3,593
Share of other comprehensive income of associate	-	-	-	(178,556)	97,798	(80,758)	1,591	(78,167)
Total comprehensive income for the year	-	-	-	-	97,798	97,798	-	97,798
Transactions with equity holders of the Company:	-	-	-	-	(5,630)	(5,630)	-	(5,630)
Dividends	-	-	-	-	(5,630)	(5,630)	-	(5,630)
Changes in scope of consolidation	-	-	-	-	-	-	7,847	7,847
Transactions with equity holders of the Company	-	-	-	-	(5,630)	(5,630)	7,847	2,217
Balance as of December 31, 2011	7,107	12,998	(15,034)	988,526	1,537,107	2,530,704	84,286	2,614,990

The accompanying notes are an integral part of these consolidated financial statements.

**Lotte Confectionery and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2011 and 2010**

	2011	2010
<i>(in millions of Korean won)</i>		
<b>Cash flows from operating activities</b>		
Profit (loss) for the year	100,361	94,074
Income tax expense	57,239	36,652
Depreciation	69,168	55,731
Amortization	930	1,358
Severance benefits	17,332	15,776
Interest expenses	21,148	19,766
Interest income	(8,045)	(6,732)
Gain on disposal of available-for-sale financial assets	(402)	(57)
Loss on disposal of available-for-sale financial assets	-	41
Share of (loss)/profit of associates	28,535	31,726
Loss on disposal of investments in associates assets	2,145	-
Gain on disposal of investments in subsidiary assets	(13,659)	-
Gain on valuation of hedging derivative	(17,390)	(41,344)
Loss on valuation of hedging derivative	-	214
Gain on derivative hedging transaction	(1,811)	-
Loss on derivative hedging transaction	275	754
Bad debts expense	1,324	153
Other bad debts expense	163	31
Reversal of allowance for doubtful accounts	(23)	(2)
Gain on disposal of property, plant and equipment	(2,836)	(845)
Loss on disposal of property, plant and equipment	227	407
Loss on impairment of property, plant and equipment	393	-
Gain on disposal of intangible assets	(3)	-
Foreign exchange gains and losses	15,402	20,334
Dividends income	(6,536)	(5,370)
Other income, expense	714	660
Decrease (increase) in inventories	(36,579)	(10,051)
Decrease (increase) in trade receivables	(29,226)	(29,285)
Decrease (increase) in other receivables	354	1,277
Decrease (increase) in other current assets	(6,378)	12,876
Decrease (increase) in other non-current assets	(3,303)	1,901
Increase (decrease) in trade Payables	10,445	4,159
Increase (decrease) other payables	13,763	(17,657)
Increase (decrease) in defined benefit liabilities	(20,412)	(15,200)
Increase (decrease) current other financial liabilities	(1,328)	(12,226)
Increase (decrease) in other current liabilities	(8,735)	583
Increase (decrease) in current other financial liabilities	2,014	478
Increase (decrease) in other non-current liabilities	(1,948)	(249)
Increase (decrease) in deferred revenue	(1,341)	10,778
Increase (decrease) in provisions	1,078	7,230
Income tax paid	(40,703)	(23,423)
<b>Net cash generated from operating activities</b>	<b>142,352</b>	<b>154,518</b>

**Lotte Confectionery and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2011 and 2010**

<i>(in millions of Korean won)</i>	2011	2010
<b>Cash flows from investing activities</b>		
Decrease in current financial instrument assets	3,090	107,000
Decrease in non-current financial instrument assets	5,710	8,652
Proceeds from disposal of available-for-sale financial assets	2,919	1,200
Proceeds from disposal of property, plant and equipment	16,249	2,207
Proceeds from disposal of intangible assets	6	-
Increases in changes in scope of consolidation	604	-
Interest received	7,947	7,135
Dividends received	6,857	5,726
Increase in current financial instrument assets	-	(3,053)
Increase in non-current financial instrument assets	(9,926)	(14,432)
Acquisition of investments in associates	(23,295)	(40,097)
Acquisition of available-for-sale financial assets	(1,650)	(20,560)
Acquisition of property, plant and equipment	(88,244)	(69,482)
Acquisition of intangible assets	(1,017)	(808)
Acquisition of investment property	-	(19,792)
Decreases in changes in scope of consolidation	(1,325)	-
<b>Net cash used in investing activities</b>	<b>(82,075)</b>	<b>(36,304)</b>
<b>Cash flows from financing activities</b>		
Proceeds from borrowings	17,442	69,376
Proceeds from disposal of hedging derivatives	40,986	-
Proceeds from issuance of debentures	99,542	-
Repayments of borrowings	(48,200)	(59,234)
Repayments of bonds	(153,795)	-
Interest paid	(20,554)	(18,702)
Dividends paid	(5,630)	(4,926)
Consolidated equity transaction	-	(1,549)
<b>Net cash used in financing activities</b>	<b>(70,209)</b>	<b>(15,035)</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>(9,932)</b>	<b>103,179</b>
<b>Exchange losses on cash and cash equivalents</b>	<b>3</b>	<b>(48)</b>
Cash and cash equivalents at the beginning of the year	192,539	89,408
<b>Cash and cash equivalents at the end of the year</b>	<b>182,610</b>	<b>192,539</b>

The accompanying notes are an integral part of these consolidated financial statements.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**1. Organization**

Lotte Confectionery Co., Ltd. (the "Parent Company") was established on March 24, 1967, in the Republic of Korea to manufacture, and sell confectionery goods and ice cream. The Parent Company listed its common stock on the Korea Exchange on February 16, 1974, and the capital stock as of December 31, 2011, amounts to ₩ 7,107 million.

The shareholders of the Parent Company and their ownership as of December 31, 2011, are as follows:

Shareholder	Number of shares	Ownership
Lotte Aluminum Co., Ltd.	217,268	15.29%
Shin Kyuk Ho	97,057	6.83%
The Lotte Foundation	123,576	8.69%
Treasury stock	14,000	0.98%
Others	969,499	68.21%
	<u>1,421,400</u>	<u>100.00%</u>

**1.1 Consolidated subsidiaries**

The Company's consolidated subsidiaries as of December 31, 2011, are as follows:

Subsidiaries	Location	Fiscal Year-end	Percentage of ownership
Lotte India Co., Ltd.	India	Dec. 31	98.37%
Lotte Qingdao Foods Co., Ltd.	China	Dec. 31	90.00%
Lotte Confectionery Holdings B.V.	Netherlands	Dec. 31	51.00%
Chocolaterie Guylian N.V. <sup>1</sup>	Belgium	Dec. 31	99.97%
Chocolaterie Guylian Deutschland <sup>2</sup>	Deutschland	Dec. 31	100.00%
GRPI BVBA <sup>2</sup>	Belgium	Dec. 31	100.00%
Guylian Asia <sup>2</sup>	Hongkong	Dec. 31	100.00%
Guylian Iberia, LDA <sup>2</sup>	Portugal	Dec. 31	100.00%
Guylian UK <sup>2</sup>	England	Dec. 31	100.00%
Guylian USA <sup>2</sup>	USA	Dec. 31	100.00%
SAS Chocolaterie Guylian France <sup>2</sup>	France	Dec. 31	100.00%
Lotte Food Holding Co., Ltd.	Hongkong	Dec. 31	100.00%
Lotte Ice (Shandong) Co., Ltd.	China	Dec. 31	65.00%
Kirin Foods Co., Ltd.	Korea	Dec. 31	100.00%
K.S. SULEMANJI ESMALJI & SONS(Private) Limited	Pakistan	Dec. 31	69.45%
Koison Industries(Private) Limited <sup>3</sup>	Pakistan	Dec. 31	85.00%
Lotte Confectionery (S.E.A) Pte., Ltd.	Singapore	Dec. 31	100.00%

<sup>1</sup> The shares of Chocolaterie Guylian NV are held by Lotte Confectionery Holdings B.V. and Lotte Europe Holdings B.V.

<sup>2</sup> The shares of Chocolaterie Guylian Deutschland and GRPI BVBA and Guylian Asia and Guylian Iberia, LDA and Guylian UK and Guylian USA and SAS Chocolaterie Guylian France are owned by Chocolaterie Guylian NV.

<sup>3</sup> The shares of Koison Industries(Private) Limited are held by K.S. SULEMANJI ESMALJI & SONS(Private) Limited.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**1.2 Summary of the relevant financial information of subsidiaries**

The significant financial data of the subsidiaries as of and for the years ended December 31, 2011 and 2010, and as of January 1, 2010, included in the accompanying consolidated financial statements are summarized as follows:

	<b>December 31, 2011</b>			
	<b>Asset</b>	<b>Liabilities</b>	<b>Sales</b>	<b>Net Income(loss)</b>
<i>(in millions of Korean won)</i>				
<b>Subsidiaries</b>				
Lotte India Co., Ltd.	108,390	13,152	65,560	1,083
Lotte Qingdao Foods Co., Ltd.	32,279	3,263	15,360	(742)
Lotte Confectionery Holdings B.V.	193,525	51,859	119,686	8,137
Lotte Food Holding Co., Ltd.	48,840	33	-	(10,096)
Lotte Ice (Shandong) Co., Ltd.	13,362	3,515	3,765	(1,799)
Kirin Foods Co., Ltd.	126,051	21,294	88,661	(2,720)
K.S. SULEMANJI ESMALLJI & SONS (Private) Limited	45,042	22,947	53,729	(1,886)
Lotte Confectionery (S.E.A) Pte., Ltd	6,948	154	515	(109)
<b>December 31, 2010</b>				
	<b>Asset</b>	<b>Liabilities</b>	<b>Sales</b>	<b>Net Income(loss)</b>
<i>(in millions of Korean won)</i>				
<b>Subsidiaries</b>				
Lotte India Co., Ltd.	123,078	12,977	53,734	607
Lotte Qingdao Foods Co., Ltd.	30,944	2,773	12,949	28
Lotte Confectionery Holdings B.V.	198,727	63,282	117,569	3,442
Lotte Food Holding Co., Ltd.	56,774	31	-	(10,310)
Lotte Ice (Shandong) Co., Ltd.	13,721	2,604	3,981	(1,274)
Kirin Foods Co., Ltd.	123,090	15,866	73,199	1,334
<b>January 1, 2010</b>				
	<b>Asset</b>	<b>Liabilities</b>		
<i>(in millions of Korean won)</i>				
<b>Subsidiaries</b>				
Lotte India Co., Ltd.	113,866	24,198		
Lotte Qingdao Foods Co., Ltd.	29,318	1,411		
Lotte Confectionery Holdings B.V.	211,172	65,255		
Lotte Food Holding Co., Ltd.	49,629	25		
Lotte Ice (Shandong) Co., Ltd.	12,856	557		
Kirin Foods Co., Ltd.	115,687	9,716		

# **Lotte Confectionery Co., Ltd. and Subsidiaries**

## **Notes to Consolidated Financial Statements**

### **December 31, 2011 and 2010, and January 1, 2010**

---

#### **1.3 Changes in the scope of consolidation**

An investee newly included and excluded in the scope of consolidation for the year ended December 31, 2011, is as follows:

<b>Subsidiaries</b>	<b>Reason</b>
The following companies are included in the scope of consolidation for the year ended December 31, 2011:	
K.S. SULEMANJI ESMALJI & SONS (Private) Limited	The company has become a subsidiary due to the parent company's acquisition of 69.45% ownership.
Lotte Natur Co., Ltd	Lotte Natur Co., Ltd. has become a subsidiary due to the physical division.
Lotte Confectionery (S.E.A) Pte., Ltd.	Lotte Confectionery (S.E.A) Pte., Ltd. has become a subsidiary because it was newly established.

The following companies are excluded in the scope of consolidation for the year ended December 31, 2011:

<b>Subsidiaries</b>	<b>Reason</b>
Lotte Pharm Co., Ltd.	Lotte Pharm Co., Ltd. was excluded from the subsidiaries because it was merged.
Lotte Natur Co., Ltd.	Lotte Natur Co., Ltd. was excluded from the subsidiaries because the Company sold 100% of its shares to Lotteria Co., Ltd.

## **2. Significant Accounting Policies**

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

### **2.1 Basis of Preparation**

The consolidated financial statements for the annual period beginning on January 1, 2011, have been prepared in accordance with Korean IFRS. These are the standards, subsequent amendments and related interpretations issued by the International Accounting Standards Board ("IASB") that have been adopted by the Republic of Korea.

The consolidated financial statements of the Company were prepared in accordance with Korean IFRS and are subject to Korean IFRS1101, 'First-time Adoption of Korean IFRS'.

The transition date, according to Korean IFRS1101, from the previous accounting principles generally accepted in the Republic of Korea (the previous K-GAAP) to Korean IFRS is January 1, 2010. Reconciliations and descriptions of the effect of the transition from the previous K-GAAP to Korean IFRS on the Company's equity, comprehensive income and cash flows are described in Note 37.

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the Company financial statements are disclosed in Note 4.

New standards, amendments and interpretations issued but not effective for the financial year beginning January 1, 2011, and not early adopted by the Company are as follows:

## **Lotte Confectionery Co., Ltd. and Subsidiaries**

### **Notes to Consolidated Financial Statements**

#### **December 31, 2011 and 2010, and January 1, 2010**

---

- Amendments to Korean IFRS1101, *Hyperinflation and Removal of Fixed Dates for first-time adopters*

As an exception to retrospective application requirements, this amendment to Korean IFRS1101 allows a prospective application of derecognition of financial assets for transactions occurring on or after the date of transition to Korean IFRS, instead of fixed date (January 1, 2004). Accordingly, the Company is not required to restate and recognize those assets or liabilities that were derecognized as a result of a transaction that occurred before the dated of transition to Korean IFRS. This amendment is effective for the Company as of July 1, 2011. The Company expects that the application of this amendment would not have material impact on its Company financial statements.

- Amendments to Korean IFRS1012, *Income Taxes*

According to the amendments to Korean IFRS1012, *Income Taxes*, for the investment property that is measured using the fair value model, the measurement of deferred tax liability and deferred tax asset should reflect the tax consequences of recovering the carrying amount of the investment property entirely through sale, unless evidences support otherwise. This amendment is effective for the Company as of January 1, 2012. The Company expects that the application of this amendment would not have material impact on its Company financial statements.

- Amendments to Korean IFRS1019, *Employee Benefits*

According to the amendments to Korean IFRS1019, *Employee Benefits*, use of a 'corridor' approach is no longer permitted, and therefore all actuarial gains and losses incurred are immediately recognized in other comprehensive income. All past service costs incurred from changes in pension plan are immediately recognized, and expected returns on interest costs and plan assets that used to be separately calculated are now changed to calculating net interest expense(income) by applying discount rate used in measuring defined benefit obligation in net defined benefit liabilities(assets). This amendment is effective for the Company as of January 1, 2013, and the Company is assessing the impact of application of the amended Korean IFRS1019 on its Company financial statements as of the report date.

- Amendments to Korean IFRS1107, *Financial Instruments: Disclosures*

According to the amendment, an entity should provide the required disclosures of nature, carrying amount, risk and rewards associated with all transferred financial instruments that are not derecognized from an entity's financial statements. In addition, an entity is required to disclose additional information related to transferred and derecognized financial instruments for any continuing involvement in transferred assets. This amendment will be effective for the Company as of July 1, 2011. The Company is assessing the impact of application of the amended Korean IFRS1107 on its Company financial statements as of the report date.

- Enactment of Korean IFRS1113, *Fair value measurement*

Korean IFRS1113, *Fair value measurement*, aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across Korean IFRSs. Korean IFRS1113 does not extend the use of fair value accounting but provides guidance on how it should be applied where its use is already required or permitted by other standards within the Korean IFRSs. This amendment will be effective for the Company as of January 1, 2013, and the Company expects that it would not have a material impact on the Company.

## **2.2 Consolidation**

The Company has prepared the Company financial statements in accordance with Korean IFRS1027, *Company and Separate Financial Statements*.

### *(a) Subsidiaries*

Subsidiaries are all entities (including special purpose entities) over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

currently exercisable or convertible are considered when assessing whether the Company controls another entity. The Company also assesses existence of control where it does not have more than 50% of the voting power but is able to govern the financial and operating policies by virtue of de-facto control. De-facto control may arise in circumstances where the size of the Company's voting rights relative to the size and dispersion of holdings of other shareholders give the Company the power to govern the financial and operating policies and others.

The Company applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is measured as the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Company. The consideration transferred includes the fair value of any asset or liability resulting from a contingent arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Company recognizes any non-controlling interest in the acquiree on an acquisition- by-acquisition basis, either at fair value or at the non-controlling interest's proportionate share of the recognized amounts of acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date and the resulting gain or loss is recognized in profit or loss.

Any contingent consideration to be transferred by the Company is recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognized in accordance with Korean IFRS1039, either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

Goodwill is initially measured as the excess of the aggregate of the consideration transferred and the fair value of non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss.

Intercompany transactions, balances, income and expenses on transactions between Company companies are eliminated. Unrealized losses are also eliminated after recognizing impairment of transferred assets. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Company.

*(b) Changes in ownership interests in subsidiaries without change of control*

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions; that is, as transactions with the owners in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

*(c) Disposal of subsidiaries*

When the Company ceases to have control any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Company had directly disposed of the related assets or liabilities. This may mean that amounts previously recognized in other comprehensive income (except for revaluation surplus) are reclassified to profit or loss (revaluation surplus is reclassified to retained earnings).

*(d) Associates*

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

Associates are all entities over which the Company has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting. Under the equity method, the investment is initially recognized at cost, and the carrying amount is increased or decreased to recognize the investor's share of the profit or loss of the investee after the date of acquisition. The Company's investment in associates includes goodwill identified on acquisition, net of any accumulated impairment loss.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognized in other comprehensive income is reclassified to profit or loss where appropriate.

The Company's share of post-acquisition profit or loss is recognized in the income statement, and its share of post-acquisition movements in other comprehensive income is recognized in other comprehensive income with a corresponding adjustment to the carrying amount of the investment. When the Company's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Company does not recognize further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

The Company determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Company calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognizes the amount as 'impairment loss on investment in an associate' in the income statement.

Unrealized gains on transactions between the Company and its associates are eliminated to the extent of the Company's interest in the associates. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Company. Dilution gains and losses arising in investments in associates are recognized in the income statement.

*(e) Joint ventures*

A joint venture is a contractual arrangement whereby two or more parties (ventures) exercise joint control. Investments in jointly controlled entities, as associates are accounted for using the equity method of accounting and are initially recognized at cost. The Company's investment in jointly controlled entities, as associates, includes goodwill identified on acquisition, net of accumulated impairment loss. The Company does not recognize its share of profits or losses from the joint venture that result from the Company's purchase of assets from the joint venture until it re-sells the assets to an independent party. However, a loss on the transaction is recognized immediately if the loss provides evidence of a reduction in the net realizable value of current assets, or an impairment loss.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

**2.3 Segment Reporting**

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the steering committee that makes strategic decisions

**2.4 Foreign Currency Translation**

*(a) Functional and presentation currency*

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The Company financial statements are presented in Korean won, which is the parent company functional and presentation currency.

*(b) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement, except when deferred in other comprehensive income as qualifying cash flow hedges and qualifying net investment hedges.

Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the income statement within 'financial income or expenses'. All other foreign exchange gains and losses are presented in the income statement within 'other gains and losses, net'.

Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analyzed between translation differences resulting from changes in the amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortized cost are recognized in profit or loss, and other changes in carrying amount are recognized in other comprehensive income.

Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognized in profit or loss as part of the fair value gain or loss.

Translation differences on non-monetary financial assets, such as equities classified as available-for-sale, are included in other comprehensive income.

*(c) Translation to presentation currency*

The results and financial position of all Company entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each statement of financial position presented are translated at the closing rate at the end of the reporting period;
- income and expenses for each income statement are translated at average exchange rates; and
- all resulting exchange differences are recognized in other comprehensive income.

Exchange differences arising from the translation of borrowings designated for hedging the investment and other currency instruments are recognized in other comprehensive income. When foreign operations are wholly or partially sold, exchange differences recognized in equity are transferred to profit or loss in the income statement. When the Company ceases to control the subsidiary, exchange differences that were recorded in equity are recognized in the income statement as part of the gain or loss on sale.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

**2.5 Cash and Cash Equivalents**

Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less.

**2.6 Financial Assets**

**2.6.1 Classification**

The Company classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, available-for-sale, and held-to-maturity. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

**(a) Financial assets at fair value through profit or loss**

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives or embedded derivatives are also categorized as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.

**(b) Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. The Company's loans and receivables comprise 'cash and cash equivalents', 'trade and other receivables', and 'other financial assets' in the statement of financial position.

**(c) Available-for-sale financial assets**

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless the investment matures or management intends to dispose of it within 12 months after the end of the reporting period.

**(d) Financial liabilities carried at amortized cost**

The Company classifies non-derivative financial liabilities, except for financial liabilities at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition. Financial liabilities carried at amortized cost are included in non-current liabilities, except for liabilities with maturities less than 12 months after the end of the reporting period, which are classified as current liabilities.

**2.6.2 Recognition and Measurement**

Regular purchases and sales of financial assets are recognized on the trade date. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are subsequently carried at amortized cost using the effective interest rate method.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

Gains or losses arising from changes in the fair value of the financial assets carried at fair value through profit or loss are presented in the income statement within 'finance income/(costs)' in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the income statement as part of 'finance income' when the Company's right to receive dividend payments is established.

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the income statement as 'finance income/(costs)'.

Interest on available-for-sale and held-to-maturity securities calculated using the effective interest method is recognized in the income statement as part of 'finance income'. Dividends on available-for-sale equity instruments are recognized in the income statement as part of 'finance income' when the Company's right to receive dividend payments is established.

#### 2.6.3 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

#### 2.6.4 Derecognition

Financial assets are derecognized when the contractual rights to receive cash flows from the investments have expired or have been transferred and the Company has substantially transferred all risks and rewards of ownership. If the risk and rewards of ownership of transferred assets have not been substantially transferred, the Company reviews the level of control retained over that asset and the extent of its continuing involvement to determine if transfers do not qualify for derecognition.

Collaterals (trade receivables and other) provided in transactions of discount and factoring of trade receivables do not meet the requirements for asset derecognition if risks and rewards do not substantially transfer in the event the debtor defaults. Financial liabilities recognized in relation to these transactions are included as borrowings in the Company's statement of financial position.

#### 2.6.5 Impairment of Financial Assets

##### (a) Assets carried at amortized cost

The Company assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or a group of financial assets that can be reliably estimated.

The criteria that the Company uses to determine that there is objective evidence of an impairment loss include:

- Significant financial difficulty of the issuer or obligor;
- Delinquency in interest or principal payments.
- For economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- It becomes probable that the borrower will enter bankruptcy or other financial reorganization;
- The disappearance of an active market for that financial asset because of financial difficulties; or
- Observable data suggesting that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, even though the decrease cannot be identified with respect to individual financial assets in

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

the portfolio, such as:

- (i) adverse changes in the payment status of borrowers in the portfolio;
- (ii) national or local economic conditions that correlate with defaults on the assets in the portfolio.

Impairment loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted using the initial effective interest rate. The carrying amount of the asset is reduced by the impairment loss amount and the amount of the loss is recognized in the income statement. In practice, the Company may measure impairment loss based on the fair value of financial asset using an observable market price.

If, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (for example, an improvement in debtor's credit rating), the reversal of the previously recognized impairment loss is recognized in the income statement.

*(b) Assets classified as available-for-sale*

The Company assesses at the end of each reporting period whether there is objective evidence that a financial asset or a Company of financial assets is impaired. For debt securities, the Company uses the criteria refer to in (a) above. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost, for example decrease in fair value of the investments significantly or consistently, is also evidence that the asset is impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss – is removed from equity and recognized in the income statement. Impairment losses recognized in the Company income statement on equity instruments are not reversed through the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed through the income statement.

**2.7 Derivative Financial Instruments and Hedging Activities**

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The method of recognizing the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The resulting gain or loss is recognized in 'financial income (costs)' according to the nature of transactions.

The effective portion of changes in the fair value of derivatives that are designated and qualified as cash flow hedges is recognized in other comprehensive income. The gain or loss relating to the ineffective portion is recognized immediately in the income statement within 'other gains(losses), or 'finance income (costs)'

Any cumulative gain or loss existing in equity at that time remains in equity and is recognized when the forecast transaction is ultimately recognized in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement within 'other gains(losses), or 'finance income (costs)'

**2.8 Trade Receivables**

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less, they are classified as current assets. If not, they are presented as non-current assets. Trade receivables are recognized

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

initially at fair value and subsequently measured at amortized cost using the effective interest method, less allowance for doubtful accounts.

**2.9 Inventories**

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the moving average method, except for the cost of inventories in-transit that is determined using the specific identification method. The cost of finished goods and work in progress consists of the design costs, raw materials, direct labor, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

**2.10 Property, Plant and Equipment**

All property, plant and equipment are stated at historical cost less depreciation and accumulated impairment loss. Historical cost includes expenditures directly attribute to the acquisition of the items. In case that revaluation occurred on past financial policy, it was noted as deemed cost at the time of that revaluation.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate the difference between their cost and their residual values over their estimated useful lives, as follows:

Buildings	5 ~ 50 years
Structures	7 ~ 40 years
Machinery	5 ~ 20 years
Tools, equipment	4 ~ 10 years
Vehicles	4 ~ 10 years
Other	3 ~ 10 years

The assets residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within 'other operating income(losses)', net in the comprehensive income statement.

**2.11 Borrowing Costs**

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization. All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

**2.12 Intangible Assets**

*(a) Goodwill*

Goodwill is measured as explained in Note 2.2(1) and goodwill arises on the acquisition of

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

subsidiaries, associates and business are included in intangible assets. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs to sell. Any impairment is recognized immediately as an expense and is not subsequently reversed.

*(b) Industrial property rights*

Industrial property rights are shown at historical cost. Industrial property rights have a finite useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of industrial property rights over their estimated useful lives of 5 to 10 years.

*(c) Other intangible assets*

Other intangible assets such as software that meet the definition of an intangible asset are amortized using the straight-line method over their estimated useful lives of 4 to 10 years when the asset is available for use. Membership rights are regarded as intangible assets with indefinite useful life and not amortized because there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity. All membership rights are tested annually for impairment and stated at cost less accumulated impairment. Impairment losses are not reversed.

**2.13 Investment Property**

Investment property is held to earn rentals or for capital appreciation or both. Investment property also includes property that is being constructed or developed for future use as investment property. Investment property is measured initially at its cost including transaction costs incurred in acquiring the asset. After recognition as an asset, investment property is carried at cost less accumulated depreciation and impairment losses.

Subsequent costs are include in the asset's carrying amount or recognized as a separate asset, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Land held for investment is not depreciated. Investment property, except for land, is depreciated using straight-line method over their useful lives from 5 to 40 years.

The depreciation method, the residual value and the useful life of an asset are reviewed at the end of each financial year and, if management judges that previous estimates should be adjusted, the change is accounted for as a change in an accounting estimate.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within 'other gains and losses, net' in the income statements.

**2.14 Impairment of Non-financial Assets**

Goodwill or intangible assets with indefinite useful lives are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets, other than goodwill, that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

**2.15 Trade Payables**

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities. Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

**2.16 Financial Guarantee Contract**

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument.

Financial guarantees are initially recognized in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Company's liabilities under such guarantees are measured at the higher of the amounts below. Any increase in the liability relating to guarantees is reported as other financial liabilities.

- Amount calculated in accordance with Korean IFRS 1037, *Provisions, Contingent Liabilities and Contingent Assets*; or
- The initial amount, less accumulated amortization recognized in accordance with Korean IFRS1018, *Revenue*.

**2.17 Borrowings**

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently carried at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method. The Company recognizes borrowings as current assets unless it has an unconditional right to delay the settlement of the borrowing. Terms on liabilities that can be settled by issuance of equity instruments according to the option of contract counterpart do not affect liquidity classification.

**2.18 Provisions**

Provisions are recognized when: the Company has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Provisions are measured at the present value of the expenditures that is expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

**2.19 Current and Deferred Income Tax**

The tax expense for the period comprises current and deferred tax. Tax is recognized in the income statement, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

The current income tax charge is calculated based on the tax laws enacted or substantively enacted at the statement of financial position date in the countries where the Company operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions, where appropriate, based on amounts expected to be paid to the tax authorities.

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Company financial statements. However, deferred tax assets and liabilities are not recognized if they arise from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit(loss). Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the statement of financial position date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that the future taxable profit against which the temporary differences can be utilized will be available.

Deferred income tax liabilities are recognized on addible temporary differences arising on investments in subsidiaries and associates, except for the cases where the timing of the reversal of the temporary differences are controlled by the Company and it is probable that the temporary differences will not be reversed in the foreseeable future.

Deferred income tax assets and liabilities are offset, when there is a legally enforceable right to offset current tax assets against current tax liabilities, and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority for the same taxable entity or when there is an intention to settle the balances on a net basis for the different taxable entities.

## **2.20 Employee Benefits**

### **(a) Retirement benefit obligations**

A defined benefit plan is a pension plan that is not a defined contribution plan. Typically defined benefit plans define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. The liability recognized in the statement of financial position in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognized past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise. Past-service costs are recognized immediately in income, while costs are amortized over the vesting period.

### **(b) Internal labor welfare fund**

A few companies in the Company operate internal labor welfare fund. The Company estimates asset amounts to the level that the net asset of internal labor welfare fund is able to decrease future related work force salary.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

*(c) Other long-term employee benefits*

The Company provides other long-term employee benefits to their employees. The entitlement to these benefits is usually conditional on the employee working for more than 10 years. The expected costs of these benefits are accrued over the period of employment using the same accounting methodology as used for defined benefit pension plans. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recognized in the income statement as they occur. These benefits are calculated annually by independent actuaries.

**2.21 Share Capital**

Ordinary shares that are not mandatorily redeemable are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received is included in equity attributable to the Company's equity holders.

**2.22 Revenue Recognition**

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for goods and services supplied, stated net of discounts, returns and value added taxes, after elimination of intra-company transactions.

The Company recognizes revenue when the amount of revenue can be reliably measured; when it is probable that future economic benefits will flow to the entity; and when specific criteria have been met for each of the Company's activities, as described below. The revenue can be reliably measured only when any contingency related to sales is resolved. The Company bases its estimate on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

*(a) Sales of goods*

Sales of goods are recognized when products are delivered to the purchaser. Delivery does not occur until the products have been shipped to the specified location, the risks of obsolescence and loss have been transferred to the wholesaler, and either the purchaser has accepted the products in accordance with the sales contract or the acceptance provisions have lapsed or the Company has objective evidence that all criteria for acceptance have been satisfied.

*(b) Interest Income*

Interest income is recognized using the effective interest method according to the time passed. When a loan and receivable is impaired, the Company reduces the carrying amount to its recoverable amount and continues unwinding the discount as interest income. Interest income on impaired loan and receivables is recognized using the original effective interest rate.

*(c) Dividend Income*

Dividend income is recognized when the right to receive payment is established.

**2.23 Lease**

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

over the period of the lease.

The Company leases specific property, plant and equipment agreement. Leases of property, plant and equipment where the Company has *substantially* all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges. The corresponding rental obligations, net of finance charges, are included in 'borrowings'. The interest element of the finance cost is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset and the lease term.

#### **2.24 Dividend Distribution**

Dividend distribution to the Company's shareholders is recognized as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders.

#### **2.25 Change of the accounting policy**

The Parent Company adopted ERP system in this fiscal year. The Company changed its inventory (except goods in transit) evaluation method from monthly total-average method to moving-average method in order to evaluate inventory more rationally. The purpose of this accounting policy change is to accurately match income and expenses, and to improve the rational distribution of periodical profit and loss. We reflected this accounting policy change from this fiscal year because it is impossible to determine the accumulated effect on the financial statements.

#### **2.26 Approval of Issuance of the Financial Statements**

The financial statements as of December 31, 2011 of the Parent Company was approved by the Board of Directors on March, 8, 2012.

### **3. Financial Risk Management**

#### **3.1 Financial Risk Factors**

The Company's activities expose it to a variety of financial risks: market risk, credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance. The Company uses derivative financial instruments to hedge certain risk exposures.

Risk management is carried out by a central treasury department. The Company treasury identifies, evaluates and hedges financial risks in close co-operation with the Company's operating units. The board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity.

##### *(a) Market risk*

##### *i) Foreign exchange risk*

The Company operates internationally and issue foreign exchange debentures exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar and the Japanese yen. Foreign exchange risk arises from future commercial transactions, recognized assets and liabilities.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Management has set up a policy manage their foreign exchange risk against their functional currency. The Company companies manage their foreign exchange risk arising from future commercial transactions and recognized assets and liabilities cooperate with Company treasury. Foreign exchange risk arises when future commercial transactions or recognized assets or liabilities are denominated in a currency that is not the entity's functional currency.

The Company entity adopted management model for foreign exchange risk to make a boundary of foreign exchange loss.

The Company's financial instruments denominated in major currencies as of December 31, 2011 and 2010, and January 1, 2010.

	December 31, 2011		December 31, 2010		January 1, 2010	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
(in millions of Korean won)						
USD	13,313	14,142	10,766	3,378	8,692	11,183
JPY	777	299,419	50	427,029	22	385,651
EUR	-	3,863	-	369	-	248
CHF	-	39	-	-	-	60
GBP	3,589	1,275	5,929	-	3,170	2,186
AUD	748	182	1,093	-	470	-
CAD	359	9	797	-	117	-
NZD	313	30	198	-	148	-
AED	-	1,155	-	-	-	-
DKK	-	105	-	-	-	97
HKD	-	8	-	-	-	1
SEK	-	-	-	-	-	3

As of December 31, 2011 and 2010, and January 1, 2010, if the foreign exchange rate of the Korean won fluctuated by 10% while other variables were fixed, the effects on income before tax would be as follows:

	December 31, 2011		December 31, 2010		January 1, 2010	
	10% increase	10% decrease	10% increase	10% decrease	10% increase	10% decrease
(in millions of Korean won)						
USD	(83)	83	739	(739)	(249)	249
JPY <sup>1</sup>	(29,864)	29,864	(42,698)	42,698	(38,563)	38,563

<sup>1</sup>The Company has entered into currency swap contracts to manage foreign exchange risk.

The above sensitivity analysis is done with foreign currency denominated assets and liabilities that are not each entity's functional currency. The changes in exchange rate can have an effect on the sales prices and gross margin ratio of the Company in the future.

iii) Cash flow interest rate risk

The Company's cash flow interest rate risk arises from debentures and others. Debentures that are issued at variable rates expose the Company to the cash flow interest rate risk that is partially offset by cash held at variable rates.

The Company analyzes its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and hedging. Based on these scenarios, the Company calculates the impact on profit and loss of a defined interest rate shift. For each simulation, the same interest rate shift is used for all currencies. The scenarios are run only for liabilities that represent the major interest-bearing positions.

Based on the simulations performed, the impact on the profit of a 1% shift would be a maximum increase of ₩ 3,069 million (2010: ₩ 4,460 million) won or decrease of ₩ 3,069 million (2010: ₩

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

4,460 million) respectively. The simulation is done on a quarterly basis to verify that the maximum loss potential is within the limit given by the management.

Based on the various scenarios, the Company manages its cash flow interest rate risk by using floating-to-fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates.

*(b) Price Risk*

The Company is exposed to the price risk of equity securities that are categorized as available-for-sale financial assets. Stocks owned by the Company entity are trading in the Korea Stock Exchange. The effect on the equity made by price fluctuations of equity securities as of December 31, 2011 and 2010, and January 1, 2010, is as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
<i>(in millions of Korean won)</i>			
10% increase	118,770	145,188	111,044
10% decrease	(118,770)	(145,188)	(111,044)

*(c) Credit Risk*

Credit risk is managed on a the Company basis. Credit risk arises from cash and cash equivalents and deposits with banks and financial institutions, as well as credit exposures to retail customers, including outstanding receivables and committed transactions. The Company trades with business parties whose credit is upper standard to manage credit risks. The entity reviews the limitation of trade by credit and adjusts collateral levels through consistent credit checking to the business parties.

No credit limits were exceeded during the reporting period, and management does not expect any losses from nonperformance by these counterparties.

The Company operates following policies and procedures to take care of credit risks.

For the aspect of receivables, the Company evaluates credits of business associates by using open financial information and information issued by credit rating agencies. Based on this evaluation, the entity determines the limitation of trade via credit. For some receivables, the entity takes insurance, collateral or guarantees.

The Company saves cash and cash equivalents, and time deposits in the financial agencies such as Woori Bank and Kookmin Bank. The entity also progresses derivative trades with a few banks. The credit risks from financial agencies are quiet low because all of the trade is arranged with the high credit rated financial agencies. For banks or financial agencies, the entity makes a trade in the case of the credit level is more than the standard that is given by independent credit rating agencies.

*(d) Liquidity Risk*

Cash flow forecasting is performed by the Company finance department. The Company finance department monitors rolling forecasts of the Company's liquidity requirements to ensure it has sufficient cash to meet operational needs while maintaining sufficient headroom on its undrawn committed borrowing facilities at all times so that the Company does not breach borrowing limits or covenants (where applicable) on any of its borrowing facilities. Such forecasting takes into consideration the Company's debt financing plans, covenant compliance, compliance with internal statements of financial position ratio targets and, if applicable external regulatory or legal requirements.

The Company finance department invests surplus cash in interest-bearing current accounts, time

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

deposits, and money market deposits, instruments with appropriate maturities or sufficient liquidity to provide sufficient headroom as determined by the above-mentioned forecasts. At the reporting date, the Company held ordinary deposits ₩ 40,717 million (2010: ₩ 35,602 million) and other liquid assets of ₩ 112,731 million (2010: ₩ 132,794 million) that are expected to readily generate cash inflows for managing liquidity risk.

The table below analyses the Company's non-derivatives financial liabilities into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. Cash flow in the table below represents undiscounted amounts. Borrowings include stated interest.

	December 31, 2011			
	Less than 1 year	1 year between 2 years	2 years between 5 years	Over 5 years
<i>(in millions of Korean won)</i>				
Borrowings <sup>1</sup>	6,838	8,119	6,954	-
Debentures <sup>1</sup>	297,397	4,080	103,060	-
Currency swap contract <sup>2</sup>	(36,847)	-	-	-
Currency swap contract <sup>2</sup>	6,463	-	-	-
Trade and other payables	259,904	-	-	-
Other financial liabilities	48,605	-	-	-
Financial guarantee contracts	58,860	-	-	-
	641,220	12,199	110,014	-
	December 31, 2010			
<i>(in millions of Korean won)</i>				
Less than 1 year	21,836	432	1,557	1,003
Borrowings <sup>1</sup>	159,825	275,988	-	-
Debentures <sup>1</sup>	(40,870)	(19,672)	-	-
Currency swap contract <sup>2</sup>	10,320	6,635	-	-
Currency swap contract <sup>2</sup>	231,277	-	-	-
Trade and other payables	49,862	-	-	-
Other financial liabilities	34,454	-	-	-
Financial guarantee contracts	466,704	263,383	1,557	1,003

	January 1, 2010			
	Less than 1 year	1 year between 2 years	2 years between 5 years	Over 5 years
<i>(in millions of Korean won)</i>				
Borrowings <sup>1</sup>	10,204	1,493	2,285	1,122
Debentures <sup>1</sup>	6,467	144,760	249,687	-
Currency swap contract <sup>2</sup>	-	(26,102)	6,509	-
Currency swap contract <sup>2</sup>	11,564	10,617	6,756	-
Trade and other payables	240,101	-	-	-
Other financial liabilities	65,949	-	-	-
Financial guarantee contracts	25,878	-	-	-
	360,163	130,768	265,237	1,122

<sup>1</sup> The amounts include interest to be paid until maturity.

<sup>2</sup> Bonds with floating rate in foreign currencies and future expecting cash outflow of currency swaps are estimated with foreign exchange rate and floating rate.

# Lotte Confectionery Co., Ltd. and Subsidiaries

## Notes to Consolidated Financial Statements

### December 31, 2011 and 2010, and January 1, 2010

#### 3.2 Capital Management

The purpose of financial management of the Company is to maximize profit of shareholders by keeping sound financial structure. The entity progresses adequate fixing methods of financial structure by monitoring financial ratio every months such as debt ratio and net borrowing ratio to achieve the best financial structure.

Consistent with others in the industry, the Company monitors capital based on of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the Company statement of financial position plus net debt.

The gearing ratios and debt to equity ratio as of December 31, 2011 and 2010, and January 1, 2010, were as follows:

	December 31,		December 31,		January 1,	
	2011		2010		2010	
<i>(in millions of Korean won)</i>						
Total borrowings (a)		406,465		449,129		398,325
Less: cash and cash equivalents (b)		(182,610)		(192,539)		(89,408)
Net debt (c)=(a)-(b)		223,855		256,590		308,917
Total liabilities (d)		1,286,275		1,299,940		1,157,633
Total equity(e)		2,614,990		2,691,940		2,344,517
Total capital (f)=(d)+(e)		3,901,265		3,991,880		3,502,150
Gearing ratio (c/f)		5.7%		6.4%		13.9%
Debt to equity ratio(d/e)		49.2%		48.3%		49.4%

#### 3.3 Fair Value Estimation

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in measurements.

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1).
- Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly(that is, as prices) or indirectly (that is, derived from prices) (Level 2).
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

The following table presents the Company's financial assets and financial liabilities that are measured at fair value.

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
<i>(in millions of Korean won)</i>				
<b>Asset:</b>				
Derivative instruments used for hedging purpose	-	34,650	-	34,650
Available-for-sale financial assets				
Equity securities	1,187,702	-	318,214	1,505,916
Debt investments	-	-	1,912	1,912
<b>Total</b>	<b>1,187,702</b>	<b>34,650</b>	<b>320,126</b>	<b>1,542,478</b>
<b>Liabilities</b>				
Derivative instruments used for hedging purpose	-	42	-	42
<b>Total</b>	<b>-</b>	<b>42</b>	<b>-</b>	<b>42</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

	December 31, 2010			Total
	Level 1	Level 2	Level 3	
<i>(in millions of Korean won)</i>				
<b>Asset:</b>				
Derivative instruments used for hedging purpose	-	53,393	-	53,393
Available-for-sale financial assets				
Equity securities	1,451,881	-	211,188	1,663,069
Debt investments	-	-	4,664	4,664
<b>Total</b>	<b>1,451,881</b>	<b>53,393</b>	<b>215,852</b>	<b>1,721,126</b>
	<b>January 1, 2010</b>			
<i>(in millions of Korean won)</i>				
<b>Asset:</b>				
Derivative instruments used for hedging purpose	-	15,126	-	15,126
Available-for-sale financial assets				
Equity securities	1,110,438	-	168,970	1,279,408
Debt investments	-	-	5,481	5,481
<b>Total</b>	<b>1,110,438</b>	<b>15,126</b>	<b>174,451</b>	<b>1,300,015</b>
<b>Liabilities</b>				
Derivative instruments used for hedging purpose	-	57	-	57
<b>Total</b>	<b>-</b>	<b>57</b>	<b>-</b>	<b>57</b>

The fair value of financial instruments traded in active markets is based on quoted market prices at the statement of financial position date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, an entity within the same industry, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Company is the current bid price. These instruments are included in Level 1. Instruments included in Level 1 consist primarily of KOSPI, KOSDAQ equity investments classified as trading securities or available for sale.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in Level 2.

If one or more of the significant inputs is not based on observable market data, the instrument is included in Level 3.

Specific valuation techniques used to value financial instruments include:

- Quoted market prices or dealer quotes for similar instruments.
- The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves.
- The fair value of forward foreign exchange contracts is determined using forward exchange rates at the statement of financial position date, with the resulting value discounted back to present value.
- Other techniques, such as discounted cash flow analysis, are used to determine fair value for the remaining financial instruments.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

The following table presents the changes in Level 3 instruments.

	<b>2011</b>		<b>2010</b>	
<i>(in millions of Korean won)</i>				
Beginning balance		215,852		174,451
Purchases / Sales		27,306		20,560
Transfers		(5,864)		(1,240)
Gains and losses on valuation of available-for-sale securities		82,832		22,081
Ending balance		<u>320,126</u>		<u>215,852</u>

The following table presents available-for-sale financial assets that are valued at historical cost as of December 31, 2011 and 2010, and January 1, 2010.

	<b>December 31,</b>		<b>January 1,</b>	
	<b>2011</b>	<b>2010</b>	<b>2010</b>	
<i>(in millions of Korean won)</i>				
Non-marketable securities	349	349		349
Equity investments	114	114		114
Total	<u>463</u>	<u>463</u>		<u>463</u>

The above securities and share capitals are excluded from fair value assessment because cash flow estimation is difficult, and comparable businesses that are similar in industry and size do not exist.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

**4. Critical Accounting Estimates and Judgments**

The Company makes estimates and assumptions concerning the future by definition, the resulting accounting estimates will seldom equal the related actual results. Estimations and assumptions are continuously evaluated with consideration to factors such as events reasonably predictable in the foreseeable future within the present circumstance according to historical experience. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

*(a) Estimated impairment of goodwill*

The Company tests annually whether goodwill has suffered any impairment in accordance with the accounting policy stated in Note 2. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates.

*(b) Income taxes*

The Company is operating in numerous countries and the income generated from these operations is subject to income taxes based on tax laws and interpretations of tax authorities in numerous jurisdictions. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Company recorded, based on its best estimate, current taxes and deferred taxes that the Company will be liable in the future for the operating results as of the financial year-end. However, the final tax outcome in the future may be different from the amounts that were initially recorded. Such differences will affect the current and deferred income tax assets and liabilities in the period in which such determination is made.

*(c) Fair value of financial instruments*

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Company uses its judgment to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

*(d) Defined benefit liability*

The present value of the defined benefit liability depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost (income) for pensions include the discount rate. Any changes in these assumptions will affect the carrying amount of the defined benefit liability. The Company determines the appropriate discount rate at the end of each year. This is the interest rate that is used to determine the present value of estimated future cash outflows expected to be required to settle the defined benefit liability. In determining the appropriate discount rate, the Company considers the interest rates of high-quality corporate bonds that are denominated in the currency in which the pension benefits will be paid, and that have terms to maturity approximating to the terms of the related pension liability. Other key assumptions for defined benefit liability are based in part on current market conditions.

*(e) Provisions*

The Company recognizes provisions for warranties estimated returns as of the reporting date. The amounts are estimated based on historical data.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**5. Segment Information**

The Company's reportable segments and details are as follows:

Segment	Products or services	Major customers
Dried fruits	Snack, Gum	E-mart, Lotte mart, Home plus
Frozen sweets	Frozen sweets	E-mart, Lotte mart, Home plus
Others	Health food, Lease	Lotte mart, Lotte logistics

(a) The following table presents segment information for the years ended December 31, 2011 and 2010. Revenue and operating profit

	2011			
	Dried fruits	Frozen sweets	Others	Adjustment Total
<i>(in millions of Korean won)</i>				
Total segment revenue	1,435,424	341,258	92,562	- 1,869,244
Inter-segment revenue	(15,086)	-	-	(15,086)
Revenue from external customers	1,420,338	341,258	92,562	- 1,854,158
Operating profit (losses)	127,913	35,783	16,369	(807)
Depreciation and amortization	51,773	10,527	7,798	- 70,098

2010

	2010			
	Dried fruits	Frozen sweets	Others	Adjustment Total
<i>(in millions of Korean won)</i>				
Total segment revenue	1,271,259	336,260	82,612	- 1,690,131
Inter-segment revenue	(30,257)	-	(9,193)	(39,450)
Revenue from external customers	1,241,002	336,260	73,419	- 1,650,681
Operating profit (losses)	122,143	34,040	15,388	(316)
Depreciation and amortization	40,247	9,600	7,242	- 57,089

(b) The segment information on assets and liabilities as of December 31, 2011 and 2010, and January 1, 2010, is as follows:

	December 31, 2011			
	Dried fruits	Frozen sweets	Others	Adjustment Total
<i>(in millions of Korean won)</i>				
Total assets for the segment <sup>1</sup>	1,538,218	496,480	110,400	1,756,167
Inter-segment revenue <sup>1</sup>	328,948	107,393	23,244	826,691
	December 31, 2010			
<i>(in millions of Korean won)</i>				
Total assets for the segment <sup>1</sup>	1,484,341	484,441	114,503	1,908,595
Inter-segment revenue <sup>1</sup>	311,773	111,866	26,058	850,243
	January 1, 2010			
<i>(in millions of Korean won)</i>				
Total assets for the segment <sup>1</sup>	1,446,921	456,512	97,464	1,501,253
Inter-segment revenue <sup>1</sup>	305,641	103,316	22,689	725,988

<sup>1</sup> Assets and liabilities are measured in a manner consistent with those in the financial

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

statements and allocated based on segment operation.

(c) Financial information by geographical segments as follows:

Location	Sales		Non-current assets <sup>1</sup>	
	2011	2010	December 31, 2011	December 31, 2010 / January 1, 2010
Korea	1,595,544	1,462,447	1,191,880	1,181,074
China	19,125	16,930	30,714	32,722
India	65,560	53,735	85,658	101,318
Europe	119,686	117,569	43,503	43,466
Others	54,244	-	33,059	-
Total	1,854,158	1,650,681	1,384,815	1,358,579
				1,322,261

<sup>1</sup> Represents the total amount of property, plant and equipment, and intangible assets and investment property.

**6. Financial Instruments by Category**

Categorizations of financial assets and liabilities are as follows:

Financial assets	December 31, 2011			
	Loans and receivables	Derivative instruments used for hedging purpose	Available-for-sale financial assets	Total
(in millions of Korean won)				
Cash and cash equivalents	182,610	-	-	182,610
Trade and other receivables	247,449	-	-	247,449
Other current financial assets	69,690	34,650	151	104,491
Other non-current financial assets	28,924	-	1,508,140	1,537,064
Total	528,673	34,650	1,508,291	2,071,614

Financial liability	December 31, 2010		
	Derivative instruments used for hedging purpose	Liabilities measured at amortized cost	Total
(in millions of Korean won)			
Trade and other payables	-	259,904	259,904
Other current financial liabilities	42	48,605	48,647
Borrowings	-	17,503	17,503
Debentures	-	388,963	388,963
Other non-current financial liabilities	-	22,109	22,109
Total	42	737,084	737,126

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

		January 1, 2010		
		Derivative instruments used for hedging purpose	Available-for-sale financial assets	Total
<b>Financial assets</b>				
<i>(in millions of Korean won)</i>				
Cash and cash equivalents	192,539	-	-	192,539
Trade and other receivables	219,965	-	-	219,965
Other current financial assets	72,682	39,705	2,803	115,190
Other non-current financial assets	30,153	13,688	1,665,393	1,709,234
<b>Total</b>	<b>515,339</b>	<b>53,393</b>	<b>1,668,196</b>	<b>2,236,928</b>
<b>December 31, 2010</b>				
<b>Financial liability</b>				
<i>(in millions of Korean won)</i>				
Trade and other payables	231,277			231,277
Other current financial liabilities	49,862			49,862
Borrowings	23,673			23,673
Debentures	425,456			425,456
Other non-current financial liabilities	22,836			22,836
<b>Total</b>	<b>753,104</b>			<b>753,104</b>
<b>Financial assets</b>				
<b>December 31, 2010</b>				
<i>(in millions of Korean won)</i>				
Cash and cash equivalents	89,408	-	-	89,408
Trade and other receivables	191,879	-	-	191,879
Other current financial assets	177,032	-	349	177,381
Other non-current financial assets	24,353	15,126	1,285,003	1,324,482
<b>Total</b>	<b>482,672</b>	<b>15,126</b>	<b>1,285,352</b>	<b>1,783,150</b>
<b>January 1, 2010</b>				
<b>Financial liability</b>				
<i>(in millions of Korean won)</i>				
Trade and other payables	-	240,101		240,101
Other current financial liabilities	-	65,949		65,949
Borrowings	-	14,162		14,162
Debentures	-	384,164		384,164
Other non-current financial liabilities	57	21,723		21,780
<b>Total</b>	<b>57</b>	<b>726,099</b>		<b>726,156</b>

Non-current financial assets and financial liabilities are estimated by book value as a fair value, except available-for-sale financial assets at fair value (Note 18), and non-current borrowings whose fair value is presented separately. Fair values of current financial assets and financial liabilities are same as book values.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Income and loss of financial instruments by category for the years ended December 31, 2011 and 2010, are as follows:

<i>(in millions of Korean won)</i>	2011	2010
<b>Available-for-sale financial assets</b>		
Gain(Loss) on valuation(other comprehensive income)	(170,769)	283,549
Gain(Loss) on disposal(profit or loss)	402	16
Gain(Loss) on disposal(profit and loss substitution) <sup>1</sup>	(254)	(43)
Dividend income	6,536	5,370
<b>Loans and receivables</b>		
Interest income	8,045	6,732
Foreign exchange gain	1,033	1,443
Foreign exchange loss	(1,029)	(1,098)
Gain on foreign currency translation	1,069	916
Loss on foreign currency translation	(905)	(1,755)
Bad debts allowance	(1,324)	(153)
Other bad debts allowance	(163)	(31)
Reversal of allowance for bad debts	23	2
<b>Liabilities at amortized cost</b>		
Interest expense	(21,148)	(19,766)
Foreign exchange gain	710	737
Foreign exchange loss	(17,923)	(41,492)
Gain on foreign currency translation	1,698	10
Loss on foreign currency translation	(3,427)	(458)
<b>Derivative Instruments used for hedging purpose</b>		
Gain on valuation of derivative	17,390	41,344
Gain on derivative transaction	1,811	-
Loss on valuation of derivative	-	(214)
Loss on derivative transaction	(275)	(754)
Gain(Loss) on valuation of derivative (other comprehensive income)	3,939	(2,128)

<sup>1</sup> Reclassification to profit/loss represents amounts transferred from components of other comprehensive income.

**7. Cash and Cash Equivalents**

Cash and cash equivalents are as follows:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Cash	50,508	41,685	37,078
Ordinary deposits	30,538	55,635	51,860
Time deposits	101,564	95,219	470
<b>Total</b>	<b>182,610</b>	<b>192,539</b>	<b>89,408</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**8. Available-for-sale Financial Assets**

The changes in available-for-sale financial assets are as follows:

<i>(in millions of Korean won)</i>	2011	2010
Beginning balance	1,668,196	1,285,352
Acquisition <sup>1</sup>	23,624	20,560
Disposal	(2,517)	(1,184)
Evaluation	(181,347)	363,524
Net gains/(losses) transfer from equity/(Note 23)	(326)	(56)
Other increase and decrease <sup>2</sup>	661	-
<b>Ending balance</b>	<b>1,508,291</b>	<b>1,668,196</b>
Less: non-current portion	(1,508,140)	(1,665,393)
<b>Current portion</b>	<b>151</b>	<b>2,803</b>

<sup>1</sup> There contains 21,974 million available-for-sale financial assets which occurred by selling subsidiary's stocks. These stocks were from physical division.

<sup>2</sup> Represents reclassification from Investment in associates to available-for-sale financial assets due to the decrease in ownership of PT, Lotte Indonesia.

Available-for-sale financial assets are as follows:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Current available-for-sale financial assets	151	2,803	349
Debt securities			
Non-current Available-for-sale financial assets			
Equity securities			
Marketable equity securities	1,187,702	1,451,881	1,110,438
Non-marketable equity securities	318,563	211,537	169,319
Equity Investments	114	114	114
Debt securities	1,761	1,861	5,132
<b>Subtotal</b>	<b>1,508,140</b>	<b>1,665,393</b>	<b>1,285,003</b>
<b>Total</b>	<b>1,508,291</b>	<b>1,668,196</b>	<b>1,285,352</b>

Available-for-sale securities (equity securities) are as follows:

<i>(in millions of Korean won)</i>	December 31, 2011			December 31, 2010	January 1, 2010	
Marketable equity securities	Number of shares	Percentage of ownership (%)	Acquisition cost	Fair value <sup>1</sup>	Book value	Book value
Lotte Shopping Co., Ltd.	2,474,543	8.52	5,644	840,107	840,107	1,170,459
Lotte Chitsung Co., Ltd. (ordinary stock)	145,237	11.74	21,379	212,772	212,772	139,428
						122,435

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Lotte Chilsung Co., Ltd. (preferred stock)	9,660	8.05	176	3,594	3,594	3,734	3,376
BS financial Company Co. Ltd.	5,536,479	2.86	27,596	61,178	61,178	79,448	77,234
Lotte Samkang Co., Ltd.	123,226	9.79	989	50,584	50,584	33,641	30,560
Shinhan Financial Company Co., Ltd.	458,111	0.1	3,315	18,210	18,210	24,234	19,790
Others	79,756	-	203	1,257	1,257	937	851
<b>Subtotal</b>			<b>59,302</b>	<b>1,187,702</b>	<b>1,187,702</b>	<b>1,451,881</b>	<b>1,110,438</b>
<b>Non-marketable equity securities</b>							
Korea seven co. Ltd.	5,977,672	16.6	37,267	95,027	95,027	32,459	12,068
Lotteria Co., Ltd.	65,374	13.59	28,922	70,662	70,662	41,626	33,848
Lotte Station B/D. Co.	319,200	8.87	1,596	63,284	63,284	61,133	53,386
Lotte Data Communication Co., Ltd.	52,376	6.12	7,616	37,528	37,528	28,518	27,724
Lotte Asset Development Ltd	Co. 2,177,458	7.19	11,074	10,887	10,887	8,284	9,444
Lotte Buyeo Resort Co., Ltd.	1,666,667	11.11	8,333	8,333	8,333	8,333	5,000
Lotte Logistics Co., Ltd.	66,308	4.64	4,000	7,060	7,060	6,340	5,144
Korea Fuji Film Co., Ltd.	1,250	0.89	41	6,190	6,190	5,988	4,806
Lotte.com Co., Ltd.	523,548	11.25	2,500	5,596	5,596	5,943	5,572
Lotte Jeju Resort Co., Ltd.	1,000,000	12.5	5,000	5,000	5,000	5,000	5,000
Lotte Trading Co., Ltd.	12,187	1.36	4,487	4,525	4,525	4,037	3,731
Lotte Fresh Delica Co., Ltd.	340,000	9.04	836	1,804	1,804	1,640	1,369
COSMO investment Management Co., Ltd.	4,668	0.55	1,664	1,401	1,401	1,664	1,664
PT, Lotte Indonesia	8,910	7.58	661	680	680	-	-
Lotte Moolisan Co., Ltd.	12,984	0.02	18	237	237	223	214
Others	73,858	-	349	235	349	349	349
<b>Subtotal</b>			<b>114,364</b>	<b>318,449</b>	<b>318,563</b>	<b>211,537</b>	<b>169,319</b>
<b>Equity Investments</b>							
Korea Analysis Research Institute and others			114	114	114	114	114
<b>Total</b>			<b>173,780</b>	<b>1,506,265</b>	<b>1,506,379</b>	<b>1,663,532</b>	<b>1,279,871</b>

The ₩ 326 million (Dec. 31, 2010: ₩ 56 million) profit was reclassified to income and loss from equity.

Maximum exposed price related to credit risk of debt securities among available-for-sale financial

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

assets is book value.

There is no assets which are impaired or in arrear among available-for-sale financial assets.

**9. Trade and Other Receivables**

Trade and other receivables are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
<i>(in millions of Korean won)</i>			
Accounts receivable	251,847	225,696	198,393
Allowance for doubtful accounts	(7,392)	(9,275)	(11,366)
Subtotal	244,455	216,421	187,027
Other accounts receivable	2,933	3,433	4,768
Other receivables	61	111	84
<b>Total</b>	<b>247,449</b>	<b>219,965</b>	<b>191,879</b>

The Company transferred trade receivables amounting to ₩ 715 million to the bank in exchange for cash for the year ended December 31, 2011. The transaction is accounted for as a borrowing (Note 18). According to the loan commitments, the Company has obligation to pay in case of the customers' default.

The aging analysis of these trade receivables is as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
<i>(in millions of Korean won)</i>			
Up to 3 months	242,219	212,552	188,684
3 to 6 months	4,965	7,463	3,603
Over 6 months	4,663	5,681	6,106
<b>Total</b>	<b>251,847</b>	<b>225,696</b>	<b>198,393</b>
<i>(in millions of Korean won)</i>			
Receivables not past due	176,704	164,172	125,938
Past due but not impaired <sup>1</sup>	70,854	54,043	64,270
Impaired <sup>2</sup>	4,289	7,481	8,185
<b>Total</b>	<b>251,847</b>	<b>225,696</b>	<b>198,393</b>

<sup>1</sup>Bonds that are not impaired or in arrears are related to a few consumers who do not have any recent history of default.

<sup>2</sup>The amount of provisions for the bonds separately impaired is ₩ 4,289 million (Dec. 31, 2010: ₩ 7,481 million; Jan. 1, 2010: ₩ 8,185 million). It is deemed difficult to collect cash from separately impaired bonds because these are usually related to business parties suffering unexpected financial problems.

The maximum exposure of trade and other receivables to credit risk at the reporting date is the carrying value of each class of receivable mentioned above.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

The movements in bad debt allowance for the years ended are as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
Beginning balance	9,275	11,366
Bad debts allowance	1,324	153
Reversed	(23)	(2)
Transfer out	(48)	-
Written-off	(3,450)	(4,192)
Reversed (written-off)	350	1,796
Exchange differences	(36)	154
Ending	<u>7,392</u>	<u>9,275</u>

**10. Other Financial Assets and Liabilities**

Other financial assets and liabilities are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
<i>(in millions of Korean won)</i>			
Short-term financial instruments	68,474	71,564	175,511
Derivative instruments used for hedging purpose	34,650	39,705	-
Current Available-for-sale financial assets	151	2,803	349
Accrued income	1,216	1,118	1,521
Subtotal	<u>104,491</u>	<u>115,190</u>	<u>177,381</u>
Long-term financial instruments	14,242	10,055	36
Derivative instruments used for hedging purpose	-	13,688	15,126
Non-Current Available-for-sale financial assets	1,508,140	1,665,393	1,285,003
Loans	175	688	159
Deposits provided	14,507	19,410	24,158
Subtotal	<u>1,537,064</u>	<u>1,709,234</u>	<u>1,324,482</u>
Total	<u>1,641,555</u>	<u>1,824,424</u>	<u>1,501,863</u>
<i>(in millions of Korean won)</i>			
Accrued expenses	48,605	49,862	65,949
Current Derivative instruments used for hedging purpose	42	-	-
Subtotal	<u>48,647</u>	<u>49,862</u>	<u>65,949</u>
Non-trade payables	46	109	1,453
Non-Current Derivative instruments used for hedging purpose	-	-	57
Current Deposits received	22,063	22,727	20,270
Subtotal	<u>22,109</u>	<u>22,836</u>	<u>21,780</u>
Total	<u>70,756</u>	<u>72,698</u>	<u>87,729</u>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**11. Inventories**

Inventories are as follows:

	December 31,		January 1,	
	2011	2010	2010	2010
(In millions of Korean won)				
Merchandise	12,887	11,534	9,947	9,947
Finished goods	72,873	62,176	53,473	53,473
Work-in-process	10,681	7,999	7,932	7,932
Raw materials	72,473	26,520	26,248	26,248
Supplies	411	3,191	3,658	3,658
Work-in-process in transit	12,196	31,396	31,736	31,736
Subtotal	181,521	142,816	132,994	132,994
Less : Provision for valuation	(276)	(574)	(802)	(802)
<b>Total</b>	<b>181,245</b>	<b>142,242</b>	<b>132,192</b>	<b>132,192</b>

The cost of inventories recognized as expense and included in 'cost of sales' amounted to ₩ 925,522 million (2010: ₩ 784,809 million).

**12. Associates and Joint ventures**

Associates and joint ventures as of December 31, 2011 and 2010, and January 1, 2010, are as follows:

	Investee	December 31, 2011		
		Acquisition cost	Net asset value	Book value
	(In millions of Korean won)			
	Lotte China Foods Co., Ltd.	40,153	41,903	45,946
	Lotte Packaging (Beijing) Co., Ltd.	6,576	6,367	6,367
	Lotte Europe Holdings B.V	138,250	98,388	98,388
	BIBICA CORPORATION	17,610	9,210	14,331
	Lotte Vietnam Co., Ltd.	5,475	3,156	4,951
	PT Lotte Trade And Distribution	2,739	(906)	-
	Lotte Taiwan Co., Ltd.	6,672	4,365	7,191
	PT, Lotte Indonesia	-	-	-
	Lotte Confectionery Pilipinas Co	2,643	1,200	1,555
	Lotte Malaysia Sdn Bhd	2,837	1,350	1,546
	Lotte giants	774	2,218	2,218
	Lotte (China) Investment Co., Ltd.	21,968	(12,119)	-
	LH Foods Co., Ltd.	44,591	48,660	48,660
	<b>Total</b>	<b>290,288</b>	<b>203,792</b>	<b>231,153</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Investee	December 31, 2010		
	Acquisition cost	Net asset value	Book value
<i>(in millions of Korean won)</i>			
Lotte China Foods Co., Ltd.	16,858	16,508	16,501
Lotte Packaging (Beijing) Co., Ltd.	6,576	6,290	6,290
Lotte Europe Holdings B.V	138,250	118,251	117,991
BIBICA CORPORATION	17,610	12,021	17,142
Lotte Vietnam Co., Ltd.	5,475	3,411	5,206
PT Lotte Trade And Distribution	2,739	822	822
Lotte Taiwan Co., Ltd.	6,672	4,092	6,907
PT, Lotte Indonesia	3,682	(532)	2,732
Lotte Confectionery Pilipinas Co	2,643	1,694	2,064
Lotte Malaysia Sdn Bhd	2,837	2,004	2,202
Lotte giants	774	1,130	1,130
Lotte (China) Investment Co., Ltd.	21,968	2,647	11,573
LH Foods Co., Ltd.	44,591	44,988	44,988
<b>Total</b>	<b>270,675</b>	<b>213,326</b>	<b>235,548</b>
<b>Investee</b>	<b>January 1, 2010</b>		
<i>(in millions of Korean won)</i>	Acquisition cost	Net asset Value	Book value
Lotte China Foods Co., Ltd.	16,858	16,858	16,858
Lotte Packaging (Beijing) Co., Ltd.	6,576	6,576	6,576
Lotte Europe Holdings B.V	115,327	115,587	115,327
BIBICA CORPORATION	17,610	12,496	17,610
Lotte Vietnam Co., Ltd.	5,475	3,681	5,475
PT Lotte Trade And Distribution	2,739	2,739	2,739
Lotte Taiwan Co., Ltd.	6,672	3,708	6,672
PT, Lotte Indonesia	3,682	419	3,682
Lotte Confectionery Pilipinas Co	2,643	2,273	2,643
Lotte Malaysia Sdn Bhd	2,837	2,639	2,837
Lotte giants	774	774	774
Lotte (China) Investment Co., Ltd.	4,794	4,794	4,794
LH Foods Co., Ltd.	44,591	44,591	44,591
<b>Total</b>	<b>230,578</b>	<b>217,135</b>	<b>230,578</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Changes in investments in associates and joint ventures are as follows:

	2011							2010								
	Beginning	Acquisition (Disposal)	Valuation Gain/Loss	Capital Adjustment	Dividends	Transfer	Foreign currency translation	Ending	Beginning	Acquisition (Disposal)	Valuation Gain/Loss	Capital Adjustment	Dividends	Transfer	Foreign currency translation	Ending
<i>(In millions of Korean won)</i>																
Lotte China Foods Co., Ltd.	16,501	23,295	200	5,950	-	-	-	45,946	16,858	-	(495)	138	-	-	-	16,501
Lotte Packaging (Beijing) Co., Ltd.	6,290	-	(271)	348	-	-	-	6,367	6,576	-	(336)	50	-	-	-	6,290
Lotte Europe Holdings B.V	117,991	-	(16,281)	(3,322)	-	-	-	98,388	115,327	22,923	(16,939)	(3,320)	-	-	-	117,991
BIBICA CORPORATION	17,142	-	(1,689)	(802)	(320)	-	-	14,331	17,610	-	438	(550)	(356)	-	-	17,142
Lotte Vietnam Co., Ltd.	5,206	-	(39)	(216)	-	-	-	4,951	5,475	-	7	(276)	-	-	-	5,206
PT Lotte Trade And Distribution	821	-	(815)	(6)	-	-	-	-	2,739	-	(1,992)	74	-	-	-	821
Lotte Taiwan Co., Ltd.	6,907	-	379	(95)	-	-	-	7,191	6,672	-	(56)	291	(2,827)	-	-	6,907
PT, Lotte Indonesia	2,732	-	89	6	-	-	-	-	3,682	-	(966)	16	-	-	-	2,732
Lotte Confectionery Pilipinas Co.	2,064	-	(514)	5	-	-	-	1,555	2,643	-	(633)	54	-	-	-	2,064
Lotte Malaysia Sdn. Bhd	2,201	-	(619)	(36)	-	-	-	1,546	2,837	-	(834)	198	-	-	-	2,201
Lotte Giants	1,130	-	1,089	-	-	-	-	2,219	774	-	356	-	-	-	-	1,130
Lotte (China) Investment Co., Ltd.	11,575	-	(11,062)	(200)	-	-	-	-	4,794	17,174	(10,298)	(41)	-	-	(54)	11,575
LH Foods Co., Ltd.	44,988	-	998	1,983	-	-	-	48,659	44,591	-	22	1,471	-	-	(1,096)	44,988
<b>Total</b>	<b>235,548</b>	<b>23,295</b>	<b>(28,535)</b>	<b>3,615</b>	<b>(320)</b>	<b>(2,827)</b>	<b>377</b>	<b>231,153</b>	<b>230,578</b>	<b>40,097</b>	<b>(31,726)</b>	<b>(1,895)</b>	<b>(356)</b>	<b>(1,150)</b>	<b>235,548</b>	

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Financial information of investees as of and for the year ended December 31, 2011, is summarized as follows:

(in millions of Korean won)	Location	Percentage of ownership (%)	Total Assets	Total Liabilities	Revenue	Net Income(loss)
Lotte China Foods Co., Ltd.	China	47.16	111,443	22,590	55,092	(441)
Lotte Packaging (Beijing) Co., Ltd.	China	25.00	31,626	6,158	12,699	(1,084)
Lotte Europe Holdings B.V.	Netherlands	31.66	772,343	461,549	128,607	(52,252)
BIBICA CORPORATION	Vietnam	38.60	34,353	10,540	53,717	(4,374)
Lotte Vietnam Co., Ltd.	Vietnam	36.84	15,945	7,378	24,794	(105)
PT Lotte Trade And Distribution	Indonesia	40.00	6,527	8,792	10,286	(4,304)
Lotte Taiwan Co., Ltd.	Taiwan	50.00	13,938	5,207	20,161	73
Lotte Confectionery Pilipinas Co	Philippines	40.00	3,801	802	1,341	(1,250)
Lotte Malaysia Sdn. Bhd	Malaysia	40.00	4,312	938	1,322	(1,547)
Lotte Giants.	Korea	30.00	12,682	5,288	40,060	3,62
Lotte Investment Co., Ltd (China)	China	43.50	60,872	88,733	70,120	(32,230)
LH Foods Co., Ltd	Hongkong	51.00	122,815	27,403	70,613	1,95

Fair value of marketable shares held by associates:

(in millions of Korean won except per share)	Shares	Market price per share	Market Price	Book Value
BIBICA CORPORATION	5,953,000	609	3,625	14,331

Unrecognized accumulated loss from discontinue applied equity method:

(in millions of Korean won)	December 31, 2011	December 31, 2010	January 1, 2010
PT, Lotte Trade And Distribution	(906)	-	-
Lotte (China) Investment Co., Ltd.	(3,079)	-	-

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**13. Property, Plant and Equipment**

Changes in property, plant and equipment are as follows:

	2011							Construction- in-progress	Total
	Land	Buildings	Structures	Machinery	Vehicles	Others	Construction- in-progress		
(in millions of Korean won)									
Balance as of January 1, 2011	706,086	244,470	2,912	205,816	1,658	34,446	8,637	1,204,025	
Acquisition	1,079	3,043	56	4,845	142	4,154	74,925	88,244	
Transfer	994	12,970	15	21,411	723	22,554	(58,592)	75	
Disposals	(10,637)	(482)	-	(1,599)	(954)	(356)	-	(14,028)	
Depreciation	-	(10,490)	(235)	(37,476)	(948)	(18,199)	-	(67,348)	
Disposal of Subsidiary	-	-	-	-	-	(1,974)	-	(1,974)	
Impairment	-	-	-	(393)	-	-	-	(393)	
Business combination	3,596	4,311	-	26,923	100	1,105	-	36,035	
Exchange differences	(2,332)	(5,854)	326	(5,627)	551	152	(226)	(13,010)	
Balance as of December 31, 2011	698,786	247,968	3,074	213,900	1,272	41,882	24,744	1,231,626	
Acquisition Cost	700,122	421,439	11,947	726,380	6,189	156,186	24,744	2,047,007	
Accumulated Depreciation	-	(173,471)	(8,873)	(510,797)	(4,917)	(114,304)	-	(812,362)	
Accumulated Impairment Loss	(1,336)	-	-	(1,683)	-	-	-	(3,019)	
<b>2010</b>									
(in millions of Korean won)									
Balance as of January 1, 2010	699,126	143,079	3,097	163,229	3,565	27,888	137,674	1,177,658	
Acquisition	1,717	19,481	138	11,193	361	17,240	19,352	69,482	
Transfer	7,378	54,764	280	40,319	-	2,860	(105,841)	(240)	
Disposals	(505)	(529)	-	(226)	(380)	(369)	(29)	(2,038)	
Depreciation	-	(10,079)	(305)	(28,092)	(1,219)	(14,476)	-	(54,171)	
Exchange differences	(1,630)	37,754	(296)	19,393	(669)	1,303	(42,519)	13,334	
Balance as of December 31, 2010	706,086	244,470	2,912	205,816	1,658	34,446	8,637	1,204,025	
Acquisition Cost	707,422	408,125	11,522	683,394	5,966	144,847	8,637	1,969,913	
Accumulated Depreciation	-	(163,655)	(8,610)	(476,289)	(4,308)	(110,401)	-	(763,263)	
Accumulated Impairment Loss	(1,336)	-	-	(1,289)	-	-	-	(2,625)	

Depreciation amounting to ₩ 39,565 million (2010: ₩ 29,592 million) has been charged to 'cost of sales', and ₩ 27,783 million (2010: ₩ 24,579 million) to 'selling and administrative expenses'.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**14. Intangible Assets**

Changes in intangible assets for are as follows:

	2011				
	Industrial property rights	Member- ships	Others	Goodwill	Total
<i>(in millions of Korean won)</i>					
Beginning balance	1,814	1,786	638	70,309	74,547
Acquisition	111	8	898	-	1,017
Transfer	98	-	170	-	268
Disposal	(1)	(3)	-	-	(4)
Amortization	(506)	-	(424)	-	(930)
Business combination	6	-	-	1,355	1,361
Disposal of Subsidiary	(10)	-	(221)	-	(231)
Foreign exchange translation	1	-	3	(907)	(903)
Ending balance	<u>1,513</u>	<u>1,791</u>	<u>1,064</u>	<u>70,757</u>	<u>75,125</u>

**2010**

	Industrial property rights	Member- ships	Others	Goodwill	Total
	<i>(in millions of Korean won)</i>				
Beginning balance	3,103	1,430	949	77,773	83,255
Acquisition	336	356	116	-	808
Transfer	182	-	-	-	182
Amortization	(1,075)	-	(283)	-	(1,358)
Foreign exchange Translation	(732)	-	(144)	(7,464)	(8,340)
Ending balance	<u>1,814</u>	<u>1,786</u>	<u>638</u>	<u>70,309</u>	<u>74,547</u>

Amortization amounting to ₩ 3 million (2010: nil) is included in the 'cost of sales', and ₩ 927 million (2010: ₩ 1,358 million) in the 'selling and administrative expenses', respectively.

**15. Impairment Tests for Goodwill**

Goodwill is monitored by the management at the operating segment level (Cash-Generating Units or group of Cash-Generating Units). The following is a summary of goodwill allocation for each operating segment:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Lotte Confectionery Holdings B. V.	69,404	70,309	77,773
K.S. SULEMANJI ESMALJI & SONS(Private) Limited	1,353	-	-
	<u>70,757</u>	<u>70,309</u>	<u>77,773</u>

Goodwill impairment reviews are undertaken annually. Impairment test suggests that, the carrying

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

value of cash generating units does not exceed the recoverable amount. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations use pre-tax cash flow projections based on financial budgets approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated using the estimated growth rates stated below. The growth rate does not exceed the long-term average growth rate for the business in which the CGU operates. In addition, a constant growth rate assumption is used for perpetual cash flow calculation. The key assumptions used for value-in-use calculations are as follows:

	<b>December 31, 2011</b>	
	Lotte Confectionery Holdings B.V	K.S. SULEMANJI ESMALJI & SONS(Private) Limited
Gross margin	30.9%	17.7%
Sales growth rate <sup>1</sup>	11.8%	5.0%
Perpetual growth rate <sup>2</sup>	0.0%	0.0%
Pretax discount rate <sup>3</sup>	11.6%	10.0%
	<b>December 31, 2010</b>	
	Lotte Confectionery Holdings B.V	K.S. SULEMANJI ESMALJI & SONS(Private) Limited
Gross margin	28.9%	-
Sales growth rate <sup>1</sup>	10.8%	-
Perpetual growth rate <sup>2</sup>	0.0%	-
Pretax discount rate <sup>3</sup>	10.1%	-
	<b>January 1, 2010</b>	
	Lotte Confectionery Holdings B.V	K.S. SULEMANJI ESMALJI & SONS(Private) Limited
Gross margin	29.0%	-
Sales growth rate <sup>1</sup>	10.1%	-
Perpetual growth rate <sup>2</sup>	0.0%	-
Pretax discount rate <sup>3</sup>	10.0%	-

<sup>1</sup> Sales growth rate is the weighted-average sales growth rate used to extrapolate cash flows for five-year period is measured based on the historical growth rate.

<sup>2</sup> Perpetual growth rate is the expected growth rate over 5 years.

<sup>3</sup> Pretax discount rate was applied to the cash flow projection.

The Company determines the sales growth rate based on its past performances and expectation on future market development. The discount rate used is the pre-tax discount rate that reflects relevant risks.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**16. Investment property**

Changes in investment property are as follows:

(in millions of Korean won)	2011			
	Land	Buildings	Structures	Total
<b>Beginning balance</b>	17,606	61,777	623	80,006
Transfer	-	(248)	-	(248)
Depreciation	-	(1,776)	(44)	(1,820)
Business combination	1,995	-	-	1,995
Foreign exchange Translation	(1,918)	49	-	(1,869)
<b>Ending balance</b>	<u>17,683</u>	<u>59,802</u>	<u>579</u>	<u>78,064</u>
Acquisition cost	17,683	63,500	664	81,847
Accumulated depreciation	-	(3,698)	(85)	(3,783)

(in millions of Korean won)	2010			
	Land	Buildings	Structures	Total
<b>Beginning balance</b>	17,429	43,918	-	61,347
Acquisition	-	19,128	664	19,792
Depreciation	-	(1,519)	(41)	(1,560)
Foreign exchange Translation	421	6	-	427
<b>Ending balance</b>	<u>17,850</u>	<u>61,533</u>	<u>623</u>	<u>80,006</u>
Acquisition cost	17,850	64,586	664	83,100
Accumulated depreciation	-	(3,053)	(41)	(3,094)

Depreciation amounting to ₩ 1,799 million (2010: ₩1,539 million) has been charged to 'cost of sales', and ₩21 million (2010: ₩21 million) to 'selling and administrative expenses' respectively.

Fair value of investment property as of December 31, 2011, is ₩ 89,758 million.

Rental income from investment property during the year ended December 31, 2011, is ₩ 9,065 million (2010: ₩ 6,958 million), and operating expenses (including repairs and maintenance) directly related to those investment property is ₩ 2,680 million (2010: ₩ 1,880 million).

**17. Accounts Payable and Other Liabilities**

Accounts payable and other liabilities as follows:

(in millions of Korean won)	December 31, 2011	December 31, 2010	January 1, 2010
	Accounts payable	169,742	154,146
Non-trade payables	90,116	77,131	89,857
Other payables	46	-	11
<b>Total</b>	<u>259,904</u>	<u>231,277</u>	<u>240,101</u>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**18. Borrowings**

Details of borrowings are as follows:

<i>(in millions of Korean won)</i>	Short-term Borrowings	Bank	Interest rate At 12/31/2011	2011.12.31	2010.12.31	2010.1.1
	Short-term borrowings	Shinhan Bank	2.30%	715	2,608	1,891
	Current maturities of bank loans	Al Falah, others	Kibor+1.4%	1,285	393	529
	Notes discounted	Hana Bank, others	Short-term loan interest+3.8% KBC EONIA +0.75%	-	5,400	5,400
	Bank overdraft	KBC, others		4,509	12,558	1,847
	<b>Total</b>			<b>6,509</b>	<b>20,959</b>	<b>9,667</b>

<i>(in millions of Korean won)</i>	Long-term Borrowings	Details	Maturity date	Interest rate At 12/31/2011	2011.12.31	2010.12.31	2010.1.1
	Kookmin Bank	Fund for renting house	2017-12-10	3.00%	-	325	366
	KBC	Fund for facilities	2017-09-22	4.75%	-	2,389	3,273
	Al Falah	Fund for facilities	2014-06-30	Kibor+1.4%	9,169	-	-
	Hana Bank	Operating fund	2013-03-08	8.65%	1,825	-	855
	<b>Total</b>				<b>10,994</b>	<b>2,714</b>	<b>4,494</b>

<i>(in millions of Korean won)</i>	Debentures	Bank	Maturity date	Interest rate At 12/31/2011	2011.12.31	2010.12.31	2010.1.1
	53rd placed	Mizuho Corporate Bank, Ltd	2011-09-11	3M Euro Yen LIBOR+150b.p	-	153,679	138,910
	54th placed	Mizuho Corporate Bank, Ltd	2012-07-10	3M Euro Yen LIBOR+150b.p	148,516	139,708	126,282
	55th placed	Mizuho Corporate Bank, Ltd	2012-12-28	3M Euro Yen TIBOR+100b.p	141,090	132,722	119,968
	56th placed	Tong Yang Securities Inc., others	2014-07-29	4.08%	100,000	-	-
	Subtotal				<b>389,606</b>	<b>426,109</b>	<b>385,160</b>
	Less : discount on debentures				<b>(643)</b>	<b>(653)</b>	<b>(996)</b>
	Book value(Current debentures)				<b>388,963</b>	<b>425,456</b>	<b>384,164</b>
	Less : Current portion				<b>289,606</b>	<b>153,679</b>	<b>-</b>
	Add : Current discounts on debentures				<b>248</b>	<b>111</b>	<b>-</b>
	Book value(Non-current debentures)				<b>99,605</b>	<b>271,888</b>	<b>384,164</b>

Debentures above will be paid upon their maturity date. Interest expense is paid every three

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

months.

Book value and fair value of non-current borrowings and debentures are as follows:

(in millions of Korean won)	December 31, 2011		December 31, 2010		January 1, 2010	
	Book value	Fair value	Book value	Fair value	Book value	Fair value
Long-term borrowings	10,994	10,994	2,714	3,013	4,494	4,831
Debentures	388,963	390,878	425,456	425,456	384,164	384,164
<b>Total</b>	<b>399,957</b>	<b>401,872</b>	<b>428,170</b>	<b>428,469</b>	<b>388,658</b>	<b>388,995</b>

Changes in borrowings and debentures:

(in millions of Korean won)	2011		2010	
	Borrowings	Debentures	Borrowings	Debentures
Beginning balance	23,673	425,456	14,162	384,164
Amortization	-	481	-	419
Repayments	(48,200)	(153,679)	(59,234)	-
Increase	17,442	99,542	69,376	-
Exchange differences	(1,160)	17,163	(631)	40,873
Business combination	25,748	-	-	-
<b>Total</b>	<b>17,503</b>	<b>388,963</b>	<b>23,673</b>	<b>425,456</b>

**19. Defined Benefit Liabilities**

Defined benefit liabilities recognized on the statements of financial position are as follows:

(in millions of Korean won)	December 31,		December 31,	
	2011	2010	2010	January 1, 2010
Present value of obligation	35,995	43,668	35,434	35,434
Fair value of plan assets <sup>1</sup>	(28,347)	(32,753)	(30,381)	(30,381)
<b>Liability in the statement of financial position</b>	<b>7,648</b>	<b>10,915</b>	<b>5,053</b>	<b>5,053</b>

<sup>1</sup> The fair value of plan assets includes ₩ 52 million in deposits to the National Pension Fund (Dec. 2010: ₩ 54 million; Jan. 2010: ₩ 55 million).

The amounts recognized in the comprehensive income statements are as follows:

(in millions of Korean won)	2011	2010
Current service cost	15,416	13,513
Interest cost	2,478	2,714
Expected return on plan assets	(1,465)	(1,734)
Curtailment of plan	282	-
<b>Total, included in employee benefit expenses</b>	<b>16,711</b>	<b>14,493</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Actuarial gains and losses recognized as other comprehensive income are as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
Cost of sales	5,705	4,804
Selling and administrative expenses	11,006	9,689
<b>Total</b>	<b>16,711</b>	<b>14,493</b>

Actual return of plan assets was ₩ 1,222 million (2010: ₩ 1,388 million).

Changes in the carrying amount of defined benefit obligations are as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
<b>Beginning balance</b>	<b>32,753</b>	<b>30,381</b>
Expected return on plan assets	1,465	1,734
Profit from settlements(Curtailment) of plan	265	-
Actuarial gains and losses	(508)	(346)
Employer contribution	9,592	9,500
Benefit paid	(4,494)	(8,517)
Curtailment of plan	(154)	-
Settlements of plan	(10,576)	-
Exchange differences	4	1
<b>Ending balance</b>	<b>28,347</b>	<b>32,753</b>

The movements in the fair value of plan assets are as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
<b>Beginning balance</b>	<b>43,668</b>	<b>35,434</b>
Business combination	529	-
Transfer in	187	-
Current service cost	15,416	13,513
Interest income	2,478	2,714
Profit from settlements(Curtailment) of plan	547	-
Actuarial gains and losses	(479)	6,222
Benefit paid	(6,083)	(14,203)
Curtailment of plan	(279)	-
Settlements of plan	(19,967)	-
Exchange differences	(22)	(12)
<b>Ending balance</b>	<b>35,995</b>	<b>43,668</b>

Actuarial gains and losses recognized as other comprehensive income are as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
Before income tax effect	(29)	(6,568)
Income tax effect	151	1,445
After income tax effect	122	(5,123)

As of December 31, 2011, ₩(-)5,001 million (December 31, 2010: ₩(-)5,123 million; January 1, 2010: nil) of accumulated actuarial losses are included in other comprehensive income.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

The principal actuarial assumptions used are as follows:

<i>(in millions of Korean won)</i>	December 31, 2011		December 31, 2010		January 31, 2010	
	Amount	Proportion	Amount	Proportion	Amount	Proportion
Discount rate	4.98%~5.34%		5.34%~5.64%		6.57%~6.62%	
Expected return of plan assets	4.90%~4.90%		4.16%~4.90%		2.87%~5.63%	
Future salary increase	2.33%~3.00%		2.33%~5.00%		2.37%~4.00%	

The sensitivity of the overall pension liability to changes in the weighted principal assumptions as follows:

<i>(in millions of Korean won)</i>	December 31, 2011	
	1% increase	1% decrease
Changes in discount rate		
Changes in defined benefit liabilities	(1,220)	1,367

Plan assets consist of :

<i>(in millions of Korean won)</i>	December 31, 2011		December 31, 2010		January 1, 2010	
	Amount	Proportion	Amount	Proportion	Amount	Proportion
Time deposits	28,295	99.82%	32,699	99.84%	30,326	99.82%
National pension fund	52	0.18%	54	0.16%	55	0.18%
<b>Total</b>	<b>28,347</b>	<b>100.00%</b>	<b>32,753</b>	<b>100.00%</b>	<b>30,381</b>	<b>100.00%</b>

The Company management estimates plan assets to be paid in 2012 to be ₩ 15,000 millions.

Adjustments for the differences between initial assumptions and actual figures are as follows:

<i>(in millions of Korean won)</i>	December 31, 2011		December 31, 2010		January 1, 2010	
	Amount	Proportion	Amount	Proportion	Amount	Proportion
Present value of defined benefit liability	35,995		43,668		35,434	
Fair value of plan assets	(28,347)		(32,753)		(30,381)	
Deficit of the funded plans	7,648		10,915		5,053	
Defined benefit liability adjustments	1,187		2,801		-	
Defined benefit asset adjustments	(243)		(346)		-	

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**20. Deferred Income Tax**

The analysis of deferred tax assets and deferred tax liabilities is as follows:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	December 31, 2009
Deferred tax assets			
Deferred tax asset to be recovered after more than 12 months	28,689	18,685	11,128
Deferred tax asset to be recovered within 12 months	12,867	17,118	16,728
Deferred tax liabilities			
Deferred tax liability to be recovered after more than 12 months	(490,003)	(475,477)	(388,212)
Deferred tax liability to be recovered within 12 months	(2,420)	(3,409)	(3,378)
Deferred tax assets(liabilities), net	<u>(450,867)</u>	<u>(443,083)</u>	<u>(363,734)</u>

The gross movements on the deferred income tax account are as follows:

<i>(in millions of Korean won)</i>	2011	2010
Beginning balance	(443,083)	(363,734)
Income statement charge	(18,776)	(3,049)
Tax charge/(credit) relating to components of other comprehensive income	9,599	(79,363)
Tax charged/(credited) directly to equity	151	1,445
Acquisition of subsidiary	889	-
Exchange differences	353	1,618
Ending balance	<u>(450,867)</u>	<u>(443,083)</u>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Changes in the temporary differences and related deferred tax assets and liabilities are as follows:

	2011						
	January 1, 2011	Income statement	Other comprehensive income	Retained earnings	Acquisition of subsidiary	Currency translation differences	December 31, 2011
<i>(in millions of Korean won)</i>							
Deferred tax liabilities	(333,148)	-	10,650	-	-	-	(322,498)
Gain on valuation of available-for-sale	(86,850)	(5,134)	-	-	(3,185)	502	(94,667)
Revaluation of land	(19,654)	(1,962)	-	-	-	-	(21,616)
Advanced depreciation provision	(7,405)	(5,507)	-	-	-	-	(12,912)
Depreciation	(5,684)	(1,249)	-	-	-	-	(6,933)
Retirement Deposits	(2,339)	(1,049)	-	-	-	-	(3,388)
Reserve for research and development	(23,835)	(2,273)	-	-	(5,153)	816	(30,445)
Others	(478,915)	(17,174)	10,650	-	(8,338)	1,318	(492,459)
Deferred tax assets	8,485	1,561	-	151	180	(6)	10,371
Accrual for retirement and severance benefits	5,373	(85)	-	-	-	-	5,288
Provision for sales returns	4,074	733	-	-	-	(18)	4,789
Bad debt expense	1,758	(400)	-	-	-	-	1,358
Leased Assets	3,495	(2,236)	-	-	-	-	1,259
Prepaid expense	12,647	(1,176)	(1,051)	-	9,047	(941)	18,527
Others	35,832	(1,603)	(1,051)	151	9,227	(965)	41,592
<b>Total</b>	<b>(443,083)</b>	<b>(18,776)</b>	<b>9,599</b>	<b>151</b>	<b>889</b>	<b>353</b>	<b>(450,867)</b>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

	2010						
	January 1, 2011	Income statement	Other compre hensive income	Retained earnings	Acquisiti on of subsidiary	Currency translation differences	December 31, 2011
<i>(in millions of Korean won)</i>							
Deferred tax liabilities Gain on valuation of available-for- sale	(253,184)	-	(79,964)	-	-	-	(333,148)
Revaluation of land	(86,902)	65	-	-	-	(13)	(86,850)
Advanced depreciation provision	(19,654)	-	-	-	-	-	(19,654)
Depreciation	(4,295)	(3,110)	-	-	-	-	(7,405)
Retirement Deposits	(3,429)	(2,255)	-	-	-	-	(5,684)
Reserve for research and development	(1,870)	(469)	-	-	-	-	(2,339)
Others	(22,830)	(2,579)	-	-	-	1,574	(23,835)
Deferred tax assets	(392,164)	(8,348)	(79,964)	-	-	1,561	(478,915)
Accrual for retirement and severance benefits	5,343	1,697	-	1,445	-	-	8,485
Provision for sales returns	3,774	1,599	-	-	-	-	5,373
Bad debt expense	4,572	(500)	-	-	-	2	4,074
Leased Assets	528	1,230	-	-	-	-	1,758
Prepaid expense	4,756	(1,261)	-	-	-	-	3,495
Others	9,458	2,534	601	-	-	55	12,647
	28,431	5,299	601	1,445	-	57	35,832
<b>Total</b>	<b>(363,734)</b>	<b>(3,049)</b>	<b>(79,363)</b>	<b>1,445</b>	<b>-</b>	<b>1,618</b>	<b>(443,083)</b>

Temporary differences not recognized as deferred tax assets:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Impairment loss on available-for- sale financial assets	1,625	1,625	1,625
Investments in subsidiaries and associates	226,441	163,706	142,731
Others	-	1,577	1,614

Deductible temporary differences from impairment loss on available-for-sale financial assets and equity method investments have not been recognized as deferred tax assets as they were determined to be not realizable in the near future.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Temporary differences not recognized as deferred tax liabilities

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Investments in subsidiaries and associates	84,033	77,633	82,522

Deductible temporary differences from equity method investments have not been recognized as deferred tax assets as it was determined to be not sale in the near future.

**21. Provisions**

Changes in the carrying amount of provisions are as follows:

<i>(in millions of Korean won)</i>	2011	2010
Beginning balance	22,852	15,622
Increase(decrease)	1,077	7,230
Ending balance	23,929	22,852

Sales return provisions have been accrued for the estimated sales return determined based on historical experience.

**22. Capital stock**

**Common Stock**

The Company is authorized to issue 3 million shares of common stock with a par value of ₩5,000 per share. As of December 31, 2011, 1,421,400 shares of common stock have been issued.  
 Capital

**Capital Adjustments**

As of December 31, 2011, the Company purchased 14,000 shares of treasury stock for ₩6,248 million in order to stabilize stock market and fulfill listing requirements. The Company intends to sell these treasury shares in the future depending on the market situation.

**23. Accumulated Other Comprehensive Income**

Accumulated other comprehensive income consists of:

<i>(in millions of Korean won)</i>	December 31, 2011	December 31, 2010	January 1, 2010
Change in value of available-for-sale financial assets	1,010,137	1,181,160	897,655
Share of other comprehensive income of associates	1,689	(1,904)	(10)
Cash flow hedge	(1,622)	(5,562)	(3,434)
Cumulative effect of Foreign Currency Translation	(21,678)	(6,612)	-
	988,526	1,167,082	894,211

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Changes in accumulated other comprehensive income for the year ended December 31, 2011, are as follows:

(in millions of Korean won)	2011			
	Beginning	Increase (Decrease)	Reclassification to profit or loss	Ending
Change in value of available-for-sale financial assets	1,181,160	(170,769)	(254)	1,010,137
Share of other comprehensive income of associates	(1,905)	3,615	(21)	1,689
Cash flow hedge	(5,562)	3,690	250	(1,622)
Cumulative Effect of Foreign Currency Translation	(6,612)	(15,066)	-	(21,678)
	<u>1,167,081</u>	<u>(178,530)</u>	<u>(25)</u>	<u>988,526</u>

(in millions of Korean won)	2010			
	Beginning	Increase (Decrease)	Reclassification to profit or loss	Ending
Change in value of available-for-sale financial assets	897,655	283,549	(44)	1,181,160
Share of other comprehensive income of associates	(10)	(1,895)	-	(1,904)
Cash flow hedge	(3,434)	(2,128)	-	(5,562)
Cumulative Effect of Foreign Currency Translation	-	(6,612)	-	(6,612)
	<u>894,211</u>	<u>272,914</u>	<u>(44)</u>	<u>1,167,082</u>

Changes in accumulated other comprehensive income represent net of tax effect amounts.

**24. Retained Earnings**

Details of retained earnings are as follows:

(in millions of Korean won)	December 31, 2011	December 31, 2010	January 1, 2010
Legal reserve <sup>1</sup>	3,554	3,636	3,554
Discretionary reserve <sup>2</sup>	1,470,900	1,335,400	1,244,900
Unappropriated retained earnings	62,653	105,903	112,998
<b>Total</b>	<u>1,537,107</u>	<u>1,444,939</u>	<u>1,361,452</u>

<sup>1</sup>The Commercial Code of the Republic of Korea requires the Company to appropriate, as a legal reserve, an amount equal to a minimum of 10% of cash dividends paid, until such reserve equals 50% of its issued capital stock. The reserve is not available for the payment of cash dividends, but may be transferred to capital stock, or used to reduce accumulated deficit, if any, with the ratification of the Company's majority shareholders. However, according to the revised regulation as of December 27, 2007, this reserve has been revised to voluntary reserve. According to the special tax treatment control law, the Company has additionally ratification of the Company's majority shareholders.

<sup>2</sup>The Company accounted for reserve for improvement of financial structure as a legal reserve in accordance with the regulations regarding securities issuance and disclosure until 2006. This reserve was not available for dividends, but may be transferred to capital stock, or used to reduce accumulated deficit, if any, with the ratification of the Company's majority shareholders. However, according to the revised regulation as of December 27, 2007, this reserve has been revised to voluntary reserve. According to the special tax treatment control law, the Company has additionally

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

reserved research and development that is deducted by adjustment report when the Company appropriates retained earnings. The reserve reversed by the special tax treatment control law can be distributed as dividend.

**25. Commitments and Contingencies**

The end of reporting period, the Company is a plaintiff in various lawsuits claiming damages totaling ₩ 3,477 million and the Company is a defendant in various lawsuits with damage claims totaling ₩ 50,985 million. The management believes that the ultimate resolutions of other legal actions will not have a material effect on the financial position or operations of the Company.

The Company has various forms of credit facility commitments with financial institutions end of reporting period, as follows:

	<i>(in millions of Korean won, foreign currencies in thousands)</i>			
	December 31, 2011	December 31, 2010	January 1, 2010	
Overdraft	Woori Bank and others	58,868	57,294	27,756
Buyer's loan	Hana Bank Industrial Bank of Korea and others	140,000	140,000	-
Buyer's credit	Woori Bank and others	6,000	6,000	240,000
Letter of credit	State Bank of India and others	20,000	20,000	20,100
Letter of credit (Local)	Korea Exchange Bank	1,283	1,017	251
Discount of bill	Hana Bank Woori Bank	1,500	1,500	1,500
Import issuance	Korea Exchange Bank	3,000 2,600	3,000 2,600	3,000 2,600
L/C		2,000	2,000	-
General loan	Hana Bank and others	-	-	20,612

Technical assistance agreements of the Company with Wilkes & Associates and others at the end of reporting period are as follows:

Contractor	Description	Fee	Maturity
Wilkes & Associates, Inc.	Prime production	1.00% of Net Sales	June 2006 (Renewal in progress)
	SPIC ice cream production	1.15% of Net Sales	Oct. 2015
	Cracker and snack production	0.75% of Net Sales	Feb. 2014
	Snack (Cheetos) production	3.00% of Sales	Dec. 2013
	Snack (Sun chips)production	3.00% of Sales	Dec. 2013
PepsiCo, Inc.	Ice cream production	1.15~3.00% of Net Sales	June, 2013
The Hershey Company	Snack (Tacos) production	1.30% of Net Sales	March 2019
Miles Willard Technologies			

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

The Company entered into technical assistance and exchange agreement with Lotte Japan Co. for 10 years, from April 1, 2004 to March 31, 2014. According to the agreement, the Company has to pay for the use of trademarks and patents and the cost incurred for the current year amounts to ₩ 315 million.

Joint ventures of the Company the end of reporting period are as follows:

<i>(in millions of Korean won)</i>				
<b>Company</b>	<b>Location</b>	<b>Other</b>	<b>Amount</b>	
Lotte China Foods Co., Ltd.	China	Lotte Holdings Co. and others	47,423	
Lotte Philippines Co., Inc.	Philippines	Lotte Holdings Co. and others	664	
Lotte Confectionery Piliipinas Co.	Philippines	Lotte Holdings Co.	2,643	
PT, Lotte Indonesia	Indonesia	Lotte Holdings Co. and others	3,682	
Lotte Vietnam Co., Ltd.	Vietnam	Lotte Holdings Co. and others	7,008	
Lotte Packaging (Beijing) Co., Ltd.	China	Lotte Holdings Co.	4,442	
Lotte Europe Holdings B.V.	Netherlands	Lotte Holdings Co.	153,963	
Lotte Taiwan Co., Ltd.	Taiwan	Lotte Holdings Co.	6,672	
Lotte Qingdao Foods Co., Ltd.	China	Lotte (China) Investment Co., Ltd.	16,769	
Lotte Ice (Shandong) Co., Ltd.	China	Lotte (China) Investment Co., Ltd.	8,466	
Lotte Confectionery Holdings B.V.	Netherlands	Lotte Holdings Co.	90,462	
PT, Lotte Trade And Distribution	Indonesia	Lotte Holdings Co.	4,269	
Lotte Malaysia Sdn. Bhd	Malaysia	Lotte Holdings Co.	2,836	
			<u>349,299</u>	

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**26. Selling and Administrative Expenses**

Selling and administrative expenses are as follows:

<i>(in millions of Korean won)</i>	2011	2010
Salaries	142,278	145,518
Severance benefits	10,624	10,014
Employee fringe benefits	26,488	26,053
Training expenses	1,872	2,421
Travel expenses	3,369	3,106
Vehicles maintenance expenses	11,683	10,702
Insurance premium	1,924	1,615
Taxes and dues	5,423	9,186
Entertainment	484	497
Supplies expenses	3,938	4,070
Publication Expenses	330	219
Communications	1,981	1,776
Water & utilities	6,481	9,145
Repairs and maintenance	4,970	5,370
Rental expense	20,268	16,043
Depreciation	27,804	24,600
Amortization	927	1,358
Commission expense	141,911	131,788
Advertising expenses	48,085	35,609
Samples expenses	132	131
Sales commission	31,429	25,554
Sales promotional expense	22,322	16,101
Bad debts expense	1,324	153
Other	25,104	22,515
	<u>541,151</u>	<u>503,544</u>

**27. Other Operating Income**

Other operating income consists of:

<i>(in millions of Korean won)</i>	2011	2010
Foreign exchange gain	2,242	924
Gain on foreign currency translation	133	248
Gain on disposal of property, plant and equipment	2,836	845
Gain on disposal of intangible assets	3	-
Reversal of allowance for doubtful accounts	23	2
Miscellaneous revenue	14,195	11,606
	<u>19,432</u>	<u>13,625</u>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**28. Other Operating Expenses**

Other operating expenses consist of:

	2011	2010
<i>(in millions of Korean won)</i>		
Foreign exchange loss	3,636	984
Loss on foreign currency translation	114	385
Loss on disposal of property, plant and equipment	227	407
Impairment loss of property, plant and equipment	393	-
Donations	4,147	4,356
Other bad debts expenses	163	-
Miscellaneous expense	4,709	4,873
	<u>13,389</u>	<u>11,005</u>

**29. Expenses by Nature**

Expenses that are recorded by nature as cost of sales, selling and administrative expenses and other operating expenses consist of:

	2011	2010
<i>(in millions of Korean won)</i>		
Changes in inventories of finished goods, merchandises and work in progress	(14,732)	(10,357)
Raw materials and consumables used	683,233	563,272
Purchase of merchandise	257,021	231,894
Employee benefit expenses	232,057	229,437
Advertising expenses	48,085	35,609
Rental expense	36,598	28,343
Commission expense	201,221	179,977
Depreciation	69,168	55,731
Amortization	930	1,358
Sales commission	31,429	25,554
Sales promotional expense	22,322	16,101
Other expenses	127,000	136,132
	<u>1,694,332</u>	<u>1,493,051</u>

**30. Classification of Operating Income (Loss)**

(1) Material items of operating income and expense

Operating income is calculated as gross profit net of selling and administrative expenses, other net income(loss), and other income and expenses (Notes 26, 27 and 28).

(2) Distinctions between the previous K-GAAP and the Korean IFRS

Under the former accounting standards, operating income(loss) was calculated as gross profit net of selling and administrative expenses. Under the Korean IFRS, operating income(loss) was calculated as gross profit net of selling and administrative expenses, other net income(loss), and other income and expenses.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

(3) Calculation of operating income

	2011	2010
<i>(in millions of Korean won)</i>		
Total revenue	714,367	672,179
Selling and administrative expenses	541,151	503,544
Other operating Income		
Foreign exchange gain	2,242	924
Gain on foreign currency translation	133	248
Gain on disposal of property, plant and equipment	2,836	845
Gain on disposal of intangible assets	3	-
Reversal of allowance for doubtful accounts	23	2
Miscellaneous revenue	14,195	11,606
Subtotal	19,432	13,625
Other operating expenses		
Foreign exchange loss	3,636	984
Loss on foreign currency translation	114	385
Loss on disposal of property, plant and equipment	227	407
Impairment loss of property, plant and equipment	393	-
Donations	4,147	4,356
Other bad debt expenses	163	-
Miscellaneous expense	4,710	4,873
Subtotal	13,390	11,005
Operating income	179,258	171,255

**31. Financial Income**

Financial income consists of:

<i>(in millions of Korean won)</i>	2011	2010
Interest income	8,045	6,732
Dividend income	6,536	5,370
Foreign exchange gain	525	2
Gain on foreign currency translation	1,611	1,931
Gain on disposal of available-for-sale financial assets	402	57
Gain on valuation of hedging derivatives	17,390	41,344
Gain on transactions of hedging derivatives	1,811	-
Gain on disposal of investments in subsidiary	13,659	-
	49,979	55,436

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**32. Financial Costs**

Financial costs consist of:

	2011	2010
<i>(in millions of Korean won)</i>		
Interest expenses	21,148	19,766
Foreign exchange loss	695	1,229
Loss on foreign currency translation	18,838	42,205
Other bad debt expenses	-	31
Loss on disposal of available-for-sale financial assets	-	41
Loss on valuation of hedging derivatives	-	214
Loss on transaction of hedging derivatives	275	754
Loss on disposal of investments in associates	2,146	-
	<u>43,102</u>	<u>64,240</u>

**33. Income Tax**

Income tax expense consists of:

	2011	2010
<i>(in millions of Korean won)</i>		
Current tax:		
Current tax on profits for the year	36,414	35,477
Adjustments in respect of prior years	(18)	(1,417)
Total current tax	36,396	34,060
Deferred tax (Note 20):		
Origination and reversal of temporary differences	10,395	4,195
Impact of change in Korean tax rate	10,563	-
Currency translation differences	(115)	(1,604)
Total deferred tax	20,843	2,591
Income tax expense	<u>57,239</u>	<u>36,651</u>

The tax on the Company's profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the Company entities as follows:

	2011	2010
<i>(in millions of Korean won)</i>		
Profit before tax	157,601	130,725
Tax calculated based on applicable tax rate	49,684	41,398
Tax effects of:		
Income not subject to tax	202	94
Expenses not deductible for tax purposes	(462)	(377)
Tax credit	(1,633)	(972)
Tax refund	(18)	(1,417)
Others	(1,097)	(2,074)
Re-measurement of deferred tax – change in the Korean tax rate	10,563	-
Tax charge	<u>57,239</u>	<u>36,651</u>

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

The income tax (charged)/credited directly to equity is as follows:

	December 31, 2011		December 31, 2010	
	Before tax	Tax (charge) credit	Before tax	Tax (charge) credit
(in millions of Korean won)				
Gain(loss) on valuation of available-for-sale financial assets	(181,673)	10,650	(171,023)	363,469
Cash flow hedge	4,990	(1,051)	3,939	(2,728)
Actuarial profit (loss) on retirement benefit obligations	(186)	308	122	(6,567)
	<u>(176,869)</u>	<u>9,907</u>	<u>(166,962)</u>	<u>354,174</u>
				<u>(77,918)</u>
				<u>276,256</u>

During the year, as a result of the change in the Korean corporation tax rate from 22% to 24.2% that was substantively enacted on December 31, 2011, and that will be effective from January 1, 2012, the relevant deferred tax balances have been re-measured. Deferred tax expected to be reversed after December 31, 2011, had been measured using the effective rate of 24.2% that would apply for the future period.

**34. Earnings per Share**

**Basic earnings per share**

	2011	2010
(in Korean won)		
Parent interest in net income	97,675,688,016	93,537,140,887
Weighted average number of common stock outstanding <sup>1</sup>	1,407,400	1,407,400
Basic earnings per share	69,402	66,461

<sup>1</sup> Calculation of the weighted average number of common stock outstanding

	Number of Shares	Weighted Average	Weighted Number of Shares
Carryover	1,421,400	365	518,811,000
Treasury stock	(14,000)	365	(5,110,000)
	<u>1,407,400</u>		<u>513,701,000</u>

Weighted average number of common stock: 513,701,000 / 365 = 1,407,400

**Diluted earnings per share**

As there are no diluted securities outstanding diluted earnings per share is identical to basic earnings per share.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

**35. Dividends**

Dividends paid by Parent Company in 2011 and 2010 are ₩ 5,630 million (₩ 4,000 per share) and ₩ 4,926 million (₩ 3,500 per share, respectively). Dividends per share and gross dividends are ₩ 4,000 and ₩ 5,630 million for 2011 will be proposed at the general meeting of shareholders on March 23, 2012. The Company financial statements for this fiscal year do not reflect these dividends payable.

**36. Related Party Transactions**

Related parties as of December 31, 2011, are as follows:

Relationship	Related parties
Ultimate parent company	-
Investors with significant influence	-
Associates	BIBICA CORPORATION, Lotte (China) Investment Co., Ltd., Lotte China Foods Co., Ltd., Lotte Packaging(Beijing) Co., Ltd., Lotte Europe Holdings B.V., Lotte Vietnam Co., Ltd., PT, Lotte Trade And Distribution, Lotte Taiwan Co., Ltd., Lotte Confectionery Pilipinas Co., Lotte Malaysia Sdn. Bhd, Lotte Giants Co., Ltd.
Joint venture	LH Foods Co., Ltd.
Other related parties	Lotte Aluminium Co., Ltd., Hotel Lotte Co., Ltd, Daehong Communications Inc., Lotte Engineering & Construction Co., Ltd., Lotte Midopa Co., Ltd, Lotteria Co., Ltd., Lotte Shopping Co., Ltd., Lotte Data Communication Company, Lotte Trading Co., Ltd., Lotte Logistics Co., Ltd, Lotte.com Inc., Korea Seven Co., Ltd, Lotte Station B/D. Co., Lotte Samkang Co., Ltd., Lotte Ham Co., Ltd, Lotte Chilsung Beverage Co., Ltd., Canon Korea Business Solutions Inc., Lotte Card Co., Ltd., PT, Lotte Indonesia, ZAO Lotte Rus, Lotte KF Rus LLC, Lotte Shopping Rus LLC, Confectionery Rus Kaluga LLC, Lotte Shanghai Foods., Ltd., others.

Significant transactions, which occurred in the normal course of business with related companies, and their related balances are as follows:

	(in millions of Korean won)		December 31, 2011	
	2011			
Associates	Sales	Purchases	Receivables	Payables
Other related parties	16,772	5,566	4,074	1,494
Total	230,424	290,204	27,374	65,554
	247,196	295,770	31,448	67,048
	<b>(in millions of Korean won)</b>			
	<b>2010</b>		<b>December 31, 2010</b>	
Associates	Sales	Purchases	Receivables	Payables
Other related parties	16,526	4,122	3,689	1,002
Total	180,335	275,338	28,237	59,240
	196,861	279,460	31,926	60,242

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Compensation for key management consists of:

<i>(in millions of Korean won)</i>	<b>2011</b>	<b>2010</b>
Short-term salaries	6,488	6,172
Post-retirement benefits	1,593	1,666
	<u>8,081</u>	<u>7,838</u>

Key management refers to the registered directors and non-registered directors who have the authority and responsibilities for planning, operation and control of the business of the Company.

As of December 31, 2011, the Company's provides guarantees to related parties are as follows: (in thousands of foreign currency)

<b>Guarantee beneficiary</b>	<b>Amount of guarantee</b>	<b>Financial institution</b>
Lotte Taiwan Co., Ltd.	JPY 200,000	Lotte Holdings Co., Ltd.
Lotte Confectionery Rus Kaluga LLC	USD 19,500	Korea Exchange Bank
Lotte (CHINA) Investment Co., Ltd.	CNY 84,500	Korea Exchange Bank
Lotte China Foods Co., Ltd.	JPY 565,000	Mizuho Corporate Bank
Lotte China Foods Co., Ltd.	JPY 695,000	The Bank of Tokyo-Mitsubishi UFJ
Lotte China Foods Co., Ltd.	JPY 300,000	Sumitomo Bank

**37. Transition to the Korean IFRS**

**37.1 First-time Adoption of the Korean IFRS**

The Company's transition date to the Korean IFRS is January 1, 2010, and adoption date is January 1, 2011.

In preparing Company financial statements in accordance with the Korean IFRS 1101(First-time Adoption of Korean International Financial Reporting Standards), the Company has applied the mandatory exceptions and certain optional exemptions allowed by the Korean IFRS.

**37.2 Exemption Options under Korean IFRS 1101**

The Company elected to apply the following optional exemptions from full retrospective application.

*(a) Business combinations*

The Company elected to apply the exemption for business combinations allowed under Korean IFRS 1101 and has not retrospectively applied Korean IFRS 1103 to past business combinations that occurred before the transition date.

*(b) Fair value as deemed cost*

The Company elected to use the revaluations of certain property, plant and equipment prior to the date of transition to the Korean IFRS as deemed cost at the transition date.

*(c) Investment on subsidiaries, joint ventures, associates*

The investment costs on subsidiaries, joint ventures, associates are book value noted by past

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

financial policy on the date of January 1, 2010 (transition date).

**37.3 Reconciliations between the previous K-GAAP to the Korean IFRS**

*(a) Effects on the financial position and financial performance*

Effects of the Korean IFRS adoption on the Company's total assets, liabilities and equity as of January 1, 2010, the date of Korean IFRS transition, are as follows:

<i>(in millions of Korean won)</i>	<b>Total assets</b>	<b>Total liabilities</b>	<b>Total equity</b>
Reported amount under K-GAAP	3,714,430	1,141,995	2,572,435
Adjustments :			
Changes in depreciation method of property, plant and equipment <sup>1</sup>	36,000	-	36,000
Employee benefit expense <sup>2</sup>	661	14,194	(13,533)
Measured at fair value deposits	(25)	(4)	(21)
Recording of loans for discounting of trade receivables <sup>3</sup>	1,904	1,891	13
Revenue recognition and allowance for doubtful accounts	1,171	-	1,171
Inventories <sup>4</sup>	(922)	-	(922)
Changes in scope of equity method investments <sup>5</sup>	(320,045)	8,380	(328,425)
Reversal of impairment loss on Goodwill	12,441	-	12,441
Changes in scope of subsidiaries	74,851	(3,161)	78,012
Income tax effect	(18,317)	(5,663)	(12,654)
Total adjustments	(212,281)	15,637	(227,918)
Adjusted amount under Korean IFRS	3,502,149	1,157,632	2,344,517

<sup>1</sup> Book value adjustment from the change of property, plant, equipment depreciation method.

<sup>2</sup> The change of defined benefit liability and the estimation of allowances for paid holiday followed by actuarial assessment.

<sup>3</sup> Estimation of borrowings among discounted trade receivables not matured as of the date of January 1, 2010.

<sup>4</sup> The adjustment of inventory book value from the change of property, plant, equipment depreciation method and employee salary.

<sup>5</sup> The adjustment from the change of equity method companies upon adoption of Korean-IFRS.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Effects of the Korean IFRS adoption on the Company's total assets, liabilities, equity as of December 31, 2010 are as follows:

<i>(in millions of Korean won)</i>	<b>Total assets</b>	<b>Total liabilities</b>	<b>Total equity</b>
Reported amount under K-GAAP	4,010,201	1,292,182	2,718,019
Adjustments :			
Changes in depreciation method of property, plant and equipment <sup>1</sup>	49,858	-	49,858
Employee benefit expense <sup>2</sup>	661	18,427	(17,766)
Measured at fair value deposits	(25)	(91)	66
Recording of loans for discounting of trade receivables <sup>3</sup>	883	883	-
Revenue recognition and allowance for doubtful accounts	1,896	-	1,896
Inventories <sup>4</sup>	(1,497)	-	(1,497)
Changes in scope of equity method investments <sup>5</sup>	34,182	2,262	31,920
Reversal of negative goodwill	10,467	-	10,467
Cancellation of goodwill and negative goodwill	(2,223)	-	(2,223)
Cancellation of amortization of Goodwill	10,578	-	10,578
Changes in scope of subsidiaries	(108,540)	(75,299)	(33,241)
Income tax effect	(14,561)	61,576	(76,137)
Total adjustments	(18,321)	7,758	(26,079)
Adjusted amount under Korean IFRS	3,991,880	1,299,940	2,691,940

<sup>1</sup> Book value adjustment from the change of property, plant, equipment depreciation method.

<sup>2</sup> The change of defined benefit liability and the estimation of allowances for paid holiday followed by actuarial assessment.

<sup>3</sup> Estimation of borrowings among discounted trade receivables not matured as of the date of January 1, 2010.

<sup>4</sup> The adjustment of inventory book value from the change of property, plant, equipment depreciation method and employee salary.

<sup>5</sup> The adjustment from the change of equity method companies upon adoption of Korean-IFRS.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

Effects of the Korean IFRS adoption on the Company's profit and comprehensive income for the year ended December 31, 2010, are as follows:

<i>(in millions of Korean won)</i>	Net income	Comprehensive income
Reported amount under K-GAAP	136,879	160,507
Adjustments :		
Changes in depreciation method of property, plant and equipment <sup>1</sup>	13,858	13,858
Application of deemed cost on property, plant and equipment <sup>2</sup>	(279)	(20,420)
Employee benefit expense <sup>3</sup>	2,329	(2,795)
Measured at fair value deposits	87	87
Recording of loans for discounting of trade receivables <sup>4</sup>	(13)	(13)
Revenue recognition and allowance for doubtful accounts	725	725
Inventories <sup>5</sup>	(574)	(574)
Changes in scope of equity method investments <sup>6</sup>	(76,191)	185,497
Cancellation reversal of negative goodwill	(486)	(486)
Recording expenses origination costs of business combination	(1,783)	(1,783)
Cancellation of amortization of Goodwill	10,578	10,578
Changes in scope of subsidiaries	(159)	781
Income tax effect	9,103	9,103
Total adjustments:	<u>(42,805)</u>	<u>194,558</u>
Adjusted amount under Korean IFRS	<u>94,074</u>	<u>355,065</u>

<sup>1</sup> Book value adjustment from the change of property, plant, equipment depreciation method.

<sup>2</sup> The difference adjustment of gains and losses followed by application of deemed cost on the property, plant, equipment.

<sup>3</sup> The change of defined benefit liability and the estimation of allowances for paid holiday followed by actuarial assessment.

<sup>4</sup> The estimation of interest expense that occurs by borrowing trade on discounted trade receivables.

<sup>5</sup> The adjustment of inventory book value from the change of property, plant, equipment depreciation method and employee salary.

<sup>6</sup> The adjustment from the change of equity method companies upon adoption of Korean-IFRS.

*(b) Effects on the cash flows*

On adoption of the Korean IFRS, cash flows from interest received, interest paid, dividends received, and income taxes paid, which had not been separately presented, are presented separately on the face of the statement of cash flows. In order to accommodate the change, cash flows related to relevant income/expenses, assets/liabilities have been adjusted. The effects of the change in exchange rate on cash and cash equivalents in a foreign currency are presented separately from cash flows from operating, investing and financing activities.

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

Cash flows from operating and financing activities are adjusted due to certain transfers of trade receivables that were derecognized under the previous K-GAAP but are treated as collateralized borrowings under the Korean IFRS. In addition, other Korean IFRS transition effects are reflected on cash flows where they have effects on cash flows.

**38. Business combination**

The Company participated in paid-in capital increase of K.S. Sulemanji Esmalji & Sons (Private) Ltd. That is located in Pakistan. After that event, the gross share rate has become 69.45% and the gross paid-in capital amount has become ₩ 18,304 million. The Company is expecting an increase of market share in this market and cost reduction effect through economies of scale.

The ₩ 1,311 million goodwill from this acquisition is based on the synergy effect with companies related to K.S. Sulemanji Esmalji & Sons (Private) Ltd. in Pakistan. Those companies are in the same business and are customer-oriented.

The Company anticipates that the goodwill will not be admitted for the purpose of income tax calculation. The assets and liabilities recognized on the purchasing day were estimated by fair values. The amounts paid to K.S. Sulemanji Esmalji & Sons (Private) Ltd. and the amounts of assets and liabilities recognized on the purchasing day are as follows:

<i>(In millions of Korean won)</i>	
I. Consideration transferred	18,304
Paid-in capital increase(cash)	
II. Recognized amounts of identifiable assets acquired and liabilities assumed	
Cash and cash equivalents	18,908
Trade and other receivables	3,752
Inventories	3,384
Investment property	1,995
Property, plant and equipment	36,035
Intangible assets	50
Other assets	1,950
Trade and other payables	6,559
Borrowings	25,748
Retirement benefit obligations	529
Other liabilities	8,398
Non-controlling interest <sup>1</sup>	371
Total identifiable net assets	24,469
Percentage of ownership	69.45%
Amount of equity in net assets	16,993
III. Non-controlling interest	7,476
IV. Goodwill <sup>2</sup>	1,311

<sup>1</sup> Non-controlling interest for Kolson Industries (Private) Ltd. which is owned by K.S. Sulemanji Esmalji & Sons (Private) Ltd. on the day of purchasing.

<sup>2</sup> The ₩ 1,311 million goodwill from a business combination was from synergy effects among inter-businesses that originally existed.

Non-controlling interest was calculated applying non-controlling interest rate of 30.55% to the fair value of recognizable net assets.

Sales and loss amounts for K.S. Sulemanji Esmalji & Sons (Private) Ltd. are ₩ 53,729 million and

**Lotte Confectionery Co., Ltd. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**December 31, 2011 and 2010, and January 1, 2010**

---

₩ 1,886 million, respectively, and losses for non-controlling interest are ₩ 610 million for this period.

**39. Supplemental Cash Flow Information**

Significant transactions not affecting cash flows for the years ended December 31, 2011 and 2010, are as follows:

<i>(In millions of Korean won)</i>	<u>2011</u>	<u>2010</u>
Reclassification of construction in-progress to property, plant and equipment	58,592	105,841
Reclassification to current portion of debentures	289,358	153,568
Disposal of a subsidiary in return of equity securities	11,226	-