

**VIRGINIA TOBACCO SETTLEMENT FOUNDATION  
RICHMOND, VIRGINIA**

**REPORT ON AUDIT  
FOR THE YEAR ENDED  
JUNE 30, 2002**



## **AUDIT SUMMARY**

Our audit of the Virginia Tobacco Settlement Foundation for the period ended June 30, 2002, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- no matters involving the internal control and its operation that we consider material weaknesses; and
- no instances of noncompliance with applicable laws and regulations tested that are required to be reported.

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## FOUNDATION OVERVIEW

The Virginia Tobacco Settlement Foundation (the Foundation), created in 1999, receives annually 10 percent of Virginia's portion of funds from the Master Settlement Agreement with tobacco manufacturers. A Board of Trustees (Board), comprised of 23 members, governs and administers the Foundation. The Board establishes specific criteria and procedures for distributing money in the Fund. The Foundation uses its funding to finance efforts to restrict the use of tobacco products by minors through such means as educational awareness programs on the health effects of tobacco use on minors and enforcement of laws restricting the distribution of tobacco products to minors.

The Virginia Department of Health acts as the fiscal agent for the Foundation and provides fiscal and payroll services to the Foundation. The Foundation employs an executive and deputy director, a business manager, and eleven staff members. The staff includes five regional Grant Program Administrators. These Administrators are responsible for managing the program grants issued throughout the Commonwealth. During fiscal year 2002, the Foundation began a marketing campaign and implemented various tobacco use prevention programs to discourage tobacco use by minors.

In September 2001, the Board of Trustees approved members for its nine Regional Advisory Boards. The Regional Advisory Boards provide a local connection between the Foundation and communities throughout the Commonwealth. The Advisory Boards oversee the review process to select program grant recipients that receive funding to implement youth tobacco use prevention programs.

## FINANCIAL OPERATIONS

Below are the cash receipts and disbursements for the years ended June 30, 2001 and June 30, 2002.

	<u>June 30, 2001</u>	<u>June 30, 2002</u>
Revenue:		
Master settlement agreement	\$12,818,938	\$14,961,389
Interest	<u>1,351,171</u>	<u>1,296,185</u>
Total revenue:	<u>14,170,109</u>	<u>16,257,574</u>
Expenses:		
Payroll	331,294	761,867
Contractual services	794,371	14,279,698
Supplies and materials	4,518	64,019
Fixed assets	42,445	45,438
Miscellaneous	<u>17,411</u>	<u>99,053</u>
Total expenses	<u>1,190,039</u>	<u>15,250,075</u>

Net increase	12,980,070	1,007,499
Beginning cash balance	<u>16,970,587</u>	<u>29,950,657</u>
Ending cash balance	<u>\$29,950,657</u>	<u>\$30,958,156</u>

*Source: Commonwealth Accounting and Reporting System for the year ended June 30, 2001 and 2002.*

While expenses increased significantly from last year, the Foundation ended fiscal year 2002 with an increase in its cash balance. The Foundation must transfer \$15,514,648 of its cash balance to the state general fund by June 30, 2003 as a result of statewide revenue shortfalls and budget reductions. This amount represents cumulative unspent cash balances due to the delayed implementation of the Foundation's operations. The Foundation intends to transfer the funds in April 2003 when the Foundation receives its annual portion of the Master Settlement Agreement. The Foundation also plans to absorb this reduction through its marketing, program and research initiatives.

Contractual services include expenses for the marketing contract, research partnership agreements, and program grants awarded under various agreements. The Foundation's largest contractual service vendor is Work, Inc., which received almost \$7 million for marketing campaigns during fiscal year 2002. The next two largest contractual expenses are for research partnerships with the University of Virginia and Virginia Commonwealth University, which received \$2.5 million and \$2.6 million, respectively.

The Foundation continues to expect annual revenues around \$13.3 million. The Board has also approved budgets for the next two years to spend about \$20 million annually, which includes adjustments for operational expenses for the cash reduction. The Foundation intends to continue its efforts in marketing, tobacco use prevention programs, research, and enforcement to discourage minors from using tobacco products.

January 21, 2003

The Honorable Mark R. Warner  
Governor of Virginia  
State Capitol  
Richmond, Virginia

The Honorable Kevin G. Miller  
Chairman, Joint Legislative Audit  
and Review Commission  
General Assembly Building  
Richmond, Virginia

### INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Virginia Tobacco Settlement Foundation** (the Foundation) for the year ended June 30, 2002. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

#### Audit Objective, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of the Foundation's internal control, and test compliance with applicable laws and regulations.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Foundation's operations. We also tested transactions and performed such other auditing procedures as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Expenditures  
Revenues  
Contract Management

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Foundation's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Foundation's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

#### Audit Conclusions

We found that the Foundation properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Foundation records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted no matters involving internal control and its operation that we consider to be material weaknesses. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to financial operations may occur and not be detected promptly by employees in the normal course of performing their duties.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

#### EXIT CONFERENCE

We discussed this report with management at an exit conference on February 3, 2003.

AUDITOR OF PUBLIC ACCOUNTS

MAM/cam  
cam: 45

VIRGINIA TOBACCO SETTLEMENT FOUNDATION  
Richmond, Virginia

Martha Kilgore, Executive Director

BOARD OF TRUSTEES  
As of June 30, 2002

Steven J. Danish, Chairman

John M. O'Bannon III, Vice Chairman

John Andrako  
Walter H. Bass III  
Kevin Bolling  
George E. Broman, Jr  
Curtis Coleburn  
Rebecca Darby  
Dennis DeSilvey  
Rickie E. Fulcher  
Emmett W. Hanger

Barbara D. Hughes  
Patrick Hughes  
William R. Janis  
Robert Leek  
V. Carole Loughheed  
James Lund McDaniel  
Becky Hart Minor  
Robert B. Stroube  
John Watkins

Percy Wootton