TOBACCO SETTLEMENT AUTHORITY

(A Component Unit of the State of Washington)

Independent Auditor's Report

and Financial Statements

with Supplemental Information

June 30, 2009 and 2008

CONTENTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Tobacco Settlement Authority

We have audited the accompanying statements of net deficit of the Tobacco Settlement Authority (the Authority), at June 30, 2009 and 2008 and the related statements of revenues, expenses, and changes in net deficit and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2009 and 2008, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying Management's Discussion and Analysis on pages 2 through 9 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Authority's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental information on pages 20 through 22 is presented for purposes of additional analysis and is not a required part of the financial statements. The supplemental information, which is the responsibility of the Authority's management, has been subjected to the procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Moss Adams LLP

Seattle, Washington
December 2, 2009

As management of the Tobacco Settlement Authority (the "Authority"), we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the years ended June 30, 2009 and 2008. This overview and analysis is required by accounting principles generally accepted in the United States of America Generally Accepted Accounting Principles ("GAAP") for governmental entities.

FINANCIAL HIGHLIGHTS

Tobacco Settlement Revenues ("TSRs") of $55 million and $54.5 million were recognized as revenue in the fiscal years ended June 30, 2009 and 2008, respectively. In accordance with GAAP*,* $24.4 million TSRs applicable to cigarette sales between January 1, 2009 and June 30, 2009 were recorded as accrued TSR Receivable as of June 30, 2009 while $24.0 million TSRs applicable to cigarette sales between January 1, 2008 and June 30, 2008 were recorded as accrued TSRs Receivable as of June 30, 2008. No additional bonds were issued during 2009.

During the fiscal year ended June 30, 2009:

- Total assets decreased by $.9 million to $86.2 million due to the net decrease in the cash, equivalents and investments ($1 million) and unamortized bond issuance costs ($.2 million), partially offset by an increase in the TSRs receivable ($.4 million). Investments decreased by $45.7 million as the reserve agreement was liquidated and funds were placed in money markets, increasing the cash equivalents by $44.6 million, and leaving a net decrease of $1 million due to the use of available liquid assets for bond payments.

- At year-end, the Authority had total net bonds payable of $432.1 million, net of discounts. This represents a net decrease of $25.8 million, or 5.6%, resulting from principal payments on bonds.

- At June 30, 2009, the Authority had a reduction of $25 million (6.7%) in the Net Deficit over that of the previous fiscal year end.

- Interest income decreased by $1.4 million as the reserve funds were invested in short term money market funds with yields less than that of the investment agreement terminated due to provider default.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements consist of three parts: Management's Discussion and Analysis, the basic financial statements and the notes to the financial statements. The financial statements are presented in a manner similar to that of a private business, using the economic resources measurement focus and the accrual basis of accounting. The financial statements report information for all Authority operations. The Statement of Net Deficit includes all of the Authority's assets and liabilities. All of the revenues and expenses of the Authority are accounted for in the Statements of Revenues, Expenses and Changes in Net Deficits.

In addition, program financial statements are presented as supplemental schedules. These statements separate the financial statements into the Restricted Bond Fund and General Operating Fund.

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Authority has applied all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989 (unless they conflict with or contradict GASB pronouncements): Statements and Interpretations of the Financial Accounting Standards Board, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures. All program and general operating funds of the Authority are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. The operating statements for all funds present increases (e.g., revenues) and decreases (e.g., expenses) in net fund equity. These funds utilize the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Management believes that the present value amount of TSRs that will be collected over time is $348,358,849, an amount equal to the net deficit. However, accounting principles generally accepted in the United States of America do not allow these future revenues to be recorded in the financial statements for prior years beginning on or after December 15, 2006. As such, the only TSRs receivable recorded in the accompanying financial statements are those estimated to accrue due to cigarette shipments from January 1 to June 30, 2009.

OVERVIEW OF THE FINANCIAL STATEMENTS (Continued)

Economic Outlook

The volume of cigarette shipments is a major factor in determining the amount of TSRs. As shipments decline resulting in lower TSRs, the amount of time it will take to fully redeem the Authority's bonds is lengthened. Shipments of cigarettes have decreased at a rate faster than was predicted when the TSA's bonds were issued in 2002. Over the past few years this has been further magnified as significant increases in tobacco excise taxes in many states at various times, and on the federal level in April 2009, have been enacted. Some tobacco companies believe that the effects of those tax increases on reducing cigarette consumption have been realized.

FINANCIAL ANALYSIS OF THE AUTHORITY

Statements of Net Deficit

The following table summarizes the changes in assets, liabilities, and net deficits between the years ended June 30, 2009 and 2008 (in millions):

	2009	2008	Change	
Assets				
Cash and cash equivalents	$ 60.0	$ 15.4	$ 44.6	289.6%
Investments	0.3	46.0	(45.7)	(99.3%)
Accrued TSR receivable	24.4	24.0	0.4	1.7%
Unamortized bond issuance costs	1.5	1.7	(0.2)	(11.8%)
Total assets	$ 86.2	$ 87.1	$ (0.9)	(1.0%)
Liabilities				
Accrued interest payable and other liabilities	$ 2.4	$ 2.5	$ (0.1)	(4.0%)
Bonds payable, net	432.1	457.9	(25.8)	(5.6%)
Total liabilities	434.5	460.4	(25.9)	(5.6%)
Net deficit	(348.3)	(373.3)	25.0	(6.7%)
Total liabilities and net deficit	$ 86.2	$ 87.1	$ (0.9)	(1.0%)

FINANCIAL ANALYSIS OF THE AUTHORITY (Continued)

Statements of Revenues, Expenses, and Changes in Net Deficit

The following table summarizes the activities in revenues and expenses between the years ended June 30, 2009 and 2008 (in millions):

	2009	2008	Change	
Revenues				
Tobacco settlement revenues	$ 55.0	$ 54.5	$ 0.5	0.9%
Bond program interest	1.3	2.7	(1.4)	(51.9%)
Total revenues	$ 56.3	$ 57.2	$ (0.9)	(1.6%)
Expenses				
Bond program interest expense	$ 30.1	$ 31.3	$ (1.2)	(3.8%)
Other bond program expenses	1.1	1.2	(0.1)	(8.3%)
General and administrative	0.2	0.1	0.1	100.0%
Total expenses	$ 31.4	$ 32.6	$ (1.2)	(3.7%)
Change in net deficit	$ 24.9	$ 24.6	$ 0.3	1.2%

TSRs of $55 million and $30.1 million in interest on debt are the primary components of total revenues and expenses, respectively, for the Restricted Bond Program.

During fiscal year 2009 revenue received for general operations included interest earned on investments. General operating expenses within the General Operating Fund ($163,443) for the fiscal year 2009 is comprised of allocable salaries and wages, legal expenses and other general and administrative expenses.

DEBT ADMINISTRATION

The Authority has long-term debt obligations of $432.2 million, net of bond discounts at June 30, 2009. The Authority's bond funds are held by a trustee who ensures that bond resolution requirements are met, including payments of debt service and funding of necessary reserves. At June 30, 2009, amounts held by the trustee and future receipts of TSRs represent full funding of these requirements.

DEBT ADMINISTRATION (Continued)

The bonds were sold pursuant to a Purchase and Sale Agreement between the Authority and the state of Washington in which TSRs ($30 million by July 1, 2003, and 29.2% of the TSRs thereafter) were purchased by the Authority for a one-time cash distribution of $450 million to the state of Washington. The bonds are solely secured by the "right to receive" TSRs from major tobacco companies under the Master Settlement Agreement. The Bonds consist of Serial Bonds and Turbo Term Bonds. The Turbo Term Bonds are subject to redemption in accordance with the schedule of Sinking Fund Installments and, in addition, are subject to mandatory redemption to the extent that the funds remain on each payment date after meeting all current bond obligations ("Turbo Redemptions").

The Authority and the state of Washington covenanted to do and perform all acts and things permitted by law and the Bond Indenture which are necessary or desirable in order to ensure that interest paid on the Tax-Exempt Bonds will be excluded from gross income for federal income tax purposes and shall take no action that would result in such interest not being excluded from gross income for federal income tax purposes.

The Authority has no general obligations bonds and does not currently have an issuer credit rating.

Additional information on the Authority's long-term liabilities can be found in Note 5 of this report.

COMPARISON OF FISCAL YEARS 2008 WITH 2007

Statements of Net Deficit

The following table summarizes the changes in combined net deficits between ended June 30, 2008 and 2007 (in millions):

	2008	2007	Change	
Assets				
Cash and cash equivalents	$ 15.4	$ 16.5	$ (1.1)	(6.7%)
Investments	46.0	45.9	0.1	0.2%
Accrued TSR receivable	24.0	20.1	3.9	19.4%
Unamortized bond issuance costs	1.7	1.8	(0.1)	(5.6%)
Total assets	$ 87.1	$ 84.3	$ 2.8	3.3%
Liabilities				
Accrued interest payable and other liabilities	$ 2.5	$ 2.6	$ (0.1)	(3.8%)
Bonds payable, net	457.9	479.5	(21.6)	(4.5%)
Total liabilities	460.4	482.1	(21.7)	(4.5%)
Net deficit	(373.3)	(397.8)	24.5	(6.2%)
Total liabilities and net deficit	$ 87.1	$ 84.3	$ 2.8	3.3%

COMPARISON OF FISCAL YEARS 2008 WITH 2007 (Continued)

Statements of Revenues, Expenses and Changes in Net Deficit

The following table summarizes the combined changes in net deficit between the fiscal years 2008 and 2007 (in millions):

	2008	2007	Change	
Revenues				
Tobacco settlement revenues	$ 54.5	$ 38.7	$ 15.8	40.8%
Bond program interest	2.7	2.7	-	- %
Total revenues	$ 57.2	$ 41.4	$ 15.8	38.2%
Expenses				
Bond program interest expense	$ 31.3	$ 31.9	$ (0.6)	(1.9%)
Other bond program expenses	1.2	0.7	0.5	71.4%
General and administrative	0.1	0.1	-	- %
Total expenses	$ 32.6	$ 32.7	$ (0.1)	(0.3%)
Change in net deficit	$ 24.6	$ 8.7	$ 15.9	182.8%

During the fiscal year ended June 30, 2008 the Authority's combined total assets increased by $2.8 million primarily due to increases in TSRs receivable balances. Combined total net income of $24.6 million for fiscal year 2008 represented an increase in net revenue of $15.7 million from fiscal year 2007. This increase was attributable to the increase in TSRs primarily due to the recognition of the first annual strategic contribution payment ($3.9 million).

Questions and inquiries may be directed to the Senior Director of Finance or the Senior Controller at Tobacco Settlement Authority, 1000 Second Avenue, Suite 2700, Seattle, WA 98104 or 206-464-7139.

ASSETS

	2009	2008
CASH AND CASH EQUIVALENTS	$ 59,970,985	$ 15,363,073
INVESTMENTS	350,000	46,034,106
TSR RECEIVABLE	24,385,541	24,048,013
UNAMORTIZED BOND ISSUANCE COSTS	1,470,793	1,636,597
PREPAID FEES	25,483	34,925
TOTAL ASSETS	$ 86,202,802	$ 87,116,714

LIABILITIES AND NET DEFICIT

	2009	2008
ACCRUED INTEREST PAYABLE	$ 2,382,072	$ 2,516,191
ACCOUNTS PAYABLE AND OTHER LIABILITIES	28,283	14,716
BONDS PAYABLE		
Current interest bonds	440,880,000	467,575,000
Unamortized bond discount	(8,728,704)	(9,712,706)
	432,151,296	457,862,294
TOTAL LIABILITIES	434,561,651	460,393,201
TOTAL NET DEFICIT	(348,358,849)	(373,276,487)
TOTAL LIABILITIES AND NET DEFICIT	$ 86,202,802	$ 87,116,714

See accompanying notes.

TOBACCO SETTLEMENT AUTHORITY
(A Component Unit of the State of Washington)
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET DEFICIT
YEARS ENDED JUNE 30, 2009 AND 2008

	2009	2008
REVENUES		
Tobacco settlement revenues and other fee income	$ 54,998,947	$ 54,479,709
Non operating revenues - interest income	1,320,166	2,732,979
	56,319,113	57,212,688
EXPENSES		
Interest on debt	30,051,725	31,337,275
Amortization of bond discount	984,002	998,313
Amortization of bond issuance costs	165,805	168,217
General and administrative	199,943	116,033
	31,401,475	32,619,838
CHANGE IN NET DEFICIT	24,917,638	24,592,850
NET DEFICIT		
Beginning of year	(373,276,487)	(397,869,337)
End of year	$ (348,358,849)	$ (373,276,487)

TOBACCO SETTLEMENT AUTHORITY
(A Component Unit of the State of Washington)
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2009 AND 2008

	2009	2008
OPERATING ACTIVITIES		
Cash received from tobacco settlement revenues	$ 54,669,926	$ 50,537,411
Cash paid for general and administrative expenses	(186,375)	(120,315)
Net cash from operating activities	54,483,551	50,417,096
INVESTING ACTIVITIES		
Cash received from sales of investments	45,684,106	-
Cash received from interest income	1,321,099	2,580,672
Net cash from financing activities	47,005,205	2,580,672
NONCAPITAL FINANCING ACTIVITIES		
Principal repayment on bonds	(26,695,000)	(22,620,000)
Cash paid for bond interest expense	(30,185,844)	(31,446,456)
Net cash from financing activities	(56,880,844)	(54,066,456)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	44,607,912	(1,068,688)
CASH AND CASH EQUIVALENTS		
Beginning of year	15,363,073	16,431,761
End of year	$ 59,970,985	$ 15,363,073
RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Excess of revenues over expenses	$ 24,917,638	$ 24,592,850
Adjustments to reconcile operating income to net cash provided by operating activities		
Amortization of bond discount	984,002	998,313
Amortization of bond issue costs	165,805	168,217
Cash paid for bond interest expense	30,185,844	31,446,456
Cash received from interest income	(1,321,099)	(2,580,672)
Increases (decreases) in cash from changes in assets and liabilities		
TSR receivable	(337,528)	(3,965,825)
Prepaid fees and other receivables	9,441	(29,319)
Unrealized loss on securities	-	(103,518)
Accounts payable and other liabilities	13,567	(225)
Accrued interest payable	(134,119)	(109,181)
Net cash from operating activities	$ 54,483,551	$ 50,417,096

See accompanying notes.

Note 1 - Organization, Program Funds and Description of Business

The Tobacco Settlement Authority (the "Authority") was formed in April 2002 pursuant to legislation passed by the Washington State Legislature in March 2002 (RCW 43.340) and signed into law by Governor Gary Locke. It is a public instrumentality separate and distinct from the State. However, because the State appoints the governing body and is entitled to the resources of the Authority, the financial accountability criteria as defined by the Governmental Accounting Standards Board ("GASB") have been met. As such, the Authority is presented as a blended component unit of the State in its Comprehensive Annual Financial Report.

The Authority board consists of five directors. The chair of the Authority is appointed by, and serves at the pleasure of, the governor. The term of the remaining directors is four years from the date of their appointment.

The Authority was created to issue bonds to securitize a portion of the future revenue stream available under the Master Settlement Agreement ("MSA") in order to generate $450 million of cash for the state of Washington (the "State") in the 2002-2004 biennium. In November 2002, $517 million of bonds were issued and $450 million was deposited by the Authority into the State general fund in exchange for acquiring 29.2% of the State's tobacco revenue settlement stream. The final maturity of the bonds is in 2032, however at the date of bond closing, it was estimated that the bonds would remain outstanding for a 17-year period. For further information on the MSA, see Note 6.

Payment on the bonds is an obligation only of the Authority and not an obligation of the state of Washington. Neither the faith and credit nor the taxing power of the state of Washington or any municipal corporation, subdivision or agency of the state is pledged to the payment of the bonds.

The Authority includes two funds - the Restricted Bond Fund and General Operating Fund. The Restricted Bond Fund accounts for the tobacco revenue settlement stream and the debt service transactions. The General Operating Fund accounts for the fiscal activities of the ongoing program responsibilities of the Authority. The Authority's fiscal year begins on July 1 and ends on June 30.

Administrative and technical support for the Authority is provided by the Washington State Housing Finance Commission, which was reimbursed for its costs from the proceeds of the sale of the bonds. Accounting and staff services are to be provided until the bonds are retired with further reimbursements for services to be drawn, as necessary, from the revenues used to repay the debt.

Note 2 - Summary of Significant Accounting Policies

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. The GASB is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Authority has applied all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989 (unless they conflict with or contradict GASB pronouncements): Statements and Interpretations of the Financial Accounting Standards Board, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures.

The most significant of the Authority's accounting policies are described below.

Measurement Focus and Basis of Accounting - All program and general operating funds of the Authority are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the statement of net assets. The statement of revenues, expenses and changes in net assets for all funds present increases (e.g., revenues) and decreases (e.g., expenses) in net fund equity. These funds utilize the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Unclassified Balance Sheet - The Authority's business cycle is greater than one year. As such, all assets and liabilities as shown on the Statement of Net Deficit are unclassified.

Cash and Cash Equivalents - Cash deposits held in the bond issue are held in the corporate trust departments of commercial banks (the "Trustee") in the bond issue's name. Cash deposits held by the general operating fund are entirely covered by Federal Depository Insurance Corporation (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission ("PDPC").

For purposes of the statement of cash flows, the Authority considers all highly liquid, interest-bearing instruments purchased with an original maturity of three months or less that are readily convertible to cash to be cash and cash equivalents.

Investments - Investments are comprised of certificates of deposits as of June 30, 2009. Investments at June 30, 2008, also included a guaranteed investment agreement. The investments are stated at cost since the redemption terms are not affected by market rates. The Authority's Trustee holds all of the Authority's investments in the name of the Authority.

Unamortized Bond Issuance Costs and Discounts - Unamortized bond issuance costs and unamortized bond discounts are amortized using the bonds outstanding method over the expected term of the life of the bonds.

Note 2 - Summary of Significant Accounting Policies (Continued)

Bonds Payable - Current interest serial and term bonds are stated at their principal amount outstanding, net of unamortized bond discount.

Income Taxes - The Authority is exempt from federal income taxes under Internal Revenue Code (IRC) Section 115(a) and accordingly, no provision for income taxes was made for the years ended June 30, 2009 and 2008.

Tobacco Settlement Revenues - The purchase and sale agreement between the Authority and the state of Washington conveyed the right to the first $30 million of the tobacco settlement revenues ("TSRs") for the fiscal year ended June 30, 2003. Effective July 1, 2003, 29.2% of the tobacco settlement revenues received by the state are to be deposited with the Authority until such time as the bond obligations are fully paid.

The Authority estimates accrued TSRs that derive from sales of cigarettes from January 1 to June 30, according to the annual TSRs payment that are based on cigarette sales from the preceding calendar year and historical payment trends. TSRs recognized for 2009 and 2008 include an accrual of $24,385,541 and $24,048,013, respectively.

Other Fee Income - The Authority is entitled to receive operating funds each year from TSRs as outlined in the bond indenture. However, the Authority has the option to deliver an officer's certificate to the Trustee on or before April 15 of each year certifying changes to the amount of operating funds to be drawn. For fiscal years 2009 and 2008, the Authority delivered officer's certificates to the Trustee directing that no operating funds be disbursed for those years.

Use of Estimates - The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions in determining the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Net Deficit - The net deficit balances of $348,358,849 at June 30, 2009 and $373,276,487 at June 30, 2008 reflect unrestricted net deficits as defined by GASB Statement No. 34. This balance is comprised of amounts from two funds. The general operating fund has a net asset balance of $414,126 at June 30, 2009 and $567,600 at June 30, 2008. The restricted bond fund has a net deficit balance of $348,772,975 at June 30, 2009 and $373,844,087 at June 30, 2008. Although, these financial statements do not recognize the TSRs to be collected over time, management believes that the present value of the TSR's allocated to the Authority approximates the net deficit.

Note 2 - Summary of Significant Accounting Policies (Continued)

Arbitrage Rebate - No arbitrage rebate is owed to the United States Treasury for the years ended June 30, 2009 and 2008.

Note 3 - Investments

Bond Issue Investment Policy - The trust indenture for the bond issue outlines the permitted investments. Although all of the program funds must be used for program purposes, certain funds have been restricted for payment of debt service as required by the indenture.

Operations Investment Policy - The Authority can invest in nongovernmental investments including certificates of deposit, banker's acceptances and repurchase agreements.

In addition, the following governmental investments are eligible:

1. Treasury bills, notes and other obligations issued by the United States Department of the Treasury and backed by the full faith and credit of the U.S. government.

2. Federal Home Loan Bank notes and bonds.

3. Federal Land Bank bonds.

4. Federal National Mortgage Association notes, debentures and guaranteed certificates of participation.

5. The obligations of certain government-sponsored corporations whose obligations are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System.

6. Shares of mutual funds with portfolios consisting of only U.S. government bonds or U.S. government guaranteed bonds issued by federal agencies with average maturities less than four years.

As of June 30, 2009 and 2008, the Authority, in its General Operating Fund, held Certificate of Deposits with Bank of America totaling $350,000 and $500,000, respectively, with original maturities from 4 to 12 months with rates ranging from 1.20% to 2.65% and 2.11% to 2.43% for 2009 and 2008, respectively.

Note 3 - Investments (Continued)

As of June 30, 2008, the Authority held a reserve fund agreement in its Bond Fund with Lehman Brothers Special Financing ("LBSF") totaling $45,534,106, net, with a term of 30 years. The agreement was guaranteed by Lehman Brothers Holdings, Inc. ("LBHI") and was fully collateralized with the collateral held by the trustee in the name of the Authority. Both LBS and LBHC subsequently filed for bankruptcy protection. On December 1, 2008, and in accordance with the terms of the agreement, the trustee liquidated the collateral and invested the proceeds with U.S. Bank in a money market fund where they remain at June 30, 2009. The proceeds represented full funding of the principal and interest due at December 1, 2008. However, current interest rates on the money market fund are less favorable than that provided in the agreement.

All other excess funds are held as cash and cash equivalents.

Note 4 - Contracted Staff Services

The Washington State Housing Finance Commission provides staff and other administrative services to the Authority. Total charges were $30,348 and $24,671 for the years ended June 30, 2009 and 2008, respectively. The Authority has no directly hired staff and as such has no pension obligations. The Authority had fees payable totaling $26,634 and $5,067 with the Washington State Housing Finance Commission at June 30, 2009 and 2008, respectively.

Note 5 - Bonds Payable

The bonds are limited obligations of the Authority payable solely from 29.2% of TSRs, and secured by a right to receive TSRs for Washington State, restricted investments, and undisbursed bond proceeds and the earnings thereon held under the indenture authorizing the bonds.

Note 5 - Bonds Payable (Continued)

As of June 30, 2009, the Authority had outstanding bonds of $432.2 million. The bonds bear interest rates ranging from 5.25% to 6.625% and mature in varying amounts through 2032. Future principal and interest requirements are shown in the following table:

Years Ending June 30,	Principal Redemptions	Interest Requirements	Total
2010	$ 9,620,000	$ 28,584,869	$ 38,204,869
2011	13,285,000	28,079,819	41,364,819
2012	14,325,000	27,249,506	41,574,506
2013	7,650,000	26,461,631	34,111,631
2014	12,975,000	25,964,381	38,939,381
2015 - 2019	76,540,000	116,427,682	192,967,682
2020 - 2024	97,180,000	88,889,132	186,069,132
2025 - 2029	121,180,000	56,038,975	177,218,975
2030 - 2033	88,125,000	10,349,906	98,474,906
	$ 440,880,000	$ 408,045,901	$ 848,925,901

Balance at July 1, 2008	Issued	Redeemed	Balance at June 30, 2009
$ 467,575,000	$ -	$ 26,695,000	$ 440,880,000

Note 6 - Tobacco Settlement Revenues

TSRs consist of the amounts to be received under the terms of a Master Settlement Agreement among participating cigarette manufacturers and 46 states and six other U.S. jurisdictions (“Settling States”). The MSA is an industry wide settlement of litigation between the Settling States and the Original Participating Manufacturers (“OPMs”) and was entered into between the attorneys general of the Settling States and the OPMs on November 23, 1998.

The national MSA requires annual payments by the four largest tobacco companies to the participating states; up to $206 billion will be received during the first 25 years of the agreement. The state of Washington is scheduled to receive approximately $4 billion during the first 25 years.

Note 6 - Tobacco Settlement Revenues (Continued)

Management believes that the present value of the amount of TSRs that will be collected by the Authority from the state of Washington over time is $348,358,849, an amount equal to the net deficit. However, the only TSRs receivable recorded in the accompanying financial statements are those estimated to accrue due to cigarette shipments from January 1 to June 30, 2009.

Note 7 - Contingencies

Certain smokers, consumer groups, cigarette manufacturers, cigarette importers, cigarette distributors, Native American tribes, taxpayers, taxpayers' groups, and other parties have instituted litigation against various tobacco manufacturers, including the Participating Manufacturers ("PMs"), as well as certain of the Settling States and other public entities. The lawsuits allege, among other things, that the MSA violates certain provisions of the United States Constitution, state constitutions, the federal antitrust laws, federal civil rights laws, state consumer protection laws and unfair competition laws, certain of which actions, if ultimately successful, could result in a determination that the MSA is void or unenforceable. The lawsuits seek, among other things, an injunction against one or more of the Settling States from collecting any monies under the MSA and barring the PMs from collecting cigarette price increases related to the MSA and/or a determination that the MSA is void or unenforceable.

In addition, class action lawsuits have been filed in several federal and state courts alleging that under the federal Medicaid law, any amount of tobacco settlement funds that the Settling States receive in excess of what they paid through the Medicaid program to treat tobacco-related diseases should be paid directly to Medicaid recipients. To date, no such lawsuits have been successful. The enforcement of the terms of the MSA may, however, continue to be challenged in the future. In the event of an adverse court ruling, the Authority may not have adequate financial resources to make payment on the Series 2002 Revenue Bond.

Members of the Authority's board of directors and persons acting on the Authority's behalf, while acting within the scope of their duties or employment, shall not be subject to any personal liability resulting from carrying out the powers and duties conferred on them, and shall have the indemnification rights under the provisions of the Authority's Public Officials and Employees Liability insurance policy.

SUPPLEMENTAL INFORMATION

TOBACCO SETTLEMENT AUTHORITY
(A Component Unit of the State of Washington)
SCHEDULE OF PROGRAM NET ASSETS (DEFICIT)
JUNE 30, 2009 AND 2008

	Restricted Bond Fund	General Operating Fund	Total 2009	Total 2008
ASSETS				
CASH AND CASH EQUIVALENTS	$ 59,886,603	$ 84,382	$ 59,970,985	$ 15,363,073
INVESTMENTS	-	350,000	350,000	46,034,106
TSR RECEIVABLE	24,385,541	-	24,385,541	24,048,013
UNAMORTIZED BOND ISSUANCE COSTS	1,470,793	-	1,470,793	1,636,597
PREPAID FEES AND INTEREST RECEIVABLE	17,456	8,027	25,483	34,925
TOTAL ASSETS	$ 85,760,393	$ 442,409	$ 86,202,802	$ 87,116,714
LIABILITIES AND NET DEFICIT				
ACCRUED INTEREST PAYABLE	$ 2,382,072	$ -	$ 2,382,072	$ 2,516,191
ACCOUNTS PAYABLE AND OTHER LIABILITIES	-	28,283	28,283	14,716
BONDS PAYABLE				
Current interest bonds	440,880,000	-	440,880,000	467,575,000
Unamortized bond discount	(8,728,704)	-	(8,728,704)	(9,712,706)
	432,151,296	-	432,151,296	457,862,294
TOTAL LIABILITIES	434,533,368	28,283	434,561,651	460,393,201
TOTAL NET DEFICIT	(348,772,975)	414,126	(348,358,849)	(373,276,487)
TOTAL LIABILITIES AND NET DEFICIT	$ 85,760,393	$ 442,409	$ 86,202,802	$ 87,116,714

TOBACCO SETTLEMENT AUTHORITY
(A Component Unit of the State of Washington)
SCHEDULE OF PROGRAM REVENUES, EXPENSES, AND CHANGES IN PROGRAM NET ASSETS (DEFICIT)
YEARS ENDED JUNE 30, 2009 AND 2008

	Restricted Bond Fund	General Operating Fund	Total	
			2009	2008
REVENUES				
Tobacco settlement revenues and other fee income	$ 54,998,947	$ -	$ 54,998,947	$ 54,479,709
Non operating revenues - interest income	1,310,197	9,969	1,320,166	2,732,979
	56,309,144	9,969	56,319,113	57,212,688
EXPENSES				
Interest on debt	30,051,725	-	30,051,725	31,337,275
Amortization of bond discount	984,002	-	984,002	998,313
Amortization of bond issuance costs	165,805	-	165,805	168,217
General and administrative	36,500	163,443	199,943	116,033
	31,238,032	163,443	31,401,475	32,619,838
CHANGE IN NET DEFICIT	25,071,112	(153,474)	24,917,638	24,592,850
NET DEFICIT				
Beginning of year	(373,844,087)	567,600	(373,276,487)	(397,869,337)
End of year	$ (348,772,975)	$ 414,126	$ (348,358,849)	$ (373,276,487)

TOBACCO SETTLEMENT AUTHORITY
(A Component Unit of the State of Washington)
SCHEDULE OF PROGRAM CASH FLOWS
YEARS ENDED JUNE 30, 2009 AND 2008

	Restricted Bond Fund	General Operating Fund	Total 2009	Total 2008
OPERATING ACTIVITIES				
Cash received from tobacco settlement and other revenues	$ 54,661,419	$ 8,507	$ 54,669,926	$ 50,537,411
Cash paid for general and administrative expenses	(36,500)	(149,875)	(186,375)	(120,315)
Net cash from operating activities	54,624,919	(141,368)	54,483,551	50,417,096
INVESTING ACTIVITIES				
Cash received from sales of investments	45,534,106	150,000	45,684,106	-
Cash received from interest income	1,321,099	-	1,321,099	2,580,672
Net cash from financing activities	46,855,205	150,000	47,005,205	2,580,672
NONCAPITAL FINANCING ACTIVITIES				
Principal repayment on bonds	(26,695,000)	-	(26,695,000)	(22,620,000)
Cash paid for bond interest expense	(30,185,844)	-	(30,185,844)	(31,446,456)
Net cash from financing activities	(56,880,844)	-	(56,880,844)	(54,066,456)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	44,599,280	8,632	44,607,912	(1,068,688)
CASH AND CASH EQUIVALENTS				
Beginning of year	15,287,323	75,750	15,363,073	16,431,761
End of year	$ 59,886,603	$ 84,382	$ 59,970,985	$ 15,363,073
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Excess of revenues over expenses	$ 25,071,112	$ (153,474)	$ 24,917,638	$ 24,592,850
Adjustments to reconcile operating income to net cash provided by operating activities				
Amortization of bond discount	984,002	-	984,002	998,313
Amortization of bond issue costs	165,805	-	165,805	168,217
Cash paid for bond interest expense	30,185,844	-	30,185,844	31,446,456
Cash received from interest income	(1,321,099)	-	(1,321,099)	(2,580,672)
Changes in assets and liabilities				
Increase in TSR	(337,528)	-	(337,528)	(3,965,825)
Decrease (increase) in prepaid fees and other receivables	10,902	(1,461)	9,441	(29,319)
Other	-	-	-	(103,518)
Increase (decrease) in accounts payable and other liabilities	-	13,567	13,567	(225)
Decrease in accrued interest payable	(134,119)	-	(134,119)	(109,181)
Net cash from operating activities	$ 54,624,919	$ (141,368)	$ 54,483,551	$ 50,417,096