

AUDITED FINANCIAL STATEMENTS AND OTHER REPORT

The Golden L.E.A.F. (Long-term Economic Advancement Foundation), Inc.
A Component Unit of the State of North Carolina
As of and for the Years Ended June 30, 2007 and 2006
With Report of Independent Auditors

The Golden L.E.A.F. (Long-term Economic
Advancement Foundation), Inc.
A Component Unit of the State of North Carolina

Audited Financial Statements and Other Report

As of and for the Years Ended June 30, 2007 and 2006

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The Golden L.E.A.F. (Long-term Economic
Advancement Foundation), Inc.
A Component Unit of the State of North Carolina

Management's Discussion and Analysis (unaudited)

June 30, 2007

Our discussion and analysis of The Golden L.E.A.F. (Long-term Economic Advancement Foundation), Inc. (the Foundation) provides an overview of the Foundation's financial activities. Please read it in conjunction with the Foundation's financial statements.

Financial Highlights

- The total assets of the Foundation increased by \$122.5 million during 2007 to \$720.1 million.
- The primary source of revenue during 2007 was net investment gains and income during 2007 of \$101.5 million compared to \$48.4 million in 2006.
- The Foundation received \$71.4 million in proceeds from the Master Settlement Agreement (MSA). This compares to \$68.2 million in MSA proceeds received during the prior year.
- The Foundation awarded grants of \$34.2 million in 2007 compared to \$27.8 million in 2006 (excluding grants rescinded discussed below). Fiscal year 2007 grant awards included \$6.7 million in special initiatives supporting the Foundation's new Community Assistance initiative and the North Carolina Biomanufacturing and Pharmaceutical Training Consortium, \$7.8 million in economic catalyst grants and \$19.7 million in annual grant awards. Fiscal year 2006 grant awards included \$4.5 million in special initiatives supporting the North Carolina Biomanufacturing and Pharmaceutical Training Consortium and the North Carolina Aerospace Manufacturing Alliance, \$6.1 million in economic catalyst grants and \$17.2 million in annual grant awards. Prior year grant awards rescinded or returned totaled \$2.4 million during 2007 and \$1.0 million during 2006.
- Administrative costs were \$2.2 million in 2007 compared to \$1.9 million in 2006.
- The Foundation ended 2007 with investments and cash and cash equivalents totaling \$718.8 million. The equivalent amount at the end of 2006 was \$597.2 million.

The Golden L.E.A.F. (Long-term Economic
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Management's Discussion and Analysis (continued)

Using This Annual Report

This annual report consists of a series of financial statements. The Statements of Net Assets and Governmental Fund Balance Sheets show the assets, liabilities and net assets at June 30, 2007 and 2006. The Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance show the revenues, expenditures, and changes in net assets for the fiscal years ended June 30, 2007 and 2006. The Notes to Financial Statements contain additional information that is essential to a full understanding of the data in the financial statements.

Statements of Net Assets and Governmental Fund Balance Sheets

Condensed Statements of Net Assets and Governmental Fund Balance Sheets:

	2007	2006	2005
Current assets	\$ 718,807,611	\$ 597,663,461	\$ 505,889,827
Capital assets-nondepreciable	1,055,714	-	-
Capital assets-depreciable, net	272,802	21,441	24,457
Total assets	\$ 720,136,127	\$ 597,684,902	\$ 505,914,284
Total liabilities	\$ 71,236,080	\$ 87,030,140	\$ 83,162,103
Net assets:			
Invested in capital assets, net of debt	1,328,516	21,441	24,457
Unrestricted	647,571,531	510,633,321	422,727,724
Total net assets	648,900,047	510,654,762	422,752,181
Total liabilities and net assets	\$ 720,136,127	\$ 597,684,902	\$ 505,914,284

The Golden L.E.A.F. (Long-term Economic
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Management's Discussion and Analysis (continued)

2007

Total assets at June 30, 2007 were \$720.1 million, an increase of \$122.5 million over June 30, 2006. The assets of the Foundation are comprised mainly of investments and cash and cash equivalents. The total of investments, cash and cash equivalents at June 30, 2007 was \$718.8 million, compared to \$597.2 million at June 30, 2006. This increase resulted primarily from investment gains and MSA proceeds net of grant disbursements and administrative expenditures. Net capital assets increased to \$1.3 million at June 30, 2007 from \$21,441 at June 30, 2006, primarily as the result of the acquisition of property for the construction of the Foundation's new headquarters (see Note 3 to the financial statements).

The liabilities of the Foundation are comprised primarily of grants payable. Grants payable totaled \$71.0 million at June 30, 2007, compared to \$86.9 million at June 30, 2006. This decrease resulted primarily from grant awards of \$34.2 million in 2007 net of \$47.6 million of grant disbursements. Prior year grant awards totaling \$2.4 million were rescinded or returned in 2007.

The Net Assets section of the Statements of Net Assets and Governmental Fund Balance Sheets shows the amount of the assets of the Foundation, less its liabilities. There were no board designations of net assets at the end of either year.

2006

Total assets at June 30, 2006 were \$597.7 million, an increase of \$91.8 million over June 30, 2005. The assets of the Foundation are comprised mainly of investments and cash and cash equivalents. The total of investments, cash and cash equivalents at June 30, 2006 was \$597.2 million, compared to \$505.7 million at June 30, 2005. This increase resulted primarily from MSA proceeds and investment gains net of grant disbursements and administrative expenditures. Net capital assets changed to \$21,441 at June 30, 2006 from \$24,457 at June 30, 2005. These capital assets consist of technological equipment and furniture and fixtures (see Note 3 to the financial statements).

The liabilities of the Foundation are comprised primarily of grants payable. Grants payable totaled \$86.9 million at June 30, 2006, compared to \$83.1 million at June 30, 2005. This increase resulted primarily from grant awards of \$27.8 million in 2006 net of \$23.0 million of grant disbursements. Prior year grant awards totaling \$1.0 million were rescinded or returned in 2006.

The Golden L.E.A.F. (Long-term Economic
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Management's Discussion and Analysis (continued)

The Net Assets section of the Statements of Net Assets and Governmental Fund Balance Sheets shows the amount of the assets of the Foundation, less its liabilities. There were no board designations of net assets at the end of either year.

Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance

Condensed Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance:

	2007	2006	2005
Total revenues	\$172,888,361	\$116,675,726	\$111,166,798
Total expenses	34,643,076	28,773,145	24,470,153
Excess of revenues over expenses	138,245,285	87,902,581	86,696,645
Net assets, at beginning of year	510,654,762	422,752,181	336,055,536
Net assets, at end of year	<u>\$648,900,047</u>	<u>\$510,654,762</u>	<u>\$422,752,181</u>

These statements show the revenues and the expenses of the Foundation for the years ended June 30, 2007, 2006, and 2005, and the corresponding effect on the net assets.

2007

Total revenues (MSA receipts, gains and/or losses from investment earnings, and other income) were \$172.9 million in 2007 and \$116.7 million in 2006.

For the first time in the Foundation's history, investment gains provided the majority of the Foundation's revenue in 2007. There was investment income of \$101.5 million during 2007 and \$48.4 million during 2006.

The other significant source of revenues for the Foundation in 2007 were proceeds from the state settlement (or MSA receipts). MSA receipts were \$71.4 million in 2007 and \$68.2 million in 2006. The calculation of the MSA receipts that are received by the Foundation is impacted by, among other things, an inflation adjustment and a volume adjustment. These factors are out of the control of the Foundation.

The Golden L.E.A.F. (Long-term Economic
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Management's Discussion and Analysis (continued)

Total expenses were \$34.6 million in 2007 and \$28.8 million in 2006.

The largest expenses were grant disbursements. Grant disbursements represent grants awarded net of grants rescinded. Grants were awarded (excluding grants rescinded) in the amount of \$34.2 million during 2007 and \$27.8 million in 2006.

The other expenses of the Foundation were administrative costs and depreciation. Administrative costs were \$2.2 million in 2007 and \$1.9 million in 2006. The primary reason for the increase in administrative costs in 2007 was higher personnel expenses as more permanent staff was added to handle the increased volume of grant applications and awards.

Depreciation increased from \$9,812 in 2006 to \$14,516 in 2007.

The net excess of revenues over expenses was \$138.2 million and \$87.9 million in 2007 and 2006, respectively. Net assets at June 30, 2007 were \$648.9 million compared to \$510.7 million at June 30, 2006.

2006

Total revenues (MSA receipts, gains and/or losses from investment earnings, and other income) were \$116.7 million in 2006 and \$111.2 million in 2005.

The majority of the revenues of the Foundation were proceeds from the state settlement (or MSA receipts). MSA receipts were \$68.2 million in 2006 and \$74.3 million in 2005. The calculation of the MSA receipts that are received by the Foundation is impacted by, among other things, an inflation adjustment and a volume adjustment. These factors are out of the control of the Foundation. In addition, some participating manufacturers in the MSA withheld a portion of their 2006 payment because they believe they were entitled to a Non-Participating Manufacturer Adjustment as described in Section IX(d) of the MSA. The Foundation's share of the withheld amount is \$9.2 million. The matter is currently in litigation in North Carolina court.

The other significant revenue source was from investment activities. There was investment income of \$48.4 million during 2006 and \$36.8 million during 2005. During 2006, the Foundation's diversified investment portfolio generated another year of solid investment gains. Performance was primarily driven by international equities, with meaningful contributions also coming from absolute return and real assets. Additional gains came from domestic equity, private equity and cash, but to a lesser extent.

The Golden L.E.A.F. (Long-Term Economic
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Management's Discussion and Analysis (continued)

Total expenses were \$28.8 million in 2006 and \$24.5 million in 2005.

The largest expenses were grant disbursements. Grant disbursements represent grants awarded net of grants rescinded. Grants were awarded (excluding grants rescinded) in the amount of \$27.8 million during 2006 and \$24.9 million in 2005.

The other expenses of the Foundation were administrative costs and depreciation. Administrative costs were \$1.9 million in 2006 and \$1.6 million in 2005. The primary reason for the increase in administrative costs in 2006 was higher personnel expenses as more permanent staff was added to handle the increased volume of grant applications and awards.

Depreciation decreased from \$16,354 in 2005 to \$9,812 in 2006.

The net excess of revenues over expenses was \$87.9 million and \$86.7 million in 2006 and 2005, respectively. Net assets at June 30, 2006 were \$510.7 million compared to \$422.8 million at June 30, 2005.

Notes to Financial Statements

The reader is referred to these notes for a more complete understanding of the financial statements of the Foundation. They contain a summary of the significant accounting policies as well as other information.

Requests for Information

This report is designed to provide a general overview of the Foundation's finances and to show the Foundation's accountability for the funds it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to The Golden L.E.A.F. Foundation, 107 SE Main St., Rocky Mount, NC 27801.

Report of Independent Auditors

The Board of Directors
The Golden L.E.A.F. (Long-term Economic
Advancement Foundation), Inc.

We have audited the accompanying Statements of Net Assets and Governmental Fund Balance Sheets of The Golden L.E.A.F. (Long-term Economic Advancement Foundation), Inc. (the Foundation), a non-profit corporation and component unit of the State of North Carolina as of June 30, 2007 and 2006, and the related Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance for the years then ended. These financial statements are the responsibility of the Foundation'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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Foundation's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and 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 Foundation at June 30, 2007 and 2006, and the changes in financial position and, cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2007 on our consideration of the Foundation's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

The management's discussion and analysis on pages i through vi is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. 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.

November 14, 2007

The Golden L.E.A.F. (Long-term Economic
 Advancement Foundation), Inc.
 A Component Unit of the State of North Carolina

Statement of Net Assets and Governmental Fund Balance Sheet

June 30, 2007

	General Fund	Reclassifications and Eliminations (Note 6)	Statement of Net Assets
Assets			
Cash and cash equivalents	\$ 3,008,068	\$ –	\$ 3,008,068
Sales tax refund and other receivables	2,594	–	2,594
Prepaid items	27,298	–	27,298
Investments	715,769,651	–	715,769,651
Capital assets-nondepreciable	–	1,055,714	1,055,714
Capital assets-depreciable, net	–	272,802	272,802
Total assets	<u>\$ 718,807,611</u>	<u>\$ 1,328,516</u>	<u>\$ 720,136,127</u>
Liabilities			
Accounts payable	\$ 184,718	\$ –	\$ 184,718
Accrued liabilities	20,193	–	20,193
Grants payable	71,031,169	–	71,031,169
Total liabilities	<u>71,236,080</u>	–	<u>71,236,080</u>
Net assets			
Reserved for prepaid items	27,298	(27,298)	–
Invested in capital assets, net of debt	–	1,328,516	1,328,516
Unrestricted	647,544,233	27,298	647,571,531
	<u>647,571,531</u>	<u>1,328,516</u>	<u>648,900,047</u>
Total liabilities and fund balances/net assets	<u>\$ 718,807,611</u>	<u>\$ 1,328,516</u>	<u>\$ 720,136,127</u>

See accompanying notes.

The Golden L.E.A.F. (Long-term Economic
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Statement of Net Assets and Governmental Fund Balance Sheet

June 30, 2006

	General Fund	Reclassifications and Eliminations (Note 6)	Statement of Net Assets
Assets			
Cash and cash equivalents	\$ 568,194	\$ —	\$ 568,194
Sales tax refund and other receivables	425,620	—	425,620
Prepaid items	30,279	—	30,279
Investments	596,639,368	—	596,639,368
Capital assets-depreciable, net	—	21,441	21,441
Total assets	<u>\$ 597,663,461</u>	<u>\$ 21,441</u>	<u>\$ 597,684,902</u>
Liabilities			
Accounts payable	\$ 140,899	\$ —	\$ 140,899
Accrued liabilities	17,171	—	17,171
Grants payable	86,872,070	—	86,872,070
Total liabilities	<u>87,030,140</u>	<u>—</u>	<u>87,030,140</u>
Net assets			
Reserved for prepaid items	30,279	(30,279)	—
Invested in capital assets, net of debt	—	21,441	21,441
Unrestricted	510,603,042	30,279	510,633,321
	<u>510,633,321</u>	<u>21,441</u>	<u>510,654,762</u>
Total liabilities and fund balances/net assets	<u>\$ 597,663,461</u>	<u>\$ 21,441</u>	<u>\$ 597,684,902</u>

See accompanying notes.

The Golden L.E.A.F. (Long-term Economic
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Statement of Activities and Governmental Fund Revenues,
Expenditures, and Changes in Fund Balance

For the Year Ended June 30, 2007

	General Fund	Reclassifications and Eliminations (Note 6)	Statement of Activities
Revenues:			
Proceeds from state settlement	\$ 71,412,539	\$ –	\$ 71,412,539
Investment income	101,469,685	–	101,469,685
Other income	6,137	–	6,137
Total revenues	172,888,361	–	172,888,361
Expenses:			
Grant distributions	31,774,950	–	31,774,950
Administrative costs	2,208,003	–	2,208,003
Capital outlays	1,320,912	(1,320,912)	–
Gain on fixed assets	–	(679)	(679)
Depreciation expense	–	14,516	14,516
Bad debt expense	638,399	–	638,399
Unrelated business income tax	7,887	–	7,887
Total expenses	35,950,151	(1,307,075)	34,643,076
Excess of revenues over expenses	136,938,210	1,307,075	138,245,285
Net assets, at beginning of year	510,633,321	21,441	510,654,762
Net assets, at end of year	\$ 647,571,531	\$ 1,328,516	\$ 648,900,047

See accompanying notes.

The Golden L.E.A.F. (Long-term Economic
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Statement of Activities and Governmental Fund Revenues,
 Expenditures, and Changes in Fund Balance

For the Year Ended June 30, 2006

	General Fund	Reclassifications and Eliminations (Note 6)	Statement of Activities
Revenues:			
Proceeds from state settlement	\$ 68,226,543	\$ —	\$ 68,226,543
Investment income	48,443,995	—	48,443,995
Other income	5,188	—	5,188
Total revenues	116,675,726	—	116,675,726
Expenses:			
Grant distributions	26,848,013	—	26,848,013
Administrative costs	1,898,430	—	1,898,430
Capital outlays	6,978	(6,978)	—
Loss on fixed assets	—	182	182
Depreciation expense	—	9,812	9,812
Unrelated business income tax	16,708	—	16,708
Total expenses	28,770,129	3,016	28,773,145
Excess of revenues over expenses	87,905,597	(3,016)	87,902,581
Net assets, at beginning of year	422,727,724	24,457	422,752,181
Net assets, at end of year	\$ 510,633,321	\$ 21,441	\$ 510,654,762

See accompanying notes.

The Golden L.E.A.F. (Long-Term Economic
Advancement Foundation), Inc.
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Notes to Financial Statements

June 30, 2007

1. Summary of Significant Accounting Policies

The following is a summary of the significant accounting principles and policies used in the preparation of these financial statements.

Reporting Entity

The Golden L.E.A.F. (Long-term Economic Advancement Foundation), Inc. (the Foundation) is a not-for-profit corporation ordered to be established by the Consent Decree and Final Judgment in the *State of North Carolina vs. Philip Morris Incorporated, et al.*

The Foundation was established for the purpose of receipt and distribution of fifty percent of the funds allocated to the North Carolina State Specific Account, such funds to be used to provide economic impact assistance to economically affected or tobacco-dependent regions of North Carolina.

For financial reporting purposes, the Foundation is deemed to be a component unit of the State of North Carolina, and is included as such in the State of North Carolina Comprehensive Annual Financial Report.

Basis of Presentation

These financial statements have been prepared in conformity with the accounting principles and reporting guidelines established by the Governmental Accounting Standards Board (GASB). The Foundation applies all statements issued by the GASB and all Financial Accounting Standards Board (FASB) statements issued on or before November 30, 1989, except those that conflict with the GASB.

General Fund

The general fund is used to account for all revenues and expenses applicable to the general operations of the Foundation that are not required either legally or by governmental accounting standards to be accounted for in another fund.

The Golden L.E.A.F. (Long-Term Economic
Advancement Foundation), Inc.
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Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Basis of Accounting

The Foundation follows the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recorded when the liability is incurred.

The Foundation's primary source of revenue is the funds received by the State of North Carolina under the settlement of the lawsuit noted above. Revenues are recorded upon receipt of the funds by the State of North Carolina and classified as Proceeds from State Settlement in the Statement of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance. In 2006, some of the participating manufacturers in the Master Settlement Agreement (MSA) withheld a portion of their 2006 payment because they believe they were entitled to a Non-Participating Manufacturer Adjustment as described in Section IX(d) of the MSA. The Foundation's share of the withheld amount is \$9.2 million. The matter is currently in litigation in North Carolina court.

Budgetary Requirement

The Foundation's enabling legislation requires that the Foundation's Board of Directors consult with the Joint Legislative Commission on Governmental Operations prior to its adopting an annual operating budget. As of June 30, 2007, the Foundation's Board of Directors has adopted a preliminary budget only for the general fund on a basis consistent with generally accepted accounting principles, subject to finalization after the Foundation consults with the Joint Legislative Commission on Governmental Operations. Budgetary control is expected to be at the object of expense classification level (personal services, operating expenditures, capital outlay). Budgetary changes within expense classifications are expected to be made at the discretion of the Foundation.

Net Assets

Reserves represent the portion of net assets committed by legislative action, legal responsibility, or designated by the Board of Directors, which restricts the use of funds to a specific purpose. Funds received from the North Carolina State Specific Accounts are unrestricted, but are invested as directed by the Board of Directors, with the income from investment being used for operating expenses and to fund grants.

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Investments

Investments include long-term fixed income investments, equity investments, money market funds, certificates of deposit, limited partnerships, real estate, and obligations of government agencies. Investments are accounted for at fair value. Depending on the underlying asset, the fair value is determined through national exchange price for securities with a readily determinable value or valuations and estimates typically determined by the underlying asset's manager. Certain investment values may differ from the values that would have been used had a ready market for these investments existed and differences could be material. The financial statements of these investments are audited annually (typically at December 31) by independent auditors.

Realized investment gains and losses are determined using the specific identification basis and are recorded as investment income in the Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance. Changes in net unrealized gain and losses are also recognized as a component of investment income.

Capital Assets

Generally, capital assets are defined by the Foundation as assets with an initial value or cost greater than or equal to \$500 and an estimated useful life of two or more years. Capital assets are stated at cost less accumulated depreciation. Estimated useful lives are five years for equipment, seven years for furniture and fixtures and forty years for buildings.

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Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Prepaid Insurance

The Foundation allocates the cost of insurance between the related accounting periods. Expenses incurred for services not yet provided are recorded as prepaid and amortized over the service period.

Grants Payable

The Foundation records grants payable when the Board of Directors approves the grant. The Programs Committee (a subset of the Board of Directors) evaluates the grant applications and makes recommendations to the entire Board of Directors. Applicants that are chosen by the Board of Directors must fill out and sign a “Grantee Acknowledgement and Agreement” which states guidelines of the contract. Several requirements must be met by the grantees prior to the disbursement of funds.

Income Taxes

The Foundation is a not-for-profit organization that is exempt from federal income taxes under Section 501 (c)(3) of the Internal Revenue Code.

2. Cash and Investments

The Foundation considers highly liquid temporary cash investments with a maturity of three months or less when purchased to be cash equivalents. However, cash investments with a maturity of three months or less that were purchased with the intent to be maintained as an investment are classified as investments.

According to the Foundation’s investment policy adopted by the Board of Directors, the Foundation may invest in any of the following broad asset classes: domestic equities; real estate; mutual funds; foreign equities; fixed income securities; cash equivalents; and alternatives.

The Foundation maintained no investments in derivatives at June 30, 2007 and 2006.

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Notes to Financial Statements (continued)

2. Cash and Investments (continued)

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Foundation has no policy that contains requirements that would limit the exposure to custodial credit risk for deposits. At June 30, 2007, the carrying amount of the Foundation's deposits was \$3,008,068 and the bank balance, excluding in-transit items, was \$3,103,677. Of the bank balance, \$400,000 was covered by Federal Depository Insurance and \$2,703,677 was uninsured and uncollateralized.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Foundation monitors the interest rate risk inherent in its portfolio by measuring the effective duration of its portfolio. The Foundation has no specific limitations with respect to duration. At June 30, 2007, the Foundation had investments in two fixed income security funds with an average duration of 5.5 years and fair value of \$82,635,751. The Foundation also had an investment in a money market fund with a fair value of \$32,251,594 at June 30, 2007, and duration of 0.08 years.

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

2. Cash and Investments (continued)

Credit risk is the risk that an issuer of an investment will not fulfill its obligations. Credit risk is measured by the assignment of a rating by a nationally recognized statistical rating organization. The Foundation's investment policy requires fixed income investments be investment grade or better at the time of purchase and that the portfolio maintain an average rating of AA or better at all times. At June 30, 2007, the Foundation had investments in two fixed income funds rated AAA with fair value of \$82,635,751.

At June 30, 2007, the Foundation had an investment in an unrated money market fund with a fair value of \$32,251,594.

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Foundation's investment policy does not limit the amount of investment in foreign currency-denominated investments. At June 30, 2007, the Foundation had investments in the following:

	Fair Value
State Street Global Advisors MSCI EAFE Index Fund	\$ 67,318,972
Capital Guardian Non-US Equity Fund for Tax-Exempt Trusts	42,002,236
Silchester International Investors International Value Equity Fund	40,158,658
State Street Global Advisors MSCI Emerging Markets Fund	23,465,106
Longleaf Partners International Fund	21,000,000
Total	\$ 193,944,972

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

2. Cash and Investments (continued)

The Foundation's investments at June 30, 2007 and 2006, are summarized below:

	2007	2006
Domestic stocks and equity funds	\$151,138,184	\$182,086,407
International stocks and equity funds	193,944,972	95,229,513
Fixed income funds	82,635,751	97,519,176
Real estate and other	55,681,246	48,238,389
Limited partnerships	201,799,478	135,919,848
Money market funds	30,362,394	37,342,957
Certificates of deposit	207,626	303,078
Total investments	<u>\$715,769,651</u>	<u>\$596,639,368</u>

The following summarizes the investment return and its classification in the Statements of Activities and Governmental Fund Revenues, Expenditures, and Changes in Fund Balance for the years ended June 30:

	2007	2006
Dividends and interest	\$ 8,546,723	\$ 8,010,880
Net realized gains	34,664,802	24,673,546
Net unrealized gains	60,370,772	17,489,546
Management fees	(2,112,612)	(1,729,977)
Total return on investments	<u>\$ 101,469,685</u>	<u>\$ 48,443,995</u>

The calculation of realized gains and losses is independent of a calculation of the net change in the fair value of investments. Realized gains and losses on investments that have been held in more than one fiscal year and sold in the current year were included as a change in the fair value of investments reported in the prior years and current year.

The Golden L.E.A.F. (Long-Term Economic
 Advancement Foundation), Inc.
 A Component Unit of the State of North Carolina

Notes to Financial Statements (continued)

3. Capital Assets

A summary of the activity related to the capital assets follows:

	Balance July 1, 2006	Additions	Disposals	Balance June 30, 2007
Capital Assets, nondepreciable:				
Land	\$ —	\$ 923,546	\$ —	\$ 923,546
Construction in progress	—	132,168	—	132,168
Total capital assets-nondepreciable	—	1,055,714	—	1,055,714
Capital Assets, depreciable:				
Buildings	—	202,532	—	202,532
Equipment	57,931	9,347	(2,121)	65,157
Furniture and fixtures	41,873	53,340	—	95,213
Total capital assets-depreciable	99,804	265,219	(2,121)	362,902
Less accumulated depreciation for:				
Buildings	—	(2,532)	—	(2,532)
Equipment	(47,310)	(4,459)	2,779	(48,990)
Furniture and fixtures	(31,053)	(7,525)	—	(38,578)
Total accumulated depreciation	(78,363)	(14,516)	2,779	(90,100)
Total capital assets-depreciable, net	21,441	250,703	658	272,802
Total capital assets, net	\$ 21,441	\$ 1,306,417	\$ 658	\$ 1,328,516

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

3. Capital Assets (continued)

	Balance July 1, 2005	Additions	Disposals	Balance June 30, 2006
Capital Assets, depreciable:				
Equipment	\$ 56,853	\$ 3,345	\$ (2,267)	\$ 57,931
Furniture and fixtures	38,240	3,633	–	41,873
Total capital assets-depreciable	95,093	6,978	(2,267)	99,804
Less accumulated depreciation for:				
Equipment	(43,547)	(5,869)	2,106	(47,310)
Furniture and fixtures	(27,089)	(3,964)	–	(31,053)
Total accumulated depreciation	(70,636)	(9,833)	2,106	(78,363)
Total capital assets-depreciable, net	24,457	(2,855)	(161)	21,441
Total capital assets, net	\$ 24,457	\$ (2,855)	\$ (161)	\$ 21,441

4. Leases

The Foundation leases office space under an operating lease agreement, which expires in June 2008. Total rent expense was \$91,556 and \$85,297 for the years ended June 30, 2007 and 2006, respectively. Future minimum lease commitments subsequent to June 30, 2007 through the end of the lease term are \$69,132.

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

5. Tobacco Settlement

In November 1998, the Attorneys General of 46 states, five U.S. territories and the District of Columbia (the States) signed the Master Settlement Agreement (MSA) with the nation's largest tobacco manufacturers. Under the MSA, the participating tobacco manufacturers must provide payments to the States. The base payments to the states are estimated to total \$206 billion through 2025. North Carolina's share of the base payments is estimated to be \$4.57 billion, of which the Foundation is expected to receive 50 percent. The Foundation has received \$626,569,409 since its inception.

While North Carolina's share of the base payments will not change over time, the amount of the annual payment is subject to a number of adjustments including, among others, inflation, and volume adjustments. These adjustments may increase or decrease the base payments. Therefore, the net effect of these adjustments is uncertain and the impact on the estimated payments cannot be determined. Any changes in the base payments will impact the amount received by the Foundation. As a result of the uncertainty of payment and amount of these funds, no receivable has been recorded for the Foundation's share of North Carolina's payments under the MSA.

6. Explanations of Differences Between the Governmental Fund Balance Sheet and the Statement of Net Assets

Total fund balances of the Foundation differ from net assets of the Foundation reported in the Statement of Net Assets. This difference primarily results from the long-term economic focus of the Statement of Net Assets versus the current financial resources focus on the Foundation's fund balance sheets. The provisions of Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, imposed this change in focus.

- (a) When fixed assets (equipment, furniture and fixtures) that are to be used in Foundation activities are purchased, the costs of those assets are reported as expenditures in general funds. However, the Statement of Net Assets includes those fixed assets among the assets of the Foundation.

The Golden L.E.A.F. (Long-Term Economic
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Notes to Financial Statements (continued)

7. Commitments

The Foundation has committed to invest in several private equity funds.

8. Retirement Plans

The Foundation administers the Defined Contribution Plan and the Tax-Deferred Annuity Plan as approved by the Board of Directors. The plans are 403(b) defined contribution plans that provide retirement benefits with options for payments to beneficiaries in the event of the participant's death. All employees of the Foundation are eligible to participate in both plans.

The Defined Contribution Plan requires the Foundation to contribute 10% of participants' gross salary. The Foundation contributed \$91,860 to the Defined Contribution Plan during the fiscal year ended June 30, 2007. The Tax-Deferred Annuity Plan permits participants to contribute a percentage of gross salary up to the maximum established by the Internal Revenue Code. Participants contributed \$42,687 to the Tax-Deferred Annuity Plan during the fiscal year ended June 30, 2007.

Plan benefits are provided by means of contracts issued and administered by the privately-operated Teachers' Insurance and Annuity Association and the College Retirement Equities Fund (TIAA/CREF).

9. Risk Management

The Foundation is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors or omissions; illnesses or injuries to employees and natural disasters. The Foundation carries commercial insurance to cover these risks of loss. Claims on this coverage have not exceeded commercial premiums

Report on Internal Control Over Financial Reporting and on Compliance
and Other Matters Based on an Audit of Financial Statements Performed
in Accordance With *Government Auditing Standards*

The Board of Directors
The Golden L.E.A.F. (Long-term Economic
Advancement Foundation), Inc.

We have audited the financial statements of The Golden L.E.A.F. (Long-term Economic Advancement Foundation), Inc. (the Foundation), a non-profit corporation and component unit of the State of North Carolina as of June 30, 2007, and for the year then ended, and have issued our report thereon dated November 14, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Foundation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Foundation's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Foundation's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Directors, the Office of the State Controller, State of North Carolina, and is not intended to be and should not be used by anyone other than these specified parties.

November 14, 2007