



STATE OF TENNESSEE COMPTROLLER OF THE TREASURY

Office of the Attorney General and Reporter

Performance Audit Report

December 2014

**Justin P. Wilson
Comptroller of the Treasury**



**Department of Audit
Division of State Audit
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December 11, 2014

Members of the General Assembly
State Capitol
Nashville, Tennessee 37243

and

The Honorable Sharon G. Lee
Chief Justice of the Supreme Court
Supreme Court Building
401 Seventh Avenue North
Nashville, TN 37219

and

The Honorable Herbert H. Slatery III
Attorney General and Reporter
425 Fifth Avenue North
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have conducted a performance audit of selected programs and activities of the Office of the Attorney General and Reporter for the period July 1, 2011, through June 30, 2014.

Our audit disclosed a finding which is detailed in the Objectives, Methodologies, and Conclusions section of this report. Management of the Office of the Attorney General and Reporter has responded to the audit finding; we have included the response following the finding. We will follow up the audit to examine the application of the procedures instituted because of the audit finding.

We have reported other less significant matters involving internal control and instances of noncompliance to the Office of the Attorney General and Reporter's management in a separate letter.

Sincerely,

Deborah V. Loveless, CPA
Director

DVL/jw
14/048-OAG

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Performance Audit

Office of the Attorney General and Reporter

December 2014

AUDIT SCOPE

We have audited the Office of the Attorney General and Reporter for the period July 1, 2011, through June 30, 2014. Our audit scope included a review of internal control and compliance with laws and regulations in the areas of revenue collections, travel claim expenditures, information systems, the Bankruptcy Division, and the Tobacco Enforcement Division. A performance audit report of the Consumer Advocate Division in the Office of the Attorney General and Reporter was released in August 2014. Management of the Office of the Attorney General and Reporter is responsible for establishing and maintaining effective internal control and for complying with applicable laws and regulations.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

CONCLUSION

AUDIT FINDING

The Office of the Attorney General and Reporter did not always maintain proper information systems security controls, increasing the risk of data loss

Based on our testwork, the Office of the Attorney General and Reporter's staff did not always maintain proper information systems security in two specific areas (page 9).

**Performance Audit
Office of the Attorney General and Reporter**

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Performance Audit Office of the Attorney General and Reporter

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the performance audit of the Office of the Attorney General and Reporter. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which requires the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The mission of the Office of the Attorney General and Reporter is “to serve its clients, the public, and the law by providing creative, independent, quality-driven, professional legal representation of the state, its agencies, and its personnel, and by fulfilling the constitutional, statutory, and common law duties of the Attorney General.” Established by Article VI, Section 5, of the Tennessee Constitution, the office is dedicated to helping the executive, legislative, and judicial branches of state government fulfill their responsibility to serve the people of Tennessee.

The Attorney General, the chief legal officer of the state, is appointed to an eight-year term by the justices of the Tennessee Supreme Court. Through the office’s staff, he represents the officers and agencies of the state in litigation before state and federal courts and the Claims Commission. In addition to performing courtroom duties, the Attorney General provides legal advice to state departments and agencies as well as the General Assembly, renders formal opinions on legal issues to state officials upon request, approves the form and legality of administrative regulations and leases, and reports the opinions of the Tennessee Supreme Court and Court of Appeals.

The Attorney General is assisted by

- the Chief Deputy, who coordinates and supervises the work of the office, including reviewing substantive work and general management of the office;

- the Chief Policy Deputy, who supervises special projects, oversees legislative and external matters, and coordinates multistate initiatives with the National Association of Attorneys General;
- the Chief of Staff, who is the main contact with the National Association of Attorneys General and the legislature and handles media inquiries; and
- the Solicitor General, who supervises the drafting of formal opinions and oversees the Office of the Solicitor General, which oversees and coordinates all appellate litigation in the Tennessee Supreme Court, Court of Appeals, and Court of Criminal Appeals as well as the United States Supreme Court and the Sixth Circuit Court of Appeals.

The Office of the Attorney General and Reporter has the following divisions:

- The Administrative Division is the internal support division of the office. Its responsibilities include human resources, budget and fiscal matters, purchasing, information systems, library services, facilities management, and records management.
- Representing state agencies in bankruptcy courts across the country, the Bankruptcy Division files proofs of claims and administrative claims in bankruptcy cases where a state entity is owed a debt. The division also collects penalties and other debts owed to state departments and agencies.
- In addition to representing the state's educational agencies and institutions and dealing with state purchasing and personnel matters, the Civil Litigation and State Services Division represents the state in employment and construction litigation and reviews state contracts.
- The Civil Rights and Claims Division defends tort and workers' compensation actions filed against all departments and agencies of state government. It also defends state employees of various departments sued in civil rights actions for monetary damages.
- The Consumer Advocate and Protection Division consists of three teams.
 - The *Consumer Advocate* team represents the interests of Tennessee consumers of public utilities services. We conducted a performance audit of the Consumer Advocate team pursuant to the Tennessee Governmental Entity Review Law, *Tennessee Code Annotated*, Title 4, Chapter 29. The Consumer Advocate team's performance audit report entitled Consumer Advocate Division was released in August 2014.
 - The *Consumer Protection* team protects consumers and businesses from unfair and deceptive trade practices, enforces state and federal antitrust laws, and enforces the Unauthorized Practice of Law statutes.
 - The *False Claims* team handles non-Medicaid-related false claims.

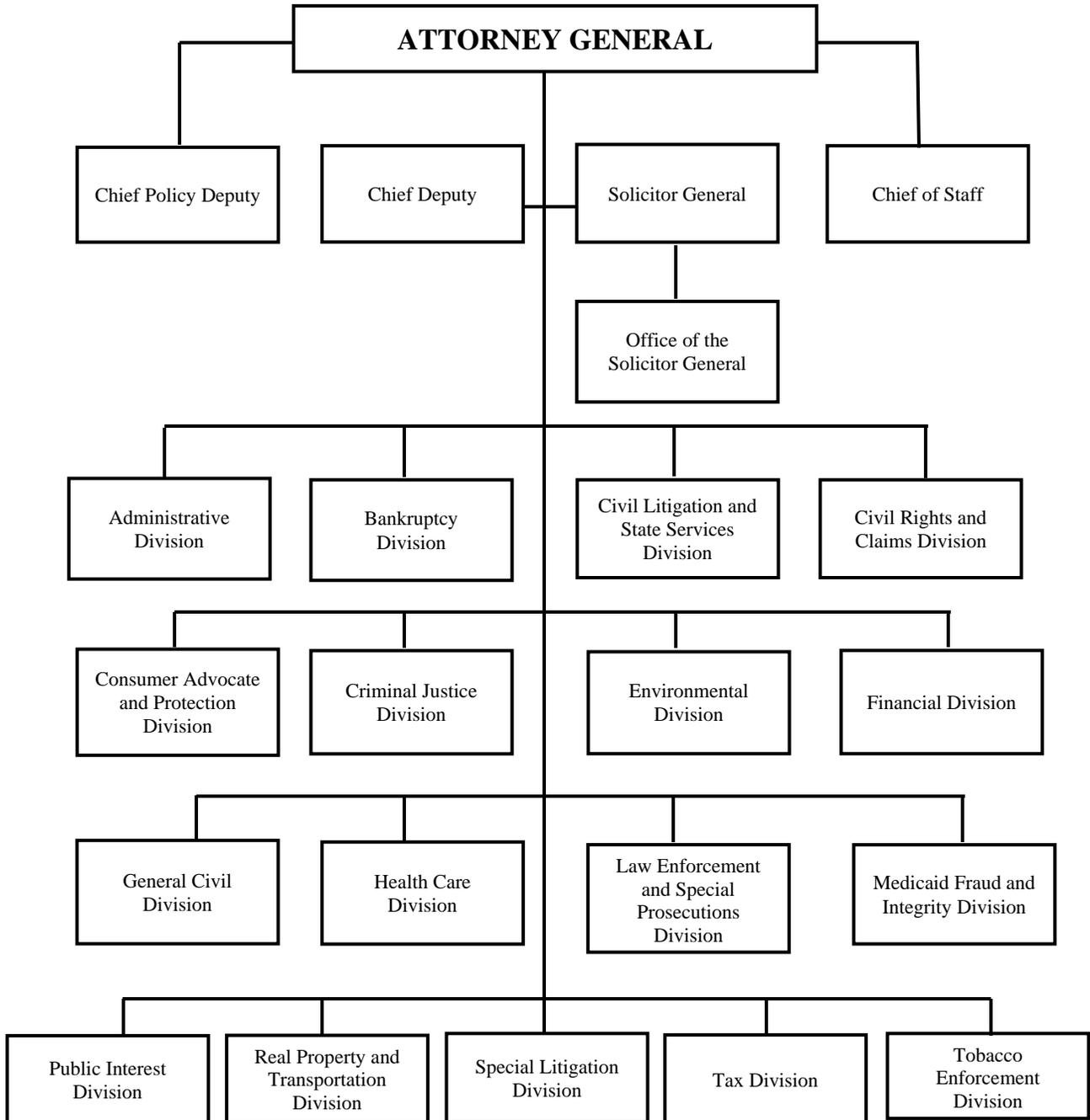
- Handling all direct and post-conviction appeals from criminal judgments, the Criminal Justice Division defends criminal judgments in habeas corpus¹ proceedings in both the trial and appellate courts. This division also handles capital cases on appellate review in both the state courts.
- As an enforcer of civil environmental protection laws regarding clean air, clean water, hazardous waste, and other areas, the Environmental Division also gives advice to and reviews regulations for the Department of Environment and Conservation and represents the Tennessee Wildlife Resources Agency.
- The Financial Division provides legal services for much of the state's business-related activities, such as investments of the State Treasury and the Tennessee Consolidated Retirement System. It represents a number of agencies handling issues of government financing, banking, and insurance regulation.
- Handling a wide variety of civil matters, the General Civil Division represents a number of state departments, boards, and agencies, including the Departments of Children's Services, Human Services, Intellectual and Developmental Disabilities, Labor and Workforce Development, Agriculture, Tourism, Veterans Affairs, and Military.
- The Health Care Division primarily provides legal advice and representation to the Bureau of TennCare and the Department of Health and its health-related boards, such as the Board of Dentistry, the Board of Medical Examiners, the Board of Nursing, and the Board of Optometry along with the Health Services Development Agency.
- The Attorney General has the authority to initiate criminal prosecution in matters involving criminal acts by elected state judicial officials, Securities Act violations, and violations of the state's Clean Water Act. These matters are handled by the Law Enforcement and Special Prosecutions Division, which also assists local district attorneys in similar prosecutions. The division also represents the state's interests in federal habeas corpus and civil forfeiture proceedings and defends state agencies, including the Department of Safety, the Tennessee Bureau of Investigation, and the Alcoholic Beverage Commission, in suits for declaratory and injunctive relief.
- The Medicaid Fraud and Integrity Division works with the Bureau of TennCare, the Tennessee Bureau of Investigation, and the Department of Finance and Administration's Office of Inspector General in combating medical provider fraud in the TennCare/Medicaid program.
- The Public Interest Division carries out the office's statutory duty to oversee the operation of nonprofit entities on behalf of Tennesseans. It also handles charitable oversight and charitable solicitations as well as issues involving open meetings, public records, and campaigns and elections.

¹ Habeas corpus is a judicial mandate that requires a prisoner to be brought before a court to determine whether the government has the right to continue detaining him.

- Most of the work performed by the Real Property and Transportation Division, which represents the State of Tennessee in land acquisitions, involves the Tennessee Department of Transportation. In addition to Nashville, the division has regional offices in Knoxville, Chattanooga, and Jackson.
- The Special Litigation Division handles unique cases and assists other divisions in litigation matters.
- Representing the Department of Revenue in defending challenges to tax liabilities, the Tax Division also represents a wide variety of other agencies, including the Board of Professional Responsibility, the Board of Law Examiners, the Commission on Continuing Legal Education, the Tennessee Regulatory Authority, the Tennessee Consolidated Retirement System, and many of the regulatory boards of the Department of Commerce and Insurance.
- The Tobacco Enforcement Division enforces the provisions of the 1998 Master Settlement Agreement and handles other tobacco-related matters.

An organization chart of the Office of the Attorney General and Reporter is presented on the following page.

**Office of the Attorney General and Reporter
Organizational Chart
February 2014**



AUDIT SCOPE

We have audited the Office of the Attorney General and Reporter for the period July 1, 2011, through June 30, 2014. Our audit scope included a review of internal control and compliance with laws and regulations in the areas of revenue collections, travel claim expenditures, information systems, the Bankruptcy Division, and the Tobacco Enforcement Division. A performance audit report of the Consumer Advocate Division in the Office of the Attorney General and Reporter was released in August 2014. Management of the Office of the Attorney General and Reporter is responsible for establishing and maintaining effective internal control and for complying with applicable laws and regulations.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

PRIOR AUDIT FINDINGS

There were no audit findings in the prior audit report dated August 2006.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

REVENUE COLLECTIONS

Several divisions within the Attorney General's Office receive revenue relating to their cases, including attorney fees, court costs, and proceeds from legal judgments. Some divisions collect approximately 8 to 10 receipts annually while other divisions collect several thousand receipts annually. When the Attorney General's Office receives mail containing receipts of fees, court costs, and proceeds, office staff who open the mail deliver the collected funds to the

appropriate division so that division staff can ensure the receipts are matched to the proper legal case. Once the division staff match the receipts to the appropriate case and account, they send the accounting detail and the funds to the office's Fiscal Office staff who record revenue in Edison, the state's accounting system, and make the deposit.

The objective of our review was to determine if the Fiscal Office appropriately recorded and promptly deposited the funds.

We interviewed personnel within four divisions that collected revenue during the audit period and personnel within the Fiscal Office to gain an understanding of the processes to collect, record, and deposit the funds.

To determine if the Fiscal Office appropriately recorded and promptly deposited revenue collections, we obtained a list of revenue transactions from Edison consisting of a population of 213 receipts, totaling \$114,436,886, which had been collected and deposited by the Attorney General's Office from July 1, 2011, through January 31, 2014. We then selected a nonstatistical random sample of 60 receipts, totaling \$47,614,517, and reviewed the corresponding legal documentation and divisional memorandums relating to the receipts to determine if the amounts were appropriately recorded. Finally, we reviewed supporting documentation to determine if the Fiscal Office made prompt deposits.

Based on procedures performed, we determined that the Fiscal Office appropriately recorded and promptly deposited the funds. We did, however, note minor exceptions relating to each division's processes for logging and securing receipts when the receipts were in the division's custody.

TRAVEL CLAIM EXPENDITURES

Even though the Office of the Attorney General and Reporter is part of the judicial branch of government, when the employees of the office travel on official business, they seek reimbursement of their travel expenditures based on the executive branch's *State of Tennessee Travel Regulations*, including the state per diem and mileage reimbursement rates. To obtain reimbursements for travel expenditures, employees complete paper travel claim forms and forward these forms to their division deputy for approval. Once the division deputy approves, the deputy then forwards the paper travel claim forms to the Fiscal Office for payment processing.

When the Fiscal Office receives a paper travel claim form from the division deputy, a Fiscal Office employee reviews the expenditures on the form to ensure the travel expenditure requests are allowed by the state's travel regulations, which includes verifying that the employee attached the appropriate supporting documentation to the form. If the Fiscal Office employee is satisfied with the travel documentation, he records a travel expenditure request into Edison, the state's accounting system. The Fiscal Director reviews and approves both the paper travel claim form and the travel expenditure request in Edison, which automatically initiates the payment process and final payment of the expenditure to the employee.

The objectives of our review of the travel claim expenditures were to

- determine the Fiscal Office’s processes for reviewing, recording, and approving travel claim expenditures, including car rental reservations; and
- determine if the Attorney General’s Office paid travel claim expenditures in accordance with the state’s travel regulations and the policies and procedures of the Attorney General’s Office.

We interviewed personnel within the Administrative Division to gain an understanding of the processes for reviewing, recording, and approving travel claim expenditures. We also conducted walkthrough procedures to determine the process for reviewing rental car reservations and reviewed the “Office of the Attorney General Policy on the Use of a WeCar”² (dated March 2012).

To determine if the Fiscal Office paid travel claim expenditures in accordance with the state’s travel regulations and internal office policies and procedures, we reviewed the *Office of the Attorney General Operations Manual* (revised July 7, 2010) and the *State of Tennessee Travel Regulations*.

From a population of 2,574 travel claim expenditures, totaling \$830,623, paid from July 1, 2011, through October 31, 2013, we selected a nonstatistical random sample of 25 travel expenditures, totaling \$10,175, to determine if Fiscal Office staff paid these expenditures in accordance with state travel regulations and the office’s policies and procedures.

Based on procedures performed, we determined that

- the processes for reviewing, recording, and approving travel claim expenditures, including rental car reservations, were appropriate; and
- the Fiscal Office paid travel claim expenditures in accordance with the state’s travel regulations and the policies and procedures of the Attorney General’s Office.

INFORMATION SYSTEMS

The Information Services section within the Administrative Division provides centralized services for all divisions within the Attorney General’s Office in the areas of technical support, network access, electronic data protection, hardware and software usage, and other computing needs. To assist legal personnel in case preparation, the section oversees numerous applications that fall into five major categories:

- office productivity applications (e.g., Microsoft Office);

² WeCar is the state’s rental car program.

- web-based legal research applications;
- statewide applications (e.g., Edison and email);
- databases; and
- information systems security applications (e.g., anti-virus and firewall protection).

Our objective in reviewing the Attorney General's information systems was to determine if management followed information systems' industry best practices and policies of the Attorney General's Office regarding computer controls.

To gain an understanding of the information systems environment, we performed walkthroughs of information systems controls with management. We obtained management policies; minutes from the meetings of the office's Information Technology Committee from July 31, 2013, through January 29, 2014; and other documents to assess the evidence of the controls that were in place during our audit. To determine industry best practices, we obtained and reviewed the industry best practices documented by the National Institute of Standards and Technology (NIST) of the United States Department of Commerce, which lists controls, supplemental guidance, and control enhancements for information systems. The NIST is responsible for developing standards and guidelines relating to information security for use by federal agencies.

Finding – The Office of the Attorney General and Reporter did not always maintain proper information systems security controls, increasing the risk of data loss

Based on our testwork, the Office of the Attorney General and Reporter's staff did not always maintain proper information systems security in two specific areas resulting in an increased risk of data loss. The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the office's systems. Disclosing those vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided management with detailed information regarding the specific vulnerabilities we identified and our recommendations for improvement.

While the conditions observed have the potential to affect office operations, we are not aware of any instances in which critical information was not available to attorneys within the Attorney General's Office. The conditions mentioned in this finding were internal control issues and do not impact the reliability or security of office systems that are critical to legal cases assigned to the office's attorneys.

Recommendation

The Attorney General should ensure that these conditions are remedied through procedures that encompass all aspects of effective information systems controls. Management should ensure that risks associated with this finding are adequately identified and assessed in the

office's documented risk assessment. Furthermore, the Attorney General should implement effective information systems controls to mitigate the potential risks of data loss, assign staff to be responsible for ongoing monitoring of the risks and mitigating controls, and take action if deficiencies occur.

Management's Comment

We concur. The Office of the Tennessee Attorney General and Reporter will ensure that the risks associated with this finding are adequately identified and assessed in the Office's documented risk assessment. Furthermore, the Attorney General will implement effective information systems controls to mitigate the potential risks of data loss, will assign staff to be responsible for ongoing monitoring of the risk and mitigating controls, and will take action if deficiencies occur.

BANKRUPTCY DIVISION

The Bankruptcy Division represents state entities in bankruptcy courts across the country. Specifically, it represents the state's interest by filing proofs of claims and administrative claims in bankruptcy cases where a state entity is owed a debt. According to its vision statement, the division strives to "deliver unsurpassed bankruptcy and collection services to our clients through a state-of-the-art practice in a unique work environment, noted for mutual respect, healthy relationships, and quality of life." The division's mission is to maximize debt recoveries and to protect the state and its citizens in all courts in the electronic era. In addition to handling bankruptcy cases, the division, through its Collection Unit, collects penalties³ and other debts owed to state agencies. Cases for collection are referred to the Collections Unit from other divisions within the Attorney General's Office, including the Bankruptcy Division, or from other state entities such as the Department of Labor and Workforce Development and the Tennessee State Veterans' Homes Board.

For our audit period, the Bankruptcy Division consisted of 28 employees, who were attorneys, bankruptcy specialists, paralegals, or administrative staff. These employees were responsible for approximately 16,000 active bankruptcy cases as of March 27, 2014. According to division management, for the period January 2011 to June 2014, the division collected over 7,700 receipts on behalf of the state.

Because the debt collections received by both the Bankruptcy Division and the Collections Unit are made payable to the state entity to whom the debt is owed, the Attorney General's Office is not responsible for the deposit of any debt collections. When the Attorney General's Office receives debt collections, division staff determine the cases to which the collections apply, document the collection information in the corresponding case notes, and deliver or mail the debt collections to the appropriate state entity for deposit.

³ Civil penalties assessed by a Professional Regulatory Board against a licensee are one example of penalties collected by the Bankruptcy Division.

The objectives of our review of the Bankruptcy Division were to determine

- if the division’s daily operations, including its process for recovering and disbursing debt collections, enabled it to serve state entities efficiently; and
- if the division properly redistributed the collections to the appropriate state entities.

To gain an understanding of the Bankruptcy Division’s daily operations, including its process for redistributing debt collections (i.e., checks, money orders, or cashier’s checks), we interviewed key division and Collections Unit personnel and conducted walkthrough procedures. We obtained and reviewed copies of the division’s mission statement; its annual risk assessment; the division’s Strategic and Operations Plan Fiscal Year 2013–2014 and Strategic Plan 2014–2016; and various other policies, procedures, and management reports, including ones that involve bankruptcy and revenue collections, which provide details about the division’s operations and its mission to serve clients. We also reviewed information relating to case tracking, case prioritization, staffing, and collection efforts.

Based on the procedures we performed, we determined that

- the division’s daily operations enabled it to serve state entities efficiently; and
- the division properly redistributed the collections to the appropriate state entities, with minor exceptions.

In addition, during our walkthrough procedures, we learned that the Bankruptcy Division infrequently received debt collections that were made payable to an individual or to a non-state entity, instead of the proper state entity. As a result, we requested that management provide copies of all debt collections received by the Bankruptcy Division and the Collections Unit from July 1, 2011, through March 21, 2014, to determine if checks were written to non-state entities. From this review, we obtained a population of 19 checks, totaling \$14,723, that were actually due to state entities but were made payable to either individuals or non-state entities. We determined that the division did not request that the debtors reissue these checks to the correct payee but did route the checks to the correct state entity for deposit. We then reviewed the supporting documentation for all 19 checks to determine if the checks were sent to the correct state entity.

TOBACCO ENFORCEMENT DIVISION

Background Information

In 1998, Tennessee and 51 other states and jurisdictions entered into the Master Settlement Agreement with major U.S. cigarette manufacturers, including Phillip Morris and R. J. Reynolds. As a result of the settlement, these tobacco manufacturers, known as “Participating Manufacturers,” are required to make annual payments to each of the settling states and jurisdictions to compensate them for health care costs incurred as a result of the health

consequences of smoking. Additionally, the settlement imposes a broad array of restrictions on Participating Manufacturers relating to cigarette advertising, marketing, and promotions.

The Master Settlement Agreement also contains a Model Statute that imposes certain financial requirements on tobacco manufacturers who did not settle. These companies are called “Non-Participating Manufacturers” (NPMs). The purpose of the Model Statute is to equalize market conditions between Participating Manufacturers and NPMs that may occur as a result of the restrictions imposed by the Master Settlement Agreement. The State of Tennessee implemented a qualifying statute on NPMs codified in *Tennessee Code Annotated*, Section 47-31-101 *et seq.*, Tobacco Manufacturers’ Escrow Fund Act or Escrow Fund Act, which requires NPMs to make escrow deposits based on the number of the manufacturers’ cigarettes sold to consumers in Tennessee. The Tobacco Enforcement Division enforces the provisions of the 1998 Master Settlement Agreement and handles other tobacco matters, such as monitoring NPMs’ compliance with Section 47-31-101 *et seq.*

In accordance with the Master Settlement Agreement, Participating Manufacturers’ payments to the state are also subject to the NPM Adjustment provision. This provision states that Participating Manufacturers may reduce their settlement payments to states, including Tennessee, if they lose a certain level of their market share to NPMs as a result of the restrictions and payments imposed by the Master Settlement Agreement.

According to the NPM Adjustment provision, Tennessee can avoid any reduction in the Participating Manufacturers’ settlement payments if

- the state continuously had the Escrow Fund Act in full force and effect during the entire calendar year immediately preceding the year in which the Participating Manufacturers’ payments are due, and
- the state diligently enforced the provisions of the Escrow Fund Act during the entire calendar year.

States who do not diligently enforce the escrow statutes can potentially lose their entire settlement payment from Participating Manufacturers each year.

Recent Arbitration, Settlement, Legislation, and Future Plans

For more than a decade, the Participating Manufacturers had asserted a right to the NPM Adjustment for each annual payment and claimed that the states had not been diligently enforcing their escrow statutes. A national arbitration concerning the NPM Adjustment for the 2003 payment year concluded in 2013, with six states being found non-diligent. During that arbitration, Tennessee and 21 other states reached a settlement with the Participating Manufacturers, and their diligence was not determined (two more states joined the settlement after the arbitration was concluded). The settlement resolved the NPM Adjustment disputes for payment years 2003-2014 and allowed for the release of more than \$2 billion from a disputed payments account. Tennessee’s share of these funds was more than \$71 million. The parties

have been working under a Term Sheet⁴ while they negotiate a final settlement agreement. It is anticipated that this agreement will be completed and submitted for approval in early 2015.

The settlement also reduces the amount of the NPM Adjustment in future years but does not eliminate it. Thus, Tennessee's enforcement of its escrow statute will be subject to challenge, starting with calendar year 2015. Additionally, the settlement imposes a penalty on states when NPMs fail to make escrow deposits as required by their escrow statutes. There are a safe harbor and other provisions limiting the scope of this penalty. When it applies, the amount of the penalty is roughly 3.3 times the escrow deposit amount, which is approximately three cents a cigarette, making the penalty about 10 cents per noncompliant cigarette.

In 2014, the General Assembly addressed the recent settlement and enhanced the ability of the state to enforce the Escrow Fund Act, Title 47, Chapter 31, *Tennessee Code Annotated*. The proposed legislation enhanced the state's ability to enforce the escrow provisions and offered some protections against future reductions of the Participating Manufacturers' Master Settlement Agreement payments related to the NPM Adjustment provision. The Governor signed the legislation into law on April 22, 2014.

The Escrow Act now requires NPMs to make quarterly escrow deposits and to meet a bonding requirement to help reduce the state's risk of a penalty for an NPM's failure to make escrow deposits. The legislation also expands the escrow deposit requirement to cover almost all NPM sales. It also clarifies the state's audit authority over tobacco distributors to ensure they are reporting the correct number of NPM sales so that the proper NPM escrow deposit amounts can be calculated and enforced. Additionally, it allows the state to share sales data and other information with outside entities involved with the application of several settlement calculation and enforcement provisions.

To increase efficiency and enhance the efforts to enforce the provisions of the Escrow Fund Act on NPMs, the Attorney General's Office and the Department of Revenue (TDOR) are jointly working on an electronic reporting system and database to track tobacco sales and monitor escrow payments. The AG's Tobacco Enforcement Division is also working with TDOR's auditing staff in monitoring tobacco distributor reports. Funding for the database and the hiring of additional TDOR audit staff was included in the budget for the 2013-14 fiscal year.

⁴ A Term Sheet is a document outlining the basic terms of a settlement. The division has been working under these terms until the final settlement agreement is approved.

APPENDIX

BUSINESS UNIT CODES

30301 Administration
30305 Publication of Tennessee Reports
30308 Special Litigation