

THE COUNCIL FOR TOBACCO RESEARCH-U.S.A., INC.  
MINUTES OF THE TWENTY-NINTH ANNUAL MEETING OF MEMBERS  
DECEMBER 10, 1998

The twenty-ninth annual meeting of members of The Council for Tobacco Research-U.S.A., Inc. was held pursuant to Article IV of the By-Laws of The Council at The Waldorf Astoria Hotel, 301 Park Avenue, New York, New York 10022 on the tenth day of December, 1998 at 2:00 P.M.

The following members were present in person or by proxy:

Class A Members

Brown & Williamson Tobacco Corporation  
Lorillard Tobacco Company  
Philip Morris Inc.  
R. J. Reynolds Tobacco Company

Class B Members

Bright Belt Warehouse Association, Inc.  
Tobacco Associates, Inc.  
United States Tobacco Company

The following officers were present:

James F. Glenn, Chairman and President  
Harmon C. McAllister, Vice President-Research  
Lorraine Pollice, Secretary and Treasurer

The following individuals were present:

N. G. Brookes, Brown & Williamson Tobacco Corporation  
Ernest Pepples, Brown & Williamson Tobacco Corporation  
Ronald S. Milstein, Lorillard Tobacco Company  
Alexander W. Spears, Lorillard Tobacco Company  
Arthur J. Stevens, Lorillard Tobacco Company  
Cathy Ellis, Philip Morris, U.S.A.

Gary T. Burger, R. J. Reynolds Tobacco Company  
Michael O. Johnson, R. J. Reynolds Tobacco Company  
Steven Klugman, Debevoise & Plimpton

Dr. Glenn, the Chairman, opened the meeting and asked the Secretary to present the Affidavit of Mailing of Notice of meeting and proxies. He announced that a quorum for the meeting was present.

The Chairman stated that the minutes of the meeting of The Council for Tobacco Research-U.S.A., Inc. held on December 11, 1997, had been sent to the members under date of February 3, 1998. Upon motion duly made and seconded, the minutes were unanimously approved.

The Chairman welcomed the group and reported on various items of interest to the members. He then introduced Dr. McAllister, Vice President-Research and Scientific Director, who reported on recent work and activities of several Council grantees and Scientific Advisory Board members.

The Chairman presented and discussed the certified financial report of The Council for 1998. Thereafter, upon motion duly made and seconded, it was unanimously

RESOLVED, that the report presented to this meeting pursuant to Section 8 of Article IV of the By-Laws and certified by PricewaterhouseCoopers be, and the same hereby is, approved and ordered filed with the records of the Council and a copy entered in the minutes of this meeting.

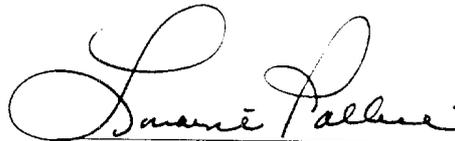
The Chairman stated that the next order of business was the election of directors of the Council to serve until the next Annual Meeting of the Members and until their respective successors are elected and qualified. He pointed out that pursuant to Article IV, Section 6 of the By-Laws, only Class A members are entitled to vote in the election of Directors. Upon motion made and seconded, the following were duly elected Directors:

N. G. Brookes  
Gary T. Burger  
Cathy Ellis  
Michael O. Johnson  
John R. Nelson  
Ernest Pepples  
Alexander W. Spears  
Arthur J. Stevens

The Chairman reported that the next Annual Meeting of the Members would be on December 9, 1999 at 2:00 P.M.

The Chairman then discussed the planned CTR Medical Insurance Trust with the members.

Thereupon, on motion duly made, the meeting was adjourned.

  
Lorraine Pollice, Secretary

**THE COUNCIL for TOBACCO RESEARCH -  
U.S.A., INC.**

**FINANCIAL STATEMENTS**

**For the year ended  
October 31, 1998**

## Report of Independent Accountants

November 20, 1998

The Board of Directors of  
The Council for Tobacco Research - U.S.A., Inc.  
New York, New York:

In our opinion, the accompanying statement of financial position and the related statements of activities and cash flows present fairly, in all material respects, the financial position of THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC. (the "Council") as of October 31, 1998 and the changes in its net assets and its cash flows for the year then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Council's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the opinion expressed above.

As discussed in Note 8 to the financial statements, the Council is in the process of dissolving pursuant to a Plan of Corporate Dissolution and Distribution of Assets (the "Plan of Dissolution"). Under the terms of the Plan of Dissolution the Council may continue to conduct its defense of pending and future-filed lawsuits for a reasonable period of time, after which it will be disbanded and dissolved.

*PricewaterhouseCoopers LLP*

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Statement of Financial Position

October 31, 1998

### ASSETS:

Cash and cash equivalents	\$ 1,634,773
Dues receivable	<u>12,606,715</u>
Total assets	<u>\$ 14,241,488</u>

### LIABILITIES:

Accounts payable and accrued expenses	\$ 5,694,931
Unexpended appropriations for authorized grants and contracts (Note 5)	7,199,843
Postretirement benefits other than pensions (Note 6)	827,000
Accrued closure costs (Note 9)	<u>1,635,523</u>
Total liabilities	15,357,297
Unrestricted net assets	<u>(1,115,809)</u>
Total liabilities and net assets	<u>\$ 14,241,488</u>

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

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Statement of Activities

For the year ended October 31, 1998

### Income:

Dues from members for current year (Note 3)	\$ 38,557,000
Less, Decrease in dues assessed for 1997	<u>(2,377,927)</u>
	36,179,073
Interest	<u>38,663</u>

Total income \$ 36,217,736

### Expenses:

Appropriations for authorized research grants and contracts (Note 5)	11,827,382
Less, Refunds of grants previously appropriated and paid	<u>(120,354)</u>
	11,707,028

### General, administrative and other operating expenses:

Salary, Chairman	350,000
Salary, Secretary	85,833
Expenses, Chairman	47,387
Salaries, Scientific Director and assistants	449,583
Expenses, Scientific Director and assistants	26,401
Per diem allowances and expenses related to activities of Scientific Advisory Board	152,142
Retirement plan (Note 2)	123,969
Postretirement benefits	766,963
Research and analysis	13,086
Printing, booklets, reprints, subscriptions and miscellaneous publications	64,609
Administrative salaries and other services	136,541
Rent and maintenance (Note 7)	305,462
Professional fees	23,555,330
Insurance, group health and other	188,821
Telephone	11,744
Payroll taxes	56,649
Postage, express and messenger service	9,656
Stationery and office supplies	1,225
Bank service charges	23,520
Closure costs (Note 9)	<u>1,635,523</u>

Total expenses 39,711,472

Change in net assets (3,493,736)

Unrestricted net assets, October 31, 1997 2,377,927

Unrestricted net assets, October 31, 1998 \$ (1,115,809)

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

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Statement of Cash Flows

*For the year ended October 31, 1998*

Cash flows from operating activities:	
Change in net assets	\$ (3,493,736)
Adjustments to reconcile change in net assets to net cash used by operating activities:	
Decrease in dues receivable	6,091,449
Increase in accounts payable and accrued expenses	1,983,975
Decrease in unexpended appropriations for authorized grants and contracts	(6,678,200)
Increase in accrued closure costs	1,635,523
Increase in postretirement benefits other than pensions	<u>675,000</u>
Net cash provided by operating activities	<u>214,011</u>
Net increase in cash and cash equivalents	214,011
Cash and cash equivalents at the beginning of the year	<u>1,420,762</u>
Cash and cash equivalents at the end of the year	<u><u>\$ 1,634,773</u></u>

The accompanying notes are an integral part of these financial statement.

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements

### 1. Organization and Policy

The Council is the sponsoring agency of a program of research into questions of tobacco use and health. The Council is the outgrowth of an organization initiated in 1954 by tobacco manufacturers, growers and warehousemen. Research support has been primarily through a program of grants-in-aid, supplemented by contracts for research with institutions and laboratories as well as co-sponsorship of various conferences and meetings. The Council itself does not operate any research facilities.

The Scientific Advisory Board to the Council, a group of distinguished leaders in various fields of biomedical research, meets regularly to evaluate applications for research support. These applications are judged on the basis of scientific merit, topical importance, innovative ideas or methodology, and relevance.

The Council awards research grants to independent scientists who are assured complete scientific freedom in conducting their investigations. Grants are administered by the institution with which the grantee is affiliated. Grantees alone are responsible for reporting their findings in the accepted scientific manner through medical and scientific journals and societies. Publication of research results is encouraged in all instances.

However, since June 1997 the Council has not awarded any new research grants-in-aid, in anticipation of the dissolution of the Council (see Note 8). All appropriations for authorized grants and contracts, expended and unexpended, included in the statement of financial position as of October 31, 1998, and the statement of activities for the year then ended, relate to grants awarded prior to June 1997.

### 2. Summary of Significant Accounting Policies

The significant accounting policies of the Council are summarized below:

- Assets and liabilities, and income and expenses are recognized on the accrual basis of accounting.
- The Council has a defined contribution retirement plan for the benefit of employees, to which employees may contribute. The plan provides for the payment of benefits to all employees (as defined), generally commencing at age 65, with 100% vesting after seven years of service. The Council makes contributions on behalf of each employee equal to 15% of the employee's annual salary. Total pension expense for the year ended October 31, 1998 amounted to \$123,969.

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

- Financial instruments which potentially subject the Council to concentrations of credit risk consist of cash and dues receivable. The Council's cash is deposited with a single, high-quality financial institution. The Council's dues receivable are payable by major cigarette-manufacturers. Management does not believe significant credit risk exists at October 31, 1998.
- The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.
- For purposes of the statement of cash flows, the Council considers all highly liquid investments, with maturities of three months or less when purchased, to be cash equivalents. No such investments were held during fiscal 1998.

### 3. Dues Assessed

The Board of Directors approved a decrease in the dues assessed against the cigarette-manufacturing corporate members for the year ended October 31, 1998. This reduction reflects a decrease in the budgeted grants for the year, following the cessation of new grant awards in June 1997 (see Note 8). Such amount includes the surplus applicable to the year ended October 31, 1997.

### 4. Functional Expense Allocation

The costs of providing research grants and other activities have been summarized on a functional basis. Accordingly, certain costs have been allocated among research grant administration and general administration.

Research grants	\$ 11,707,028
Research grant administration	1,824,860
General administration	<u>26,179,584</u>
	<u>\$ 39,711,472</u>

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

### 5. Unexpended Appropriations for Authorized Grants and Contracts

The change in unexpended appropriations for authorized grants and contracts since October 31, 1997 is as follows:

Balance, October 31, 1997	\$ 13,878,043
Appropriations for authorized research grants and contracts	<u>11,827,382</u>
	25,705,425
Payments, net	<u>18,505,582</u>
Balance, October 31, 1998	<u>\$ 7,199,843</u>

Unexpended appropriations for authorized grants and contracts at October 31, 1998 include \$3,569,000 in respect of unconditional offers issued to certain grantees in final settlement of outstanding grant awards, which would otherwise have extended into the years ended October 31, 1999 and October 31, 2000. The payment of these amounts has been accelerated in accordance the Plan of Dissolution approved on October 21, 1998 (see Note 8 for further details).

### 6. Postretirement Health Benefits

The Council provides certain health care benefits for active and retired employees. These benefits are provided through an insurance company whose premiums are based on the benefits paid during the year.

As of November 1, 1995, the Council adopted Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" ("SFAS 106"). The Council had elected to use the prospective transition approach and was amortizing the transition obligation of \$694,000 over a twenty-year period. However, in anticipation of the dissolution of the Council (see Note 8), which is treated as a SFAS 106 curtailment, the amortization of this transition obligation has been accelerated. Accordingly, all of the remaining transition obligation has been recognized in the current year, which resulted in a net curtailment loss of \$589,000.

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

The following sets forth the plan's funded status reconciled with amounts reported in the Council's statement of financial position as of October 31, 1998:

Accumulated postretirement benefit obligation (APBO):	
Retirees and dependents	\$ (849,000)
Actives fully eligible for benefits	(120,000)
Actives not yet fully eligible	<u>(133,000)</u>
Total APBO	(1,102,000)
Plan assets at fair value	<u>-</u>
APBO in excess of plan assets	(1,102,000)
Unrecognized net (gain) loss	275,000
Unrecognized transition obligation	<u>-</u>
(Accrued)/prepaid postretirement health benefit cost	<u>\$ (827,000)</u>

Net periodic postretirement benefit cost for fiscal 1998 was calculated using a discount rate of 7.25% and included the following components:

Service cost – benefits attributed to service during the period	\$ 21,000
Interest cost on accumulated postretirement benefit obligation	73,000
Net amortization and deferral	<u>48,000</u>
Net periodic postretirement benefit cost	<u>\$ 142,000</u>

An 8.0% annual rate of increase in the per capita costs of covered health care benefits was assumed for fiscal 1999. This rate was assumed to decrease gradually to 5.0% in fiscal 2006 and remain at that level thereafter. Increasing the assumed health care cost trend rates by one percentage point in each year would increase the APBO as of October 31, 1998 by approximately \$82,000 and increase the aggregate of the service cost and interest cost components of net periodic postretirement benefit cost for the year then ended by approximately \$9,000. A discount rate of 6.75% was used to determine the APBO at October 31, 1998.

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

### 7. Lease Commitments

Under the terms of the lease agreement for office space expiring December 31, 2002, the Council is obligated for the payment of annual base rent plus escalation charges. Rent expense amounted to \$305,462 for fiscal 1998. Minimum lease payments under this noncancelable lease are as follows:

<u>Years</u>	<u>Amounts</u>
1999	\$ 297,267
2000	300,125
2001	300,125
2002	300,125
2003	50,021
	<u>\$ 1,247,663</u>

In accordance with the Plan of Dissolution (see Note 8), management of the Council has commenced negotiations with their landlord in an effort to renegotiate their existing lease and thereby minimize their obligations under this agreement.

### 8. Dissolution of the Council

On or about June 20, 1997, the four Class A members of the Council (Brown & Williamson Tobacco Corporation, Lorillard Tobacco Company, Philip Morris Incorporated and R.J. Reynolds Tobacco Company (the "Companies")) entered into a Memorandum of Understanding ("The Memorandum"), dated June 20, 1997, in which the Companies agreed to support a comprehensive resolution of tobacco-related issues that would have, among other things, resulted in the dissolution of the Council. Based on the Memorandum, in June 1997 the Council stopped awarding new research grants-in-aid.

On May 8, 1998, in connection with an action titled Minnesota v. Philip Morris Incorporated, then pending in the District Court for Ramsey County, Minnesota (the "Minnesota Action"), the Companies entered into a Settlement Agreement and Stipulation for Entry of a Consent Judgment, dated May 8, 1998, with the State of Minnesota (the "Minnesota Settlement Agreement"), in which, among other things, the Companies agreed to dissolve the Council and agreed to the entry of a consent judgment in the form attached to the Minnesota Settlement Agreement (the "Minnesota Consent Judgment"), which was entered on May 19, 1998. Section VI of the Minnesota Consent Judgment provides, in part, as follows:

Within 90 days of May 8, 1998, The Council for Tobacco Research - U.S.A., Inc. shall cease all operations except as necessary to comply with existing grants or contracts and to continue its defense of other lawsuits and will be disbanded and dissolved within a reasonable time period thereafter.

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

Promptly after the Companies entered into the Minnesota Settlement Agreement, the Council's Board of Directors and management began to plan for and to take appropriate steps for the dissolution of the Council, consistent with the terms of the Minnesota Settlement Agreement.

At a special meeting of the Council's Board of Directors, on October 19, 1998, the Board of Directors adopted a resolution approving and adopting the Plan of Dissolution. At a special meeting of the Council's members on October 19, 1998, the Council's members also approved and adopted the Plan of Dissolution. On October 21, 1998, the Council filed a petition with the Supreme Court of New York seeking approval of the Plan of Dissolution and a Certificate of Dissolution for the Council (the "Certificate"). On October 21, 1998, that court entered an order approving the Plan of Dissolution and the Certificate. The Certificate was filed with the New York State Department of State of November 6, 1998, and that filing effected the dissolution of the Council under New York law.

### 9. Contingent Liabilities

The Council is now in the process of dissolving and winding up its activities pursuant to the Plan of Dissolution. Under the laws of New York and the terms of the Plan of Dissolution, the Council may continue to conduct its defense of pending and future-filed lawsuits as it sees fit. Accordingly, the Council's dissolution does not affect its ability to continue to defend itself vigorously in all actions filed against it. The Council expects to continue to defend itself vigorously in all pending and future-filed lawsuits.

The Council, together with cigarette manufacturers and others, is a defendant in numerous actions brought by individual plaintiffs (exclusive of the actions brought as class actions, as described below). In some of these cases, plaintiffs allege that one or more of them (or a decedent represented by one or more of them) was injured because such persons contracted one or more diseases as a result of smoking cigarettes; plaintiffs in other cases allege that they or their decedents were injured as a result of exposure to environmental tobacco smoke. In most of these actions, plaintiffs assert that the Council fraudulently and/or negligently misrepresented and/or concealed information regarding the hazards of tobacco and the addictive nature of nicotine. In each of these pending cases, plaintiffs seek compensatory and punitive damages, in some cases in unspecified amounts and in other cases in very substantial amounts that are specified.

The Council, together with cigarette manufacturers and others, is also a defendant in various cases brought as class actions in which plaintiffs allege various causes of action against the Council and seek various forms of relief. Classes have been certified in some of these cases, although the courts have refused to certify classes in a number of classes. Relief sought includes compensatory and punitive damages. Plaintiffs in certain of these actions (like those individual actions described above) allege personal injury. Plaintiffs in other putative class

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

actions seek the reimbursement of costs paid by consumers to purchase cigarettes and costs for continued medical monitoring.

The Council, together with cigarette manufacturers and others, is also a defendant in pending actions brought by the attorneys general (and/or other agencies and officers) of certain states and Puerto Rico. These actions seek various forms of relief, including money damages (including recovery of amounts allegedly spent by the states and Puerto Rico for medical expenses of persons who smoked cigarettes and payment of future such expenses on an ongoing basis), together with treble damages and punitive damages, injunctive relief (including the funding of smoking cessation programs and public education programs, injunctions against certain marketing practices and the marketing of cigarettes to minors, the provision of nicotine replacement therapy, the funding of agricultural programs for non-tobacco crops, and disclosures about the nature and effects of tobacco), disgorgement of profits from the sale of cigarettes, reimbursement for the costs of medical monitoring and restitution of amounts allegedly spent by plaintiffs because of defendants' unlawful conduct.

Actions brought by the states of Mississippi, Florida, Texas and Minnesota have been dismissed pursuant to settlements. In these cases, the Council was released from all liabilities as part of the settlements; the Council did not make, and is not obligated to make, any payment in respect of these settlement agreements.

The Council, together with cigarette manufacturers and others, is a defendant in three actions in one state brought as "private attorney general" actions seeking to enjoin certain alleged unlawful business practices under that State's Business and Professions Code. Relief sought includes a variety of injunctive relief, such as corrective advertising and smoking cessation programs, as well as disgorgement and restitution. The Council, together with the cigarette manufacturers and others, is also a defendant in a fourth action brought by taxpayers as "private attorneys general" in Tennessee in which the plaintiff seeks relief similar to that sought in the actions brought by the attorneys general of certain states described above.

The Council, together with cigarette manufacturers and others, is also a defendant in a number of actions brought by pension/trust funds and other similar entities whose purpose is to provide health and related benefits to their beneficiaries and members. These actions seek money damages to recover costs paid by the funds for health care costs allegedly arising from the detrimental use of tobacco products by their members and other related relief similar to that sought in the class actions discussed above.

The Council, together with cigarette manufacturers and others, is a defendant in three actions brought by certain asbestos companies and in one action brought by the trustees of a trust created for the purpose of processing claims asserted against another asbestos company. In these actions, the plaintiffs allege that the personal injuries of persons who have brought claims against the asbestos companies were contributed to or caused by smoking, and they seek contributions and/or indemnity from the Council for an unidentified portion of the

# THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.

## Notes to Financial Statements, Continued

amounts paid to such claimants in judgments or settlements. The plaintiffs assert claims against the Council based on negligence, strict liability and fraud.

The Council, together with cigarette manufacturers and others, is a defendant in an action brought by the Republic of the Marshall Islands pending in that government's High Court. The Council is also a defendant in an action filed by the Republic of Guatemala in the United States District Court for the District of Columbia. The Republic of the Marshall Islands and the Republic of Guatemala seek damages for money that has been and will be spent for health care expenditures on their citizens for treatment of diseases and illnesses associated with tobacco products, as well as other forms of relief similar to those sought in the states' actions discussed above.

On August 27, 1998, two orders were issued by the Judicial Council of California coordinating several pending California State actions, in which plaintiffs filed similar claims. These actions were coordinated into two groups due to the similarities of plaintiff's claims. These coordination groups will be referred to as Tobacco Cases Land Tobacco Cases II, and they consist of actions brought by countries, private attorneys general, class representatives and private individuals.

The Council intends to continue to contest vigorously the claims brought against it. The Council cannot predict the outcome of the litigation at this time.

### **Other commitments**

Commitments of the Council include not only the grants outstanding, but also certain commitments with respect to certain benefits of its employees. These obligations must be met over a number of years into the future, and accordingly, the Council has taken appropriate measures to see to it that these obligations are met.

In particular, the Plan of Dissolution includes a provision that requires the Council to cause a trust to be created for the payment of the Council's ongoing obligations to current and former employees in respect to certain health insurance benefits. The impact of this requirement has been reflected in the calculation of the Council's postretirement health benefit obligation as set out in Note 6.

In addition, under the terms of the Plan of Dissolution, the Council intends to make payments to all of its existing employees, and two former employees, during the year ended October 31, 1999, in compensation for prior services rendered to the Council, and in contemplation of the early termination of their employment. Management has estimated that the total payments under this program will be approximately \$1,636,000, and this amount has been recognized in the fiscal 1998 financial statements.

# **THE COUNCIL for TOBACCO RESEARCH - U.S.A., INC.**

## **Notes to Financial Statements, Continued**

### **10. Taxation**

The Council is a nonprofit organization exempt from Federal income taxes under Section 501(c)(6) of the Internal Revenue Code.