

**MONROE TOBACCO ASSET
SECURITIZATION CORPORATION
(A Blended Component Unit of the
County of Monroe, New York)**

**Basic Financial Statements
as of December 31, 2010 and 2009
Together with
Independent Auditors' Report**

MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)

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INDEPENDENT AUDITORS' REPORT

March 15, 2011

To the Board of Directors of the
Monroe Tobacco Asset Securitization Corporation:

We have audited the accompanying financial statements of the governmental activities and major fund of the Monroe Tobacco Asset Securitization Corporation (MTASC), a blended component unit of the County of Monroe, New York, as of and for the years ended December 31, 2010 and 2009, which collectively comprise MTASC's basic financial statements as listed in the table of contents. These financial statements are the responsibility of MTASC's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits 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. Those standards 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. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and major fund of the Monroe Tobacco Asset Securitization Corporation as of December 31, 2010 and 2009, and the respective changes in financial position 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 March 15, 2011, on our consideration of the Monroe Tobacco Asset Securitization Corporation's internal control over financial reporting and on 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.

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INDEPENDENT AUDITORS' REPORT

(Continued)

Accounting principles generally accepted in the United States require that the management's discussion and analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

**MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
DECEMBER 31, 2010 AND 2009**

The following Management's Discussion and Analysis (MD&A) provides a comprehensive overview of the Monroe Tobacco Asset Securitization Corporation's (MTASC) financial position as of December 31, 2010 and 2009 and its changes in financial position for the years then ended. This MD&A should be read in conjunction with the financial statements and related footnotes of MTASC, which directly follow the MD&A.

General Overview

MTASC is a special purpose, bankruptcy remote local development corporation organized under the Not-For-Profit Corporation Laws of the State of New York (the State). MTASC was established on May 11, 2000; however, there were no substantive operations until August 15, 2000. MTASC is an instrumentality of, but separate and apart from the County of Monroe, New York (the County). Pursuant to a Purchase and Sale Agreement with the County, the County sold to MTASC all of its future rights, title and interest in the Tobacco Settlement Revenues (TSRs) under the Master Settlement Agreement (MSA) and the Decree and Final Judgment (the Decree). The MSA resolved cigarette smoking related litigation between the settling states and the Participating Manufacturers (PMs), released the PMs from past and present smoking related claims, and provided for a continuing release of future smoking related claims, in exchange for certain payments to be made to the settling states, as well as certain tobacco advertising and marketing restrictions, among other things. The Decree, which was entered by the Supreme Court of the State, allocated to the County a share of the TSRs under the MSA. The future rights, title and interest of the County's share were sold to MTASC and were financed by the issuance of bonds.

Overview of the Financial Statements

The financial statements of MTASC have been prepared in accordance with accounting principles generally accepted in the United States as prescribed by the Governmental Accounting Standards Board. The financial statement presentation consists of the following four basic financial statements:

- Statement of Net Assets (Deficit)
- Statement of Activities and Changes in Net Assets (Deficit)
- Governmental Fund Balance Sheet
- Statement of Governmental Fund Revenues, Expenditures and Change in Fund Balance

The Statement of Net Assets (Deficit) and the Statement of Activities and Change in Net Assets (Deficit) are prepared using the economic resource measurement focus and the accrual basis of accounting. Revenues, expenses, assets and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place. Revenues, expenses, assets and liabilities resulting from non-exchange transactions are recognized when the amounts to be received are measurable and collection is probable. The Governmental Fund Balance Sheet and the Statement of Governmental Fund Revenues, Expenditures and Change in Fund Balance are presented using the current financial resources measurement focus and the modified accrual basis of accounting. These policies are more fully described in the accompanying notes to the basic financial statements.

The Statement of Net Assets (Deficit) presents all of MTASC's asset and liability information, with the difference between the two reported as net assets. Fluctuations in net assets can be a useful indicator of MTASC's financial position. Restricted net assets are those that are restricted based on externally imposed conditions and consist of funds in the debt service and liquidity reserve accounts. These accounts were established to provide for debt service payments for at least one year in the event of insufficient revenues. All other net assets are considered unrestricted.

Overview of the Financial Statements (Continued)

The Statement of Activities and Change in Net Assets (Deficit) presents all of MTASC's revenues, both program and general, expenses, and transfers.

The Governmental Fund Balance Sheet presents MTASC's assets, liabilities and fund balance. This statement uses the debt service fund, a governmental fund type, to report its financial position.

The Statement of Governmental Fund Revenues, Expenditures and Change in Fund Balance presents the changes in financial position of the debt service fund.

Financial Highlights

MTASC reported liabilities in excess of assets of \$214.82 million as of December 31, 2010. This was an increase of \$4.0 million from the prior year.

The Series 2005C Bonds (taxable) were replaced with the Series 2010A Bond (tax-exempt) on June 1, 2010. MTASC made the 2010 debt service payments with the TSRs received. There were no new debt obligations issued during 2010.

Condensed Statement of Net Assets (Deficit) (In millions)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Total assets	\$ <u>31.48</u>	\$ <u>32.06</u>	\$ <u>31.59</u>
Bonds payable	226.67	227.39	230.28
Other liabilities	<u>19.63</u>	<u>15.50</u>	<u>11.63</u>
Total liabilities	<u>246.30</u>	<u>242.89</u>	<u>241.91</u>
Net deficit	\$ <u>(214.82)</u>	\$ <u>(210.83)</u>	\$ <u>(210.32)</u>

Total Assets

The total assets decreased \$0.6 million from 2009 to 2010 (\$32.1 million and \$31.5 million, respectively). The decrease in total assets from 2009 to 2010 was primarily due to a decrease in accounts receivable of \$0.5 million and a decrease in restricted cash and cash equivalents of \$0.1 million. The decrease in accounts receivable was the result of anticipated 2011 TSR's being less than those that were expected in 2010. The decrease in restricted cash and investments is primarily due to a reduction in Debt Service requirements on the Series 2005 Bonds. The decrease in bond issuance cost from 2009 to 2010 was the result of amortization of costs incurred in connection with the issuance of the Series 2005 Bonds and Series 2006 Bonds offset by the addition of the Series 2010A Bond issuance costs. The total assets increased from 2008 to 2009 by \$0.5 million, \$31.6 million and \$32.1 million, respectively primarily due to an increase in accounts receivable.

Total Liabilities

The total liabilities increased by \$3.4 million from 2009 to 2010. This increase is due to accrued interest payable on outstanding bonds increasing from \$15.5 million in 2009 to \$19.6 million in 2010, offset by a decrease in bonds payable from \$227.4 million in 2009 to \$226.7 million in 2010. The increase in total liabilities from 2008 to 2009 of \$1.0 million was due to the increase in accrued interest payable on outstanding bonds (approximately \$3.9 million) and a decrease in bonds payable (approximately \$2.9 million).

**Condensed
Statement of Activities and Change in Net Assets (Deficit)**
(In millions)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Total expenses	\$ 14.66	\$ 14.66	\$ 14.57
Program revenues - tobacco settlement	<u>10.67</u>	<u>14.15</u>	<u>12.54</u>
Net program revenue	(3.99)	(0.51)	(2.03)
General revenues - investment income	<u>0.00</u>	<u>0.00</u>	<u>0.51</u>
Change in net assets	(3.99)	(0.51)	(1.52)
Net deficit - beginning of year	<u>(210.83)</u>	<u>(210.32)</u>	<u>(208.80)</u>
Net deficit - end of year	<u>\$ (214.82)</u>	<u>\$ (210.83)</u>	<u>\$ (210.32)</u>

Expenses

Expenses incurred in 2010 were unchanged from those incurred in 2009. Expenses incurred in 2009 were also virtually unchanged when compared to those incurred in 2008.

Revenues

Program revenues recorded during 2010 were down by \$3.5 million over those recorded in 2009. Investment income was minimal due to the historic low interest rates. Total revenues recorded during 2009 increased by \$1.1 million over those recorded in 2008. The increase was due to increased TSR's of \$1.6 million offset by a decrease of \$0.5 million in the market value of securities held at December 31, 2009 and 2008.

Financial Analysis of MTASC's Fund Financial Statements

The focus of MTASC's governmental fund reporting is to provide information on near-term inflows, outflows and balances of spendable resources.

As of December 31, 2010, MTASC's debt service fund reported fund balances of \$13.6 million, virtually unchanged from the prior year. Approximately \$0.4 million of fund balance is unreserved fund balance and is available for MTASC's future needs. The remainder of fund balance is reserved to indicate that it is not available for spending because it has already been committed to pay future debt service and fund bond issuance costs.

As of December 31, 2009, MTASC's debt service fund reported an ending fund balance of \$13.6 million, a decrease of \$0.2 million from the prior year due to a decrease in the debt service account. Approximately \$0.3 million of the fund balance was unreserved with the remaining balance to be used to fund MTASC's future debt service and fund bond issuance costs.

Debt

Debt obligations of MTASC as of December 31, 2010 consist of the remaining balance of the MTASC Series 2005 Tobacco Settlement Asset-Backed Bonds, the Series 2006 Tobacco Settlement Asset-Backed Bonds and the Series 2010 Tobacco Settlement Asset-Backed Bonds. The proceeds of the Series 2005 Bonds were used to advance refund/defease the remaining outstanding Series 2000 Bonds, make a payment to the Trust, and to pay related costs of issuance of the Series 2005 Bonds. The total amount of the Series 2005 Bonds, Series 2006 Bonds and Series 2010 Bonds outstanding at December 31, 2010 was \$226.7 million. None of the outstanding Series 2005 Bonds, Series 2006 Bonds or Series 2010 Bonds was considered current since none were due within twelve months of year-end. The Series 2006 Bonds were not rated as MTASC did not apply for, and the rating agencies have not issued, a rating for the bonds. The Series 2005 Bonds were not rated since they were sold to the New York Counties Tobacco Trust IV, a trust established by participating local development corporations, including MTASC. The Series 2005 Bonds were structured, however, to enable the New York Counties Tobacco Trust IV bonds to attain the following ratings:

<u>Bond Series</u>	<u>Standard & Poor's</u>	<u>Fitch</u>
2005A	BBB -	BBB
2005B	BBB -	BBB
2005D (CABS)	Non-rated	BBB -
2005E (CABS)	Non-rated	BB
2005F (CABS)	Non-rated	Non-rated
2010A	Non-rated	BBB

MTASC entered into a forward purchase contract in connection with the issuance of Tobacco Settlement Asset-Backed Bonds, Series 2010A to be in an amount equal to the amount of Series 2005C Bonds outstanding on the date of issuance of the Series 2010A Bonds. The Series 2005C Bonds were replaced by the Series 2010A Bonds on June 1, 2010 with a maturity date of June 1, 2041 and an interest rate of 6.25%.

All of MTASC's turbo bonds are subject to prepayment from Turbo Redemption Payments. Turbo Redemption Payments are made from collections (other than partial and lump sum payments) in excess of the amount needed to pay certain operating expenses. To the extent possible, the Turbo Redemption Payments will amortize the Series 2005 Bonds, Series 2006 Bonds and Series 2010 Bonds earlier than their maturity dates at their accreted values. Payments of \$720,000 and \$2,890,000 were made in 2010 and 2009, respectively, against the Series 2005 Bonds.

Payments on the outstanding capital appreciation bonds are based on the accreted value of the capital appreciation bonds at their stated maturity. The accretion of these capital appreciation bonds over their life results in the recognition of substantial annual costs until the capital appreciation bonds are redeemed. Reference should be made to the Bonds Payable footnote in the financial statements for a summary of the required principal and interest (which includes accretion of the capital appreciation bonds) payments.

Details on the debt outstanding is provided in Note 4 to the basic financial statements.

Contacting Monroe Tobacco Asset Securitization Corporation's Management

This financial report is designed to provide a general overview of MTASC's finances and to demonstrate MTASC's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Treasurer, Monroe Tobacco Asset Securitization Corporation, 39 West Main Street, Room 400, Rochester, New York, 14614.

MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)

STATEMENT OF NET ASSETS (DEFICIT)
DECEMBER 31, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
ASSETS		
Cash and cash equivalents	\$ 357,266	\$ 283,448
Accrued interest receivable	100	99
Accounts receivable	11,659,163	12,133,986
Restricted cash and cash equivalents	13,206,430	13,342,974
Bond issuance costs, net	6,249,690	6,301,490
Prepaid expenses	2,023	1,722
	<hr/>	<hr/>
Total assets	31,474,672	32,063,719
	<hr/>	<hr/>
LIABILITIES		
Accrued interest payable	19,628,473	15,502,895
Bonds payable	226,669,794	227,389,794
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Total liabilities	246,298,267	242,892,689
	<hr/>	<hr/>
NET ASSETS (DEFICIT)		
Restricted for:		
Debt service	12,876,326	12,942,906
Other purposes	330,104	400,068
Unrestricted	(228,030,025)	(224,171,944)
	<hr/>	<hr/>
Total net assets (deficit)	\$ (214,823,595)	\$ (210,828,970)
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The accompanying notes are an integral part of these statements.

MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)

STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS (DEFICIT)
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
EXPENSES:		
General government -		
Materials and services	\$ 68,734	\$ 80,707
Administrative costs	30,554	30,500
Interest and amortization	<u>14,571,028</u>	<u>14,553,568</u>
Total expenses	14,670,316	14,664,775
PROGRAM REVENUE:		
Tobacco settlement	<u>10,673,996</u>	<u>14,152,279</u>
Net program revenues	(3,996,320)	(512,496)
GENERAL REVENUES - INVESTMENT INCOME	<u>1,695</u>	<u>3,391</u>
CHANGE IN NET ASSETS	(3,994,625)	(509,105)
NET DEFICIT - beginning of year	<u>(210,828,970)</u>	<u>(210,319,865)</u>
NET DEFICIT - end of year	<u>\$ (214,823,595)</u>	<u>\$ (210,828,970)</u>

The accompanying notes are an integral part of these statements.

MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)

GOVERNMENTAL FUND BALANCE SHEET
DECEMBER 31, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
ASSETS		
Cash and cash equivalents	\$ 357,266	\$ 283,448
Accrued interest receivable	100	99
Accounts receivable	11,659,163	12,133,986
Restricted cash and cash equivalents	13,206,430	13,342,974
Prepaid expenses	<u>2,023</u>	<u>1,722</u>
Total assets	<u>\$ 25,224,982</u>	<u>\$ 25,762,229</u>
LIABILITIES AND FUND BALANCES		
LIABILITIES:		
Deferred revenue	<u>\$ 11,659,163</u>	<u>\$ 12,133,986</u>
Total liabilities	<u>11,659,163</u>	<u>12,133,986</u>
FUND BALANCES:		
Reserved for -		
Debt service	12,876,326	12,942,906
Other purposes	330,104	400,068
Unreserved - undesignated	<u>359,389</u>	<u>285,269</u>
Total fund balances	<u>13,565,819</u>	<u>13,628,243</u>
Total liabilities and fund balances	<u>\$ 25,224,982</u>	<u>\$ 25,762,229</u>
Amounts reported for governmental activities in the statement of net assets (deficit) are different because:		
Total fund balances	\$ 13,565,819	\$ 13,628,243
Tobacco settlement revenue was not received in the current period and therefore, is not reported as revenues at the fund level	11,659,163	12,133,986
Bonds payable and accrued interest are not due and payable in the current period and therefore, are not reported at the fund level	(246,298,267)	(242,892,689)
Certain items, including bond issuance costs, premiums and original issue discount are fully expensed in the governmental fund statement, but amortized over a period of time in the statement of activities	<u>6,249,690</u>	<u>6,301,490</u>
Total net deficit	<u>\$ (214,823,595)</u>	<u>\$ (210,828,970)</u>

The accompanying notes are an integral part of these statements.

MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)

**STATEMENT OF GOVERNMENTAL FUND REVENUES, EXPENDITURES AND
CHANGE IN FUND BALANCE
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	<u>2010</u>	<u>2009</u>
REVENUES:		
Tobacco settlement	\$ 11,148,819	\$ 13,396,788
Investment income	<u>1,695</u>	<u>3,391</u>
Total revenues	<u>11,150,514</u>	<u>13,400,179</u>
EXPENDITURES:		
General and administrative	68,734	80,707
Bond issuance and administration costs	100,554	30,500
Debt service - principal	720,000	2,890,000
Debt service - interest	<u>10,323,650</u>	<u>10,558,150</u>
Total expenditures	<u>11,212,938</u>	<u>13,559,357</u>
NET CHANGE IN FUND BALANCES	(62,424)	(159,178)
FUND BALANCES - beginning of year	<u>13,628,243</u>	<u>13,787,421</u>
FUND BALANCES - end of year	<u>\$ 13,565,819</u>	<u>\$ 13,628,243</u>
Amounts reported for governmental activities in the statements of activities are different because:		
Net change in fund balances	\$ (62,424)	\$ (159,178)
Tobacco settlement revenues reported in the statement of activities were not received in time to pay current financial obligations and therefore, have not been reported as revenue in the governmental fund	(474,823)	755,491
Certain expenses reported in the statement of activities (amortization of bond issuance costs, premiums and interest) do not require the use of current financial resources and therefore, are not reported as expenditures in the governmental fund	(51,800)	(121,800)
The net effect of bond proceeds received, repayments of the Series 2005 and 2006 bonds and interest expense are activities of the governmental fund but not reported in the statement of activities	<u>(3,405,578)</u>	<u>(983,618)</u>
Change in net assets (deficit)	<u>\$ (3,994,625)</u>	<u>\$ (509,105)</u>

The accompanying notes are an integral part of these statements.

**MONROE TOBACCO ASSET SECURITIZATION CORPORATION
(A Blended Component Unit of the County of Monroe, New York)**

**NOTES TO BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

1. ORGANIZATION

Monroe Tobacco Asset Securitization Corporation (MTASC) is a special purpose, bankruptcy remote local development corporation organized under the Not-For-Profit Corporation Law of the State of New York (the State). MTASC was established on May 11, 2000; however, there were no substantive operations until August 15, 2000 as discussed herein. The Corporation is an instrumentality of, but separate and apart from the County of Monroe, New York (the County). MTASC will have not less than three nor more than five directors, consisting of two ex-officio positions including the Executive of the County and the Director of Finance - Chief Financial Officer of the County, up to two additional directors and one independent director. Although legally separate from the County, MTASC is a component unit of the County and, accordingly, is included in the County's basic financial statements as a blended component unit.

On August 15, 2000, pursuant to a Purchase and Sale Agreement with the County, the County sold to MTASC all of its future rights, title and interest in the Tobacco Settlement Revenues (TSRs) under the Master Settlement Agreement (MSA) and the Decree and Final Judgment (the Decree). The MSA resolved cigarette smoking related litigation between the settling states and the Participating Manufacturers (PMs), released the PMs from past and present smoking related claims, and provides for a continuing release of future smoking related claims, in exchange for certain payments to be made to the settling states, as well as certain tobacco advertising and marketing restrictions, among other things. The Decree, which was entered by the Supreme Court of the State, allocated to the County a share of the TSRs under the MSA. The future rights, title and interest of the County's share were sold to MTASC.

MTASC's purchase of the County's future rights, title and interest in the TSRs was financed by the issuance of bonds. A Residual Certificate exists that represents the County's entitlement to receive all amounts required to be distributed after payment of debt service, operating expenses, and certain other costs by MTASC as set forth in the Amended and Restated Indenture (the Indenture). Payments on the Residual Certificate from TSR collections are subordinate to payments on the bonds and payment of certain other costs specified in the Indenture. Excess TSRs not required by MTASC to pay various expenses, debt service or required reserves with respect to the bonds are transferred to the Monroe Tobacco Tax Stabilization Trust (the Trust), as owner of the Residual Certificate. The County is the beneficial owner of the Trust and thus the funds received by the Trust will ultimately transfer to the County.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

MTASC's financial statements are prepared in conformity with accounting principles generally accepted in the United States as prescribed by the Governmental Accounting Standards Board (GASB). MTASC's government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus, Basis of Accounting, and Financial Statement Presentation (Continued)

Private sector Standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent they do not conflict or contradict guidance of GASB.

MTASC's fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, MTASC considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures and claims and judgments, are recorded only when payment is due.

The major governmental fund is the Debt Service Fund. The Debt Service Fund accounts for the resources accumulated and payments made for operations and principal debt service on long-term general obligation debt.

Net Assets (Deficit)

Generally accepted accounting principles require that resources be classified for accounting purposes into applicable net asset categories.

Unrestricted net assets are net assets that are not restricted, but which may be internally designated by the Board of Directors. At December 31, 2010 and 2009, the amount of unrestricted net assets (deficit) were (\$228.0) million and (\$224.2) million respectively, of which none were internally designated.

Net assets are reported as restricted when constraints placed on net asset use are either externally imposed by creditors, grantors, contributors, laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. Restricted net assets of MTASC are those net assets that are restricted based on externally imposed conditions and include amounts restricted for debt service and bond issuance and rebate costs.

MTASC has adopted a practice of generally utilizing its restricted net assets when available, prior to unrestricted net assets.

Cash and Cash Equivalents

MTASC considers bank deposit accounts and all highly liquid debt instruments with remaining maturities, when purchased, of 10 months or less to be cash equivalents and these are stated at fair value. MTASC maintains a liquidity reserve account, which was initially funded from the Series 2000 Bond proceeds and has been increased by funds from the Series 2005 Bonds. This account must be maintained at a minimum of \$12,849,750 until such time that all bonds, other than subordinated bonds, are paid. All amounts withdrawn from this account are replenished, as needed, and amounts in excess of the required amount are transferred out. This account is included in restricted cash and cash equivalents on the balance sheet.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred Bond Issuance Costs, Original Issue Discount and Bond Premium

MTASC recognizes bond premium, original issue discount and issuance costs fully in the year of issuance for the governmental fund statements. These costs are amortized on the straight line basis over the term of the related bonds for the government-wide financial statements as additional interest expense.

	<u>2010</u>	<u>2009</u>
Series 2005	\$ 6,051,797	\$ 6,051,797
Series 2006	769,000	769,000
Series 2010	<u>70,000</u>	<u>-</u>
Subtotal	6,890,797	6,820,797
Accumulated amortization	<u>(641,107)</u>	<u>(519,307)</u>
Total	<u>\$ 6,249,690</u>	<u>\$ 6,301,490</u>

Amortization expense was \$121,800 for the years ended December 31, 2010 and 2009. MTASC recognizes all interest paid as interest expenditures on the modified accrual basis for the governmental fund statements and all interest incurred as expenses on the full accrual basis for the government-wide financial statements.

Deferred Revenue

Deferred revenue represents amounts earned under the modified accrual basis of accounting used in the Debt Service Fund, but not meeting the definition of available for use.

Income Taxes

MTASC is a not-for-profit corporation and is exempt from income taxes as an organization qualified under Section 501(c)(3) of the Internal Revenue Code. MTASC has also been classified by the Internal Revenue Service as an entity that is not a private foundation.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

3. DEPOSITS AND INVESTMENTS

Investment and Deposit Policy

MTASC follows an investment and deposit policy as outlined in the Indenture, the overall objective of which is to adequately safeguard the principal amount of funds invested or deposited; conformance with federal, state and other legal requirements; provide sufficient liquidity of invested funds in order to meet obligations as they become due; and attainment of a market rate of return. Oversight of investment activity is the responsibility of the Treasurer of MTASC.

Interest Rate Risk

Interest rate risk is the risk that the fair value of investments will be affected by changing interest rates. MTASC does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

3. DEPOSITS AND INVESTMENTS (Continued)

Credit Risk

MTASC's policy is to minimize the risk of loss due to failure of an issuer or other counterparty to an investment to fulfill its obligations. MTASC's investment and deposit policy authorizes the reporting entity to purchase the following types of investments:

- Obligations of the United States of America;
- Obligations guaranteed by the United States of America where payment of principal and interest are guaranteed by the United States of America;
- Obligations of the State of New York;
- Special time deposit accounts;
- Certificates of deposit;
- Commercial paper;
- Repurchase agreements limited to obligations of the United States of America, or obligations whose principal and interest are fully guaranteed, or insured by the United States of America. The term of each agreement shall generally not exceed 180 days. The agreement shall be confirmed in writing by the seller, and each security purchased under the agreement shall be specifically identified; segregated from the assets of the seller and delivered for safekeeping into an account designated and controlled by MTASC. Also, each seller shall enter into a master Repurchase Agreement with MTASC which shall specify the rights and obligations of MTASC and the Seller in all transactions;
- Obligations of public authorities, public housing authorities, urban renewal agencies, and industrial development agencies where the general State statutes governing such entities or whose specific enabling legislation authorizes such investments; and
- Obligations issued pursuant to New York State Local Finance Law Section 24.00 and 25.00 (with approval of the New York State Comptroller) by any municipality, school district or district corporation other than MTASC.

Custodial Credit Risk - Deposits

Custodial credit risk - deposits is the risk that in the event of a failure of a depository financial institution, the reporting entity may not recover its deposits. In accordance with the Corporation's investment and deposit policy, all deposits of MTASC including certificates of deposit and special time deposits, in excess of the amount insured under the provisions of the Federal Deposit Insurance Act (FDIA) shall be secured by a pledge of securities with an aggregate value equal to the aggregate amount of deposits. MTASC restricts the securities to the following eligible items:

- Obligations issued, or fully insured or guaranteed as to the payment of principal and interest, by the United States of America, an agency thereof or a United States government sponsored corporation;
- Obligations issued or fully guaranteed by the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, and the African Development Bank;
- Obligations partially insured or guaranteed by any agency of the United States of America;
- Obligations issued or fully insured or guaranteed by the State of New York;
- Obligations issued by a municipal corporation, school district or district corporation of New York State;
- Obligations of any public benefit corporation, which under a specific State statute may be accepted as security for deposit of public monies;
- Obligations issued by states (other than the State of New York) of the United States rated in one of the two highest rating categories by at least one Nationally Recognized Statistical Rating Organization (NRSRO);
- Obligations of Puerto Rico rated in the highest rating category by at least one NRSRO;

3. DEPOSITS AND INVESTMENTS (Continued)

Custodial Credit Risk - Deposits (Continued)

- Obligations of counties, cities and other governmental entities of a state other than the State of New York having the power to levy taxes that are backed by the full faith and credit of such governmental entity and rated in one of the two highest categories by at least one NRSRO;
- Obligations of domestic corporations rated in one of the two highest rating categories by at least one NRSRO; and
- Zero coupon obligations of the United States of America marketed as “treasury strips.”

As of December 31, 2010 and 2009, the carrying amount of MTASC’s cash and cash equivalents was \$357,266 and \$283,448, respectively, and was exposed to custodial credit risk as follows:

	<u>2010</u>	<u>2009</u>
Federal Depository Insurance Coverage	\$ <u>357,266</u>	\$ <u>283,448</u>

Custodial Credit Risk - Investments

Custodial credit risk - investments is the risk that an entity will not be able to recover the value of an investment or collateral securities that are in the possession of an outside party if the counterparty to the transaction fails. MTASC’s investment and deposit policy requires that all custodial investments be registered or insured in MTASC’s name and held in the custody of the bank or the bank’s trust department. MTASC requires that all repurchase agreements be limited to obligations of the United States of America or obligations whose principal and interest are fully guaranteed, or insured by the United States of America. As of December 31, 2010 and 2009, MTASC’s investments, with maturities of less than one year, were in compliance with the investment and deposit policy as follows:

<u>Investment Type</u>	<u>2010</u>	<u>2009</u>
Money market fund (U.S. Treasuries)	\$ <u>13,206,430</u>	\$ <u>13,342,974</u>

Concentration of Credit Risk

MTASC places no limit on the amount that may be invested in any one investment type. At December 31, 2010 and 2009 the Corporation’s investments were invested in money market funds.

Restricted Cash and Cash Equivalents

MTASC had the following restricted funds as of December 31:

<u>Restricted Cash and Cash Equivalents</u>	<u>2010</u>	<u>2009</u>
Liquidity reserves	\$ 12,849,856	\$ 12,849,857
Debt service reserves	26,470	93,049
Bond issuance and rebate costs	<u>330,104</u>	<u>400,068</u>
Total	\$ <u>13,206,430</u>	\$ <u>13,342,974</u>

4. BONDS PAYABLE

The Series 2005 and Series 2010 Bonds are secured by a perfected security interest in, and pledge of, the Trust Estate, as defined in the Indenture, which includes, among other things, the TSRs and all investment earnings on amounts on deposit in the accounts established under the Indenture (collectively, the Collections). Among the accounts so established are the Liquidity Reserve Account and the Debt Service Account. MTASC retains TSRs in an amount sufficient to service its debt and pay its operating expenses. The Series 2006 Bonds are subordinate to the Series 2005 Bonds and Series 2010 Bonds.

MTASC entered into a forward purchase contract in connection with the issuance of Tobacco Settlement Asset-Backed Bonds, Series 2010A (Tax Exempt Turbo Term Bonds) to be in an amount equal to the amount of Series 2005C Bonds outstanding on the date of issuance of the Series 2010A Bonds. The Series 2005C Bonds were replaced by the Series 2010A Bonds on June 1, 2010 with a maturity date of June 1, 2041 and an interest rate of 6.25%.

The Series 2006 Bonds are composed of the following:

- \$14,579,370 Tobacco Settlement Asset-Backed Bonds, Series 2006A (Tax Exempt Turbo Capital Appreciation Bonds), maturity date is June 1, 2061, interest rate of 0.00%, with an accreted value at maturity of \$952,900,000.

The Series 2005 Bonds are composed of the following:

- \$91,120,000 Tobacco Settlement Asset-Backed Bonds, Series 2005A (Tax Exempt Turbo Bonds), maturity date is June 1, 2042, interest rate of 5.00%.
- \$36,665,000 Tobacco Settlement Asset-Backed Bonds, Series 2005B (Taxable Turbo Bonds), maturity date is June 1, 2027, interest rate of 6.00% (\$27,935,000 principal amount remains outstanding as of December 31, 2010 as a result of Turbo Redemption payments which have been made since 2006).
- \$5,386,580 Tobacco Settlement Asset-Backed Bonds, Series 2005D (Tax Exempt Turbo Capital Appreciation Bonds), maturity date is June 1, 2050, interest rate of 0.00%, with an accreted value at maturity of \$71,965,000.
- \$8,923,514 Tobacco Settlement Asset-Backed Bonds, Series 2005E (Tax Exempt Turbo Capital Appreciation Bonds), maturity date is June 1, 2055, interest rate of 0.00%, with an accreted value at maturity of \$202,715,000.
- \$15,625,329 Tobacco Settlement Asset-Backed Bonds, Series 2005F (Tax Exempt Turbo Capital Appreciation Bonds), maturity date is June 1, 2060, interest rate of \$0.00%, with an accreted value at maturity of \$608,700,000.

The Series 2010 Bonds are composed of the following:

- \$63,100,000 Tobacco Settlement Asset-Backed Bonds, Series 2010A (Tax Exempt Turbo Term Bonds), maturity date is June 1, 2041 with an interest rate of 6.25%.

Long-term indebtedness for the Corporation's bonds payable consisted of the following:

	<u>2010</u>	<u>2009</u>
Balance - beginning of year	\$ 227,389,794	\$ 230,279,794
Repayments of bonds	<u>(720,000)</u>	<u>(2,890,000)</u>
Balance - end of year	<u>\$ 226,669,794</u>	<u>\$ 227,389,794</u>
Payments due within one year	<u>\$ -</u>	<u>\$ -</u>

4. BONDS PAYABLE (Continued)

Principal and interest payments (including accretion on capital appreciation bonds) based upon the required maturities are as follows for the years ended December 31:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2011	\$ -	\$ 10,175,850	\$ 10,175,850
2012	-	10,175,850	10,175,850
2013	-	10,175,850	10,175,850
2014	-	10,175,850	10,175,850
2015	-	10,175,850	10,175,850
2016 - 2020	-	50,879,250	50,879,250
2021 - 2025	-	50,879,250	50,879,250
2026 - 2030	27,935,000	45,012,900	72,947,900
2031 - 2035	-	42,498,750	42,498,750
2036 - 2040	-	42,498,750	42,498,750
2041 - 2045	154,220,000	14,125,625	168,345,625
2046 - 2050	5,386,580	66,578,420	71,965,000
2051 - 2055	8,923,514	193,791,486	202,715,000
2056 - 2060	15,625,330	593,074,670	608,700,000
2061	<u>14,579,370</u>	<u>938,320,630</u>	<u>952,900,000</u>
	<u>\$ 226,669,794</u>	<u>\$ 2,088,538,981</u>	<u>\$ 2,315,208,775</u>

Required maturities for the Series 2005, Series 2006 and Series 2010 Bonds represent the minimum amount of principal that MTASC must pay as of the specific distribution dates in order to avoid a default. Turbo (accelerated) amortization payments are required to be made against outstanding principal providing that MTASC receives sufficient TSRs to make the Turbo payments. The interest payment requirements shown are based on the required principal maturity schedule and include the accreted value portion of capital appreciation bonds in the year in which they are required to be redeemed.

Under the terms of the Indenture, MTASC is required to maintain certain deposits to fund debt service payments, if needed. Such deposits are included in restricted cash and cash equivalents in the basic financial statements. In addition, MTASC is subject to various debt covenants, including limitations on expenses/expenditures, and compliance with Trustee indenture agreement requirements. MTASC was in compliance with all covenants and indenture agreement requirements at December 31, 2010 and 2009.

Principal payments in the amount of \$720,000 and \$2,890,000 were made during 2010 and 2009, respectively, in accordance with the Turbo Redemption requirements of the Series 2005B bonds.

Interest

Interest expense on bonds payable was \$14,449,229 and \$14,431,768 in 2010 and 2009, respectively. In 2010 and 2009, cash paid for interest was \$10,323,650 and \$10,558,150 respectively.

Advance Refunding/Defeasance

On June 1, 2010 the outstanding Series 2000 Tobacco Settlement Asset-Backed Bonds in the amount of \$143,475,000 were redeemed and paid with funds generated by the Series 2005 Bonds. The Series 2000 Bonds were deemed to have been advance refunded and defeased since the issuance of the Series 2005 Bonds.

5. TRANSACTIONS WITH MONROE COUNTY

In addition to setting forth the terms and conditions of the sale and purchase of the TSRs, the Purchase and Sale Agreement also provides for separate consideration to retain the County to act as Administrator with respect to the preparation of all reports and other instruments and documents that it is the duty of MTASC to prepare, execute, file or deliver pursuant to the Indenture and the related agreements.

The Purchase and Sale Agreement also contemplates the lease by MTASC of office space and telephone service from the County, and the sharing of overhead and operating services and expenses (including shared employees, consultants and agents and reasonable legal and auditing expenses) on the basis of actual use or value of such services, or otherwise on a basis reasonably related thereto.

The cost to MTASC for the services provided by the County was approximately \$30,000 in each of the years ended December 31, 2010 and 2009.

No funds considered a residual amount in accordance with the Amended and Restated Indenture were available or transferred to the Trustee and ultimately the County in 2010 or 2009.

6. CONTINGENCIES

Future TSRs are subject to adjustment based upon tobacco consumption, inflation and other factors. Pursuant to the Indenture, these adjustments and other events could trigger additional debt service reserve requirements.

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

March 15, 2011

To the Board of Directors of the
Monroe Tobacco Asset Securitization Corporation:

We have audited the financial statements of the governmental activities and major fund of Monroe Tobacco Asset Securitization Corporation (MTASC) as of and for the year ended December 31, 2010, which collectively comprise MTASC's basic financial statements and have issued our report thereon dated March 15, 2011. 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 audits, we considered MTASC'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 MTASC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MTASC's internal control over financial reporting.

A deficiency in internal control 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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.

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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*

(Continued)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether MTASC'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 or other matters 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 and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.