

**ONONDAGA TOBACCO ASSET  
SECURITIZATION CORPORATION**

**FINANCIAL STATEMENTS**

**December 31, 2008**

**ONONDAGA TOBACCO ASSET  
SECURITIZATION CORPORATION**

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## INDEPENDENT AUDITOR'S REPORT

**To the Board of Directors of  
Onondaga Tobacco Asset Securitization Corporation  
Syracuse, New York**

We have audited the accompanying financial statements of the governmental activities, the business-type activities and the major fund, and the aggregate remaining fund information of Onondaga Tobacco Asset Securitization Corporation as of and for the year ended December 31, 2008, which collectively comprise the Corporation's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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, the business-type activities, and the major fund, and the aggregate remaining fund information of Onondaga Tobacco Asset Securitization Corporation, as of December 31, 2008, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 27, 2009, on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting 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 audit.

The Management's Discussion and Analysis on pages 3 through 7 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

*Green & Seifter, CPAs*

February 27, 2009  
Syracuse, New York

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**Year ended December 31, 2008**

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Our discussion and analysis of Onondaga Tobacco Asset Securitization Corporation's (the Corporation) financial performance provides an overview of the Corporation's financial activities during 2008. It should be read in conjunction with the financial statements and their associated notes that follow this section to properly evaluate the Corporation's financial position. The financial statements present only the information for the year ended December 31, 2008.

**Financial Highlights**

As discussed further in the notes to the financial statements, the Corporation was formed to acquire from the County of Onondaga all future right, title and interest in the Tobacco Settlement Revenues (TSRs) under the Master Settlement Agreement (MSA) with respect to tobacco related litigation among various states and participating manufacturers. The Corporation is a component unit of Onondaga County and, accordingly, is included in the County's financial statements as a blended component unit. The Corporation is classified as a special-purpose government under GASB Statement No. 14 and consists of one governmental fund. The fund and government-wide financial statements are presented together and include a reconciliation of the individual line items between the two statement types in a separate column. Some of the more significant reconciling items are noted below:

1. An adjustment was made to report the cost and discount fees associated with the Series II and Series V bond issue as an asset and to record as an expense the amortization of these costs over the life of the bonds on the government-wide financial statements.
2. An adjustment was made to report the Series II and Series V bonds and interest accrued on the bonds as a liability and the principal payments on the bonds as an expense.

**Using This Annual Report**

This annual report consists of a series of financial statements and notes to those statements. The statement of net assets and the statement of activities provide information about the Corporation's activity and present a long-term view of the Corporation's finances. The fund financial statements tell how the governmental activity's services were financed in the short term as well as what remains for future spending.

## Reporting the Corporation as a Whole

### Government-Wide Financial Statements

The Corporation presents its government-wide financial statements as the statement of net assets and the statement of activities. These include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Corporation's net assets and changes in them. You can think of the Corporation's net assets – the difference between assets and liabilities – as one way to measure the Corporation's financial health or financial position. Over time, increases or decreases in the Corporation's net assets are one indicator of whether its financial health is improving or deteriorating.

Below is a condensed version of the government-wide financial statements for the years ended December 31:

	2008	2007
Assets	\$ 684,708,145	\$ 683,680,681
Liabilities	\$ 807,305,302	\$ 807,194,745
Net Deficit	\$ (122,597,157)	\$ (123,514,064)
Revenues	\$ 9,154,710	\$ 8,221,114
Expenses	\$ 8,237,803	\$ 8,193,416
Change in Net Assets	\$ 916,907	\$ 27,698

The Corporation's assets increased by approximately \$1,027,500. The Corporation's liabilities increased by approximately \$110,600. Net deficit decreased by approximately \$916,900 or 0.7%.

## **Reporting the Corporation as a Whole – Continued**

### **Government-Wide Financial Statements – Continued**

The most significant variance between years was in program revenues and expenses. Under the Master Settlement Agreement, the tobacco companies are required to make annual payments to the Corporation. During 2008, approximately \$8.4 million in tobacco revenues were received compared to \$7.5 million in 2007. In 2008, approximately \$8.2 million in expenses were incurred compared to \$8.2 million in 2007.

During the year ended December 31, 2008, no new bonds were issued and no distributions were made to the County. However, during 2008, interest expense of approximately \$2,850,000 was accrued on the Series 2005 bonds, while approximately \$2,713,000 was accrued during 2007.

No residual payments were made to the County in 2008 and 2007 due to the trapping events that occurred. Those monies that would have been paid out to the County are now required to be used to fund a trapping account as required by the Corporation's Indenture. In addition, as a result of the issuance of the 2005 Series Bonds, the County relinquished the right to use these monies for anything other than Corporation debt retirement.

The recognition of the bonds payable liability in 2001 and 2005 has created a deficit in the Corporation's net assets. The deficit is expected to be satisfied over time as the tobacco settlement proceeds are received.

### **Fund Financial Statements**

A governmental entity can have various types of funds such as governmental and proprietary. The Corporation only has one fund, the debt service fund, which is a governmental fund.

- Governmental funds focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the Corporation's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Corporation's programs.

## Reporting the Corporation as a Whole – Continued

### Fund Financial Statements – Continued

Below is a condensed version of the fund financial statement for the years ended December 31:

	<u>2008</u>	<u>2007</u>
Assets	\$ 12,148,533	\$ 11,002,250
Liabilities	\$ -	\$ -
Fund Balance	\$ 12,148,533	\$ 11,002,250
Revenues	\$ 9,154,710	\$ 8,221,114
Expenditures	\$ 8,008,427	\$ 7,750,830
Excess of Revenues over Expenditures	\$ 1,146,283	\$ 470,284

The most significant variance between years was in revenues and expenditures. In 2008, approximately \$8.4 million in tobacco revenues were received compared to \$7.5 million in 2007. Under the Master Settlement Agreement, the tobacco companies are required to make annual payments to the Corporation. The Corporation also recorded an accounts receivable of approximately \$0.7 million for funds to be received in settlement of a 2006 payment that was not previously made. Expenditures in 2008 were approximately \$0.7 million higher than the previous year. In 2008, the Corporation's principal and interest payments on the bonds increased approximately \$0.3 million from the prior year.

The debt service fund has two distinct fund balances: reserved for debt service and unreserved-undesignated. Unreserved-undesignated fund balance is generated from general operations and is not restricted in its use. Fund balance reserved for debt service results from monies set aside for future payment of the bond principal and interest.

Unlike the government-wide financial statements, in the fund financial statements, the bond payable is not recognized as a liability as it is long-term in nature. Because of this, there is not the issue of the large fund balance deficit under this methodology that is present in the government-wide presentation.

### Long-Term Debt Activity

The Corporation issued debt which will be repaid by its purchases from the County of the future right, title and interest in the Tobacco Settlement Revenues. Debt is amortized through 2043.

Serial Bonds principal payments are due annually and interest semiannually. At December 31, 2008, the Corporation had \$799,945,000 in bonds outstanding. There was a 0.3% decrease from the previous year as a result of the \$2,260,000 principal payments scheduled for 2008.



## **Reporting the Corporation as a Whole – Continued**

### **Analysis of Overall Financial Position**

Under the government-wide methodology, the Corporation showed an increase to its net assets. This increase results from the tobacco settlement proceeds and interest income providing enough revenue to meet the Corporation's current expenditure/expense demands. Specifically, the government-wide financial statements show a decrease to the Corporation's net deficit by \$916,907. The Corporation continues to meet expectations and has improved at December 31, 2008 as a result of the Corporation's equity position increase.

### **Budget**

GASB 34 requires an analysis of significant variations between the original budget and final budget amounts and between final budget amounts and actual budget results. Management has prepared a budget for its operating expenses only, and there were no changes or amendments to the operating budget. Because the budget is not a complete budget, comparison to current operations could be misleading. As such, it has not been presented in this report.

### **Other Known Facts**

Two trapping events have occurred and one is continuing. The first was a Downgrade Trapping event that occurred in 2003. According to the Master Settlement Agreement (MSA), each of the four original participating manufacturers (OPM) had a market share of 7% or more in 2003. The credit ratings of each were monitored. The rating of R.J. Reynolds Tobacco Holdings, Inc. was below the allowable threshold as described in the Official Statement, therefore a downgrade trapping event has occurred. The second trapping event occurred in 2004 when the non-participating manufacturers (NPM) market share was greater than 7% in 2003. According to the MSA Report, the NPM Market Share in the year 2005 and subsequently has been less than 7%, and, therefore, the NPM Trapping Event is no longer occurring. As a result of these trapping events, the Corporation is required to withhold residual payments to the County until the time that the trapping events have been resolved. Those payments to the County that would have been made on the Residual Certificate are now required to be deposited into a trapping account to the extent required by the Corporation's Indenture.

As a result of the issuance of the 2005 Series Bonds, the County relinquished the right to use these monies for anything other than Corporation debt retirement.

### **Contacting the Corporation's Financial Management**

This financial report is designed to provide to the readers of these financial statements an overview of the Corporation's finances and to show the Corporation's accountability for the money it received. If you have questions about this report or need additional financial information, contact the Corporation's President, James Rowley at 421 Montgomery Street, Syracuse, NY 13202.

# ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION

## GOVERNMENTAL FUND BALANCE SHEET/STATEMENT OF NET ASSETS (DEFICIT)

December 31, 2008

<b>ASSETS</b>			
	Debt Service Fund	Adjustments	Statement of Net Assets
<b>Assets:</b>			
Unrestricted cash	\$ 83,409	\$ -	\$ 83,409
Accounts receivable	670,657	\$ -	\$ 670,657
Investments	11,394,467	-	11,394,467
Bond issuance costs, net of accumulated amortization	-	2,374,469	2,374,469
Bond discount fees, net of accumulated amortization	-	670,185,143	670,185,143
<b>Total assets</b>	<b>\$ 12,148,533</b>	<b>\$ 672,559,612</b>	<b>\$ 684,708,145</b>
<b>LIABILITIES AND FUND BALANCE/NET (DEFICIT)</b>			
<b>Liabilities:</b>			
Accrued interest payable	\$ -	\$ 7,360,302	\$ 7,360,302
Bonds payable:			
Due after one year	-	799,945,000	799,945,000
<b>Total liabilities</b>	-	807,305,302	807,305,302
Contingencies (Note 9)			
<b>Fund balance:</b>			
Reserved for debt service	12,065,124	(12,065,124)	-
Unreserved - undesignated	83,409	(83,409)	-
<b>Total fund balance</b>	12,148,533	(12,148,533)	-
<b>Total liabilities and fund balance</b>	<b>\$ 12,148,533</b>		
<b>Net assets (deficit):</b>			
Restricted for debt service		11,394,467	11,394,467
Unrestricted net deficit		(133,991,624)	(133,991,624)
<b>Total net deficit</b>		(122,597,157)	(122,597,157)
<b>Total liabilities and net deficit</b>		<b>\$ 672,559,612</b>	<b>\$ 684,708,145</b>

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

# ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION

## STATEMENT OF GOVERNMENTAL FUND REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES/STATEMENT OF ACTIVITIES

Year ended December 31, 2008

	Debt Service Fund	Adjustments	Statement of Activities
Revenues:			
Tobacco settlement proceeds	\$ 8,358,345	\$ -	\$ 8,358,345
Interest income	796,365	-	796,365
Total revenues	9,154,710	-	9,154,710
Expenditures/expenses:			
Insurance	4,576	-	4,576
Audit fee	5,470	-	5,470
Legal fees	3,250	-	3,250
Trustee fee	7,557	-	7,557
Administrative agency fee	29,938	-	29,938
Rating agency fee	16,326	-	16,326
General and administrative costs	28,054	-	28,054
Amortization expense	-	118,819	118,819
Principal	2,260,000	(2,260,000)	-
Interest	5,653,256	2,370,557	8,023,813
Total expenditures/expenses	8,008,427	\$ 229,376	8,237,803
Excess of revenues over expenditures	1,146,283		
Change in net assets			916,907
Fund balances/net assets (deficit), beginning of year	11,002,250		(123,514,064)
Fund balances/net assets (deficit), end of year	\$ 12,148,533		\$ (122,597,157)

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

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**1. DESCRIPTION OF THE CORPORATION AND REPORTING ENTITY**

The Onondaga Tobacco Asset Securitization Corporation (the Corporation) is a Not-For-Profit Local Development Corporation under Section 1411 of the Not-For-Profit Corporation Law of the State of New York. The Corporation was established on July 3, 2001 and became active August 8, 2001.

The Corporation was formed to acquire from the County of Onondaga all future rights, title and interest in the Tobacco Settlement Revenues (TSRs) under the Master Settlement Agreement (MSA) with respect to tobacco related litigation among various states and participating manufacturers. The County's future right, title and interest in the TSRs has been pledged to repay the serial bonds issued by the Corporation. The County is the beneficial owner of the Trust and thus the funds received by the Trust will ultimately transfer to the County.

The Corporation is primarily dependent on the future proceeds from the Tobacco Settlement Rights to meet future obligations under the indenture agreement.

The Corporation is classified as a special purpose government under GASB Statement No. 14. A special-purpose government is defined as a legally separate entity that performs only one activity. Although legally separate from the County, the Corporation is a component unit of the County, and accordingly, is included in the County's financial statements as a blended component unit.

**2. SIGNIFICANT ACCOUNTING POLICIES**

The financial statements of the Onondaga Tobacco Asset Securitization Corporation have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. Those principles are prescribed by the Governmental Accounting Standards Board (GASB), which is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Certain significant accounting principles and policies utilized by the Corporation are described below:

**A. Basis of Presentation**

The Corporation is classified as a single-program special-purpose government. Consistent with Appendix C of GASB No. 34, the fund and government-wide financial statements are presented together and include a reconciliation of the individual line items between the two statement types in a separate column.

**1. Government-Wide Statements**

The statement of net assets and the statement of activities present financial information about the Corporation's governmental activities. These statements include the financial activities of the Corporation.

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2. Fund Financial Statements**

The fund financial statements provide information about the Corporation's fund. The emphasis of fund financial statements is on major governmental funds.

The Corporation reports the debt service fund as its major governmental fund. This fund is used to account for and report on the accumulation of resources to be used for redemption of general long-term indebtedness and supports the operations of the Corporation.

**B. Measurement Focus and Basis of Accounting**

The 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 at the time liabilities are incurred, regardless of when the related cash transaction takes place.

The fund statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The Corporation considers all revenues reported in the governmental funds to be available if the revenues are collected within 60 days after the end of the fiscal year.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt which are recognized as expenditures to the extent they have matured. Proceeds of general long-term debt are reported as other financing sources.

**C. Fund Balance Reserve**

In the fund financial statements, the reserve for debt service is used to account for and report on the accumulation of resources to be used for redemption of general long-term indebtedness and supports the operations of the Corporation.

**D. Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates. The Corporation recorded an accounts receivable for the collection of funds for the settlement of a 2006 payment within the December 31, 2008 financial statements. The Corporation believes that the funds are collectible and accordingly has not recorded a reserve against the receivable balance.

**E. Cash Equivalents**

The Corporation considers all short-term instruments purchased with original maturities of three months or less to be cash equivalents.

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

**F. Income Tax Status**

The Corporation is exempt from federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3).

**3. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN FUND STATEMENTS AND GOVERNMENT-WIDE STATEMENTS**

Due to the differences in the measurement focus and basis of accounting used in the fund statements and the government-wide statements, certain financial transactions are treated differently. The basic financial statements contain a full reconciliation of these items. The differences result primarily from the economic focus on the statement of activities, compared with the current financial resources focus on the statement of governmental fund revenue, expenditures and changes in fund balance.

**A. Total Fund Balances of the Fund Statements versus Net Assets of Government-Wide Statements**

Total fund balances of the Corporation's fund statements differ from "net assets" of government-wide statements reported in the statement of net assets. This difference primarily results from the additional long-term economic focus on the statement of net assets versus the solely current financial resources focus on the fund balance sheet.

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**3. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN FUND STATEMENTS AND GOVERNMENT-WIDE STATEMENTS (continued)**

1. Explanation of Differences between the Governmental Fund Balance Sheet and the Statement of Net Assets:

Fund Balance - Governmental Funds	
Balance Sheet	\$ 12,148,533

The costs and discount fees associated with the Series 2001 Bond issue are reported as expenditures in the year they are incurred. As a result, these are not recorded as assets on the balance sheet. However, the statement of net assets includes those costs and discount fees among the assets of the Corporation, and their original costs are expensed annually over the life of the related debt. The balances at December 31, 2008 are as follows:

Original cost of bond issuance	\$ 2,923,366	
Less: Accumulated amortization	<u>548,897</u>	
Net cost of bond issuance	2,374,469	
Original cost of bond discount fees	670,526,808	
Less: Accumulated amortization	<u>341,665</u>	
Net cost of bond discount fees	670,185,143	
Total net costs of bond issuance and bond discount fees		672,559,612
Bonds payable are reported in the statement of net assets, but not on the balance sheet because they are not due and payable in the current period.		(799,945,000)
Accrued interest payable is reported in the statement of net assets, but not on the balance sheet because they are not due and payable in the current period.		<u>(7,360,302)</u>
Total		<u>(134,745,690)</u>
Net Deficit - Government-Wide Statements		<u>\$ (122,597,157)</u>

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**3. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN FUND STATEMENTS AND GOVERNMENT-WIDE STATEMENTS. (continued)**

**B. Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance Versus Statement of Activities**

Differences between the statement of governmental fund revenues, expenditures and changes in fund balances and the statement of activities fall into one of three broad categories. The amounts shown below represent:

**1. Long-Term Revenue and Expense Differences**

Long-term revenue differences arise because the governmental statement of fund revenue, expenditures and changes in fund balances report revenues only when they are considered "available", whereas the statement of activities reports revenues when earned. Differences in long-term expenses arise because the statement of governmental fund revenue, expenditures, and changes in fund balances report on a modified accrual basis, whereas the accrual basis of accounting is used on the statement of activities.

**2. Capital Related Differences**

Capital related differences include the difference between proceeds from the sale of capital assets reported on the fund financial statements and the gain or loss on the sale of assets as reported on the statement of activities, and the difference between recording an expenditure for the purchase of capital items in the fund financial statements and depreciation expense on those items as recorded in the statement of activities. Capital related differences at December 31, 2008 include payment and amortization of bond issuance costs and discount fees (refer to note 6).

**3. Long-Term Debt Transaction Differences**

Long-term debt transaction differences occur because both interest and principal payments are recorded as expenditures in the fund financial statements, whereas interest payments are recorded in the statement of activities as incurred, and principal payments are recorded as a reduction of liabilities in the statement of net assets. These differences are explained in greater detail in the following section.



**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**3. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN FUND STATEMENTS AND GOVERNMENT-WIDE STATEMENTS. (continued)**

**C. Explanation of Differences between Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance and the Statement of Activities.**

1. Total Expenditures/Expenses

- a. Amounts reported for governmental activities in the statement of activities are different because:

Excess of revenues over expenditures	\$ 1,146,283
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The statement of government fund revenue, expenditures and changes in fund balances reports issuance costs and discount fees associated with a bond issuance as expenditures in the year they are incurred. However, in the statement of activities, the cost of those assets is allocated over the life of the related debt and reported as amortization expense. This is the amount charged to amortization expense in the current year.	(118,819)
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Repayment of bond principal is an expenditure in the fund financial statements, but it reduces long-term liabilities in the statement of net assets, and does not affect the statement of activities.	2,260,000
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In the statement of activities, interest is accrued on outstanding bonds, whereas in fund financial statements, an interest expenditure is reported when due.	<u>(2,370,557)</u>
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Total adjustments between statement of governmental fund revenue, expenditures and changes in fund balances and the statement of activities.	<u>(229,376)</u>
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Change in net assets - Statement of Activities	<u><u>\$ 916,907</u></u>
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**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**4. CASH AND INVESTMENTS**

**Cash**

At December 31, 2008, the carrying amount and the bank balance on the Corporation's deposits totaled \$83,409. These monies are on deposit with a FDIC-insured commercial bank located within Onondaga County.

**Investments**

Investments are reported at fair market value. The Corporation's trustee holds investments for the funds included in the financial statements. The Corporation invests in authorized investments as described in the bond resolution such as commercial paper or finance company paper; special time deposits accounts; certificates of deposit and obligations of the United States of America.

All investments are insured, registered or held by the Corporation's trustee in the Corporation's name.

**5. INVESTMENTS**

A trustee holds the Corporation's investments in the following accounts:

**Debt Service Account**

This is the account from which payments to bondholders are made with money transferred in from the collection account.

**Liquidity Reserve Account**

This reserve has been established pursuant to the Corporation's indenture and was initially funded in an amount equal to the maximum annual debt service on the Series 2001 Bonds. Amounts exceeding the reserve requirement will be transferred to the debt service account and will be available to make flexible amortization bond payments.

**Collection Account**

This account has been established to receive the Tobacco Settlement Revenues under the MSA agreement. The monies received in this account will be transferred to the debt service account to pay the Corporation's bondholders.

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

**5. INVESTMENTS (continued)**

**Trapping Account**

This account has been established pursuant to the Corporation's indenture and is required to be funded when a trapping event has occurred. Following the occurrence of a trapping event, amounts that otherwise would have been paid on the Residual Certificate are deposited into this account to the extent required by the Corporation's Indenture until such time that a trapping event is no longer occurring. The balance in the trapping account at December 31, 2008 was \$2,776,027.

At December 31, 2008, investments are stated at fair value, which approximate cost, and consist of the following:

Cash and Money Market Funds	\$ 483,352
Federal National Mortgage Association Discount Notes	2,564,060
Commercial Paper	<u>8,347,055</u>
Total	<u><u>\$ 11,394,467</u></u>

**6. BOND ISSUANCE COSTS AND DISCOUNT FEES**

The Corporation has incurred issuance costs and discount fees associated with the Series 2005 and Series 2001 Bond issues. As is stated previously in the notes to the financial statements, these costs are expensed as incurred in the Corporation's fund financial statements. Such costs and discount fees are deferred and amortized over the life of related debt in the government-wide statements. Discount fees and bond issuance costs totaling \$670,064,414 will be amortized over 16 years (June 1, 2017 through June 1, 2033). This will result in a matching of the amortization of the asset related to the 2005 series bonds with the related payment of the liability. Balances at December 31, 2008 are as follows:

	2005 Series		2001 Series	
	<u>Issuance Costs</u>	<u>Discount Fees</u>	<u>Issuance Costs</u>	<u>Discount Fees</u>
Cost	\$ 836,558	\$669,227,856	\$ 2,086,808	\$ 1,298,952
Less: Accumulated Amortization	<u>-</u>	<u>-</u>	<u>548,897</u>	<u>341,665</u>
Net	<u><u>\$ 836,558</u></u>	<u><u>\$669,227,856</u></u>	<u><u>\$ 1,537,911</u></u>	<u><u>\$ 957,287</u></u>

Amortization charged to expense in 2008 for bond issuance costs and discount fees was \$73,234 and \$45,585, respectively.

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**7. LONG-TERM DEBT**

On August 8, 2001, the Corporation issued \$111,470,000 in variable rate bonds bearing interest rates ranging from 5% - 6%. These bonds were part of the \$215,220,000 New York Counties Tobacco Trust II, Tobacco Settlement Pass-Through Bonds, Series 2001. The debt is payable solely from pledged Tobacco Settlement Rights and investment earnings on amounts on deposit.

On November 29, 2005 the Corporation issued \$ 700,630,000 variable rate bonds with a face value of \$700,630,000, discount fees totaling \$669,227,856, bond issuance costs of \$836,558 and a distribution to the County of \$30,565,586. The bonds bear interest at rates ranging from 6.00% to 7.15%. These bonds were part of the \$199,375,348 (net of discount) New York Counties Tobacco Trust V, Tobacco Settlement Pass-Through Bonds, Series 2005. The debt is payable from pledged Tobacco Settlement Rights and investment earnings on amounts on deposit. The Corporation is required to make annual debt service payments beginning June 1, 2017 through June 1, 2033. These bonds are Capital Appreciation Bonds and pay interest at maturity, not every year. During 2008, interest expense of \$2,381,006 was accrued on these bonds. The Series 2005 Bonds are subordinate to the Series 2001 Bonds.

The changes in the Corporation's long-term debt during the year ended December 31, 2008 is summarized as follows:

	Balance January 1, 2008	Additions	Payments	Balance December 31, 2008
Serial Bonds	<u>\$ 802,205,000</u>	<u>\$ -</u>	<u>\$ 2,260,000</u>	<u>\$ 799,945,000</u>

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

**7. LONG-TERM DEBT (continued)**

The Corporation's required principal and interest payments at December 31, 2008, on the above Bonds are as follows:

	Series 2001		Series 2005	
	Principal	Interest	Principal	Interest
2009	\$ 625,000	\$ 6,162,206	\$ -	\$ -
2010	685,000	6,127,744	-	-
2011	770,000	6,087,731	-	-
2012	860,000	6,041,831	-	-
2013	945,000	5,989,938	-	-
2014-2018	7,105,000	28,963,438	14,640,000	2,307,429
2019-2023	14,540,000	26,021,020	71,875,000	12,979,194
2024-2028	17,095,000	21,743,824	186,175,000	28,290,356
2029-2033	17,510,000	16,841,844	427,940,000	49,834,557
2034-2038	20,645,000	11,656,384	-	-
2039-2043	18,535,000	4,497,794	-	-
	<u>\$ 99,315,000</u>	<u>\$ 140,133,754</u>	<u>\$ 700,630,000</u>	<u>\$ 93,411,536</u>

Depending on the extent of actual collections from TSR payments and availability of funds, the Corporation has agreed to make principal payments in accordance with a flexible amortization payment schedule that allows for increased payments and a final maturity of December 31, 2028 on the Series 2001 Bonds.

Under the flexible amortization payment schedule, the Corporation's payments at December 31, 2008, on the Bonds are as follows:

	Series 2001	
	Principal	Interest
2009	2,480,000	5,530,238
2010	2,645,000	5,395,631
2011	2,900,000	5,248,256
2012	3,100,000	5,087,644
2013	3,295,000	4,915,263
2014-2018	20,270,000	21,508,073
2019-2023	30,580,000	14,334,533
2023-2028	34,045,000	4,439,431
Total	<u>\$ 99,315,000</u>	<u>\$ 66,459,069</u>

**ONONDAGA TOBACCO ASSET SECURITIZATION CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**

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**8. RELATED PARTY**

The Corporation is a special-purpose local development corporation and is considered by legal counsel to be bankruptcy-remote from the County of Onondaga. However, the Corporation's board of directors is comprised of a majority of elected or appointed officials of the County of Onondaga and one independent director.

**9. CONTINGENCIES AND CONCENTRATION OF CREDIT RISK**

During 2001, the Corporation purchased the rights to receive TSRs (Tobacco Settlement Revenues) from the County of Onondaga. There are a number of risks associated with receipts of such TSRs, including litigation affecting participating manufacturers and possible bankruptcy as a result thereof, and future adjustments to the calculation of the TSRs. The Corporation's financial existence is contingent upon receiving the TSR from the tobacco manufacturers. While the risk of non-collection of the TSR is considered remote, being of a material nature, it must be disclosed.

**10. NET ASSETS (DEFICIT)**

Net assets at December 31, 2008 have a deficit of \$122,597,157. As the TSR monies are received and recognized as revenue, the bonds will be paid off and the unrestricted net deficit will be eliminated.

**11. SUBSEQUENT EVENTS**

One of the settling tobacco manufacturers did not make a payment of the calculated TSR for 2006. During February 2009, the Corporation received payment for the settlement with the manufacturer. The Corporation recorded an accounts receivable for the payment of approximately \$670,700 within the December 31, 2008 financial statements.



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**INDEPENDENT AUDITOR'S 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***

**To the Board of Directors of  
Onondaga Tobacco Asset Securitization Corporation  
Syracuse, New York**

We have audited the financial statements of the governmental activities, the business-type activities and major fund, and the aggregate remaining fund information of Onondaga Tobacco Asset Securitization Corporation, as of and for the year ended December 31, 2008, which collectively comprise the Corporation's basic financial statements, and have issued our report thereon dated February 27, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

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

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

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

#### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Corporation'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*.

We noted certain matters that we reported to management of the Corporation, in a separate letter dated February 27, 2009.

This report is intended solely for the information and use of management, the Board of Directors, others within the entity, and is not intended to be and should not be used by anyone other than these specified parties.

*Green & Seifter, CPAs*

February 27, 2009  
Syracuse, New York



