

SENECA TOBACCO ASSET
SECURITIZATION CORPORATION

FINANCIAL STATEMENTS

December 31, 2010

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Dermody, Burke & Brown, CPAs, LLC

INDEPENDENT AUDITORS' REPORT

DIRECTORS

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

We have audited the accompanying statement of net assets of **SENECA TOBACCO ASSET SECURITIZATION CORPORATION** (the Corporation), a component unit of the County of Seneca, New York as of December 31, 2010 and the related statements of revenue, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion 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. 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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Seneca Tobacco Asset Securitization Corporation as of December 31, 2010, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 to 6 is not a required part of the 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 supplementary information. However, we did not audit the information and express no opinion on it.

Dermody, Burke & Brown

DERMODY, BURKE & BROWN, CPAs, LLC

Auburn, NY

February 28, 2011

443 North Franklin Street • Syracuse, NY 13204-1441 • (315) 471-9171 • Fax (315) 471-8555
1120 Corporate Drive • Auburn, NY 13021-1634 • (315) 253-6273 • Fax (315) 253-0890
4350 Middle Settlement Road • New Hartford, NY 13413-5328 • (315) 732-2991 • Fax (315) 732-0282

<http://www.dbbllc.com>

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2010

Our discussion and analysis of **SENECA TOBACCO ASSET SECURITIZATION CORPORATION'S** (the Corporation) financial performance provides an overview of the Corporation's financial activities during 2010. 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, 2010.

Financial Highlight

As discussed further in the notes to the financial statements, the Corporation was formed to acquire from the County of Seneca 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 Seneca County based on the guidance provided in Technical Bulletin No. 2004-01 and is included as part of the County's financial reporting entity as a blended component unit as of December 31, 2010.

Using This Annual Report

Because the Corporation is treated as a proprietary fund for auditing purposes, it has in the past and will continue to use the accrual basis of accounting. The accrual basis of accounting provides both short-term and long-term information about the Corporation's overall financial status.

The financial statements also include notes that explain some of the information in the statements and provide more detailed data.

The remainder of this overview section of MD&A highlights the structure and contents of the statements.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2010

Using This Annual Report – Continued

Summary of Statement of Net Assets

	ASSETS	
	2010	2009
Cash	\$ 200,208	\$ 184,774
Deposits Held with Trustee:		
Debt Service Account	1,605	324,947
Liquidity Reserve Account	511,292	511,292
Trapping Account	0	658
Collection Account	692	(168)
	<hr/>	<hr/>
Total Deposits Held with Trustee	513,589	836,729
Prepaid Insurance	5,856	5,856
Interest Receivable	0	5,533
Tobacco Settlement Rights Receivable	487,663	948,744
Bond Issuance Costs, Net of Accumulated Amortization	218,499	225,316
Bond Discount, Net of Accumulated Amortization	82,772,369	84,490,154
	<hr/>	<hr/>
TOTAL ASSETS	\$ 84,198,184	\$ 86,697,106
	<hr/>	<hr/>
LIABILITIES AND NET DEFICIT		
LIABILITIES		
Accrued Interest Payable	\$ 27,418	\$ 27,418
Bonds Payable, Due Within One Year	40,000	35,000
Bonds Payable, Due After One Year	99,405,000	99,535,000
	<hr/>	<hr/>
Total Liabilities	99,472,418	99,597,418
UNRESTRICTED NET DEFICIT	(15,274,234)	(12,900,312)
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TOTAL LIABILITIES AND NET DEFICIT	\$ 84,198,184	\$ 86,697,106
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The Corporation's assets decreased by approximately \$2.5 million. In 2010, \$338,000 of the bond proceeds from the 2005 bond issuance that was on deposit with trustee was paid to Seneca County to defease debt. The bond discount decreased by approximately \$2.5 million due to \$1.7 million in amortization. Bonds payable decreased by \$135,000 which represents the principal payments made in 2010. The recognition of the bond payable liability in 2000 and 2005 created a deficit in the Corporation's net assets. This deficit is expected to be satisfied over time as the tobacco settlement proceeds are received and the debt is paid.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2010

Using This Annual Report – Continued

Summary of Revenue and Expenses

	2010	2009
OPERATING REVENUE		
Administrative Fee Income	\$ 39,745	\$ 38,697
Interest Income	<u>9,393</u>	<u>26,220</u>
Total Operating Revenue	49,138	64,917
OPERATING EXPENSES		
Payments to Seneca County	338,000	429,000
Interest Expense	325,251	375,272
Administrative Agent Fee	14,682	14,705
Liability Insurance	10,000	10,000
Professional Fees	10,525	10,500
Amortization	<u>1,724,602</u>	<u>1,741,409</u>
Total Operating Expenses	<u>2,423,060</u>	<u>2,580,886</u>
CHANGE IN UNRESTRICTED NET ASSETS (DEFICIT)	<u>\$ (2,373,922)</u>	<u>\$ (2,515,969)</u>

The Corporation showed a decrease in net assets in 2010 and 2009. This decrease results from interest earnings, which does not provide enough revenue to meet the Corporation's current expense for bond interest payments and amortization expense.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2010

Using This Annual Report – Continued

Analysis of Overall Financial Position

Overall, the Corporation continues to show a decrease in net assets, which meets expectations. Cash received on the tobacco settlement rights receivable has been sufficient to meet the Corporation's current expenditure demands. However, interest expense on debt continues to exceed interest revenue generated on deposits. As the debt is paid down, the interest expense is scheduled to decline.

Long-Term Debt Activity

The Corporation issued debt to fund its purchases of the future right, title, and interest in the Tobacco Settlement Revenues. Debt is amortized through 2042 for the 2000 Series Bonds and 2060 for the 2005 Series Bonds.

Serial bond principal payments are due annually and interest semiannually for the 2000 Series Bonds. At December 31, 2010, the Corporation had \$4,970,000 in 2000 serial bonds outstanding. This was a 2% decrease from the previous year due to scheduled principal payments.

The Corporation is required to make annual debt service payments beginning June 2038 for the 2005 Series Bonds. These bonds are Capital Appreciation Bonds and pay interest at maturity, not every year. The series 2005 Bonds are subordinate to the 2000 bonds. In December 2009, \$1,055,000 of the Series 1 Bonds was retired with the monies held in the trapping fund.

More detailed information about the Corporation's long-term liabilities is presented in Note 6 to the financial statements.

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.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2010

Using This Annual Report – Continued

Other Known Facts

Trapping Events

In 2010, according to the MSA Report, each of the OPMs had a Market Share of 7% or more in the calendar year preceding the deposit date. The credit ratings of each were monitored. The rating of Reynolds American had previously been below the allowable threshold as described in the Official Statement, and therefore, a Downgrade Trapping Event had occurred. The rating of Reynolds American is now above the allowable threshold and therefore, a Downgrade Trapping Event is no longer occurring. In December 2009, approximately \$195,000 of the funds on deposit in the trapping account was used to retire Series 1 Bonds with a face value of \$1,055,000.

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 receives. If you have questions about this report or need additional financial information, contact the Corporation's Treasurer, Nicholas Sciotti at 1 DiPronio Drive, Waterloo, NY 13165.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

AUDITED FINANCIAL STATEMENTS

STATEMENT OF NET ASSETS

December 31, 2010

ASSETS

Cash	\$ 200,208
Deposits Held with Trustee:	
Debt Service Account	1,605
Liquidity Reserve Account	511,292
Collection Account	<u>692</u>
Total Deposits Held with Trustee	513,589
Prepaid Insurance	5,856
Tobacco Settlement Rights Receivable	487,663
Bond Issuance Costs, Net of Accumulated Amortization	218,499
Bond Discount, Net of Accumulated Amortization	<u>82,772,369</u>
TOTAL ASSETS	<u>\$ 84,198,184</u>

LIABILITIES AND NET DEFICIT

LIABILITIES

Accrued Interest Payable	\$ 27,418
Bonds Payable, Due Within One Year	40,000
Bonds Payable, Due After One Year	<u>99,405,000</u>
Total Liabilities	99,472,418
UNRESTRICTED NET DEFICIT	<u>(15,274,234)</u>
TOTAL LIABILITIES AND NET DEFICIT	<u>\$ 84,198,184</u>

See notes to financial statements.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS

Year Ended December 31, 2010

OPERATING REVENUE

Administrative Fee Income	\$ 39,745
Interest Income	<u>9,393</u>
Total Operating Revenue	49,138

OPERATING EXPENSES

Payments to Seneca County	338,000
Interest Expense	325,251
Administrative Agent Fee	14,682
Liability Insurance	10,000
Professional Fees	10,525
Amortization	<u>1,724,602</u>
Total Operating Expenses	<u>2,423,060</u>

CHANGE IN UNRESTRICTED NET ASSETS (DEFICIT) (2,373,922)

NET DEFICIT

Balance, Beginning of Year	<u>(12,900,312)</u>
Balance, End of Year	<u><u>\$ (15,274,234)</u></u>

See notes to financial statements.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

STATEMENT OF CASH FLOWS

Year Ended December 31, 2010

CASH FLOWS FROM OPERATING ACTIVITIES

Change in Unrestricted Net Assets (Deficit)	\$ (2,373,922)
Adjustments to Reconcile Change in Unrestricted Net Assets (Deficit) to Net Cash Used In Operating Activities:	
Amortization of Bond Issuance and Bond Discount Costs	1,724,602
(Increase) Decrease in Operating Assets:	
Interest Receivable	5,533
Tobacco Settlement Rights Receivable	<u>461,081</u>
Net Cash Used In Operating Activities	(182,706)

CASH FLOWS FROM INVESTING ACTIVITIES

Decrease in Deposits Held with Trustee	<u>323,140</u>
Net Cash Provided By Investing Activities	323,140

CASH FLOWS FROM FINANCING ACTIVITIES

Principal Payments on Bonds Payable	<u>(125,000)</u>
Net Cash Used In Financing Activities	<u>(125,000)</u>
Net Increase in Cash	15,434
Cash, Beginning of Year	<u>184,774</u>
Cash, End of Year	<u><u>\$ 200,208</u></u>

See notes to financial statements.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 1 – NATURE OF OPERATIONS

The Seneca Tobacco Asset Securitization Corporation (the Corporation), is a Non-Profit Local Development Corporation under Section 1411 of the Not-For-Profit Corporation Law of the State of New York.

The Corporation was formed to acquire from the County of Seneca 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 purchase price of the County's future right, title and interest in the TSRs has been financed by the issuance of serial bonds. A Residual Certificate exists which represents the entitlement to receive all amounts required to be distributed after payment of debt service, operating expenses and certain other costs as set forth in the indenture. Payments on the Residual Certificate from TSR collections are subordinate to payments on bonds and certain other costs specified in the indenture. Excess TSRs not required by the Corporation to pay various expenses, debt service or required reserves with respect to the bonds are transferred to 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.

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.

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

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The financial statements of the Corporation have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Corporation has adopted GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting" and GASB Statement No. 29, "The Use of Not-for-Profit Accounting and Financial Accounting Principles by Governmental Entities." In 2004, the Corporation was required and has implemented GASB Statement No. 34 "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments."

Basis of Accounting

The financial statements have been prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Corporation uses the indirect method of reporting net cash flows from operating activities, and considers all short-term investments with an original maturity of three months or less to be cash equivalents. At December 31, 2010, there were no cash equivalents.

Income Taxes

The Seneca Tobacco Asset Securitization Corporation is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code.

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.

Subsequent Events

Management has evaluated subsequent events through February 28, 2011, which is the date the financial statements were available to be issued.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 3 – TOBACCO SETTLEMENT RIGHTS RECEIVABLE

The tobacco settlement rights receivable represents estimated future payments to be received from the MSA. The receivable was recorded at the cost of the purchase price from the County of \$5,600,904. As the payments are received under the MSA, the receivable is reduced. The receivable balance at December 31, 2010 was \$487,663.

NOTE 4 – DEPOSITS HELD WITH TRUSTEE

Deposits held with trustee include the following:

Liquidity Reserve Account – This reserve has been established pursuant to the Corporation's indenture and was initially funded in the amount equal to the maximum annual debt service on the Series 2000 Bonds. At December 31, 2010, these deposits consisted primarily of money market funds.

Debt Service Account – This is the account from which payments to bondholders are made with money transferred in from the collection account. At December 31, 2010, these deposits consisted primarily of money market funds.

Collection Account – This account has been established to receive the Tobacco Settlement payments under the MSA agreement. The monies received in this account are transferred to the debt service account to pay the Corporation's bondholders. At December 31, 2010, these deposits consisted primarily of money market funds.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 5 – BOND ISSUANCE COSTS AND DISCOUNT FEES

The Corporation has incurred issuance costs and discount fees associated with the Series 2005 and 2000 Bond issues. Such costs and discount fees are deferred and amortized over the life of related debt. Balances at December 31, 2010 are as follows:

	Issuance Costs	Discount Fees
Cost	\$ 269,390	\$ 91,727,104
Less: Accumulated Amortization	<u>50,891</u>	<u>8,954,735</u>
Net	<u>\$ 218,499</u>	<u>\$ 82,772,369</u>

Amortization charged to expense in 2010 for bond issuance costs and discount fees was \$6,817 and \$1,717,785, respectively.

NOTE 6 – LONG-TERM DEBT

On December 7, 2000, the Corporation issued \$6,450,000 in variable rate bonds. These bonds were part of the \$227,130,000 New York Counties Tobacco Trust I, Tobacco Settlement Pass-Through Bonds, Series 2000. The debt is payable solely from pledged Tobacco Settlement Rights and investment earnings on amounts on deposit. According to the terms of the required amortization payments, the Corporation is required to make annual debt service payments through 2042 with interest ranging from 5% to 6.3%.

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 June 1, 2024 on the Series 2001 Bonds.

On November 29, 2005, the Corporation issued variable rate bonds with a face value of \$95,530,000, discount fees totaling \$92,436,115, and bond issuance costs of \$197,730. The bonds bear interest at rates ranging from 6% to 7.85%. These bonds were part of the \$199,375,348 (net of discount) New York Counties Tobacco Trust V., Settlement Pass-Through Bonds, Series 2005. The debt is payable from pledged Tobacco Settlement Rights and investment earnings on deposit. The Corporation is required to make annual debt service payments beginning June 2038 through June 2060. These bonds are Capital Appreciation Bonds and pay interest at maturity, not every year. The series 2005 Bonds are subordinate to the 2000 bonds. In December 2009, Series 1 Bonds with a face value of \$1,055,000 were retired.

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 6 – LONG-TERM DEBT – Continued

The Corporation's required amortization payments at December 31, 2010 on the above bonds are as follows:

	Series 2000 Principal	Interest	Series 2005 Principal	Interest
2011	\$ 40,000	\$ 396,646	\$ 0	\$ 0
2012	45,000	394,264	0	0
2013	50,000	391,544	0	0
2014	60,000	388,344	0	0
2015	65,000	384,672	0	0
Thereafter	<u>4,710,000</u>	<u>6,064,867</u>	<u>94,475,000</u>	<u>11,381,526</u>
Total	<u>\$ 4,970,000</u>	<u>\$ 8,020,337</u>	<u>\$ 94,475,000</u>	<u>\$ 11,381,526</u>

The Corporation's flexible amortization payments at December 31, 2010 on the Series 2000 bonds are as follows:

	Series 2000 Principal	Interest
2011	\$ 320,000	\$ 308,813
2012	235,000	294,556
2013	245,000	279,643
2014	270,000	254,771
2015	275,000	246,040
Thereafter	<u>3,625,000</u>	<u>1,143,057</u>
Total	<u>\$ 4,970,000</u>	<u>\$ 2,526,880</u>

Cash paid for interest in 2010 was \$325,251.

Changes in long-term liabilities are as follows:

	Balance at December 31, 2009	Additions	Reductions	Balance at December 31, 2010
Serial Bonds	<u>\$ 99,570,000</u>	<u>\$ 0</u>	<u>\$ 125,000</u>	<u>\$ 99,445,000</u>

SENECA TOBACCO ASSET SECURITIZATION CORPORATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE 7 – RELATED PARTY

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

NOTE 8 – CONTINGENCY AND CONCENTRATION OF CREDIT RISK

During 2000, the Corporation purchased the rights to receive TSRs (Tobacco Settlement Revenues) from the County of Seneca. 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 TSR's. The Corporation's financial existence is contingent upon receiving these TSRs from the tobacco manufacturers. While the risk is considered remote, being of a material nature, it must be disclosed.

NOTE 9 – FINANCIAL INSTRUMENTS

The Corporation maintains its cash accounts with a local financial institution. Accounts are guaranteed by the Federal Deposit Insurance Corporation (FDIC). The FDIC insurable limit is \$250,000 per depositor per bank. Throughout the year, the Corporation's cash balances may exceed FDIC insured limits.

NOTE 10 – NET ASSET DEFICIT

The Corporation has a net deficit of \$15,274,234 at December 31, 2010. This deficit results from operating costs exceeding revenue since the initial period of operation. This deficit will be eliminated through subsequent interest earnings.