ULSTER TOBACCO ASSET SECURITIZATION CORPORATION

(A Blended Component Unit of the County of Ulster, New York)

Basic Financial Statements and Required Supplementary Information

For the year ended December 31, 2017

(With Independent Auditors' Reports Thereon)

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Prepared by:
Burton Gulnick, Jr.
Vice President/Secretary/Treasurer

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SECURITIZATION CORPORATION
(A BLENDED COMPONENT UNIT OF THE COUNTY OF ULSTER, NEW YORK)

Basic Financial Statements and Required Supplementary Information

For the year ended December 31, 2017

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Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Ulster Tobacco Asset Securitization Corporation:

Report on the Financial Statements

We have audited the accompanying financial statements of the Ulster Tobacco Asset Securitization Corporation (the "Corporation"), a component unit of the County of Ulster, New York, as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the Corporation's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

The Corporation's management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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 the major fund of the Corporation, as of December 31, 2017, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis 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 of America, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 13, 2018 on our consideration of the 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Corporation's internal control over financial reporting and compliance.

Drescher & Malecki LLP

March 13, 2018

Our discussion and analysis of the Ulster Tobacco Asset Securitization Corporation's (the "Corporation") financial performance provides an overview of the Corporation's financial activities for the fiscal year ended December 31, 2017. This document should be read in conjunction with additional information that we have furnished in the Corporation's financial statements, which follows this narrative.

Financial Highlights

- The Corporation had a net deficit position of $40.636 million at December 31, 2017.
- The Corporation's net position increased by approximately $357 thousand for the year ended December 31, 2017.
- During the year, the Corporation had general revenues of $1.997 million, which included approximately $1.970 million in tobacco settlement revenues (TSRs) and approximately $27 thousand in interest income.
- The total cost of the Corporation's operations was $1.640 million, which includes $1.586 million for interest on the Corporation's outstanding bonds payable, and approximately $54 thousand for general administration expenses.
- The Corporation's total bonded debt outstanding at year end was $36.312 million of bonds payable, net of accreted capital appreciation, and bond premium.

Using This Annual Report

This annual report consists of four financial statements presented on two pages. The first two financial statements are the Governmental Fund Balance Sheet/Statement of Net Position found on page 6. The final two financial statements are the Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance/Statement of Activities found on page 7.

The Statement of Net Position and the Statement of Activities provide information about the activities of the Corporation as a whole and present a long-term view of the Corporation's finances by focusing on the total available resources and changes therein. The fund financial statements tell how the operations were financed in the short-term, as well as what remains for future spending. The Corporation has only one fund, a debt service fund. The Debt Service Fund is used to account for the accumulation of resources to pay for future debt service, and the Corporation's general administrative costs related to such debt service.

For the Corporation, the change in the focus between current spendable resources and total available resources is identified in the adjustment columns found on each of the financial statements as noted above. To arrive at the Statement of Net Position, the accrued tobacco settlement revenues, the accrued interest expense on the Corporation's bonds, the outstanding balance of bonds payable and certain other adjustments are added to the total on the Governmental Activities column. This is displayed in the Adjustments Column. To arrive at the Statement of Activities, certain adjustments are made to the Statement of Revenues, Expenditures and Changes in Fund Balance. For the Corporation, transactions not affecting its reported net position are payments of debt service-principal. Accounts relating to the aforementioned transactions are displayed in the Adjustments column to the left of the Governmental Activities column.

Reporting the Corporation as a Whole

The Statement of Net Position and the Statement of Activities

These two statements report the Corporation's net position and changes in them. Annual changes in the Corporation's net position – the difference between assets and deferred outflows, and liabilities and deferred inflows – is the way to measure the Corporation's financial health, or financial position. Over time, increases or decreases in the Corporation's net position are one indicator of whether its financial health is improving or deteriorating. As the Corporation is entirely dependent on tobacco settlement revenues, in evaluating the financial health of the Corporation, the reader will also need to consider the likelihood that the amount of payments from the primary tobacco manufacturers will continue to support the debt service on the Corporation's bonds as well as operating expenses.

The Corporation will annually report a deficit in its net position. The deficit in the Corporation's net position arose as it carried out its statutory purpose of acting as a facilitator for the issuance of debt to finance the purchase of all right, title and interest in Ulster County's future revenues under the Master Settlement Agreement for future Tobacco Settlement Revenues. This debt will be repaid from amounts expected to be received from primary tobacco manufacturers in subsequent years. The unrestricted net position deficit can be expected to continue until the outstanding debt is retired.

The Corporation had total assets of $4.595 million, total liabilities of $36.472 million, and total deferred inflows of resources of $8.759 million at the end of the year. Unrestricted net position – the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements – was a net position deficit of $42.924 million at the end of this year. In addition, there was a restricted net position in the amount of $2.288 million for debt service.

Reporting the Corporation's Fund

Fund Financial Statements

The fund financial statements provide detailed information about its Debt Service Fund. The fund financial statements are prepared using a different approach than the Corporation-wide financial statements. The Corporation's expenditures are reported in its governmental fund, which focuses on how money flows into and out of this fund and the balance left at year-end that is available for spending. This fund is reported using the modified accrual basis of accounting, which measures cash and all other financial assets that can readily be converted to cash. The Debt Service Fund statements provide a detailed short-term view (less than one year) of the Corporation's operations.

As the Corporation completed the year, its Debt Service Fund (as presented in the governmental fund balance sheet on page 6) reported a combined fund balance of $2.381 million.

During the year, the Corporation received TSRs of $2.006 million for its administrative costs and to provide funds for the payment of debt service on its outstanding bonds payable. The Corporation earned approximately $27 thousand in interest income on investments, which was collectively used to fund approximately $54 thousand in general administrative expenses.

Debt

In 2001, the Corporation was authorized to issue up to $28.352 million of debt. The Series 2001 Bonds consist of the Series 2001 Convertible Capital Appreciation Bonds (CABs) in the amount of $6.397 million and the Series 2001 Current Interest Bonds in the amount of $21.955 million. The Series 2001 Bonds were issued at a net original issue premium of $583 thousand and the Corporation paid issuance costs of $1.069 million. In 2005, the Corporation was authorized to issue an additional $15.852 million of debt. The County participated in the New York Counties Tobacco Trust V (NYCTT V) to facilitate this transaction. These bonds consist of Series 2005 S1 Subordinate Turbo CABs in the amount of $5.486 million, Series 2005 S2 Subordinate Turbo CABs in the amount of $3.127 million, Series 2005 S3 Subordinate Turbo CABs in the amount of $1.736 million and Series 2005 S4B Subordinate CABs in the amount of $5.503 million. In 2016, the Corporation was authorized to refund and issue $31.060 million of debt. The County participated in the New York Counties Tobacco Trust VI (NYCTT VI) to facilitate this transaction. These bonds consist of Series 2016 Tobacco Settlement Asset Backed Bonds in the amount of $31.060 million, and were used to defease, redeem, and/or exchange the Series 2001 Tobacco Settlement Asset Backed Bonds, to cancel the Series 2005 S2 Subordinate Turbo CAB's, and to acquire by negotiated price the Series 2005 S4B Subordinate CAB's. During 2017, the Corporation made the final payment on the Series 2001 Bonds. At December 31, 2017, the Corporation had $30.980 million in Tobacco Settlement Bonds outstanding, an unamortized premium of $1.412 million, and accreted CAB's outstanding of $3.919 million.

Contacting The Corporation's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the Corporation's finances and to show the Corporation's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Ulster County Department of Finance at the Ulster County Office Building, 4th Floor, Kingston, New York 12402.

ULSTER TOBACCO ASSET
SECURITIZATION CORPORATION
(A BLENDED COMPONENT UNIT OF THE COUNTY OF ULSTER, NEW YORK)

Governmental Fund Balance Sheet / Statement of Net Position

December 31, 2017

	Debt Service Fund	Adjustments (Note 8)	Governmental Activities
Assets			
Restricted cash and cash equivalents	$ 2,395,106	$ -	$ 2,395,106
Due from New York State	-	2,200,000	2,200,000
Total assets	$ 2,395,106	$ 2,200,000	$ 4,595,106
Liabilities			
Due to other governments	$ 14,049	$ -	$ 14,049
Accrued interest	-	146,443	146,443
Tobacco settlement bonds payable (net)	-	32,392,364	32,392,364
Capital appreciation bonds (net)	-	3,919,495	3,919,495
Total liabilities	14,049	36,458,302	36,472,351
Deferred Inflows of Resources - Gain on refunding	-	8,758,842	8,758,842
Fund Balances / Net Position			
Restricted for debt service	2,287,783	(2,287,783)	-
Assigned to subsequent years expenditures	44,169	(44,169)	-
Assigned to other purposes	49,105	(49,105)	-
Total fund balances	2,381,057	(2,381,057)	-
Total liabilities, deferred inflows of resources, and fund balances	$ 2,395,106	42,836,087	45,231,193
Net position:			
Restricted for debt service		2,287,783	2,287,783
Unrestricted		(42,923,870)	(42,923,870)
Total net position		$ (40,636,087)	$ (40,636,087)

See accompanying notes to financial statements.

ULSTER TOBACCO ASSET
SECURITIZATION CORPORATION
(A BLENDED COMPONENT UNIT OF THE COUNTY OF ULSTER, NEW YORK)

Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance / Statement of Activities

For the year ended December 31, 2017

	Debt Service Fund	Adjustments (Note 9)	Governmental Activities
General revenues:			
Tobacco settlement revenues	$ 2,005,770	$ (35,756)	$ 1,970,014
Interest income	27,227	-	27,227
Total general revenues	2,032,997	(35,756)	1,997,241
Expenditures / Expenses:			
General administration	53,947	-	53,947
Debt service - principal	1,010,000	(1,010,000)	-
Debt service - interest and fiscal charges	1,941,025	(354,858)	1,586,167
Total expenditures / expenses	3,004,972	(1,364,858)	1,640,114
Change in fund balance / net position	(971,975)	1,329,102	357,127
Fund balances / Net position:			
Beginning of year	3,353,032	(44,346,246)	(40,993,214)
End of year	$ 2,381,057	$ (43,017,144)	$ (40,636,087)

See accompanying notes to financial statements.

(1) Organization

The Ulster Tobacco Asset Securitization Corporation (the Corporation) 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). The Corporation was established on January 12, 2001, however there were no substantive operations until February 1, 2001 as discussed herein. The Corporation is an instrumentality of, but separate and apart from the County of Ulster, New York (the County). The Corporation has a board of directors comprised of nine directors, all but one of whom shall be one or more of the following: an employee of the County, an elected official of the County or a member of the County legislature; and one director who shall be independent. 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.

On February 1, 2001, pursuant to a Purchase and Sale Agreement with the County, the County sold to the Corporation all of its future right, title and interest (that the market would allow) in the Tobacco Settlement Revenues (TSRs) under the Master Settlement Agreement (MSA) and the Decree and Final Judgment (the Decree). On November 29, 2005, the County participated in the New York Counties Tobacco Trust V (NYCTT V) whereby the County sold all of its future right, title and interest (that the present market would allow) in the TSRs under the MSA. 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 right, title and interest of the County's share were sold to the Corporation.

The MSA was entered into on November 23, 1998, among the attorneys general of 46 states (including New York), the District of Columbia, the Commonwealth of Puerto Rico, Guam, the U.S. Virgin Islands, American Samoa and the Territory of the Northern Marianas and for the four largest United States tobacco manufacturers: Philip Morris Incorporated, R.J. Reynolds Tobacco Company, Brown and Williamson Tobacco Company and Lorillard Tobacco Company (collectively the "Original Participating Manufacturers" or "OPMs") in settlement of certain smoking-related litigation and the Decree entered in New York Supreme Court, including the County's right to receive certain initial and annual payments to be made by the OPMs under the MSA.

The purchase price of the County's future right, title and interest in the TSRs has been financed by the issuance of serial bonds. 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 Ulster Tobacco Asset Securitization Corporation Residual 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. 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 the bonds and payment of certain other costs specified in the indenture.

In September 2016, the County and the Corporation participated in New York Counties Tobacco Trust VI (NYCTT VI) whereby the Corporation issued new Series 2016 bonds.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The Corporation has prepared its financial statements in accordance with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standards setting body for establishing governmental accounting and financial reporting principles.

The accompanying financial statements present only activities of the Ulster Tobacco Asset Securitization Corporation and do not purport to, and do not, represent fairly the financial position of the County of Ulster as of December 31, 2017, and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

The Corporation has prepared corporation-wide financial statements titled "Statement of Net Position" and "Statement of Activities" as well as the required supplementary information titled "Management's Discussion and Analysis" which precedes the financial statements. The Corporation also prepares the fund financial statements, which are the "Governmental Fund Balance Sheet," and "Statements of Revenues, Expenditures and Changes in Fund Balance." The basic financial statements include both the corporation-wide and the fund financial statements.

The Corporation follows the principles of fund accounting in that each segment of operations is represented under a discrete fund presentation in the fund financial statements. The Corporation uses one governmental fund type to report its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain functions and activities. The Debt Service Fund accounts for the accumulation of resources for payment of principal and interest on long-term debt and supports the operations of the Corporation.

The Collection Account within the Debt Service Fund will be used to deposit all Collections (excluding certain investment earnings). Funds on deposit in the Collection Account will be transferred to various other accounts under the Indenture. The Debt Service Account within the Debt Service Fund will be used to deposit amounts transferred from the Collection Account in respect of interest and principal payments and from which the Trustee will make payments on the bonds in accordance with the priority of payments. The Corporation is required to maintain a balance of, to the extent of available funds, equal to the lesser of: (i) 125% of the average annual Debt Service on the Bonds of each Series of Bonds of which one or more Bonds remain Outstanding Bonds, measured as of their respective dates of original issuance; or (ii) the maximum amount that may be held in the Liquidity Reserve Account, in the opinion of Counsel, without adversely affecting the tax-exempt status of the Series 2001 Bonds and any other subsequently issued debt. The Extraordinary Payment Account within the Debt Service Fund will be used to deposit, following the occurrence of any Event of Default, Collections after the payment of certain expenses. The Trustee will make interest payments, Extraordinary Payments and various other payments related to the Bonds.

The Trapping Account within the Debt Service Fund will be funded from Collections at the amount necessary to make the amount in the Trapping Account equal to the sum of (i) the Trapping Requirement during the existence of a Trapping Event and (ii) the Lump Sum Payment Requirement as a result of a Lump Sum Payment Event.

For further information regarding the above accounts, events, and requirements refer to the Corporation's Tobacco Settlement Asset-Backed Bonds, Series 2001 Resolution dated February 8, 2001.

(b) Measurement Focus and Basis of Accounting

The Corporation follows the modified accrual basis of accounting in its Debt Service Fund, which focuses on changes in available resources, in preparation of the fund financial statements. Under the modified accrual basis of accounting, revenues and related receivables are recorded in the accounting period that they become both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period (ninety days or less). Expenditures and related liabilities are recognized in the accounting period the liability is due and payable.

General administration expenditures are direct costs incurred by the Corporation, such as legal and auditing fees, financial advisory fees, printing costs, trustee fees and other related costs. General administration expenditures are paid from either bond proceeds or from TSRs.

The Corporation utilizes the full accrual basis of accounting, which focuses on changes in total economic resources, in preparation of the corporation-wide financial statements. Under the full accrual basis of accounting changes in long-term assets and liabilities are incorporated into the financial statements. Since the fund financial statements are prepared on a different measurement focus and basis of accounting than the corporation-wide financial statements, an adjustments column is presented to transform the fund based financial statements into the corporation-wide financial statements.

(c) Restricted Cash and Cash Equivalents

The Corporation considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents.

(d) Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources,* represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/expenditure) until then. At December 31, 2017, the Corporation does not have any deferred outflows of resources.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources,* represents an acquisition of net position that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. At December 31, 2017, the Corporation had deferred inflows of resources in the amount of $8.759 million related to a deferred gain on refunding, which will be amortized over the life of the bonds. A deferred gain or loss on refunding results from the difference in carrying value of refunded debt and its acquisition price.

(e) Net Position Flow Assumption

Sometimes the Corporation will fund outlays for a particular purpose from both restricted (e.g., restricted bond proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted–net position and unrestricted–net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the Corporation’s policy to consider restricted–net position to have been depleted before unrestricted–net position is applied.

(f) Fund Balance Flow Assumption

Sometimes the Corporation will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. If the Corporation must use funds for emergency expenditures it shall expend funds first from funds classified under GASB as nonspendable (if funds become available) then restricted funds. The use of committed and assigned funds as classified by GASB will occur after the exhaustion of available restricted funds. Finally, if no other fund balances are available the Corporation will use unassigned fund balance.

(g) Fund Balance

The Corporation's fund equity is classified as fund balance. Fund balance classifications indicate the level of constraints placed upon how resources can be spent and identify the sources of those constraints. In the fund financial statements, fund balance is defined as:

Restricted – consists of amounts that are subject to externally enforceable legal purpose restrictions imposed by creditors, grantors, contributors, or laws and regulations of other governments, or through constitutional provisions, charter requirements, or enabling legislation.

Committed – consists of amounts that are subject to a purpose constraint by a formal action of the Board before the end of the fiscal year. Commitments may be established, modified, or rescinded only through resolutions approved by the Board. The Corporation has no committed fund balances as of December 31, 2017.

Assigned – consists of amounts that are subject to a purpose constraint that represents an intended use established by the Board, or by their designated body or official. The purpose of the assignment must be narrower than the purpose of a general fund, and in funds other than a general fund, assigned fund balance represents the residual amount of fund balance.

- *Subsequent years' expenditures* – to reflect the portion of fund balance designated for resource utilization in a future period.
- *Other purposes* – to reflect the residual amount of fund balance to be used for future debt payments.

Unassigned – consists of a deficit fund balance resulting from overspending for specific purposes for which amounts have been restricted, committed, or assigned. The Corporation has no unassigned fund balances as of December 31, 2017.

(h) Program Revenues

Amounts reported as *program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions (including special assessments) that are restricted to meeting the operational or capital requirements of a particular function or segment. There are no program revenues in the current year. Items not properly included among program revenues are reported instead as *general revenues*.

(i) Expenditures/Expenses

Expenditures are recorded on a modified accrual basis of accounting. Payments to the County are recorded when the obligation is incurred. General administration costs consist of operating expenses for professional service fees and are paid using interest income on investments. *Direct expenses* are those that are clearly identifiable with a specific function. Indirect expenses have been included as part of the program expenses reported for the various functional activities.

(j) Interest

The Corporation recognizes all interest paid as interest expenditures on a modified accrual basis for the revenue, expenditures and changes in fund balance statement and as expensed on the full accrual basis for the statement of activities.

(k) Amortized Bond Premiums and Bond Discounts

The Corporation recognizes bond premiums and bond discounts fully in the year of issuance for the governmental fund statements and are amortized over the life of the related bonds for the Corporation-wide statements.

(l) Investments

The Corporation considers all debt instruments with original maturities of more than three months to be investments. The Corporation reports its investments with an original maturity of greater than one year at quoted market price (fair value) and reports investments with an original maturity of one year or less at cost. At December 31, 2017, the Corporation does not report any investments.

(m) Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America require the Corporation's management to make estimates and assumptions in determining the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

(n) Adoption of New Accounting Pronouncements

During the year ended December 31, 2017, the Corporation implemented GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68,* GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans,* GASB Statement No. 80, *Blending Requirements for Certain Component Units – an Amendment of GASB Statement No. 14*, GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, and GASB Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67, No. 68, and No. 73*. GASB Statement Nos. 73, 74, 80, 81, and 82 did not have a material impact on the Corporation's financial position or results from operations.

(o) Future Impacts of Accounting Pronouncements

The Corporation has not completed the process of evaluating the impact that will result from adopting the following GASB Statements:

- No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*, effective for the year ending December 31, 2018.
- No. 83, *Certain Asset Retirement Obligations*, effective for the year ending December 31, 2019.
- No. 84, *Fiduciary Activities*, effective for the year ending December 31, 2019.
- No. 85, *Omnibus 2017*, effective for the year ending December 31, 2018.
- No. 86, *Certain Debt Extinguishment Issues*, effective for the year ending December 31, 2018.
- No. 87, *Leases,* effective for the year ending December 31, 2020.

The Corporation is, therefore, unable to disclose the impact that adopting these statements will have on its financial position and results of operations.

(p) Subsequent Events

The Corporation has evaluated subsequent events after December 31, 2017, and through March 13, 2018, which is the date the financial statements were available to be issued, and have determined that there are no subsequent events that require disclosure under generally accepted accounting principles.

(q) Tax Status

The Corporation received a determination letter dated January 3, 2003, finding the Corporation exempt from federal income tax under section 501(a) of the Internal Revenue Code (IRC) as an organization described in section 501(c)(3).

(3) Restricted Cash and Cash Equivalents

At December 31, 2017, total restricted cash and cash equivalents of $2.395 million consist primarily of short-term U.S. Government guaranteed securities held by the Corporation's agent in the Corporation's name. At year end the carrying amount of restricted cash and cash equivalents for the Corporation was $2.395 million and the bank balance was $2.395 million.

The Corporation invests in authorized investments as described in the bond resolution, including: commercial or finance company paper rated "P-1" by Moody's; special time deposit accounts; certificates of deposit; obligations of the United States of America; obligations guaranteed by agencies of the United States of America; obligations of the State of New York; obligations issued pursuant to LFL Sect. 24.00 or 25.00 (with approval of the State Comptroller) by any municipality, school district or district corporation other than the County of Ulster; 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 repurchase agreements limited to obligations of the United States of America and obligations guaranteed by agencies of the United States of America.

Credit risk, for cash and cash equivalents, is the risk that in the event of a bank failure, the Corporation's deposits may not be returned to it. All deposits of the Corporation, including certificates of deposit and special time deposits, in excess of the amount insured under the provisions of the Federal Deposit Insurance Act are secured at December 31, 2017.

Custodial risk, for cash and cash equivalents, is the risk that, in the failure of the counterparty, the Corporation will not be able to recover the value of its cash equivalents or collateral securities that are in possession of an outside party.

Interest rate risk is the risk of fair value losses arising from fluctuating interest rates. The Corporation limits its exposure to interest rate risk by generally limiting investments to 180 days or less.

(4) Bonds Payable

As discussed in Note 1, the purchase price of the County's future right, title and interest in the TSRs, was financed through the issuance of Series 2001 Bonds in the amount of $31.330 million bearing interest at rates ranging from 5.950% to 6.262%, Series 2005 NYCTT V Bonds in the amount of $15.852 million bearing interest rates ranging from 6.00% to 7.85%, and Series 2016 NYCTT VI Bonds in the amount of $31.060 million bearing interest rates ranging from 2.000% to 6.750%. The Series 2001 Bonds consisted of the Series 2001 Convertible Capital Appreciation Bonds in the amount of $6.397 million (with $2.978 million in Capital Appreciation that is recognized by the Corporation over a period of 10 years) and the Series 2001 Current Interest Bonds in the amount of $21.955 million. During 2016, the Series 2001 Tobacco Settlement Asset Backed Bonds in the amount of $25.280 million were defeased, redeemed, and/or exchanged with the issuance of the Series 2016 Tobacco Settlement Bonds and additional consideration. Also during 2016, as a result of the refunding transaction, the Series 2005 S2 Subordinate Turbo CAB's were canceled, and the Series 2005 S4B Subordinate CABs were acquired by negotiated purchase price. As of December 31, 2017, the Series 2005 S3 Subordinate Turbo CABs totaled $3.919 million, net of capital appreciation, and the Series 2016 Tobacco Settlement Bonds totaled $32.392 million, net of unamortized premium.

The 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. The Corporation retains TSRs in an amount sufficient to service its debt, not otherwise provided for from bond proceeds, and pay its operating expenses, and remits the remaining balance to the Trust (see note 1).

Changes in Tobacco Settlement Bonds payable for the year ended December 31, 2017, are as follows:

Description	Beginning Balance 1/1/17	Additions	Deletions	Ending Balance 12/31/17
Tobacco Settlement Bonds:				
Series 2001	$ 930,000	$ -	$ 930,000	$ -
Series 2016	31,060,000	-	80,000	30,980,000
Total Tobacco Settlement Bonds	31,990,000	-	1,010,000	30,980,000
Bond premium	1,495,444	-	83,080	1,412,364
Net Tobacco Settlement Bonds	$33,485,444	$ -	$ 1,093,080	$32,392,364

Principal and interest debt service requirements for required maturity payments at the December 31, 2017 for the Series 2016 Tobacco Settlement Bonds are as follows:

Year ended December 31:	Principal	Interest	Total
2018	$ 945,000	$ 1,755,064	$ 2,700,064
2019	755,000	1,725,989	2,480,989
2020	1,145,000	1,664,889	2,809,889
2021	1,230,000	1,585,870	2,815,870
2022	1,305,000	1,500,314	2,805,314
2023-2027	8,085,000	6,003,106	14,088,106
2028-2032	11,240,000	3,085,346	14,325,346
2033-2034	6,275,000	338,125	6,613,125
Debt service payable	$ 30,980,000	$ 17,658,703	$ 48,638,703

The Corporation paid $930 thousand in principal payments in 2017 on the Series 2001 Tobacco Settlement Bonds.

The Corporation had a liquidity reserve in the amount of $2.209 million to fund debt service payments if needed, at December 31, 2017.

Interest on the Subordinate Turbo CABs is compounded semiannually on June 1 and December 1, but is not payable until bond maturity. Interest accretes until both principal and accreted interest are paid. The accreted interest on the Subordinate Turbo CABs is reflected within the Subordinate Turbo CABs payable liability.

A summary of the Subordinate Turbo CABs net bond balance activity for the year ended December 31, 2017 follows:

Description	Beginning Balance 1/1/17	Additions & Annual Net Interest Accretion	Deletions	Ending Balance 12/31/17
Subordinate Turbo CABs	$ 3,664,199	$ 255,296	$ -	$ 3,919,495

The remaining projected debt service requirements as of December 31, 2017, including principal of $3.919 million, capital appreciation and interest for the Series 2005 NYCTT V Bonds are to be paid starting in June 1, 2034, and maturing on June 1, 2039, totaling $13.841 million as follows:

Year ended December 31:	Principal & Interest
2018	$ -
2019	-
2020	-
2021	-
2022	-
2023-2027	-
2028-2032	-
2033-2037	10,138,689
2038-2039	3,702,898
Debt service payable	$ 13,841,587

During the course of 2017, there were no payments of principal and accreted interest on the Series 2005 NYCTT V Bonds.

(5) Net Position and Fund Balance

The government-wide financial statements utilize a net position presentation. Net position is categorized as restricted and unrestricted components.

- ***Restricted for Debt Service* –** This category restricts a portion of net position for payment of the debt service obligations of the Corporation. At December 31, 2017, the balance of this restriction was $2,287,783.
- ***Unrestricted Component of Net Position* –** This component represents net position of the Corporation not restricted for any other purpose.

In the fund financial statements, restricted fund balances are amounts constrained to specific purposes (such as grantors, bondholders, and higher levels of government) through constitutional provisions or by enabling legislation. At December 31, 2017, the Corporation reported $2,287,783 of fund balance restricted for debt service that must be used toward the future repayment of bonded debt.

In the fund financial statements, assignments are not legally required segregations but are segregated for a specific purpose by the Corporation. At December 31, 2017, the Corporation reported $44,169 of fund balance assigned to subsequent year expenditures, and $49,105 of fund balance assigned to other purposes.

As of December 31, 2017, the Corporation reported no nonspendable, committed, or unassigned fund balance.

(6) Transactions with Ulster 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 the Corporation to prepare, execute, file or deliver pursuant to the indenture and the related agreements.

The Corporation uses office space and telephone services from the County, and shares overhead and operating services and expenses with the County (including employees, consultants and agents). The Contract provides for payments to the County on the basis of actual use or value of such services, or on a basis reasonably related thereto. For the year ended December 31, 2017, the Corporation owes approximately $14 thousand for services rendered by Ulster County.

(7) Contingencies

Future Tobacco Settlement Revenues are subject to adjustment based upon tobacco consumption, inflation and other potential reductions. Pursuant to the Purchase and Sale Agreement these adjustments, and other events, could trigger additional debt service reserve requirements.

Certain smokers, smokers' rights organizations, consumer groups, cigarette importers, cigarette distributors, cigarette manufacturers, Native American tribes, taxpayers, taxpayers' groups and other parties have filed actions against some, and in certain cases all, of the signatories to the MSA. In the event of an adverse court ruling in such types of litigation, Bondholders could incur a complete loss of their investment.

Additionally, the OPM's are also exposed to liability from various lawsuits including individual lawsuits, class action lawsuits and health care cost recovery litigation. Ultimately, the outcome of these and any other pending or future lawsuits is uncertain. One or more adverse judgment could result in delays in, or reductions of amounts available for, payments on the bonds.

(8) Explanation of Certain Differences between the Governmental Fund Balance Sheet and the Statement of Net Position

Long-term liabilities of the Corporation's activities are not due and payable in the current period and, therefore, are not reported as fund liabilities. In addition, certain items are fully expensed in the governmental fund statements, but amortized over a period of time in the Statement of Net Position. All assets, liabilities, and deferred inflows of resources – both current and long-term – are reported in the Statement of Net Position. The adjustments required to the reported governmental fund asset and liabilities to arrive at the Statement of Net Position are as follows:

Total fund balances-debt service fund	$	2,381,057
Accounts receivable - tobacco settlement revenues		2,200,000
Accrued interest expense		(146,443)
Tobacco settlement bonds payable (net of bond premium)		(32,392,364)
Capital appreciation bonds (net of accreted capital appreciation)		(3,919,495)
Deferred gain on refunding		(8,758,842)
Total net position	$	(40,636,087)

(9) Explanation of Certain Differences between the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balance and the Statement of Activities

Repayment of bond principal is reported as an expenditure in governmental funds and therefore contributes to the change in fund balance. In the Statement of Net Position, however, repaying bond principal decreases long-term liabilities and does not affect the statement of activities. Similarly, recognition of revenues not expected to be received in the current year and expenditures not due and payable will not affect the fund balance reported for the governmental funds. In the Statement of Activities prepared on the full accrual basis, however, all revenues and expenses are recognized in the year they are earned or incurred regardless of when they are paid, and will therefore be reflected in the Statement of Activities. These differences in measurement recognition affect both the reported fund balance and reported net position. The adjustments required to the reported governmental funds revenues and expenditures to arrive at the Statement of Activities are as follows:

Change in net position - debt service fund	$	(971,975)
Tobacco settlement revenues		(35,756)
Debt service - principal		1,010,000
Debt service - interest		11,847
CAB accreted interest		(255,296)
Bond premium recognized		83,080
Change in deferred gain on refunding		515,227
Change in net position	$	357,127

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INDEPENDENT AUDITORS' 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
Ulster Tobacco Asset Securitization Corporation:

We have audited, in accordance with the 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, the financial statements of the governmental activities and the major fund of Ulster Tobacco Asset Securitization Corporation (the "Corporation") as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the Corporation's basic financial statements, and have issued our report thereon dated March 13, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Corporation's internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control.

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 a 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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control 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 material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Corporation's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Drescher & Malecki LLP

March 13, 2018