

**ROCKLAND SECOND
TOBACCO ASSET SECURITIZATION
CORPORATION**

*(A Component Unit of the County of Rockland, New York)
Basic Financial Statements and Required
Supplementary Information for the
Years Ended December 31, 2018 and 2017
and Independent Auditors' Reports*

ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A COMPONENT UNIT OF THE COUNTY OF ROCKLAND, NEW YORK)

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Years Ended December 31, 2018 and 2017

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Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Rockland Second Tobacco Asset Securitization Corporation

Report on the Financial Statements

We have audited the accompanying financial statements of Rockland Second Tobacco Asset Securitization Corporation ("RSTASC"), a component unit of County of Rockland, New York, as of and for the year ended December 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise RSTASC's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

RSTASC'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 an opinion on these financial statements based on our audits. We conducted our audits 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 RSTASC, as of December 31, 2018 and 2017, and the respective changes in its financial position and cash flows 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 21, 2019 on our consideration of RSTASC'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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of RSTASC's 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 RSTASC's internal control over financial reporting and compliance.

Drescher + Malecki LLP

March 21, 2019

ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A Component Unit of the County of Rockland, New York)
Management's Discussion and Analysis
Years Ended December 31, 2018 and 2017

As management of the Rockland Second Tobacco Asset Securitization Corporation ("RSTASC"), a blended component unit of the County of Rockland, New York (the "County"), we offer readers of RSTASC's financial statements this narrative overview and analysis of the financial activities of RSTASC for the fiscal year ended December 31, 2018 and 2017. This document should be read in conjunction with additional information that we have furnished in RSTASC's financial statements, which follow this narrative.

Financial Highlights

- RSTASC's liabilities exceeded the assets by \$809,558, representing net position at December 31, 2018. This compares to RSTASC's liabilities exceeding assets by \$1,332,851 at December 31, 2017.
- RSTASC's net position increased \$523,293 for the year ended December 31, 2018.
- RSTASC's total Tobacco Settlement Bonds decreased by \$510,000 as a result of principal payments made during the year.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to RSTASC's basic financial statements. The financial statements are organized as follows:

- The *Statement of Net Position* presents information on all of RSTASC's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as "net position". Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the RSTASC is improving or deteriorating.
- The *Statement of Revenues, Expenses, and Changes in Net Position* presents information showing how RSTASC's net position changed during the most recent reporting period. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future periods.
- The *Statement of Cash Flows* presents information depicting RSTASC's cash flow activities for the most recent reporting period and the effect that these activities had on RSTASC's cash and cash equivalents balances.
- The *Notes to the Financial Statements* present additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found following the financial statements section of this report.

Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of an entity's financial position. In the case of RSTASC, liabilities exceeded assets by \$809,558 at December 31, 2018, as compared to \$1,332,851 and \$1,841,395 at December 31, 2017 and 2016, respectively, as presented below in Table 1:

Table 1—Condensed Statements of Net Position

	December 31,	
	2018	2017
Current assets	\$ 1,584,477	\$ 1,563,116
Total assets	<u>1,584,477</u>	<u>1,563,116</u>
Current liabilities	14,475	17,025
Noncurrent liabilities	<u>2,379,560</u>	<u>2,878,942</u>
Total liabilities	<u>2,394,035</u>	<u>2,895,967</u>
Net position	<u>\$ (809,558)</u>	<u>\$ (1,332,851)</u>

	December 31,	
	2017	2016
Current assets	\$ 1,563,116	\$ 1,546,204
Total assets	<u>1,563,116</u>	<u>1,546,204</u>
Current liabilities	17,025	69,275
Noncurrent liabilities	<u>2,878,942</u>	<u>3,318,324</u>
Total liabilities	<u>2,895,967</u>	<u>3,387,599</u>
Net position	<u>\$ (1,332,851)</u>	<u>\$ (1,841,395)</u>

RSTASC's unrestricted net position totals \$(809,558), \$(1,332,851), and \$(1,841,395) at December 31, 2018, 2017, and 2016, respectively.

At December 31, 2018, total assets were \$1,584,477 compared to \$1,563,116 and \$1,546,204 at December 31, 2017 and 2016, respectively. The largest asset held by RSTASC at December 31, 2018, 2017, and 2016 represents cash and cash equivalents.

Total liabilities at December 31, 2018 were \$2,394,035 compared to \$2,895,967 and \$3,387,599 at December 31, 2017 and 2016, respectively. The largest portion of the liabilities was outstanding debt (net Tobacco Settlement Bonds) totaling \$2,379,560, \$2,878,942, and \$3,318,324 at December 31, 2018, 2017, and 2016, respectively.

During the current year, RSTASC's net position increased \$523,293 from the prior fiscal year for an ending net position of \$(809,558). Table 2 on the following page, shows the changes in net position for the years ended December 31, 2018, 2017, and 2016.

Table 2—Changes in Net Position

	Year Ended December 31,	
	2018	2017
Operating revenues	\$ 711,178	\$ 738,259
Operating expenses	<u>53,902</u>	<u>42,868</u>
Operating income	<u>657,276</u>	<u>695,391</u>
Nonoperating revenues (expenses):		
Interest income	48,085	24,321
Interest expense	<u>(182,068)</u>	<u>(211,168)</u>
Total nonoperating revenues (expenses)	<u>(133,983)</u>	<u>(186,847)</u>
Change in net position	523,293	508,544
Net position—beginning	<u>(1,332,851)</u>	<u>(1,841,395)</u>
Net position—ending	<u>\$ (809,558)</u>	<u>\$ (1,332,851)</u>

	Year Ended December 31,	
	2017	2016
Operating revenues	\$ 738,259	\$ 782,129
Operating expenses	<u>42,868</u>	<u>32,960</u>
Operating income	<u>695,391</u>	<u>749,169</u>
Nonoperating revenues (expenses):		
Interest income	24,321	46,180
Interest expense	<u>(211,168)</u>	<u>(257,126)</u>
Total nonoperating revenues (expenses)	<u>(186,847)</u>	<u>(210,946)</u>
Net income before transfers	508,544	538,223
Transfer to County	<u>-</u>	<u>(50,000)</u>
Change in net position	508,544	488,223
Net position—beginning	<u>(1,841,395)</u>	<u>(2,329,618)</u>
Net position—ending	<u>\$ (1,332,851)</u>	<u>\$ (1,841,395)</u>

A summary of sources of revenues for the years ended December 31, 2018, 2017, and 2016 is presented below in Table 3.

Table 3—Summary Source of Revenues

	Year Ended December 31,		Increase/(Decrease)	
	2018	2017	Dollars	Percent (%)
Operating revenues:				
Tobacco settlement revenues	\$ 711,178	\$ 737,888	\$ (26,710)	(3.6)
Other operating revenue	-	371	(371)	(100.0)
Total operating revenues	<u>711,178</u>	<u>738,259</u>	<u>(27,081)</u>	<u>(3.7)</u>
Nonoperating revenues:				
Interest income	<u>48,085</u>	<u>24,321</u>	<u>23,764</u>	<u>97.7</u>
Total nonoperating revenues	<u>48,085</u>	<u>24,321</u>	<u>23,764</u>	<u>97.7</u>
Total revenues	<u>\$ 759,263</u>	<u>\$ 762,580</u>	<u>\$ (3,317)</u>	<u>(0.4)</u>
	Year Ended December 31,		Increase/(Decrease)	
	2017	2016	Dollars	Percent (%)
Operating revenues:				
Tobacco settlement revenues	\$ 737,888	\$ 781,393	\$ (43,505)	(5.6)
Other operating revenue	<u>371</u>	<u>736</u>	<u>(365)</u>	<u>(49.6)</u>
Total operating revenues	<u>738,259</u>	<u>782,129</u>	<u>(43,505)</u>	<u>(5.6)</u>
Nonoperating revenues:				
Interest income	<u>24,321</u>	<u>46,180</u>	<u>(21,859)</u>	<u>(47.3)</u>
Total nonoperating revenues	<u>24,321</u>	<u>46,180</u>	<u>(21,859)</u>	<u>(47.3)</u>
Total revenues	<u>\$ 762,580</u>	<u>\$ 828,309</u>	<u>\$ (65,729)</u>	<u>(7.9)</u>

Total revenues for the years ended December 31, 2018, 2017, and 2016 were \$759,263, \$762,580 and \$828,309, respectively. Total revenues for the years ended December 31, 2018, 2017 and 2016 consisted of \$711,178 (93.7 percent), \$737,888 (96.8 percent), and \$781,393 (94.3 percent), respectively, of tobacco settlement revenues, and \$48,085, \$24,692 and \$46,916, respectively, of interest income and other operating revenue.

A summary of expenses for the years ended December 31, 2018, 2017, and 2016 is presented below in Table 4.

Table 4—Summary Source of Expenses

	Year Ended December 31,		Increase/(Decrease)	
	2018	2017	Dollars	Percent (%)
Operating expenses:				
Directors' fees	\$ 13,000	\$ 13,000	\$ -	-
Professional fees	40,902	29,868	11,034	36.9
Total operating expenses	<u>53,902</u>	<u>42,868</u>	<u>11,034</u>	25.7
Nonoperating expenses:				
Interest expense	182,068	211,168	(29,100)	(13.8)
Total nonoperating expenses	<u>182,068</u>	<u>211,168</u>	<u>(29,100)</u>	(13.8)
Total expenses	<u>\$ 235,970</u>	<u>\$ 254,036</u>	<u>\$ (18,066)</u>	(7.1)
	Year Ended December 31,		Increase/(Decrease)	
	2017	2016	Dollars	Percent (%)
Operating expenses:				
Directors' fees	\$ 13,000	\$ 13,000	\$ -	-
Professional fees	29,868	19,960	9,908	49.6
Total operating expenses	<u>42,868</u>	<u>32,960</u>	<u>9,908</u>	30.1
Nonoperating expenses:				
Interest expense	211,168	257,126	(45,958)	(17.9)
Total nonoperating expenses	<u>211,168</u>	<u>257,126</u>	<u>(45,958)</u>	(17.9)
Transfer to County	<u>-</u>	<u>50,000</u>	<u>(50,000)</u>	(100.0)
Total expenses	<u>\$ 254,036</u>	<u>\$ 340,086</u>	<u>\$ (86,050)</u>	(25.3)

Total expenses for the years ended December 31, 2018, 2017, and 2016 were \$235,970, \$254,036 and \$340,086, respectively. Expenses for the years ended December 31, 2018, 2017, and 2016 primarily consisted of \$182,068 (77.2 percent), \$211,168 (83.1 percent), and \$257,126 (75.6 percent), respectively, of interest expense, and \$53,902 (22.8 percent), \$42,868 (16.9 percent), and \$32,960 (9.7 percent), of operating expenses. Additionally, there was a transfer to the County in the amount \$50,000 (14.7 percent), during the year ended December 31, 2016.

Debt Administration

Long-Term Debt—At the end of the current fiscal year, RSTASC had net Tobacco Settlement Bonds outstanding of \$2,379,560. During the years ended December 31, 2018 and 2017, RSTASC made principal payments of \$510,000 and \$450,000, respectively on its Tobacco Settlement Bonds. Additional information on RSTASC's long-term debt can be found in Note 4 to the financial statements.

Requests for Information

This financial report is designed to provide a general overview of RSTASC's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Rockland Second Tobacco Asset Securitization Corporation, c/o Commissioner of Finance, Rockland County, 18 New Hempstead Road, New City, New York 10956.

BASIC FINANCIAL STATEMENTS

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ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A Component Unit of the County of Rockland, New York)
Statements of Net Position
December 31, 2018 and 2017

	2018	2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 852,850	\$ 813,503
Interest receivable	10,925	11,725
Due from New York State	720,702	737,888
Total assets	1,584,477	1,563,116
 LIABILITIES		
Current liabilities:		
Accounts payable	1,250	1,250
Accrued interest payable	13,225	15,775
Noncurrent liabilities:		
Tobacco Settlement Bonds, net	2,379,560	2,878,942
Total liabilities	2,394,035	2,895,967
 NET POSITION		
Unrestricted	(809,558)	(1,332,851)
Total net position	\$ (809,558)	\$ (1,332,851)

The notes to the financial statements are an integral part of this statement.

ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A Component Unit of the County of Rockland, New York)
Statements of Revenues, Expenses, and Changes in Net Position
Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating revenues:		
Tobacco settlement revenue	\$ 711,178	\$ 737,888
Other operating revenue	-	371
Total operating revenue	<u>711,178</u>	<u>738,259</u>
 Operating expenses:		
Directors' fees	13,000	13,000
Professional fees	<u>40,902</u>	<u>29,868</u>
Total operating expenses	<u>53,902</u>	<u>42,868</u>
 Operating income	<u>657,276</u>	<u>695,391</u>
 Nonoperating revenues (expenses):		
Interest income	48,085	24,321
Interest expense	<u>(182,068)</u>	<u>(211,168)</u>
Total nonoperating revenues (expenses)	<u>(133,983)</u>	<u>(186,847)</u>
 Change in net position	523,293	508,544
 Net position—beginning	<u>(1,332,851)</u>	<u>(1,841,395)</u>
Net position—ending	<u>\$ (809,558)</u>	<u>\$ (1,332,851)</u>

The notes to the financial statements are an integral part of this statement.

ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A Component Unit of the County of Rockland, New York)
Statements of Cash Flows
Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from tobacco settlement revenues	\$ 728,364	\$ 672,594
Other operating revenue	-	371
Payments to directors	(13,000)	(13,000)
Payments to vendors	(40,902)	(29,868)
Net cash provided by operating activities	<u>674,462</u>	<u>630,097</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest income	48,885	24,321
Net cash provided by investing activities	<u>48,885</u>	<u>24,321</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Repayment of Tobacco Settlement Bonds	(510,000)	(450,000)
Payment to County	-	(50,000)
Interest paid	(174,000)	(202,800)
Net cash (used for) non-capital financing activities	<u>(684,000)</u>	<u>(702,800)</u>
Net increase (decrease) in cash and cash equivalents	39,347	(48,382)
Cash and cash equivalents—beginning	813,503	861,885
Cash and cash equivalents—ending	<u>\$ 852,850</u>	<u>\$ 813,503</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating income:	\$ 657,276	\$ 695,391
Adjustments to reconcile operating income to net cash provided by operating activities:		
Decrease (increase) in amounts due from New York State	17,186	(65,294)
Total adjustments	<u>17,186</u>	<u>(65,294)</u>
Net cash provided by operating activities	<u>\$ 674,462</u>	<u>\$ 630,097</u>

The notes to the financial statements are an integral part of this statement.

ROCKLAND SECOND TOBACCO ASSET SECURITIZATION CORPORATION
(A Component Unit of the County of Rockland, New York)
Notes to the Financial Statements
Years Ended December 31, 2018 and 2017

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Rockland Second Tobacco Asset Securitization Corporation ("RSTASC") have been prepared in conformity with accounting principles generally accepted in the United States of America applied to government units. The Governmental Accounting Standards Board ("GASB") is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of RSTASC's accounting policies are described below.

Reporting Entity

RSTASC is a special purpose, bankruptcy-remote, local development corporation. RSTASC was organized under the provisions of Section 1411 of the New York State Not-For-Profit Corporation Law and pursuant to the Public Authorities Law of the State of New York. The Board of Directors of RSTASC consists of five members; two designees of the County of Rockland, New York's ("County") County Executive, one designee of the Chairman of the County's Board of Legislators, one designee of the Chairman of the Budget and Finance Committee of the County's Board of Legislators and a fifth director who meets certain requirements of independence and shall be designated by a majority of the other four members. Although legally separate from the County, RSTASC is a component unit of the County. Based on the nature and significance of RSTASC's relationship with the County and the criteria set forth by GASB, RSTASC is included within the County's basic financial statements as a blended component unit. The Board of Directors has elected to present the activity of RSTASC as a proprietary fund type (Enterprise Fund).

The Master Settlement Agreement ("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.

During 2001, the County sold all of its future rights, title and interest to receive payments under the MSA and the Consent Decree to the Rockland Tobacco Asset Securitization Corporation ("RTASC"). Pursuant to an assignment from RTASC to RSTASC and a purchase and sale agreement by and among the County, the Rockland Residual Trust (of which the County is the beneficial owner) and RSTASC, the RSTASC is acquiring all of the right, title and interest to the twenty percent share of Tobacco Settlement Revenues ("TSR's") that are not pledged to the RTASC bondholders. The debt issued by RSTASC to securitize these revenues is not considered debt of the County and is secured only by future tobacco settlement payments.

In accordance with the Bond Indenture and to the extent contained in the MSA Report, a trapping event has occurred. A Consumption Decline Trapping Event occurs when shipments of cigarettes in or to the 50 United States, the District of Columbia and Puerto Rico as measured under the MSA, are less in any year preceding a deposit date than the amount opposite such year under the “Consumption Decline Trapping Event” definition, which number for the year 2017 was 248,544,765,996. According to the MSA Report, the amount shown as relevant shipments for the year 2017 was less than the shipment amount specified above, and therefore a Consumption Decline Trapping Event has occurred.

Measurement Focus and Basis of Accounting

The financial statements of RSTASC 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 activities of RSTASC are accounted for similar to those often found in the private sector using the flow of economic resources measurement focus and the accrual basis of accounting. All assets, deferred outflows, liabilities, deferred inflows, net position, revenues and expenses are accounted for through a single enterprise fund with revenues recorded when earned and expenses recorded at the time liabilities are incurred.

Tobacco settlement revenues are exchange transactions, based on the notion that the payments are made to the settling states in exchange for their agreement to release the tobacco companies from present and future litigation. Under the terms of the MSA, the tobacco companies have agreed to make annual payments in perpetuity. The MSA includes a schedule of projected annual base payments, subject to certain adjustments based on future events or circumstances. The most significant factor affecting the annual payments is a *volume adjustment*, which creates a direct relationship between domestic shipments of cigarettes and the annual payments. Based on the MSA, the tobacco companies have no obligation to make settlement payments until cigarettes are shipped.

The event that results in the recognition of an asset and revenue by a settling government is the domestic shipment of cigarettes (sales). Therefore, RSTASC recognizes a receivable and revenue for tobacco settlement revenues when that event occurs. Because annual tobacco settlement revenue payments are based on cigarette sales from the preceding calendar year, RSTASC estimates accrued tobacco settlement revenues that derive from sales from January 1 to their respective fiscal year ends.

Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position

Cash, Cash Equivalents and Investments—Cash and cash equivalents consist of cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date acquired by RSTASC. At December 31, 2018 and 2017, RSTASC does not report any investments; however, when RSTASC does have investments they are recorded at fair value in accordance with GASB.

Due From New York State—Represents an estimate of RSTASC’s portion of the Master Settlement Agreement.

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) until then. At December 31, 2018 and 2017, RSTASC reports no 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, 2018 and 2017, RSTASC reported no deferred inflows of resources.

Net Position Flow Assumption—Sometimes RSTASC 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 statement of net position, a flow assumption must be made about the order in which the resources are considered to be applied. It is RSTASC’s policy to consider restricted—net position to have been depleted before unrestricted—net position is applied.

Revenues and Expenses

Tobacco Settlement Revenues—During the fiscal year ended December 31, 2018, RSTASC recognized tobacco settlement revenues as a result of a New York State settlement agreement. Payments are made according to a set formula based on tobacco sales.

Expenses—Expenses are recorded on the accrual basis of accounting. Operating expenses consist of administrative costs for professional service fees and directors’ fees and are paid from revenues.

Other

Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets, liabilities, deferred inflows of resources, deferred outflows of resources, and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

Adoption of New Accounting Pronouncements—During the year ended December 31, 2018, RSTASC implemented GASB Statements No. 75, *Accounting and Financial Reporting for Postemployment Benefit Plans Other Than Pensions*; No. 85, *Omnibus 2017*; and No. 86, *Certain Debt Extinguishment Issues*. GASB Statement No. 75 improves accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). GASB Statement No. 85 addressed practice issues that have been identified during implementation and application of certain GASB Statements. GASB Statement No. 86 improves consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. GASB Statements No. 75, 85, and 86 did not have a material impact on RSTASC’s financial position or results from operations.

Future Impacts of Accounting Pronouncements—RSTASC has not completed the process of evaluating the impact that will result from adopting GASB Statements No. 83, *Certain Asset Retirement Obligations*; No. 84, *Fiduciary Activities*; No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*; and No. 90, *Majority Equity Interests—an amendment of GASB Statements No. 14 and No. 61*, effective for the year ending December 31, 2019,

and No. 87, *Leases*; and No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, effective for the year ending December 31, 2020. RSTASC is, therefore, unable to disclose the impact that adopting GASB Statements No. 83, 84, 87, 88, 89 and 90 will have on its financial position and results of operations when such statements are adopted.

Deficit Net Position—At December 31, 2018, RSTASC reported a net position of \$(809,558). The deficit is caused by long-term obligations that are greater than currently available resources.

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

2. CASH AND CASH EQUIVALENTS

RSTASC’s investment policies are governed by New York State statutes. All deposits are carried at fair value. Collateral is required for demand deposit accounts, time deposit accounts and certificates of deposit not covered by Federal deposit insurance (FDIC). RSTASC has entered into custodial agreements with the various banks which hold their deposits. These agreements authorize the obligation that may be pledged as collateral. Obligations that may be pledged as collateral are outlined in Chapter 623 of the laws of the State of New York.

Cash and cash equivalents of RSTASC at December 31, 2018 and 2017 consisted of the following:

	2018	2017
Cash on deposit	\$ 109,247	\$ 83,882
Money market funds	32,547	18,660
Commercial paper	711,056	710,961
Total	<u>\$ 852,850</u>	<u>\$ 813,503</u>

Deposits—All deposits including cash in bank and certain investments (i.e. certificates of deposit) are carried at fair value and are classified by custodial credit risk at December 31, 2018 and 2017 as follows:

	Bank Balance	Carrying Amount
Deposits at December 31, 2018:		
FDIC insured	<u>\$ 109,247</u>	<u>\$ 109,247</u>
Deposits at December 31, 2017:		
FDIC insured	<u>\$ 83,882</u>	<u>\$ 83,882</u>

Cash Equivalents—Cash equivalents held by RSTASC includes money market accounts and commercial paper with maturity dates within three months of year-end. These cash equivalents are carried at amortized cost.

Custodial Credit Risk—Deposits—In the case of deposits, this is the risk that in the event of a bank failure, RSTASC’s deposits may not be returned to it. As noted above, by State statute all deposits in excess of FDIC insurance coverage must be collateralized. As of December 31, 2018 and 2017, the RSTASC’s deposits were FDIC insured.

Custodial Credit Risk—Cash Equivalents—For cash equivalents, this is the risk that, in the event of the failure of the counterparty, RSTASC will not be able to recover the value of its cash equivalents or collateral securities that are in the possession of an outside party. For cash equivalents, this is the risk that in the event of a bank failure, RSTASC’s cash equivalents may not be returned to it.

Interest Rate Risk—As a means of limiting its exposure to fair value losses arising from fluctuating interest rates, it is RSTASC’s practice to generally limit investments to 180 days or less.

3. RECEIVABLES

Due from New York State—Represents amounts owed to RSTASC for tobacco settlement revenue of the MSA. RSTASC has accrued tobacco settlement revenue due from New York State of \$720,702 and \$737,888 within the statement of net position at December 31, 2018 and 2017, respectively.

Interest Receivable—Represents interest income earned in 2018 and 2017 on commercial paper owed to RSTASC.

4. LONG-TERM DEBT

RSTASC issued Tobacco Settlement Bonds on December 18, 2003 to finance the purchase of the tobacco rights from RTASC and the related costs of issuance. The bonds were issued for \$9,275,102, net of original issue discount of \$439,898 and bear interest at rates ranging from 5.027% to 6.27%, depending on maturity. Annual principal payments on Tobacco Settlement Bonds are dependent on TSR revenue received, therefore, the current portion considered payable during the year ending December 31, 2019 is not determinable. The stated maturity date for the bonds is June 1, 2043; the bonds must be paid in full by this date in order to avoid an event of default.

Changes in bonds payable for the Tobacco Settlement Bonds, Series 2003 for the years ended December 31, 2018 and 2017 are as follows:

Description	Year of Maturity	Yield	Beginning Balance			Ending Balance
			1/1/2018	Additions	Deletions	12/31/2018
2003 Tobacco Settlement Bonds	2043	5.027-6.27	\$ 3,155,000	\$ -	\$ 510,000	\$ 2,645,000
Less:						
Bond discount			(276,058)	-	(10,618)	(265,440)
Net Tobacco Settlement Bonds			<u>\$ 2,878,942</u>	<u>\$ -</u>	<u>\$ 499,382</u>	<u>\$ 2,379,560</u>
Description	Year of Maturity	Yield	Beginning Balance			Ending Balance
			1/1/2017	Additions	Deletions	12/31/2017
2003 Tobacco Settlement Bonds	2043	5.027-6.27	\$ 3,605,000	\$ -	\$ 450,000	\$ 3,155,000
Less:						
Bond discount			(286,676)	-	(10,618)	(276,058)
Net Tobacco Settlement Bonds			<u>\$ 3,318,324</u>	<u>\$ -</u>	<u>\$ 439,382</u>	<u>\$ 2,878,942</u>

5. NET POSITION

The RSTASC financial statements utilize a net position presentation. The total net position of \$(809,558) and \$(1,332,851) is categorized as unrestricted at December 31, 2018 and 2017, respectively. Unrestricted net position indicates that it is not restricted for any other purpose.

6. CONTINGENCIES

The ability of RSTASC to meet debt service payments of the turbo term bonds is contingent upon the receipt of TSRs. TSRs are principally dependent upon future levels of domestic consumption. A significant decline in the overall consumption of cigarettes could have a material adverse effect on the payments by the OPMs under the MSA and the amounts available to RSTASC to make payments of principal and interest on their bonds.

Certain smokers, smokers' rights organizations, consumer groups, cigarette importers, cigarette distributors, cigarette manufacturers, Native American tribes, taxpayer, 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 OPMs 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.

7. SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 21, 2019, which is the date the financial statements are available for issuance, and have determined there are no subsequent events that require disclosure under generally accepted accounting principles.

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Certified Public Accountants

**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
Rockland Second 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 Rockland Second Tobacco Asset Securitization Corporation ("RSTASC") as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise RSTASC's basic financial statements, and have issued our report thereon dated March 21, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered RSTASC'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 RSTASC's internal control. Accordingly, we do not express an opinion on the effectiveness of the RSTASC'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 RSTASC'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 21, 2019