

**CHEMUNG TOBACCO ASSET SECURITIZATION
CORPORATION**

FINANCIAL STATEMENTS

DECEMBER 31, 2009

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Chemung Tobacco Asset Securitization Corporation
Elmira, New York

We have audited the accompanying statements of financial position of Chemung Tobacco Asset Securitization Corporation, a blended component unit of the County of Chemung New York, as of December 31, 2009 and 2008, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of management. 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Chemung Tobacco Asset Securitization Corporation as of December 31, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 15, 2010, on our consideration of Chemung Tobacco Asset Securitization Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

EFP Rotenberg, LLP

EFP Rotenberg, LLP
Elmira, New York
March 15, 2010

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Statements of Financial Position
December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ASSETS		
Assets		
Cash and cash equivalents	\$ 54,273	\$ 36,791
Tobacco settlement proceeds receivable	710,142	701,666
Restricted cash - liquidity reserve	648,254	656,212
Restricted cash - trapping reserve	378,249	317,321
Restricted securities - held in trust	-	22,904
Unamortized bond issuance costs - net	<u>168,601</u>	<u>179,602</u>
Total Assets	<u>\$ 1,959,519</u>	<u>\$ 1,914,496</u>
LIABILITIES AND NET DEFICIT		
Liabilities		
Accounts payable	\$ 80	\$ -
Bonds payable - net of discount	<u>6,398,438</u>	<u>6,628,750</u>
Total Liabilities	<u>6,398,518</u>	<u>6,628,750</u>
Net Deficit		
Unrestricted net deficit	<u>(4,438,999)</u>	<u>(4,714,254)</u>
Total Liabilities and Net Deficit	<u>\$ 1,959,519</u>	<u>\$ 1,914,496</u>

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

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Statements of Activities
For the Years Ended December 31, 2009 and 2008

	<u>2009</u>	<u>%</u>	<u>2008</u>	<u>%</u>
Revenues				
Tobacco settlement proceeds	\$ 748,090	99.9	\$ 679,758	93.6
Interest and investment income	<u>261</u>	<u>0.1</u>	<u>46,607</u>	<u>6.4</u>
Total revenues	<u>748,351</u>	<u>100.0</u>	<u>726,365</u>	<u>100.0</u>
Expenses				
Administrative fees	10,650	1.4	2,855	0.4
Amortization expense	11,001	1.5	12,651	1.7
Bank fees	40	-	40	-
Insurance expense	7,589	1.0	8,003	1.1
Interest expense	429,791	57.4	444,264	61.2
Investment fees	6,765	0.9	6,765	0.9
Miscellaneous	-	-	56	-
Professional fees	6,250	0.8	5,650	0.8
Utilities	<u>1,010</u>	<u>0.1</u>	<u>858</u>	<u>0.1</u>
Total expenses	<u>473,096</u>	<u>63.1</u>	<u>481,142</u>	<u>66.2</u>
Change in Net Assets	275,255	<u>36.9</u>	245,223	<u>33.8</u>
Net Deficit - Beginning	<u>(4,714,254)</u>		<u>(4,959,477)</u>	
Net Deficit - Ending	<u>\$ (4,438,999)</u>		<u>\$ (4,714,254)</u>	

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

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Statements of Cash Flows
For the Years Ended December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Cash Flows from Operating Activities		
Proceeds of tobacco receipts	\$ 739,615	\$ 670,696
Interest and dividends received	261	48,981
Payments of operating expenses	(32,225)	(28,976)
Payments of bond interest expense	<u>(425,103)</u>	<u>(438,906)</u>
Net cash flows from operating activities	<u>282,548</u>	<u>251,795</u>
Cash Flows from Investing Activities		
Increase in restricted cash and investments	<u>(30,066)</u>	<u>(13,178)</u>
Cash Flows from Financing Activities		
Principal repayment of bonds payable	<u>(235,000)</u>	<u>(215,000)</u>
Net Change in Cash and Cash Equivalents	17,482	23,617
Cash and Cash Equivalents - Beginning	<u>36,791</u>	<u>13,174</u>
Cash and Cash Equivalents - Ending	<u>\$ 54,273</u>	<u>\$ 36,791</u>
Reconciliation of Change in Net Assets to Net Cash Flows from Operating Activities		
Change in net assets	\$ 275,255	\$ 245,223
Adjustments		
Unrealized gain	-	(2,374)
Amortization	11,001	12,651
Consumption of discount on bonds	4,688	5,358
Changes in assets and liabilities		
Tobacco proceeds receivable	(8,476)	(9,063)
Increase in accounts payable	<u>80</u>	<u>-</u>
Net cash flows from operating activities	<u>\$ 282,548</u>	<u>\$ 251,795</u>

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

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

Nature of the Organization - In January 1997, the State of New York filed a lawsuit against the tobacco industry, seeking to recover the costs that the State and local governments had incurred in treating smoking related illnesses. Chemung Tobacco Asset Securitization Corporation (the Corporation) was established to acquire from Chemung County all or a portion of the rights, title and interest under the Master Settlement Agreement (the "MSA") and the Consent Decree and Final Judgment (the "Decree") as described herein.

The MSA includes New York and 45 other states, 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 four of the largest United States tobacco product manufacturers: Philip Morris Incorporated, R.J. Reynolds Tobacco Company, Brown and Williamson Tobacco Company (B&W), and Lorillard Tobacco Company (collectively, the "Original Participating Manufacturers" or "OPMs"). On January 5, 2004, Reynolds American Inc. was incorporated as a holding company to facilitate the combination of the U.S. assets, liabilities, and operations of B&W with those of Reynolds Tobacco. The agreement was entered into 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 Corporation was formed to raise funds by issuing bonds, use those funds to acquire the rights to future proceeds from a settlement agreement with various tobacco companies payable to the County, and remain in existence during the term of the bonds to collect the tobacco settlement proceeds and service the debt.

The Corporation is dependent on future proceeds from the settlement agreement. Proceeds received in excess of the Corporation's operational expenses, debt service and required reserves are transferred to the County, as the beneficial owner of the residual certificate, subject to restrictions imposed by certain trapping events.

During 2003, the Corporation adopted its first amendment to the indenture, dated as of December 1, 2000, between the Corporation and Manufacturers and Traders Trust Company (M&T), as Trustee. The amendment effectively modifies the indenture to be consistent with the official statement concerning downgrade trapping events as being immediate, in the year in which the event occurred.

The Corporation is a local development corporation created in October 2000 under Section 1411 of the New York State Not-for-Profit Corporation Law. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 39, Determining Whether Certain Organizations are Component Units, and Technical Bulletin 2004-1, Tobacco Settlement Recognition and Financial Reporting Entity Issues, the Corporation is required to be included in the basic financial statements of the Chemung County, New York. Accordingly, the Corporation is presented as a blended component unit of the County.

Basis of Presentation - The preparation of financial statements is in conformity with accounting principles generally accepted in the United States of America.

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 assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - For purposes of the statements of financial position and statements of cash flows, cash and cash equivalents includes commercial paper, cash in money market funds, certificates of deposit, and all highly liquid investments with original maturities of three months or less. The Corporation maintains cash and cash equivalents at financial institutions which periodically may exceed federally insured limits.

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Notes to Financial Statements

Income Taxes - The Organization is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. In June 2006, the Financial Accounting Standards Board (FASB) issued Accounting Standards Codification (ASC) 740-10-50 (prior authoritative literature: FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes), which prescribed a comprehensive model for how an organization should measure, recognize, present, and disclose in its financial statements uncertain tax positions that the organization has taken or expects to take on their informational returns. ASC 740-10-50 is effective for nonpublic entities for years beginning after December 15, 2008. The Organization adopted ASC 740-10-50 as of January 1, 2009 and, thereafter, recognizes the tax benefits from uncertain tax positions only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities. Management believes that the Organization is currently operating in compliance with the applicable requirements of the Internal Revenue Code. Therefore, no liability for unrecognized tax benefits has been included on the Organization's financial statements. The Organization is exempt from the filing of any informational returns and therefore there are no open audit periods.

Subsequent Events - On May 28, 2009, the FASB issued ASC 855-10 (prior authoritative literature: Statement of Financial Accounting Standards No. 165, Subsequent Events). ASC 855-10 provides guidance on management's assessment of subsequent events and requires additional disclosure about the timing of management's assessment of subsequent events. ASC 855-10 does not significantly change the accounting requirements for the reporting of subsequent events. ASC 855-10 is effective for interim or annual financial periods ending after June 15, 2009. The Corporation adopted ASC 855-10 as of December 31, 2009 and accordingly assessed subsequent events in these financial statements from December 31, 2009 through March 15, 2010. The adoption of this standard did not materially impact the Corporation's financial position, results of operations, changes in net assets or disclosures in the financial statements.

Note 2. Tobacco Settlement Proceeds Receivable

This asset represents estimated payments to be received from the MSA between various tobacco manufacturers and state and local governments. The MSA resolved cigarette smoking-related litigation between the manufacturers and the states. The right to receive the payments was acquired by the Corporation through a purchase from the County. As of December 31, 2009 and 2008 the tobacco settlement proceeds receivable amounted to \$710,142 and \$701,666, respectively.

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Notes to Financial Statements

Note 3. Bonds Payable

The bonds were issued on December 7, 2000 as part of the New York State Counties Tobacco Trust/Tobacco Settlement Pass-Through Bond Series 2000. Face value of the bonds issued was \$8,090,000. The bonds were sold at a discount of \$116,695, for a net issue price of \$7,973,305. The discount will be amortized over the maturity period of the bonds. The weighted average maturity period of the bonds is 15.914 years with a final maturity date of December 31, 2025. Interest on the bonds ranges from 5.000% to 6.625%. The repayment schedule is based on the flexible amortization payments which accelerates the maturity date. In the event sufficient funds are not available to meet maturities, rated maturity dates will be used to extend the maturity schedule of the bonds. As of December 31, 2009 and 2008 the face value of the bonds was \$6,470,000 and \$6,705,000 with remaining discount of \$71,562 and \$76,250, respectively.

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 265,000	\$ 409,759	\$ 674,759
2011	270,000	393,359	663,359
2012	285,000	376,321	661,321
2013	300,000	358,271	658,271
2014	315,000	338,971	653,971
2015 - 2019	2,010,000	1,350,941	3,360,941
2020 - 2024	2,965,000	532,198	3,497,198
2025	60,000	1,987	61,987
	<u>\$ 6,470,000</u>	<u>\$ 3,761,807</u>	<u>\$ 10,231,807</u>

The cost of issuing the bonds has been capitalized and is reported on the statement of financial position as unamortized bond issuance costs. Amortization of the costs, using the effective interest method, is as follows:

	<u>2009</u>	<u>2008</u>
Bond issuance cost	\$ 275,016	\$ 275,016
Accumulated amortization	<u>(106,415)</u>	<u>(95,414)</u>
Unamortized bond issuance costs	<u>\$ 168,601</u>	<u>\$ 179,602</u>

Note 4. Restricted Cash - Liquidity Reserve

The Corporation is required to place a portion of the bond proceeds in trust as a reserve to partially secure payments to the bond holders. The restriction on these funds will be released as the bonds mature and are paid. As of December 31, 2009 and 2008, the restricted cash - liquidity reserve amounted to \$648,254 and \$656,212, respectively.

Note 5. Restricted Cash - Trapping Reserve

The Corporation is required to place a portion of the bond proceeds in excess of debt service and operational expenses in this account when a "trapping" event occurs. The trapping events include "consumption decline," "downgrade," "lump sum" and "NPM" trapping requirements. During 2003, a downgrade trapping event occurred whereby an Original Participating Manufacturer, with a market share of 7% or more, received a credit rating below "Baa3" by Moody's or "BBB" by Standard and Poors. The downgrade event requires that an amount equal to 25% of the outstanding bond principal be trapped until one year after the end of the downgrade trapping condition. As of December 31, 2008, there were insufficient available assets to fully satisfy the 25% trapping requirement. Future payments of residual certificates will be suspended, and available monies trapped, until the 25% trapping requirement is satisfied or the downgrade condition is removed. The Corporation began funding this account during 2003 and the outstanding balance at December 31, 2009 and 2008 was \$378,249 and \$317,321, respectively.

In August 2008 the trapping event ended and as of December 31, 2009 the balance in the trapping account is due to the County, the holder of the residual certificate.

CHEMUNG TOBACCO ASSET SECURITIZATION CORPORATION
Notes to Financial Statements

Note 6. Restricted Cash - Held in Trust

Tobacco proceeds are held in trust by M&T on behalf of the Corporation. M&T invests the proceeds in highly liquid, interest bearing securities, and performs the transfer of the debt obligations upon the instruction of Bond Logistics, the administrator retained by the Corporation. As of December 31, 2009 and 2008, the restricted cash - held in trust amounted to \$- and \$22,904, respectively.

Note 7. Residual Receivable/Payable to Chemung County

The Corporation receives 100% of the County's tobacco settlement proceeds, although only 40% are applicable to the Corporation. The residual 60% is refundable to the County. As of December 31, 2009 and 2008, none of the residual assets due to the County were held by the Corporation, respectively.

Note 8. Related Party

The Corporation is a special purpose local development corporation, and is considered by legal counsel to be bankruptcy-remote from the County. However, the Corporation's board of directors is comprised of four elected or appointed officials of the County, and one independent director. For financial statement purposes, the Corporation is considered to be a blended component unit of the County.

Note 9. Net Deficit

The net deficit is due to various expenses associated with the bonds. The future cash receipts from the Master Settlement Agreement (MSA) are expected to offset this deficit. The largest payments provided for in the MSA are called initial payments and annual payments. Both are subject to certain adjustments, reductions and offsets, which are described in the following paragraphs.

Initial payments to New York State will be made in the first five years of the agreement, starting with \$2.4 billion in 1999; the last four of these will be subject to the volume adjustments, the non-settling states reduction, and the offset for miscalculated or disputed payments. The Corporation is receiving the County's share of the payment in the last three years of the agreement, starting in 2001.

Annual payments to the State commenced on April 15, 2000, starting at \$2.5 billion in 2000 and continuing into perpetuity at a cap of \$9 billion to be reached in 2018. The annual payments will be subject to inflation adjustment, the volume adjustment, the previously settled states reduction, the non-settling states reduction, the non-participating manufacturers adjustment, the offset for miscalculated or disputed payments, the federal tobacco legislation offset, the litigating parties offset, and the offsets for claims. The Corporation started receiving the County's portion of the annual payments on April 15, 2001.

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

The Board of Directors
Chemung Tobacco Asset Securitization Corporation
Elmira, New York

We have audited the financial statements of the Chemung Tobacco Asset Securitization Corporation, a blended component unit of the County of Chemung New York, as of and for the year ended December 31, 2009, and have issued our report thereon dated March 15, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Chemung Tobacco Asset Securitization Corporation's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclose no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors and management of the Chemung Tobacco Asset Securitization Corporation and is not intended to be and should not be used by anyone other than these specified parties.

EFP Rotenberg, LLP

EFP Rotenberg, LLP
Elmira, New York
March 15, 2010