



TSASC, Inc.

A COMPONENT UNIT OF THE CITY OF NEW YORK

Financial Statements
(Together with Independent Auditors' Report)

Years Ended June 30, 2017 and 2016

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ACCOUNTANTS & ADVISORS

TSASC, INC.
FINANCIAL STATEMENTS
(Together with Independent Auditors' Report)
YEARS ENDED JUNE 30, 2017 AND 2016

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INDEPENDENT AUDITORS' REPORT

To the Members of the Board of Directors of
TSASC, Inc.

We have audited the accompanying financial statements of the governmental activities of TSASC, Inc. ("TSASC"), a component unit of The City of New York, as of and for the years ended June 30, 2017 and 2016, which collectively comprise TSASC's basic financial statements as listed in the table of contents, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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.

Auditors' 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit 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 opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities of TSASC, Inc. as of June 30, 2017 and 2016, and the respective changes in financial position thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 11 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 audits 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.



New York, NY
September 21, 2017

TSASC, INC.

(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017 AND 2016

(unaudited)

The following is a narrative overview and analysis of the financial activities of TSASC, Inc. ("TSASC") for the fiscal years ended June 30, 2017 and 2016. It should be read in conjunction with TSASC's government-wide financial statements, governmental funds financial statements and the notes to the financial statements. The financial statements consist of four parts: (1) management's discussion and analysis (this section); (2) the government-wide financial statements; (3) the governmental funds financial statements; and (4) the notes to the financial statements.

The government-wide financial statements, which include the statements of net position (deficit) and the statements of activities, are presented to display information about the reporting entity as a whole, in accordance with Governmental Accounting Standards Board ("GASB") standards. This is to provide the reader with a broad overview of TSASC's finances. The government-wide financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Accordingly, revenue is recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows.

TSASC's governmental funds financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting, in which revenue is recognized when it becomes susceptible to accrual; that is, when it becomes both measurable and available to finance expenditures in the current fiscal period. As such, revenues are considered available if received within two months after the fiscal year end. Expenditures are recognized when the related liability is incurred, except for principal and interest on bonds payable, which are recognized when due.

The reconciliations of the governmental funds balance sheets to the statements of net position (deficit) and the reconciliations of the governmental funds statements of revenues, expenditures and changes in fund balances to the statements of activities are presented to assist the reader in understanding the differences between government-wide and governmental funds financial statements.

On February 8, 2006, TSASC issued \$1.35 billion of Series 2006-1 bonds, the proceeds of which were used to restructure all of TSASC's outstanding indebtedness. The Amended and Restated Indenture dated January 1, 2006, (the "2006 Indenture") provides that 62.6% of TSASC's annual collection of Tobacco Settlement Revenues ("TSRs") and the related interest earnings are transferred to the TSASC Tobacco Settlement Trust (the "Trust"), as owner of the Residual Certificate. The City of New York (the "City") is the beneficial owner of the Trust and the funds received by the Trust, net of the Trust's expenses, are transferred to the City.

The 2006 Indenture also provides that a defined portion of the TSRs and other revenues (collectively, "Collections") are applied to the payment of the Series 2006-1 debt service. The proportion of Collections pledged to the payment of the Series 2006-1 debt service is 37.4%. The turbo redemption feature requires all the pledged Collections, after funding of operating costs, be applied to the payment of principal and interest on the Series 2006-1 bonds.

On January 19, 2017, TSASC issued \$613.4 million 2017 Series A senior bonds and \$489.7 million 2017 Series B subordinate bonds, which allowed TSASC to refund all of its Series 2006-1 bonds outstanding. Of the \$489.7 million 2017 Series B subordinate bonds, \$450.0 million were exchanged rather than refunded. The Amended and Restated Indenture dated December 1, 2016, (the "2016 Indenture") continues to provide that 37.4% of Collections are pledged for the payment of debt service and the operating costs of TSASC and that 62.6% are transferred to the Trust. During fiscal years 2017 and 2016, TSASC transferred to the Trust \$100.3 million and \$229.0 million, respectively.

In 2015, New York State entered into an agreement with the tobacco companies that resolved all past and future disputes relating to the sales by non-participating manufacturers ("NPM Adjustment"). The New York State NPM Settlement Agreement ("NPM Settlement Agreement") released 90% of withheld TSRs between 2004 through 2014. New York State received a total of \$701 million from the disputed escrow account, of which TSASC received \$176 million.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS – GOVERNMENT-WIDE FINANCIAL STATEMENTS

The following summarizes the activities of TSASC for the years ended June 30,

	2017	2016	2015	Variance	
				2017/2016	2016/2015
	(in thousands)				
Revenues:					
Tobacco settlement revenue	\$ 164,161	\$ 368,783	\$ 180,094	\$ (204,622)	\$ 188,689
Investment earnings	580	1,271	503	(691)	768
Total revenues	164,741	370,054	180,597	(205,313)	189,457
Expenses:					
Transfer to the Trust	102,811	230,910	112,743	(128,099)	118,167
Cost of issuance	7,575	-	-	7,575	-
Interest expense	55,741	62,359	63,002	(6,618)	(643)
Loss on defeasance	2,967	-	-	2,967	-
Other expense	659	423	440	236	(17)
Total expenses	169,753	293,692	176,185	(123,939)	117,507
Change in net position	(5,012)	76,362	4,412	(81,374)	71,950
Net position (deficit), beginning of year	(980,376)	(1,056,738)	(1,061,150)	76,362	4,412
Net position (deficit), end of year	<u>\$ (985,388)</u>	<u>\$ (980,376)</u>	<u>\$ (1,056,738)</u>	<u>\$ (5,012)</u>	<u>\$ 76,362</u>

TSRs generally earned during the fiscal year are based upon tobacco sales of the previous calendar year; adjusted by factors such as inflation, volume, and disputed amounts deposited/released by the participating cigarette manufacturers into a MSA disputed escrow account, and the amount of reduction tied to the volume of cigarettes manufactured and sold on Native American reservations. TSASC earned TSRs of approximately \$164.2 million, \$368.8 million, and \$180.1 million in fiscal years 2017, 2016 and 2015, respectively. The large fluctuation in tobacco revenue between fiscal years was primarily due to the release, in fiscal year 2016, of funds from the disputed payment escrow account for settlement payments related to the years 2004 through 2014, discussed later.

The variances of investment earnings in fiscal years 2017, 2016 and 2015 were primarily attributable to market value fluctuations of long-term investments. The large decrease in fiscal year 2017 when compared to fiscal year 2016 was due to the liquidation of high yielding long-term investments held in the previous year.

Transfers to the Trust are based on TSRs received during the fiscal year and fluctuated each year as previously discussed. Interest expense decreased in fiscal year 2017 due to the bond refunding transaction. Interest expense decreased in fiscal years 2016 and 2015 because of the declining bond principal balances, which were being reduced by the turbo redemption feature. Other expenses in fiscal years 2017, 2016 and 2015 were composed of general and administrative costs and the increase in fiscal year 2017 was due to the increased allocated administrative costs associated with management's time spent on the refunding transaction.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS – GOVERNMENT-WIDE FINANCIAL STATEMENTS (continued)

The following summarizes TSASC's assets, deferred outflows of resources, liabilities, and net position (deficit) as of June 30,

	2017	2016	2015	Variance	
				2017/2016	2016/2015
	(in thousands)				
Assets:					
Total assets - non-capital	\$ 193,204	\$ 193,255	\$ 191,595	\$ (51)	\$ 1,660
Deferred outflows of resources	18,492	-	-	18,492	-
Liabilities:					
Current liabilities	73,840	53,025	51,464	20,815	1,561
Long-term liabilities	1,123,244	1,120,606	1,196,869	2,638	(76,263)
Total liabilities	1,197,084	1,173,631	1,248,333	23,453	(74,702)
Net position (deficit):					
Unrestricted	(985,388)	(980,376)	(1,056,738)	(5,012)	76,362
Net position (deficit), end of year	\$ (985,388)	\$ (980,376)	\$ (1,056,738)	\$ (5,012)	\$ 76,362

TSASC's total assets for the fiscal years 2017, 2016 and 2015 primarily consisted of cash equivalents and investments restricted for debt service and of TSRs due to TSASC at fiscal year-end.

The deferred outflows of resources reported in fiscal year 2017 resulted from the 2017 bond refunding transaction and represents the difference between removing the carrying amount of the Series 2006-1 bonds and recording the 2017 Series A and B bonds transaction.

Current liabilities are composed of accrued operating expenses, accrued interest expenses, TSRs payable to the Trust and bonds payable due within one year. The increase in current liabilities in fiscal year 2017 was due to the structure of the 2017 Series A and 2017 Series B bonds scheduled annual principal payments.

Long-term liabilities decreased significantly in fiscal year 2016 due to the NPM Settlement Agreement (discussed later) and turbo redemption feature (Note 1) of the Series 2006-1 bonds.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - GOVERNMENTAL FUNDS FINANCIAL STATEMENTS

TSASC reports governmental activity using two funds: (1) a general fund ("GF") and (2) a debt service fund ("DSF").

The following summarizes the changes in the GF for the years ended June 30,

	2017	2016	2015	Variance	
				2017/2016	2016/2015
	(in thousands)				
Revenues:					
Tobacco settlement revenue	\$ 101,011	\$ 229,332	\$ 113,781	\$ (128,321)	\$ 115,551
Investment earnings	48	54	5	(6)	49
Total revenues	<u>101,059</u>	<u>229,386</u>	<u>113,786</u>	<u>(128,327)</u>	<u>115,600</u>
Expenditures:					
Transfer to the Trust	100,307	229,032	113,369	(128,725)	115,663
Other expense	659	423	440	236	(17)
Total expenditures	<u>100,966</u>	<u>229,455</u>	<u>113,809</u>	<u>(128,489)</u>	<u>115,646</u>
Net change in fund balances	93	(69)	(23)	162	(46)
Fund balances, beginning of year	<u>708</u>	<u>777</u>	<u>800</u>	<u>(69)</u>	<u>(23)</u>
Fund balances, end of year	<u>\$ 801</u>	<u>\$ 708</u>	<u>\$ 777</u>	<u>\$ 93</u>	<u>\$ (69)</u>

Revenues recorded in the GF are primarily composed of TSRs collected each year. As the majority of TSRs recorded in the GF belongs to the Trust and are also recorded as expenditures, there is very little net impact on the GF fund balance. The large fluctuation between fiscal years 2017, 2016 and 2015 in TSRs and offsetting transfers to the Trust was due to the NPM Settlement Agreement, discussed later.

The remaining TSRs not transferred to the Trust are used for operations and reported as other expenses. This amount fluctuates each year based on management's time spent on conducting TSASC's operations, which determines the amount of general and administrative costs. Operating expenditures in fiscal year 2017 were greater than in fiscal years 2016 and 2015 due to increased allocated costs associated with management's time spent on the refunding transactions.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - GOVERNMENTAL FUNDS FINANCIAL STATEMENTS (continued)

The following summarizes the changes in TSASC's DSF for the years ended June 30,

	2017	2016	2015	Variance	
				2017/2016	2016/2015
	(in thousands)				
Revenues:					
Tobacco settlement revenue	\$ 59,150	\$ 136,451	\$ 67,313	\$ (77,301)	\$ 69,138
Investment earnings	532	1,217	498	(685)	719
Total revenues	59,682	137,668	67,811	(77,986)	69,857
Expenditures:					
Cost of issuance	7,575	-	-	7,575	-
Interest expenditure	51,749	61,419	61,720	(9,670)	(301)
Defeasance escrow	86,895	-	-	86,895	-
Principal amount of bonds retired	13,530	77,510	6,335	(63,980)	71,175
Total expenditures	159,749	138,929	68,055	20,820	70,874
Other Financing Sources	95,922	-	-	95,922	-
Net change in fund balances	(4,145)	(1,261)	(244)	(2,884)	(1,017)
Fund balance, beginning of year	115,535	116,796	117,040	(1,261)	(244)
Fund balance, end of year	\$ 111,390	\$ 115,535	\$ 116,796	\$ (4,145)	\$ (1,261)

TSRs recorded in the DSF for fiscal years 2017, 2016 and 2015 were based on the amount collected each year to pay debt service obligations, pursuant to the applicable indenture. The large increase in the 2016 TSRs was due to the NPM Settlement Agreement, discussed later. The variances of investment earnings in fiscal years 2017, 2016 and 2015 were primarily due to market value fluctuations of long-term investments. The large decrease between fiscal years 2017 and 2016 was because of the liquidation of high yielding long-term investments held in the previous year.

As a result of the refunding transaction, fiscal year 2017 expenditures included cost of issuance of \$7.6 million and defeasance escrow payments of \$86.9 million.

Interest expenditures in fiscal year 2017 decreased due to the bond refunding transaction. Interest expenditures decreased in fiscal year 2016 and 2015 because of the declining bond principal balances, which were being reduced by the turbo redemption feature. The large increase in the 2016 principal retired was due to the NPM Settlement Agreement, discussed later.

Due to the refunding transaction in fiscal year 2017, other financing sources increased by approximately \$95.9 million, which included \$653.1 million of bond proceeds and \$56.5 million of bond premium, which was offset by \$613.6 million of refunded bond principal payments.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - GOVERNMENTAL FUNDS FINANCIAL STATEMENTS (continued)

The following summarizes GF assets, liabilities, deferred inflows of resources, and fund balances as of June 30,

	<u>2017</u>	<u>2016</u>	<u>2015</u>	Variance	
				<u>2017/2016</u>	<u>2016/2015</u>
	(in thousands)				
Assets:					
Cash equivalents and investments	\$ 670	\$ 556	\$ 632	\$ 114	\$ (76)
Tobacco settlement revenue receivable	50,706	48,202	46,324	2,504	1,878
Prepaid expenditures	144	164	167	(20)	(3)
	<u>51,520</u>	<u>48,922</u>	<u>47,123</u>	<u>2,598</u>	<u>1,799</u>
Total assets	<u>\$ 51,520</u>	<u>\$ 48,922</u>	<u>\$ 47,123</u>	<u>\$ 2,598</u>	<u>\$ 1,799</u>
Liabilities	<u>\$ 13</u>	<u>\$ 12</u>	<u>\$ 22</u>	<u>\$ 1</u>	<u>\$ (10)</u>
Deferred inflows of resources	<u>50,706</u>	<u>48,202</u>	<u>46,324</u>	<u>2,504</u>	<u>1,878</u>
Fund Balances:					
Nonspendable prepaid expenditures	144	164	167	(20)	(3)
Unassigned	657	544	610	113	(66)
	<u>801</u>	<u>708</u>	<u>777</u>	<u>93</u>	<u>(69)</u>
Total fund balances	<u>801</u>	<u>708</u>	<u>777</u>	<u>93</u>	<u>(69)</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 51,520</u>	<u>\$ 48,922</u>	<u>\$ 47,123</u>	<u>\$ 2,598</u>	<u>\$ 1,799</u>

The GF assets at June 30, 2017, 2016 and 2015, totaled approximately \$51.5 million, \$48.9 million and \$47.1 million, respectively. The slight variances of total assets between fiscal years were primarily due to the change of estimated TSRs receivable, which is based on current year's TSRs collections, as previously discussed. As the majority of the assets recorded in the GF are TSRs receivable belonging to the Trust, which are also recorded as deferred inflows of resources, there is little net impact on the GF fund balance.

Prepaid expenditures represent the value of prepaid insurance.

TSASC, INC.
(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016
(unaudited)

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - GOVERNMENTAL FUNDS FINANCIAL STATEMENTS (continued)

The following summarizes the DSF assets, liabilities, deferred inflows of resources, and fund balances as of June 30,

	2017	2016	2015	Variance	
				2017/2016	2016/2015
	(in thousands)				
Assets:					
Cash equivalents and investments	\$ 111,390	\$ 115,535	\$ 116,796	\$ (4,145)	\$ (1,261)
Tobacco settlement revenue receivable	30,294	28,798	27,676	1,496	1,122
Total assets	<u>\$ 141,684</u>	<u>\$ 144,333</u>	<u>\$ 144,472</u>	<u>\$ (2,649)</u>	<u>\$ (139)</u>
Deferred inflows of resources	<u>\$ 30,294</u>	<u>\$ 28,798</u>	<u>\$ 27,676</u>	<u>\$ 1,496</u>	<u>\$ 1,122</u>
Fund Balances:					
Restricted for debt service	<u>111,390</u>	<u>115,535</u>	<u>116,796</u>	<u>(4,145)</u>	<u>(1,261)</u>
Total fund balances	<u>111,390</u>	<u>115,535</u>	<u>116,796</u>	<u>(4,145)</u>	<u>(1,261)</u>
Total deferred inflows of resources and fund balances	<u>\$ 141,684</u>	<u>\$ 144,333</u>	<u>\$ 144,472</u>	<u>\$ (2,649)</u>	<u>\$ (139)</u>

The changes in cash equivalents and investments each year result from the amount held for debt service and from market value fluctuations of long-term investments, as previously discussed.

Variances in receivables and deferred inflows of resources from year to year are primarily due to changes in TSRs receivable each year.

RISK FACTORS AND FUTURE REVENUE

The Master Settlement Agreement ("MSA"), dated November 23, 1998, is an industry-wide settlement of litigation between participating cigarette manufacturers and 46 States (the "Settling States"), including the State of New York (the "State"). The MSA governs the amount of TSRs received by TSASC, which is 3.4% of total TSRs paid by the participating cigarette manufacturers. TSRs reflect numerous adjustments as described in the MSA, including adjustments relating to inflation, sales volume, non-settling states, NPM Adjustment, and miscalculated or disputed payments.

Under the MSA's dispute-resolution procedures, the tobacco companies withheld over \$700 million in combined annual settlement payments to the State (and consequently to the counties, including the City and TSASC) since 2003 in connection with a dispute relating to the NPM Adjustment.

In 2013, an arbitration panel ruling found that the State had met its 2003 obligations in connection with the NPM Adjustment, which allowed for the release of \$92 million of TSRs withheld in that year, including \$28.4 million to TSASC.

TSASC, INC.

(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016

(unaudited)

RISK FACTORS AND FUTURE REVENUE (continued)

In 2015, the State entered into a settlement agreement with the tobacco companies that resolved all past and future disputes relating to the NPM Adjustment. The NPM Settlement Agreement provided for:

- Release of 90% of withheld TSRs relating to years 2004 through 2014;
- The reduction of future TSRs payment in accordance with a set formula tied to the volume of cigarettes manufactured and sold on Native American reservations; and
- The termination of further disputed withholdings related to the NPM Adjustment.

The settlement does not preclude disputes related to other adjustments. The State received a total of \$701 million from the disputed escrow account, of which TSASC received \$176 million. Of that amount, \$66 million was pledged for debt service and the remainder was remitted to the City, in accordance with the indenture.

TSASC has no control over the amount of TSRs it receives. Risks in connection with future receipts of TSRs include the reduction of TSRs tied to the volume of cigarettes manufactured and sold on Native American reservations, litigation involving the participating manufacturers ("PM") that could lead to bankruptcy of the PMs, continuing increased decline in cigarette consumption materially beyond forecasted levels, tobacco excise taxes, restrictions on smoking in public areas, and other potential unforeseen future adjustments to the calculation of TSRs. Further, adverse court rulings, independent of the settlement, could impact upon future MSA payments to TSASC. Reductions in TSRs payments to TSASC could impair TSASC's ability to meet its payment obligations.

ECONOMIC OUTLOOK

On January 19, 2017, TSASC issued \$613.4 million 2017 Series A senior bonds and \$489.7 million 2017 Series B subordinate bonds under the 2016 Indenture, which allowed TSASC to refund all of its Series 2006-1 bonds outstanding and established a Senior Liquidity Reserve of \$48.0 million and Subordinate Liquidity Reserve of \$40.3 million. Future debt service payments on all outstanding bonds are contingent on TSRs collected by TSASC. TSRs are dependent on a number of factors, including, but not limited to a discount adjustment on the volume of cigarettes manufactured and sold on Native American reservations, pursuant to the NPM Settlement Agreement, as previously discussed. In structuring the financial transaction for the issuance of bonds, TSASC engaged the services of an independent consultant to develop forecasts of the TSRs.

In April 2017, TSASC received \$59.9 million of pledged TSRs, which differed from the previous forecast of \$66.7 million. The reduced payment resulted primarily from the determination by an Independent Investigator that 175 million Tribal NPM Packs were sold in 2015, which figure was used in determining the 2017 payment. Due to the reduced payment of TSRs, TSASC will need to draw upon its Subordinate Liquidity Reserve Account an estimated \$4.2 million in order to meet its debt service requirement due December 1, 2017. The approximate balance of the Subordinate Liquidity Reserve Account after the draw will be \$36.1 million. Pursuant to the NPM Settlement Agreement, the Independent Investigator's determination applies for a two year period. As such, given that the determination impacts 2018 TSRs, this increases the likelihood that TSASC will draw against its Subordinate Liquidity Reserves in December 2018.

TSASC, INC.

(A Component Unit of The City of New York)

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

JUNE 30, 2017 AND 2016

(unaudited)

RATINGS

During the years reported herein, the rating agencies maintaining credit ratings on TSASC issued one or more rating changes to TSASC's outstanding debt. On May 16, 2017, Standard & Poor's placed the TSASC ratings on CreditWatch with negative implications. Currently, Standard & Poor's rates TSASC's 2017 Series A: the 2017-2026 serial bonds A, the 2027-2036 serial bonds A-, and the 2041 term bonds BBB+. Standard & Poor's rates TSASC's 2017 Series B: the 2018 serial bonds A-, the 2019 serial bonds BBB+, the 2020-2025 serial bonds BBB, the 2045 term bonds BBB- and the 2048 term bonds are unrated. As of June 30, 2017, Fitch and Moody's do not rate TSASC bonds.

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of TSASC's finances. Questions concerning any of the information in this report or requests for additional financial information should be directed to Investor Relations, TSASC, Inc., 255 Greenwich Street, New York, NY 10007.

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TSASC, INC.
(A Component Unit of The City of New York)
STATEMENTS OF NET POSITION (DEFICIT)
AS OF JUNE 30, 2017 AND 2016

	2017	2016
	(in thousands)	
ASSETS:		
Unrestricted cash equivalents	\$ 670	\$ 204
Restricted cash equivalents	75	314
Unrestricted investments	-	352
Restricted investments	111,315	115,221
Tobacco settlement revenue receivable	81,000	77,000
Prepaid expenses	144	164
	193,204	193,255
DEFERRED OUTFLOWS OF RESOURCES:		
Unamortized deferred bond refunding costs	18,492	-
	18,492	-
LIABILITIES:		
Accrued expenses	13	12
Accrued interest payable	4,496	4,811
Remittance payable to the Trust	50,706	48,202
Bonds payable:		
Portion due within one year	18,625	-
Portion due after one year	1,123,244	1,120,606
	1,197,084	1,173,631
NET POSITION (DEFICIT):		
Unrestricted (deficit)	(985,388)	(980,376)
	(985,388)	(980,376)
Total net position (deficit)	\$ (985,388)	\$ (980,376)

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

TSASC, INC.

(A Component Unit of The City of New York)

STATEMENTS OF ACTIVITIES**FOR THE YEARS ENDED JUNE 30, 2017 AND 2016**

	<u>2017</u>	<u>2016</u>
	(in thousands)	
REVENUES:		
Tobacco settlement revenue:		
Tobacco settlement revenue - pledged	\$ 61,396	\$ 137,925
Tobacco settlement revenue - unpledged	102,765	230,858
Total tobacco settlement revenue	<u>164,161</u>	<u>368,783</u>
Investment earnings	<u>580</u>	<u>1,271</u>
Total revenues	<u>164,741</u>	<u>370,054</u>
EXPENSES:		
Transfer to the Trust	102,811	230,910
Cost of issuance	7,575	-
Interest expense	55,741	62,359
Loss on defeasance	2,967	-
General and administrative	659	423
Total expenses	<u>169,753</u>	<u>293,692</u>
Change in net position	(5,012)	76,362
NET POSITION (DEFICIT) - beginning of year	<u>(980,376)</u>	<u>(1,056,738)</u>
NET POSITION (DEFICIT) - end of year	<u>\$ (985,388)</u>	<u>\$ (980,376)</u>

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

TSASC, INC.
(A Component Unit of The City of New York)
GOVERNMENTAL FUNDS BALANCE SHEETS

AS OF JUNE 30, 2017

	General Fund	Debt Service Fund	Total Governmental Funds
		(in thousands)	
ASSETS:			
Unrestricted cash equivalents	\$ 670	\$ -	\$ 670
Restricted cash equivalents	-	75	75
Restricted investments	-	111,315	111,315
Tobacco settlement revenue receivable	50,706	30,294	81,000
Prepaid expenditures	144	-	144
	<u>\$ 51,520</u>	<u>\$ 141,684</u>	<u>\$ 193,204</u>
Total assets			
LIABILITIES:			
Accounts payable	\$ 13	\$ -	\$ 13
	<u>13</u>	<u>-</u>	<u>13</u>
Total liabilities			
DEFERRED INFLOWS OF RESOURCES:			
Unavailable tobacco settlement revenue	50,706	30,294	81,000
	<u>50,706</u>	<u>30,294</u>	<u>81,000</u>
Total deferred inflows of resources			
FUND BALANCES:			
Nonspendable prepaid expenditures	144	-	144
Restricted for debt service	-	111,390	111,390
Unassigned	657	-	657
	<u>801</u>	<u>111,390</u>	<u>112,191</u>
Total fund balances			
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 51,520</u>	<u>\$ 141,684</u>	<u>\$ 193,204</u>

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

TSASC, INC.
(A Component Unit of The City of New York)

GOVERNMENTAL FUNDS BALANCE SHEETS

AS OF JUNE 30, 2016

	General Fund	Debt Service Fund	Total Governmental Funds
		(in thousands)	
ASSETS:			
Unrestricted cash equivalents	\$ 204	\$ -	\$ 204
Restricted cash equivalents	-	314	314
Unrestricted investments	352	-	352
Restricted investments	-	115,221	115,221
Tobacco settlement revenue receivable	48,202	28,798	77,000
Prepaid expenditures	164	-	164
	<u>\$ 48,922</u>	<u>\$ 144,333</u>	<u>\$ 193,255</u>
Total assets	<u>\$ 48,922</u>	<u>\$ 144,333</u>	<u>\$ 193,255</u>
LIABILITIES:			
Accounts payable	\$ 12	\$ -	\$ 12
	<u>12</u>	<u>-</u>	<u>12</u>
Total liabilities	<u>12</u>	<u>-</u>	<u>12</u>
DEFERRED INFLOWS OF RESOURCES:			
Unavailable tobacco settlement revenue	48,202	28,798	77,000
	<u>48,202</u>	<u>28,798</u>	<u>77,000</u>
Total deferred inflows of resources	<u>48,202</u>	<u>28,798</u>	<u>77,000</u>
FUND BALANCES:			
Nonspendable prepaid expenditures	164	-	164
Restricted for debt service	-	115,535	115,535
Unassigned	544	-	544
	<u>708</u>	<u>115,535</u>	<u>116,243</u>
Total fund balances	<u>708</u>	<u>115,535</u>	<u>116,243</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 48,922</u>	<u>\$ 144,333</u>	<u>\$ 193,255</u>

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

TSASC, INC.

(A Component Unit of The City of New York)

**RECONCILIATIONS OF GOVERNMENTAL FUNDS BALANCE SHEETS
TO THE STATEMENTS OF NET POSITION (DEFICIT)**

AS OF JUNE 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
	(in thousands)	
Total fund balances - governmental funds	\$ 112,191	\$ 116,243
Amounts reported for governmental activities in the statements of net position (deficit) are different because:		
Bond premiums/discounts are reported as other financing uses in the governmental funds financial statements upon issuance. However, in the statements of net position (deficit), bond premiums/discounts are reported as a component of bonds payable and amortized over the life of the bonds.		
	(52,329)	23,919
Costs of bond refundings are reported as expenditures in governmental funds financial statements. However, in the statements of net position (deficit), those costs and the related gain or loss are deferred and amortized over the shorter of the remaining life of the old debt or life of the new debt.		
	18,492	-
Unavailable tobacco settlement revenue accrued but not received within two months after year end is reported as a deferred inflows of resources in the governmental funds financial statements because it is not currently available; however, it is recognized as revenue in the statements of net position (deficit).		
	81,000	77,000
Liabilities not due and not payable in the current period from current financial resources are not reported in the governmental funds financial statements, but are reported in the statements of net position (deficit). Those liabilities consist of:		
Bonds payable	(1,089,540)	(1,144,525)
Accrued interest payable	(4,496)	(4,811)
Remittance payable to the Trust	(50,706)	(48,202)
Net position (deficit) of governmental activities	<u>\$ (985,388)</u>	<u>\$ (980,376)</u>

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

TSASC, INC.
(A Component Unit of The City of New York)

GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

FOR THE YEAR ENDED JUNE 30, 2017

	General Fund	Debt Service Fund	Total Governmental Funds
		(in thousands)	
REVENUES:			
Tobacco settlement revenue:			
Tobacco settlement revenue - pledged	\$ 750	\$ 59,150	\$ 59,900
Tobacco settlement revenue - unpledged	100,261	-	100,261
Total tobacco settlement revenue	101,011	59,150	160,161
Investment earnings	48	532	580
Total revenues	101,059	59,682	160,741
EXPENDITURES:			
Transfer to the Trust:			
Tobacco settlement revenue and interest earnings	100,307	-	100,307
Cost of issuance	-	7,575	7,575
Interest expenditure	-	51,749	51,749
Principal amount of bonds retired	-	13,530	13,530
Defeasance escrow	-	86,895	86,895
General and administrative	659	-	659
Total expenditures	100,966	159,749	260,715
OTHER FINANCING SOURCES (USES):			
Refunding bond proceeds	-	653,070	653,070
Premium on issuance	-	56,491	56,491
Payments of refunded bonds	-	(613,639)	(613,639)
Total other financing sources (uses)	-	95,922	95,922
Net change in fund balances	93	(4,145)	(4,052)
FUND BALANCES - beginning of year	708	115,535	116,243
FUND BALANCES - end of year	\$ 801	\$ 111,390	\$ 112,191

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

TSASC, INC.
(A Component Unit of The City of New York)

**GOVERNMENTAL FUNDS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES**

FOR THE YEAR ENDED JUNE 30, 2016

	General Fund	Debt Service Fund	Total Governmental Funds
		(in thousands)	
REVENUES:			
Tobacco settlement revenue:			
Tobacco settlement revenue - pledged	\$ 352	\$ 136,451	\$ 136,803
Tobacco settlement revenue - unpledged	228,980	-	228,980
Total tobacco settlement revenue	229,332	136,451	365,783
Investment earnings	54	1,217	1,271
Total revenues	229,386	137,668	367,054
EXPENDITURES:			
Transfer to the Trust:			
Tobacco settlement revenue and interest earnings	229,032	-	229,032
Interest expenditure	-	61,419	61,419
Principal amount of bonds retired	-	77,510	77,510
General and administrative	423	-	423
Total expenditures	229,455	138,929	368,384
Net change in fund balances	(69)	(1,261)	(1,330)
FUND BALANCES - beginning of year	777	116,796	117,573
FUND BALANCES - end of year	\$ 708	\$ 115,535	\$ 116,243

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

TSASC, INC.

(A Component Unit of The City of New York)

**RECONCILIATIONS OF THE GOVERNMENTAL FUNDS STATEMENTS OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES TO THE STATEMENTS OF ACTIVITIES**

FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
	(in thousands)	
Net change in fund balances - governmental funds	\$ (4,052)	\$ (1,330)
Amounts reported for governmental activities in the statements of activities are different because:		
Refunding bond proceeds and payments to refunded bond escrow holder are reported as other financing sources and uses in the governmental funds financial statements, but increase and decrease long-term liabilities in the statements of net position (deficit).	(39,431)	-
The governmental funds financial statements report costs of bond refundings as expenditures. However, in the statements of activities, the costs of bond refundings are amortized over the shorter of the life of the bonds refunded or the life of the bonds issued to refund the bonds.	(771)	-
Tobacco settlement revenue not available in the current period is deferred in the governmental funds financial statements and included in revenue in the statements of activities.	4,000	3,000
Payment of bond principal is an expenditure in the governmental funds financial statements, but the payment reduces bonds payable in the statements of net position (deficit).	13,530	77,510
Payments to defease bonds prior to maturity are reported expenditures in the governmental funds financial statements. However, in the statements of net position (deficit), only the difference between the carrying value of the defeased bonds and the amount paid to defease the bonds are reported as period revenues and expenses.	83,928	-
The governmental funds financial statements report bond premium/discounts as other financing uses upon issuance. However, in the statements of activities, bond premiums/discounts are amortized to interest expense over the life of the bond.	(52,329)	(1,247)
Interest is reported in the statements of activities on the accrual basis. However, interest is reported as an expenditure in the governmental funds financial statements when the outlay of financial resources is paid.	(7,383)	307
Transfer to the Trust is reported in the statements of activities on the accrual basis, but is reported only as an expenditure in the general fund when the payment is actually made.	<u>(2,504)</u>	<u>(1,878)</u>
Change in net position (deficit) - governmental activities	<u>\$ (5,012)</u>	<u>\$ 76,362</u>

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

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2017 AND 2016

NOTE 1 – ORGANIZATION AND NATURE OF ACTIVITIES

TSASC, Inc. (“TSASC”) is a special purpose, local development corporation organized under the Not-For-Profit Corporation Law of the State of New York (the “State”). TSASC is an instrumentality of, but separate and apart from, The City of New York (the “City”). TSASC is governed by a Board of five directors, consisting of the following officials of the City: the Director of Management and Budget, the Commissioner of Finance, the Corporation Counsel of the City, the Comptroller and the Speaker of the Council. Although legally separate from the City, TSASC is a component unit of the City and is included in the City’s financial statements as a blended component unit in accordance with Governmental Accounting Standards Board (“GASB”) standards.

Pursuant to a Purchase and Sale Agreement with the City, the City sold to TSASC all of its future right, title and interest in the Tobacco Settlement Revenues (“TSRs”) under the Master Settlement Agreement (“MSA”) and the Decree and Final Judgment (the “Decree”). 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 provided 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 City a share of the TSRs under the MSA. The future right, title and interest of the City to the TSRs were sold to TSASC.

The purchase price of the City’s future right, title and interest in the TSRs was financed by the issuance of a series of bonds and the Residual Certificate. Prior to the restructuring of TSASC’s debt (discussed below) the Residual Certificate represented the entitlement to receive all TSRs after payment of debt service, operating expenses and certain other costs as set forth in the original bond indenture.

On February 8, 2006, TSASC issued \$1.35 billion of Series 2006-1 bonds, the proceeds of which were used to restructure all of TSASC’s outstanding indebtedness. The Amended and Restated Indenture dated January 1, 2006, (the “2006 Indenture”) provides that 62.6% of TSASC’s annual collection of TSRs and the related interest earnings are transferred to the TSASC Tobacco Settlement Trust (the “Trust”), as owner of the Residual Certificate. The City is the beneficial owner of the Trust and the funds received by the Trust, net of the Trust’s expenses, are transferred to the City.

The 2006 Indenture also provides that a defined portion of the TSRs and other revenues (collectively, “Collections”) are applied to the payment of the Series 2006-1 debt service. The proportion of Collections pledged to the payment of the Series 2006-1 debt service is 37.4%. The turbo redemption feature requires all the pledged Collections, after funding of operating costs, be applied to the payment of principal and interest on the Series 2006-1 bonds.

On January 19, 2017, TSASC issued \$613.4 million 2017 Series A senior bonds and \$489.7 million 2017 Series B subordinate bonds, which allowed TSASC to refund all of its Series 2006-1 bonds outstanding. Of the \$489.7 million 2017 Series B subordinate bonds, \$450.0 million were exchanged rather than refunded. The Amended and Restated Indenture dated December 1, 2016, (the “2016 Indenture”) continues to provide that 37.4% of Collections are pledged for the payment of debt service and the operating costs of TSASC and that 62.6% are transferred to the Trust. During fiscal years 2017 and 2016, TSASC transferred to the Trust \$100.3 million and \$229.0 million, respectively.

TSASC does not have any employees; its affairs are administered by employees of the City and of another component unit of the City, for which TSASC pays a management fee, rent and overhead based on its allocated share of personnel and overhead costs.

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 1 – ORGANIZATION AND NATURE OF ACTIVITIES (continued)

The government-wide financial statements of TSASC, which include the statements of net position (deficit) and the statements of activities, are presented to display information about the reporting entity as a whole, in accordance with GASB standards. The government-wide financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

TSASC's governmental funds financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting, in which revenue is recognized when it becomes susceptible to accrual; that is, when it becomes both measurable and available to finance expenditures in the current fiscal period. Expenditures are recognized when the related liability is incurred, except for principal and interest on bonds payable, which are recognized when due.

TSASC uses two governmental funds for reporting its activities: a debt service fund ("DSF") and a general fund ("GF"). The DSF is used to account for the accumulation of resources for payment of principal and interest on debt and the GF is used to account for all financial resources not accounted for in the DSF, which are TSASC's unpledged TSRs due to the City, and administrative and operating expenditures. Fund balances are classified as either: 1) nonspendable, 2) restricted, 3) committed, 4) assigned, or 5) unassigned in accordance with GASB standards.

The Board of Directors of TSASC (the "Board") constitutes TSASC's highest level of decision-making authority. If and when resolutions are adopted by the Board that constrain fund balances for a specific purpose, such resources are accounted for and reported as committed for such purpose; unless and until a subsequent resolution altering the commitment is adopted by the Board.

If and when fund balances which are constrained for use for a specific purpose, based on the direction of any officer of TSASC who is duly authorized under TSASC's bond indenture to direct the movement of such funds, are accounted for and reported as assigned for such purpose unless and until a subsequent authorized action by the same or another duly authorized officer, or by the Board, is taken which removes or changes the assignment.

When both restricted and unrestricted resources are available for use for a specific purpose, it is TSASC's policy to use restricted resources first then unrestricted resources as they are needed. When committed, assigned, or unassigned resources are available for use for a specific purpose, it is TSASC's policy to use committed resources first, then assigned resources, and then unassigned resources as they are needed.

Investments are reported at fair value as of the reporting date.

TSASC records TSRs receivable at June 30th. The TSRs receivable is expected to be received the following April of each year and is based on an estimate of cigarette sales for the six-month period from January 1 to June 30. As it is not expected to be received within two months of the fiscal year end, the unavailable revenue related to the TSRs receivable is deferred in the governmental funds financial statements. Per the 2006 Indenture and 2016 Indenture, 62.6% of TSRs receivable is due to the Trust. As such, a corresponding payable is recorded in the government-wide financial statements.

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Bond premiums and discounts are capitalized and amortized over the life of the related debt using the interest method in the government-wide financial statements. The governmental funds financial statements recognize the premiums and discounts, as well as bond issuance costs, during the current period. Bond premiums and discounts are presented as additions or reductions to the face amount of the bonds payable. Bond issuance costs are recognized as an expense/expenditure in the period incurred in the government-wide and governmental funds financial statements, respectively.

Deferred bond refunding costs represent the accounting gain or loss incurred on a refunding of outstanding bonds and is reported as a deferred outflows of resources in the government-wide financial statements. The deferred bond refunding costs are amortized over the shorter of the remaining life of the old debt or the life of the new debt. In the debt service funds, costs of the bond refunding are reported as expenditures when incurred

Interest expense is recognized on the accrual basis in the government-wide financial statements. Interest expenditures are recognized when paid in the governmental funds financial statements.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) requires TSASC’s management to make estimates and assumptions in determining the reported amounts of assets, deferred outflows of resources, liabilities, and deferred inflows of resources as of the date of the financial statements and the amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

As a component unit of the City, TSASC implements new GASB standards in the same fiscal year as they are implemented by the City. The following are discussions of the standards requiring implementation in the current year and standards which may impact TSASC in the future years.

- In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* (“GASB 74”). GASB 74 establishes financial reporting standards to state and local governmental other postemployment benefit (“OPEB”) plans. The requirements of GASB 74 are effective for fiscal years beginning after June 15, 2016. The adoption of GASB 74 did not have an impact on TSASC’s financial statements, as TSASC is not an OPEB plan.
- In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (“GASB 75”). GASB 75 establishes accounting and financial reporting standards for OPEB that is provided to employees of state and local governmental employees. The requirements of GASB 75 are effective for fiscal years beginning after June 15, 2017. The adoption of GASB 75 did not have an impact on TSASC’s financial statements, as it has no employees.
- In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, (“GASB 83”). GASB 83 addresses accounting and financial reporting for certain asset retirement obligations. This statement establishes criteria for determining the timing and pattern of recognition of a liability and corresponding deferred outflow of resources for asset retirement obligations. The requirements of GASB 83 are effective for fiscal years beginning after June 15, 2018. TSASC has not completed the process of evaluating GASB 83, but does not expect it to have an impact on TSASC’s financial statements.
- In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, (“GASB 84”). The objective of GASB 84 is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of GASB 84 are effective for fiscal years beginning after December 15, 2018. TSASC has not completed the process of evaluating GASB 84, but does not expect it to have an impact on TSASC’s financial statements, as it does not enter in fiduciary activities.

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- In March 2017, GASB issued Statement No. 85, *Omnibus 2017*, (“GASB 85”). The objective of GASB 85 is to address practice issues that have been identified during implementation and application of certain GASB statements. The requirements of GASB 85 are effective for fiscal years beginning after June 15, 2017. The adoption of GASB 85 did not have an impact on TSASC’s financial statements.
- In May 2017, GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, (“GASB 86”). The primary objective of GASB 86 is to improve 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. This statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished. The requirements of GASB 86 are effective for fiscal years beginning after June 15, 2017. TSASC has not completed the process of evaluating GASB 86, but does not expect it to have an impact on TSASC’s financial statements.
- In June 2017, GASB issued Statement No. 87, *Leases*, (“GASB 87”). The objective of GASB 87 is to improve accounting and financial reporting for leases by governments. This statement increases the usefulness of governments’ financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments’ leasing activities. The requirements of GASB 87 are effective for fiscal years beginning after December 15, 2019. TSASC has not completed the process of evaluating GASB 87, but does not expect it to have an impact on TSASC’s financial statements, as it does not enter into any lease agreements.

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 3 – BONDS PAYABLE

In accordance with the 2006 Indenture and 2016 Indenture, Pledged Collections were used to fund operating expenses; then to fund debt service payments. Outstanding bonds payable bear interest at rates ranging from 2% to 5%.

A summary of changes in outstanding bonds in fiscal years 2017 and 2016 is as follows (in thousands):

	Outstanding Principal Balance at June 30, 2015	Additions	Deletions	Outstanding Principal Balance at June 30, 2016	Additions	Deletions	Outstanding Principal Balance at June 30, 2017
Series 2006-1	\$ 1,222,035	\$ -	\$ (77,510)	\$ 1,144,525	\$ -	\$ (1,144,525)	\$ -
Series 2017A	-	-	-	-	613,370	(13,530)	599,840
Series 2017B	-	-	-	-	489,700	-	489,700
Total before premium/discount (net)	1,222,035	-	(77,510)	1,144,525	1,103,070	(1,158,055)	1,089,540
Premium/(discount) (net)	(25,166)	-	1,247	(23,919)	56,491	19,757	52,329
Total Bonds Payable	<u>\$ 1,196,869</u>	<u>\$ -</u>	<u>\$ (76,263)</u>	<u>\$ 1,120,606</u>	<u>\$ 1,159,561</u>	<u>\$ (1,138,298)</u>	<u>\$ 1,141,869</u>
Due within one year	<u>\$ -</u>			<u>\$ -</u>			<u>\$ 18,625</u>

Debt service requirements, including principal and interest as of June 30, 2017 are as follows (in thousands):

Year ended June 30,	SENIOR		SUBORDINATE		TOTAL		
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Debt Service</u>
2018	\$ 17,625	\$ 29,463	\$ 1,000	\$ 24,485	\$ 18,625	\$ 53,948	\$ 72,573
2019	17,655	28,934	700	24,435	18,355	53,369	71,724
2020	23,375	28,228	6,000	24,400	29,375	52,628	82,003
2021	24,370	27,059	6,200	24,100	30,570	51,159	81,729
2022	20,375	25,841	6,300	23,790	26,675	49,631	76,306
2023 to 2027	119,490	112,805	19,500	114,460	138,990	227,265	366,255
2028 to 2032	138,340	80,533	-	112,500	138,340	193,033	331,373
2033 to 2037	131,245	46,353	-	112,500	131,245	158,853	290,098
2038 to 2042	107,365	13,799	-	112,500	107,365	126,299	233,664
2043 to 2047	-	-	175,000	95,000	175,000	95,000	270,000
2048	-	-	275,000	13,750	275,000	13,750	288,750
Total	<u>\$ 599,840</u>	<u>\$ 393,015</u>	<u>\$ 489,700</u>	<u>\$ 681,920</u>	<u>\$ 1,089,540</u>	<u>\$ 1,074,935</u>	<u>\$ 2,164,475</u>

As of June 30, 2017 and 2016, TSASC has funded its debt service and reserve accounts according to the indenture requirements. As of June 30, 2017 and 2016, debt service accounts holdings totaled \$22.8 million and \$28.9 million, respectively. As of June 30, 2017 and 2016, the TSASC Liquidity Reserve Account balances were \$88.5 million and \$86.7 million, respectively, and in compliance with the indenture.

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 4 – CASH EQUIVALENTS

TSASC's cash equivalents consist of money market funds. As of June 30, 2017 and 2016, total cash equivalents are summarized as follows:

	2017	2016
	(in thousands)	
Restricted:		
Cash equivalents (see note 5)	\$ 75	\$ 314
Total restricted	75	314
Unrestricted:		
Cash equivalents (see note 5)	\$ 670	\$ 204
Total unrestricted	670	204
Total cash equivalents	\$ 745	\$ 518

NOTE 5 – INVESTMENTS

The investments, including cash equivalents, as of June 30, 2017 and 2016 are summarized as follows:

	2017	2016
	(in thousands)	
Restricted:		
Money Market Funds	\$ 75	\$ 314
United States Treasury notes (Maturing within one year)	-	68,952
Freddie Mac discount notes (Maturing within one year)	111,315	-
Fannie Mae discount notes (Maturing within one year)	-	28,880
Municipal Bonds--various states (Maturing over five years)	-	17,389
Total restricted	111,390	115,535
Unrestricted:		
Money Market Funds	670	204
Fannie Mae discount notes (Maturing within one year)	-	352
Total unrestricted	670	556
Total investments including cash equivalents	112,060	116,091
Less amounts reported as cash equivalents (see note 4)	(745)	(518)
Total investments	\$ 111,315	\$ 115,573

TSASC, INC.
(A Component Unit of The City of New York)

NOTES TO FINANCIAL STATEMENTS (continued)

JUNE 30, 2017 AND 2016

NOTE 5 – INVESTMENTS (continued)

TSASC categorizes its fair value measurements within the fair value hierarchy established by U.S. GAAP. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. TSASC had the following recurring fair value measurements as of June 30, 2017 and 2016:

- Money Market Funds are valued based on various market and industry inputs (Level 2 inputs).
- U.S. Agency securities are valued using a matrix pricing model (Level 2 inputs).
- Municipal bonds are valued using a matrix pricing model (Level 2 inputs).

Each account of TSASC is held pursuant to the indenture between TSASC and its Trustee and may be invested in securities or categories of investments that are specifically enumerated as permitted investments for such account pursuant to the indenture.

Custodial credit risk: Is the risk that, in the event of the failure of the custodian, TSASC may not be able to recover the value of its investments that are in the possession of an outside party. TSASC's investments are not collateralized. All investments are held in the Trustee's name by the Trustee.

Credit risk: All investments held by TSASC at June 30, 2017 were securities invested in Freddie Mac discount notes rated by Moody's P-1, Standard & Poor's A-1+ and Fitch F1+.

Interest rate risk: TSASC's investments mature in less than one year, unless otherwise specified above. Investments with longer term maturities are not expected to be liquidated prior to maturity, thereby limiting exposure from rising interest rates.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of TSASC's investment in a single issuer (5% or more). TSASC's investment policy places no limit on the amount TSASC may invest in any one issuer of eligible government obligations as defined in the Indenture. As of June 30, 2017, more than 5% of TSASC's investments were in U.S. Government-sponsored entities. These investments are 99.3% of TSASC's total investments.
