TSASC, Inc.

Financial Statements
Years Ended June 30, 2007 and 2006 and

Independent Auditors' Report

TSASC, INC.

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INDEPENDENT AUDITORS' REPORT

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, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of the TSASC's 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of TSASC's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, 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 respective financial position of the governmental activities of TSASC, Inc. as of June 30, 2007 and 2006, and the respective changes in financial position thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 2 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of TSASC's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Deloitte & Touche LLP

September 26, 2007

OVERVIEW OF THE FINANCIAL STATEMENTS

The following is a narrative overview and analysis of the financial activities of TSASC, Inc. ("TSASC") for the fiscal years ended June 30, 2007 and 2006. It should be read in conjunction with TSASC's entity-wide financial statements, governmental fund financial statements and the notes to the financial statements.

The annual financial statements consist of three parts: (1) management's discussion and analysis (this section); (2) the entity-wide financial statements; and (3) the governmental fund financial statements.

The entity-wide financial statements of TSASC, which include the statements of net assets (deficits) 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") Statement No. 34 - Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as amended. This is to provide the reader with a broad overview of TSASC's finances, which is similar to private-sector financial statements. The entity-wide financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting in which all revenues and expenses are taken into account regardless of when cash is paid or received.

TSASC's debt service (governmental) fund financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized when it becomes susceptible to accrual, which 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 unmatured interest on bonds payable, which is recognized when due.

The reconciliations of the statements of revenues, expenditures and changes in fund balances of the debt service fund to the statements of activities are presented to assist the reader in understanding the differences between entity-wide and debt service fund financial statements.

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - ENTITY-WIDE FINANCIAL STATEMENTS

On February 8, 2006, TSASC completed a total restructuring of all its outstanding indebtedness. On that date TSASC issued $1.353 billion of its Series 2006-1bonds. The proceeds of the Series 2006-1 bonds, together with amounts on-hand at that date, were used: (1) to fund a legal defeasance escrow account held by the Trustee for holders of all Series 1999-1 and Series 2002-1 bonds then outstanding, (2) to redeem all bonds then outstanding under the TIFIA Loan Agreement, (3) to fund the reserve required under the amended and restated bond indenture dated as of January 1, 2006 ("Indenture") and (4) to cover costs of issuance of the Series 2006-1 bonds, and the remaining funds were deposited into the Unpledged TSR account held by the Trustee for transfer on or after December 6, 2007 (together with the unpledged portions of tobacco settlement revenues ("TSRs") received from February 8, 2006 to December 6, 2007), to the TSASC Tobacco Settlement Trust (the "Trust"), as owner of the Residual Certificate. The City is the beneficial owner of the Trust and thus the funds received by the Trust are transferred to The City of New York (the "City").

As a result of the restructuring, the Series 2006-1 bonds are the only indebtedness of TSASC outstanding at June 30, 2007 and 2006. The Indenture provides that a defined portion of the TSRs and other revenues (collectively, "Collections") are applied to the payment of the Series 2006-1. The proportion of Collections pledged to the payment of the Series 2006-1 bonds is currently 37.40%, is subject to reduction at June 1, 2024, and at each June 1st thereafter, depending on the magnitude of cumulative bond redemptions under the Series 2006-1 turbo redemption feature (which requires all the pledged Collections, after funding of operating costs, to be applied to payment of interest and principal on the Series 2006-1 bonds).

The following summarizes the activities of TSASC for the years ended June 30, 2007 and 2006:

($ 000's)	2007	2006	FYE 2007 Change
Revenues:			
Tobacco settlement revenue	$ 214,433	$ 192,133	$ 22,300
Tobacco settlement revenue not remitted to the Trust	-	36,880	(36,880)
Other income	21,728	24,191	(2,463)
Total revenue	236,161	253,204	(17,043)
Expenses:			
Bond interest	67,932	73,561	(5,629)
Other	19,212	28,367	(9,155)
Total expenses	87,144	101,928	(14,784)
Change in net deficit	149,017	151,276	(2,259)
Net deficit, beginning of year	(759,665)	(910,941)	151,276
Net deficit, end of year	$ (610,648)	$ (759,665)	$ 149,017

The Master Settlement Agreement ("MSA") between participating cigarette manufacturers and 46 States, including the State of New York, governs the amount of TSRs received by TSASC. Under the MSA, Original Participating Manufacturers ("OPMs") may deposit a portion of their payments for that year into an account held by the MSA escrow agent for amounts in dispute ("Dispute Account"). As is provided for under the MSA, the funds in that escrow are not distributed to the settling states until the dispute is resolved.

TSRs received in 2007 increased for two reasons: (1) as a result of the operation of the inflation-adjustment in the MSA, and (2) because the proportion of the 2007 payments from the OPMs that were deposited into the Dispute Account was lower than in 2006.

The TSRs not remitted to the Trust in 2006 is the result of the February 2006 restructuring of TSASC's debt. That restructuring, including the establishment of the Unpledged TSR account, resulted in a reduction of $36.9 million of TSRs payments to the Trust. The estimated payable at June 30, 2005 was $42.3 million of which $5.5 million was paid to the Trust during the year ended June 30, 2006 and the balance was retained in the Unpledged TSR account from which distributions can not occur until after December 6, 2007.

Bond interest expense on outstanding bonds was lower for 2007 than for 2006, when a larger principal amount of bonds were outstanding. Other expenses, composed primarily of the amortization of deferred bond refunding costs was lower in 2007 than in 2006 because 2006 included the full write-off of COI pertaining to the bonds issued to TIFIA which were retired as part of the restructuring in 2006.

The following summarizes TSASC's assets, liabilities, and net deficit as of June 30, 2007 and 2006:

($ 000's)	2007	2006	FYE 2007 Change
Assets:			
Total Assets - non-capital	$ 624,220	$ 472,032	$ 152,188
Liabilities:			
Current liabilities	$ 5,494	$ 5,560	$ (66)
Long-term liabilities–Bonds payable:			
Bonds payable after one year	1,316,860	1,333,565	(16,705)
Unamortized – bond discounts	(35,791)	(37,152)	1,361
Unamortized deferred bond refunding costs	(51,695)	(70,276)	18,581
Total Liabilities	1,234,868	1,231,697	3,171
Net Assets (Deficits):			
Restricted	(1,021,827)	(1,024,483)	2,656
Unrestricted	411,179	264,818	146,361
Total Deficit	$ (610,648)	$ (759,665)	$ 149,017

The increase in total assets is primarily the result of an increase in the amount of Unpledged TSRs held at year end.

The increase in total liabilities is primarily due to the decrease in bonds payable, which was more than offset by the decreases in unamortized bond discount and deferred bond refunding costs.

The net deficits are primarily the result of the issuance of bonds which are and will continue to be repaid from future TSR revenues.

FINANCIAL HIGHLIGHTS AND OVERALL ANALYSIS - GOVERNMENTAL FINANCIAL STATEMENTS

The following summarizes the changes in debt service fund balances for the years ended June 30, 2007 and 2006:

($ 000's)	2007	2006	FYE 2007 Change
Revenues:			
Tobacco settlement revenue	$ 208,433	$ 193,688	$ 14,745
Investment income	21,728	24,191	(2,463)
Total revenues	230,161	217,879	12,282
Expenditures:			
Bond interest	66,637	96,345	(29,708)
Principal amount of bonds retired	16,705	193,540	(176,835)
Other	237	11,724	(11,487)
Total expenditures	83,579	301,609	(218,030)
Other financing sources, net	-	134,833	(134,833)
Change in fund balance	146,582	51,103	95,479
Fund balance, beginning of year	384,277	333,174	51,103
Fund balance, end of year	$ 530,859	$ 384,277	$ 146,582

TSR revenue increased in 2007 compared to 2006, as previously discussed. Bond interest expenditures on outstanding bonds was lower for 2007 than for 2006, because the 2006 interest payments represented approximately 16 months of bond interest compared to the 12 months of interest paid during 2007. The additional interest in 2006 resulted from the final interest payment on the defeased bonds as well as the change in interest payment dates for the newly issued Series 2006-1 bonds. The principal amount of bonds retired in 2006 was higher than in 2007 because of the restructuring in that year, as previously discussed. Other financing sources, net in 2006 is higher than in 2007 because the 2006 amount reflects refunding bond proceeds in excess of the amount used to fund the refunding escrow; those funds were used to retire TIFIA bonds, as previously discussed, and to fund costs of issuing the refunding bonds.

The following summarizes the changes in the debt service fund assets, liabilities, and fund balances as of June 2007 and 2006:

($ 000's)	2007	2006	FYE 2007 Change
Assets:			
Cash and investments	$ 530,663	$ 384,277	$ 146,386
Tobacco settlement revenue receivable	83,000	77,000	6,000
Other assets	196	-	196
Total assets	$ 613,859	$ 461,277	$ 152,582
Liabilities:			
Deferred tobacco settlement revenue	$ 83,000	$ 77,000	$ 6,000
Fund Balance:			
Reserved for debt service	119,484	119,459	25
Unreserved	411,375	264,818	146,557
Total fund balance	530,859	384,277	146,582
Total liabilities and fund balance	$ 613,859	$ 461,277	$ 152,582

Cash and investments increased primarily due to an increase in the amount of Unpledged TSRs held by TSASC, as discussed above. The growth in the TSRs receivable reflects the increase in TSR revenue, also discussed above, as a portion of the revenue is related to estimated cigarette sales which occur prior to the end of the fiscal year but for which manufacturers will make payment in the future. Other assets represent the value of prepaid insurance at fiscal year end 2007.

The growth in the unreserved and total fund balance during 2007 primarily results from the increase in Unpledged TSRs held at year end.

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TSASC, INC.

STATEMENTS OF NET ASSETS (DEFICITS)
AS OF JUNE 30, 2007 AND 2006
(In Thousands)

	2007	2006
ASSETS		
Restricted cash and cash equivalents	$ 3	$ 33,499
Unrestricted cash and cash equivalents	1,532	264,289
Restricted investments	119,481	85,960
Unrestricted investments	409,647	529
Tobacco settlement revenue receivable	83,000	77,000
Other assets	196	-
Unamortized bond issuance cost	10,361	10,755
Total assets	624,220	472,032
LIABILITIES		
Accrued expenses	-	-
Accrued interest payable	5,494	5,560
Bonds payable:		
Portion due within one year	-	-
Portion due after one year	1,316,860	1,333,565
Unamortized bond discount	(35,791)	(37,152)
Unamortized deferred bond refunding costs	(51,695)	(70,276)
Total liabilities	1,234,868	1,231,697
NET ASSETS (DEFICITS)		
Restricted	(1,021,827)	(1,024,483)
Unrestricted	411,179	264,818
Total deficit	$ (610,648)	$ (759,665)

See notes to financial statements.

TSASC, INC.

STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED JUNE 30, 2007 AND 2006
(In Thousands)

	2007	2006
EXPENSES		
General and administrative expenses	$ 237	$ 573
Interest expense	67,932	73,561
Amortization of bond issuance expense	394	396
Amortization of deferred bond refunding costs	18,581	27,398
Total program expenses	87,144	101,928
GENERAL REVENUES		
Tobacco settlement revenue	214,433	192,133
Plus not remittable to the Trust	-	36,880
Net tobacco settlement revenue	214,433	229,013
Investment earnings	21,728	24,191
Total general revenues	236,161	253,204
CHANGES IN DEFICIT	149,017	151,276
DEFICIT, beginning of year	(759,665)	(910,941)
DEFICIT, end of year	$ (610,648)	$ (759,665)

See notes to financial statements.

TSASC, INC.

GOVERNMENTAL FUND BALANCE SHEETS
AS OF JUNE 30, 2007 AND 2006
(In Thousands)

	Debt Service	
	2007	2006
ASSETS		
Restricted cash and cash equivalents	$ 3	$ 33,499
Unrestricted cash and cash equivalents	1,532	264,289
Restricted investments	119,481	85,960
Unrestricted investments	409,647	529
Tobacco settlement revenue receivable	83,000	77,000
Other assets	196	-
Total assets	$ 613,859	$ 461,277
LIABILITIES AND FUND BALANCES		
Liabilities		
Deferred tobacco settlement revenue	$ 83,000	$ 77,000
Total liabilities	83,000	77,000
Fund balances		
Reserved for debt service	119,484	119,459
Unreserved	411,375	264,818
Total fund balances	530,859	384,277
Total liabilities and fund balances	$ 613,859	$ 461,277

See notes to financial statements.

TSASC, INC.

STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUND
FOR THE YEARS ENDED JUNE 30, 2007 AND 2006
(In Thousands)

	Debt Service	
	2007	**2006**
REVENUES		
Tobacco settlement revenue	$ 208,433	$ 199,133
Less remittances to the Trust	-	(5,445)
Tobacco settlement revenue retained	208,433	193,688
Investment earnings	21,728	24,191
Total revenues	230,161	217,879
EXPENDITURES		
Interest	66,637	96,345
Principal amount of bonds retired	16,705	193,540
Refunding bond issuance costs	-	11,151
General and administrative	237	573
Total expenditures	83,579	301,609
Excess of revenues over (expenditures); (expenditures) over revenues	146,582	(83,730)
OTHER FINANCING SOURCES (USES)		
Refunding bond proceeds	-	1,314,990
Payments to refunded bond escrow holder	-	(1,180,157)
Total other financing sources	-	134,833
NET CHANGES IN FUND BALANCES	146,582	51,103
FUND BALANCES, beginning of year	384,277	333,174
FUND BALANCES, end of year	$ 530,859	$ 384,277

See notes to financial statements.

TSASC, INC.

RECONCILIATIONS OF THE GOVERNMENTAL FUND BALANCE SHEETS TO THE STATEMENTS OF NET ASSETS (DEFICITS) AS OF JUNE 30, 2007 AND 2006
(In Thousands)

	2007	2006
Total fund balances - governmental fund	$ 530,859	$ 384,277
Amounts reported for governmental activities in the statements of net assets (deficits) are different because:		
Costs of debt issuance are expenditures in governmental activities. However, in the statements of net assets (deficits), the costs of debt issuance are reported as capitalized assets and amortized over the life of the related debt.	10,361	10,755
Bond discounts are reported as other financing uses in the governmental fund financial statements. However, in the statements of net assets (deficits), bond discounts are reported as a component of bonds payable and amortized over the life of the related debt.	35,791	37,152
Costs of bond refundings are reported as expenditures in the governmental fund financial statements. However, in the statements of net assets (deficits), those costs and the related gain or loss are deferred and amortized over the shorter of the remaining life of the old debt or the life of the new debt.	51,695	70,276
Deferred tobacco settlement revenue in the governmental fund financial statements is recognized as revenue and not deferred in the statements of net assets (deficits).	83,000	77,000
Some liabilities are not due and payable in the current period from currently available financial resources and therefore are not reported in the governmental fund financial statements. Those liabilities consist of:		
Bonds payable	(1,316,860)	(1,333,565)
Accrued interest on bonds	(5,494)	(5,560)
Net deficit of governmental activities	$ (610,648)	$ (759,665)

See notes to financial statements.

TSASC, INC.

RECONCILIATIONS OF THE STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUND TO THE STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED JUNE 30, 2007 AND 2006
(In Thousands)

	2007	2006
Net changes in fund balances - total governmental funds	$ 146,582	$ 51,103
Amounts reported for governmental activities in the statement of activities are different because:		
Bond refunding proceeds and expenditures provide current financial resources and expenditures to governmental fund, but the proceeds and amount expended increase and decrease the long-term liabilities in the statementS of net assets (deficits).	-	(134,833)
Tobacco settlement revenue not available in the current period is deferred in governmental fund and included in revenue in the statements of activities.	6,000	(7,000)
Tobacco settlement revenue not available in the current period is deferred in governmental fund and included in remittances to the Trust in the statements of activities.	-	42,325
Interest expense in the statements of activities recorded as additional debt on the TIFIA loan is not reported as expenditure in governmental fund.	-	(268)
Repayment of bond principal is an expenditure in the governmental fund, but the repayment reduces long-term liabilities in the statements of net assets (deficits).	16,705	193,540
Governmental fund reports the cost of debt issuance as expenditures. However, in the statements of activities, the cost of debt issuance is amortized over the life of the related debt.	(394)	10,755
Governmental fund reports the cost of bond refundings as expenditures. However, in the statements of net assets (deficits), those costs and the related gain or loss are deferred and amortized over the shorter of the remaining life of the old debt or the life of the new debt.	(18,581)	(27,398)
Governmental fund reports bond discounts as other financing uses. However, in the statements of activities, bond discounts are amortized over the lives of the related debt as interest expense.	(1,361)	(1,368)
Interest expense is reported in the statements of activities on the accrual basis, but interest is reported as an expenditure in the governmental fund when the outlay of financing resources is required.	66	24,420
Change in net deficit of governmental activities	$ 149,017	$ 151,276

See notes to financial statements.

1. ORGANIZATION

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 (who also serves as Chairperson), 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, accordingly, included in the City's financial statements.

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 provides for a continuing release of future smoking-related claims, in exchange for certain payments to be made to the settling states, as well as certain tobacco advertising and marketing restrictions, among other things. The Decree, which was entered by the Supreme Court of the State, allocated to the City a share of the TSRs under the MSA. The future rights, 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 restructured all outstanding indebtedness by issuing the Series 2006-1 bonds in the amount of $1.353 billion. This restructuring relieved TSASC of its obligation under the original bond indenture to deposit a portion of Collections into a trapping account.

Under the Amended and Restated Indenture dated January 1, 2006 (the "Indenture"), the Residual Certificate represents the entitlement to receive all amounts in excess of specified percentages of TSRs and other revenues (collectively, "Collections") used to fund debt service and operating expenses of TSASC. The Collections in excess of the specified percentages will be transferred to the TSASC Tobacco Settlement Trust (the "Trust"), as owner of the Residual Certificate and then to the City as the beneficial owner of the Trust. The Indenture allows transfers to the Trust after December 6, 2007.

The Indenture provides that a specified percentage of Collections are pledged, and required to be applied to the payment of debt and operating costs. That percentage is 37.40% and is subject to reduction at June 1, 2024, and at each June 1st thereafter, depending on the magnitude of cumulative bond redemptions under the turbo redemption feature of the Series 2006-1 bonds (which requires all pledged Collections, after payment of operating costs, to be applied to payment of principal of and interest on the Series 2006-1 bonds).

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The entity-wide financial statements of TSASC, which include the statements of net assets (deficits) and the statements of activities, are presented to display information about the reporting entity as a whole, in accordance with Statement No. 34 of the Governmental Accounting Standards Board, as amended. The entity-wide financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

TSASC's debt service (governmental) fund financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized when it becomes susceptible to accrual, which 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 unmatured interest on bonds payable, which is recognized when due. TSASC's sole governmental fund is the debt service fund, which accounts for the accumulation of resources for payment of principal and interest on debt, as well as for TSASC's generals operations. TSASC does not anticipate issuing additional debt for capital projects.

Investments, including accrued interest, are reported at fair value as of the reporting date.

In accordance with GASB Technical Bulletin No. 2004-1, Tobacco Settlement Recognition and Financial Reporting Entity Issues, TSASC records a receivable for TSRs at June 30th. The TSRs are expected to be received the following April and are based on an estimate of cigarette sales for the six month period January 1 to June 30.

Bond premiums, discounts and issuance costs are capitalized and amortized over the life of the related debt using the interest method in the entity-wide financial statements. The debt service fund financial statements recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Deferred bond refunding costs represent the accounting loss incurred in advance refunding of outstanding bonds. 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.

Interest expense is recognized on the accrual basis in the entity-wide financial statements. Interest expenditures are recognized when paid in the individual debt service fund financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

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 pronouncement has been issued by GASB but not yet implemented by TSASC:

- GASB Statement 48: *Sales and Pledges of Receivables and Future Revenues and Intra-entity Transfers of Assets and Future Revenues*. TSASC has not completed the process of evaluating the impact that will result from adopting Statement 48. Therefore, TSASC is unable to disclose the impact adopting this statement will have on its financial statements. This statement is effective for fiscal periods beginning after December 15, 2006, which will be for TSASC's fiscal year ending June 30, 2008.

3. BONDS PAYABLE

On February 8, 2006, TSASC issued $1.353 billion of Fiscal Series 2006-1 bonds to restructure all of its outstanding indebtedness. The restructuring advance refunded all bonds outstanding in Series 1999-1 and Series 2002-1 and fully paid all of the bonds issued to TIFIA. This refunding resulted in a legal defeasance of the refunded bonds. In a legal defeasance, the proceeds, net of costs of issuance, are invested in Defeasance Collateral (as defined in TSASC's original Indenture) consisting of U.S. Government securities and are deposited in an escrow account with the TSASC's Trustee to provide for all future debt service on the legally defeased bonds. This advance refunding resulted in an accounting loss of $97.7 million, which was recorded on the statement of net assets as deferred bond refunding costs, net of accumulated amortization. The advance refunding relieved TSASC of its obligations under the original bond indenture, including the requirement to deposit a portion of the Collections into a trapping account.

The Amended and Restated Indenture dated January 1, 2006 (the "Indenture") provides that a specified percentage of Collections are pledged and required to be applied to the payment of debt and operating costs. That percentage is 37.40% and is subject to reduction at June 1, 2024, and at each June 1st thereafter, depending upon attainment of pre-defined levels of cumulative bond redemptions under the turbo redemption feature of the Series 2006-1 bonds (which requires all pledged Collections to be applied, after funding of operating costs, to the payment of interest and principal on the Series 2006-1 bonds).

Under the Indenture, the Residual Certificate represents the entitlement to receive all amounts in excess of specified percentages of Collections pledged and required to be applied to fund debt service and operating costs of TSASC. The Collections in excess of the specified percentages will be transferred to the Trust, as owner of the Residual Certificate, and then to the City as the beneficial owner of the Trust. The Indenture allows transfers to the Trust after December 6, 2007.

3. BONDS PAYABLE (CONTINUED)

In accordance with the Indenture, Pledged Collections during 2007 were used to fund operating expenses, then to fund interest payments due on June 1, 2007 and December 1, 2007, then to fund and make turbo redemption payments of $3.340 million on December 1, 2006 and of $13.365 million on June 1, 2007.

The Pledged TSRs retained in April 2006 were used to fund operating expenses first, then to fund the interest payments due on June 1, 2006 and December 1, 2006. The remaining Pledged TSRs were then used to fund and make a sinking fund payment of $8.685 million on June 1, 2006 and $11.260 million of "turbo" principal payments payable on June 1, 2006.

Outstanding bonds payable bear interest at rates ranging from 4.750% to 5.125%. A summary of changes in outstanding bonds during the fiscal year ended June 30, 2007 is as follows (in thousands):

	Fiscal Year Ended June 30, 2007			
	Balance June 30, 2006	Bonds Issued	Bonds Retired or Defeased	Balance June 30, 2007
Series 2006-1	1,333,565	-	(16,705)	1,316,860
Totals	$ 1,333,565	$	$ (16,705)	$ 1,316,860

Outstanding bonds payable bear interest at rates ranging from 4.750% to 5.125%. A summary of changes in outstanding bonds during the fiscal year ended June 30, 2006 is as follows (in thousands):

	Fiscal Year Ended June 30, 2006				
	Balance June 30, 2005	Bonds Issued		Bonds Retired or Defeased	Balance June 30, 2006
Series 1999-1	$ 670,280	$ -		$ (670,280)	$ -
Bonds issued under TIFIA Agreement	161,047	268	(a)	(161,315)	-
Series 2002-1	451,970	-		(451,970)	-
Series 2006-1	-	1,353,510		(19,945)	1,333,565
Totals	$ 1,283,297	$ 1,353,778		$ (1,303,510)	$ 1,333,565

(a) During the years ended June 30, 2006 bonds issued under the TIFIA Agreement include capitalized interest of $268.

3. BONDS PAYABLE (CONTINUED)

Debt service requirements for term bond maturities and anticipated sinking fund principal payments, including principal and interest at June 30, 2007, are as follows (in thousands):

	Term Bond Maturities			Sinking Fund Principal Payments		
	Principal	Interest	Total	Principal	Interest	Total
Year ended June 30,						
2008	$ -	$ 65,923	$ 65,923	$ -	$ 65,923	$ 65,923
2009	-	65,923	65,923	-	65,923	65,923
2010	-	65,923	65,923	2,590	65,923	68,513
2011	-	65,923	65,923	13,555	65,800	79,355
2012	-	65,923	65,923	13,060	65,156	78,216
2013 to 2017	-	329,616	329,616	80,040	315,647	395,687
2018 to 2022	247,420	329,616	577,036	138,175	291,166	429,341
2023 to 2027	137,765	263,966	401,731	176,700	254,068	430,768
2028 to 2032	-	236,413	236,413	226,510	205,111	431,621
2033 to 2037	372,650	180,515	553,165	290,390	142,286	432,676
2038 to 2042	559,025	143,250	702,275	375,840	59,807	435,647
	$ 1,316,860	$ 1,812,991	$ 3,129,851	$ 1,316,860	$ 1,596,810	$ 2,913,670

Term bond maturities for these bonds represent the minimum amount of principal that TSASC must pay as of the specific distribution dates in order to avoid a default. The sinking fund principal payments represent the amount of principal that TSASC expects to pay from the pledged TSRs collected. If pledged TSRs collected exceed the principal and interest required under the Term Bond Maturities, then the excess will be applied first to the sinking fund payment and then to “turbo” redemptions.

At June 30, 2007 and 2006 TSASC has funded its debt service according to the Indenture requirements. At June 30, 2007 and 2006 debt service accounts totaled $32.962 million and $33.358 million, respectively.

At June 30, 2007 and 2006, TSASC has funded its required liquidity reserves of $85.399 million and $85.399 million, respectively. At June 30, 2007 and 2006 the liquidity reserve funds were invested in commercial paper.

As of June 30, 2007, TSASC had refunded, with Defeasance Collateral, bonds totaling $1.110 million of which $1.095 million is still to be paid from the Defeasance Collateral held in the escrow account on deposit with TSASC’s escrow trustee.

At June 30, 2007 and 2006 TSASC had on deposit $0.526 million and $0.704 million, respectively, of interest earnings. On June 30, 2007 and 2006 TSASC had on deposit $410.174 million and $263.923 million, respectively, in the Unpledged TSR account, which can not be transferred to the Trust until after December 6, 2007.

4. CASH AND CASH EQUIVALENTS

TSASC's cash and cash equivalents consist of bank deposits, forward delivery contracts, commercial paper and short-term U.S. Government-guaranteed securities with original maturities of three months or less and are held by TSASC's trustee in TSASC's name valued at fair value. The commercial paper was rated A1+ by Standard & Poor's Rating Services and P1 by Moody's Investor Services. At June 30, 2007 and 2006, total cash and cash equivalents are summarized as follows:

	(in thousands) June 30,	
	2007	2006
Restricted cash and cash equivalents		
Cash	$ 3	$ 3
U.S. Government securities	-	33,496
	$ 3	$ 33,499
Unrestricted Cash and cash equivalents		
Cash	$ 87	$ 64
Commercial paper	1,026	
U.S. Government securities	419	264,225
	$ 1,532	$ 264,289

5. INVESTMENTS

TSASC is generally authorized to invest in direct obligations of or obligations guaranteed by the U.S. government and highly rated U.S. municipal obligations. TSASC is also authorized to invest in certain highly rated commercial paper, highly rated short-term corporate securities, highly rated taxable money market funds, and investment agreements or guaranteed investment contracts with highly rated financial institutions or corporations.

At June 30, 2007 and 2006 investments were held by TSASC's trustee in TSASC's name. The commercial paper was rated A1+ by Standard & Poor's Rating Services and P1 by Moody's Investor Services and the investments are summarized as follows:

	(in thousands) June 30,	
	2007	**2006**
Restricted investments		
Commercial paper	$ 118,876	$ 85,960
U.S. Government securities	605	-
	$ 119,481	$ 85,960
Unrestricted investments		
Commercial paper	$ 409,147	$ -
U.S. Government securities	500	529
	$ 409,647	$ 529

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