

In the opinion of Kutak Rock LLP, Bond Counsel, under existing laws, regulations, rulings and judicial decisions, interest on the Bonds (including original issue discount treated as interest) is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, except that such interest must be included in the "adjusted current earnings" of certain corporations for purposes of calculating alternative minimum taxable income. Bond Counsel also is of the opinion that, under existing laws of the Commonwealth of Kentucky, interest on the Bonds is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Bonds are exempt from ad valorem taxes by the Commonwealth of Kentucky and all political subdivisions thereof. See "Tax Exemption" herein.

\$21,670,000

**KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
MULTI-COUNTY CORRECTIONAL FACILITIES REVENUE REFUNDING BONDS,
SERIES 2004**

Dated: Date of delivery

Due: November 1, as shown below

Interest on the Series 2004 Bonds is payable on May 1, 2005, and semi-annually on each May 1 and November 1 thereafter until Maturity. The Series 2004 Bonds will be issued only as fully registered bonds, without coupons, in denominations of \$5,000 or any integral multiple thereof, registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York, which will act as securities depository for the Series 2004 Bonds. Purchasers will not receive certificates representing their ownership interest in the Series 2004 Bonds purchased. So long as DTC or its nominee is the registered owner of the Series 2004 Bonds, payments of the principal of and interest due on the Series 2004 Bonds will be made directly to DTC.

The Series 2004 Bonds are being issued by the Kentucky Local Correctional Facilities Construction Authority (the "Authority") for the purpose of (i) providing the funds required to redeem and discharge the outstanding Kentucky Local Correctional Facilities Construction Authority Multi-County Correctional Facilities Revenue Refunding Bonds, Series 1994 and (ii) paying the costs of issuing the Series 2004 Bonds.

The Series 2004 Bonds are special obligations of the Authority secured under a Trust Indenture dated as of October 1, 2004 (the "Trust Indenture") between the Authority and U.S. Bank National Association, Louisville, Kentucky, as trustee (the "Trustee"), and a Series 2004 Resolution of the Authority adopted on September 15, 2004. The Series 2004 Bonds are payable solely from the hereinafter defined Pledged Receipts designated under the Trust Indenture, including the Court Costs, Rental Payments to be made by certain Local Governments under the hereinafter defined Leases, Investment Earnings, and other monies pledged under the Trust Indenture.

The scheduled payment of principal of and interest on the Series 2004 Bonds, when due, will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Series 2004 Bonds by MBIA Insurance Corporation.



The Series 2004 Bonds are not subject to redemption prior to maturity.

The Series 2004 Bonds will bear interest at the rates and will mature in the amounts and on the dates set forth below.

<u>Maturity</u> <u>(November 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Yield</u>	<u>Maturity</u> <u>(November 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Yield</u>
2005	\$1,845,000	3.00%	1.68%	2010	\$2,170,000	5.25%	3.00%
2006	1,940,000	3.00	1.96	2011	2,280,000	5.25	3.21
2007	1,995,000	2.25	2.16	2012	2,400,000	5.25	3.36
2008	2,040,000	3.00	2.45	2013	2,530,000	5.25	3.50
2009	2,105,000	3.00	2.74	2014	2,365,000	5.25	3.61

THE SERIES 2004 BONDS DO NOT CONSTITUTE A DEBT, LIABILITY OR OBLIGATION OF THE COMMONWEALTH OR OF ANY POLITICAL SUBDIVISION THEREOF, OR A PLEDGE OF THE FAITH AND CREDIT OF THE COMMONWEALTH OR OF ANY SUCH POLITICAL SUBDIVISION. THE ONLY SECURITY PLEDGED FOR THE SERIES 2004 BONDS IS THE INDEPENDENT REVENUES AND OTHER MONEYS DISCUSSED HEREIN. THE GENERAL ASSEMBLY DOES NOT INTEND TO APPROPRIATE ANY STATE FUNDS TO FULFILL THE FINANCIAL OBLIGATION REPRESENTED BY THE SERIES 2004 BONDS. THE AUTHORITY HAS NO TAXING POWER.

The Series 2004 Bonds are offered when, as and if issued by the Authority and accepted by the Underwriters, subject to prior sale, withdrawal or modification of the offer without notice, and to the approval of legality by Kutak Rock LLP, Omaha, Nebraska, Bond Counsel. Certain legal matters will be passed upon for the Underwriter by its counsel, Peck, Shaffer & Williams LLP, Covington, Kentucky. It is expected that the Series 2004 Bonds will be available for delivery through DTC in New York, New York on or about October 13, 2004.

MORGAN STANLEY
J.J.B. Hilliard, W.L. Lyons, Inc.

Dated: September 29, 2004

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**KENTUCKY LOCAL CORRECTIONAL FACILITIES
CONSTRUCTION AUTHORITY**

MEMBERS

R. B. RUDOLPH, JR. – Chairman
JOHN D. REES – Secretary
HON. TOMMY TURNER
HON. HUGH MCCORMICK

HON. ADRIAN ARNOLD – Vice Chairman
HON. JIM TOWNSEND
HON. JAMES KEMPER
CHRISTY LYNN CAMPBELL

STAFF

Office of Financial Management
Room 261, Capitol Annex
Frankfort, Kentucky 40601
(502) 564-2924

F. THOMAS HOWARD
Acting Executive Director of the Office of Financial Management

MELISSA JOHNSON
Treasurer of the Authority

No dealer, broker, salesman or other person has been authorized by the Authority or the Underwriters to give any information or to make any representations other than those contained in this Official Statement and, if given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Series 2004 Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

The information set forth herein has been obtained from the Authority, the Local Governments and other sources which are believed to be reliable, but it is not guaranteed as to accuracy or completeness and is not to be construed as a representation by the Underwriter. The information herein is subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Authority or any of the Local Governments since the date hereof.

IN CONNECTION WITH THE OFFERING OF THE SERIES 2004 BONDS, THE UNDERWRITER MAY OVER ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF SUCH BONDS AT LEVELS ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

SUMMARY STATEMENT

This Summary Statement is subject in all respects to the more complete information set forth in the Official Statement.

The Issue

The Multi-County Correctional Facilities Revenue Refunding Bonds, Series 2004 (the "Series 2004 Bonds"), in the aggregate principal amount of \$21,670,000, are being issued by the Kentucky Local Correctional Facilities Construction Authority (the "Authority"). The Series 2004 Bonds will be issued in registered form only, in denominations of \$5,000 or any integral multiple thereof, registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Series 2004 Bonds. The principal amount, interest rates and maturities of the Series 2004 Bonds, are set forth on the cover page of this Official Statement.

Purpose of Issue

The Series 2004 Bonds are being issued for the purpose of (i) providing the funds required to redeem and discharge the Authority's outstanding Multi-County Correctional Facilities Revenue Refunding Bonds, Series 1994 and (ii) paying the costs of issuing the Series 2004 Bonds.

Security for the Series 2004 Bonds

The Series 2004 Bonds are special obligations of the Authority and, except to the extent payable from the proceeds of such Series 2004 Bonds and other monies pledged therefor, are payable solely from the Pledged Receipts which will be secured under a Trust Indenture dated as of October 1, 2004 (the "Trust Indenture") between the Authority and U.S. Bank National Association, Louisville, Kentucky, acting as trustee, and a Series 2004 Resolution of the Authority adopted on September 15, 2004 (the "Series 2004 Resolution"). The Pledged Receipts include (i) all monies collected and deposited in the State Treasury for the benefit of the Authority (the "Court Costs") pursuant to Sections 24A.175(1), 24A.180(5) and 42.320(2)(b) of the Kentucky Revised Statutes ("KRS"); (ii) all Rental Payments received by the Authority under the Leases entered into by the Local Governments which have requested that the Authority act as an issuing agency on their behalf in order to provide the Local Government's financial contribution to a particular Project (the "Rental Payments"); (iii) all Supplemental Rental Payments received by the Authority under Supplemental Leases from Local Governments in repayment of and as interest on Construction Completion Loans; (iv) all other available monies received by the Authority in the form of gifts, grants and appropriations; and (v) investment earnings and gains on certain monies on deposit under the Trust Indenture. The amount of Court Costs received by the Authority is based on a schedule of fees respecting certain criminal cases in the Commonwealth, which schedule is determined by the Kentucky General Assembly. Consequently, increases or decreases in the amount of Court Costs (through an increase or decrease of the fee schedule) cannot be dictated by the Authority. The Series 2004 Bonds will also be secured by the Debt Service Reserve which is required to be funded in an amount equal to the Aggregate Debt Service Reserve Requirement, which requirement may be satisfied with a surety bond (or other credit facility).

THE ONLY SECURITY WHICH IS PLEDGED FOR THE SERIES 2004 BONDS IS THE INDEPENDENT REVENUES AND ASSETS DESCRIBED IN THE PRECEDING PARAGRAPH. THE GENERAL ASSEMBLY DOES NOT INTEND TO APPROPRIATE ANY STATE FUNDS TO FULFILL THE FINANCIAL OBLIGATIONS REPRESENTED BY THE SERIES 2004 BONDS OTHER THAN SUCH REVENUES AND FUNDS.

The scheduled payment of principal of and interest on the Series 2004 Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Series 2004 Bonds by MBIA Insurance Corporation.

Additional Parity Bonds

The Trust Indenture provides that the Authority may issue additional bonds ranking on a basis of parity as to security and sources of payment with the Series 2004 Bonds if the following requirements are met: (i) there is on deposit in the Debt Service Reserve an amount equal to the Aggregate Debt Service Reserve Requirement and (ii) a certificate of an Authorized Officer of the Authority is delivered to the Trustee stating, in effect, that annual Court Costs receipts plus annual Rental Payments from all Leases made and to be made with Local Governments shall be projected to be at least equal to 1.20 times the maximum Annual Debt Service Requirement of the Outstanding Bonds and the Series of Bonds then proposed to be issued.

Redemption Provisions

The Series 2004 Bonds are not subject to redemption prior to maturity.

The Authority

The Authority is a body corporate and politic and an agency and instrumentality of the Commonwealth created in 1982 pursuant to KRS Sections 441.605 through 441.695, as amended, to provide an additional and alternative method of constructing, improving or repairing and financing local and regional jails and other correctional facilities in the Commonwealth.

The Projects

The Projects (as defined herein) consist of the acquisition, construction, repair or improvement of regional and local jails and other correctional facilities. In 1983, the Department of Corrections, a part of the Justice and Public Safety Cabinet, adopted new Kentucky Jail Standards relating to health and safety conditions, fire safety and custody, care and treatment of prisoners. Many existing jails did not comply with the new standards and some jails were ordered closed by the Department of Corrections resulting in the necessity of building the Projects. The Projects, encompassing jails and correctional facilities, have been completed. The Local Governments participated in the Authority's Bond Program on the basis of an application and selection process established by the Department of Corrections and the Authority.

Definitions

Except as the context otherwise indicates or as otherwise defined herein, capitalized terms used in this Official Statement have the same meanings as in "SUMMARY OF BOND DOCUMENTS" included as Appendix C and have the same meanings as in the Trust Indenture and the Series 2004 Resolution.

General

The Official Statement speaks only as of its date, and the information contained herein is subject to change. All summaries of documents and agreements in the Official Statement are qualified in their entirety by reference to such documents and agreements, copies of which are available from the Office of Financial Management.

Information

Information regarding the Series 2004 Bonds is available by contacting the Office of Financial Management, 702 Capitol Avenue, Suite 261, Frankfort, Kentucky 40601, (502) 564-2924; or, during the initial offering period, by contacting the representative of the Underwriters, Morgan Stanley & Co. Incorporated, 2000 Westchester Avenue, Purchase, NY 10577-2530, phone: 914-225-0203.

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OFFICIAL STATEMENT
relating to

\$21,670,000
Kentucky Local Correctional Facilities Construction Authority
Multi-County Correctional Facilities Revenue Refunding Bonds,
Series 2004

INTRODUCTION

The purpose of this Official Statement, including the cover page, Summary Statement and Appendices hereto, is to provide certain information concerning the sale by the Kentucky Local Correctional Facilities Construction Authority (the "Authority") of \$21,670,000 principal amount of its Multi-County Correctional Facilities Revenue Refunding Bonds, Series 2004 (the "Series 2004 Bonds").

The Authority is a body corporate and politic and an agency and instrumentality of the Commonwealth of Kentucky (the "Commonwealth" or the "State") created in 1982 pursuant to Sections 441.605 through 441.695 of the Kentucky Revised Statutes ("KRS"), as amended (the "Act"), to provide an additional and alternative method of constructing, improving or repairing and financing jails, as that term is defined in the Act (hereinafter called "jails" or "Correctional Facilities"). The Series 2004 Bonds are being issued pursuant to the Act and are secured under a Trust Indenture dated as of October 1, 2004 (the "Trust Indenture") by and between the Authority and U.S. Bank National Association, Louisville, Kentucky, as trustee (the "Trustee"), and a Series 2004 Resolution of the Authority adopted on September 15, 2004 (the "Series 2004 Resolution"). The Trustee also acts in the capacities of Bond Registrar and Paying Agent under the Trust Indenture.

The Series 2004 Bonds are being issued for the purposes of (i) providing the funds required to redeem and discharge the Authority's outstanding Multi-County Correctional Facilities Revenue Refunding Bonds, Series 1994 (the "Prior Bonds") and (ii) paying the costs of issuing the Series 2004 Bonds. See "PLAN OF REFUNDING" and "SOURCES AND USES OF FUNDS."

The Court Costs constituting part of the Pledged Receipts are authorized under the provisions of KRS 42.320(2)(b), which mandates that 10.8% of all court costs collected pursuant to KRS 24A.175(1), which presently requires that court costs in the amount of \$100 be imposed in certain criminal cases within the jurisdiction of the district courts of the Commonwealth, be paid to the State Treasury for the use and benefit of the Authority. Under the terms of the Trust Indenture, all Court Costs, together with all interest earnings thereon, are to be remitted by the Authority to the Trustee monthly. In addition, the Authority has assigned to the Trustee the right to collect the Rental Payments due under the Leases thirty (30) days in advance of each principal and interest due date on the Bonds.

There are currently eleven Leases outstanding between the Authority and Local Governments. Rental Payments received by the Authority under the Leases constitute part of the Pledged Receipts. See "SECURITY FOR THE SERIES 2004 BONDS - Pledged Receipts - Lease Amounts."

THE SERIES 2004 BONDS DO NOT CONSTITUTE A DEBT OF THE COMMONWEALTH OR OF ANY POLITICAL SUBDIVISION THEREOF, OR A PLEDGE OF THE FAITH AND CREDIT OF THE COMMONWEALTH OR OF ANY POLITICAL SUBDIVISION THEREOF. THE GENERAL ASSEMBLY DOES NOT INTEND TO APPROPRIATE ANY STATE FUNDS TO FULFILL THE FINANCIAL OBLIGATIONS REPRESENTED BY THE SERIES 2004 BONDS OTHER THAN SUCH REVENUES AND FUNDS. THE AUTHORITY HAS NO TAXING POWER.

The scheduled payment of the principal of and interest on the Series 2004 Bonds, when due, will be guaranteed under a financial guaranty insurance policy to be issued concurrently with the delivery of the Series 2004 Bonds by MBIA Insurance Corporation. (See "BOND INSURANCE" herein and APPENDIX F).

This Official Statement also includes summaries of the Leases and Participation Agreements, the Trust Indenture, the Series 2004 Resolution, the Act, other Kentucky statutes, information about the Projects and certain reports. The summaries of and references to all documents, statutes, reports and other instruments referred to herein do not purport to be complete, comprehensive or definitive and each such summary and reference is qualified in its entirety by reference to each such document, statute, report or instrument. Certain capitalized terms which are not otherwise defined herein shall have the respective meanings set forth in such documents.

PLAN OF REFUNDING

The Series 2004 Bonds are being issued for the purposes of (i) providing the funds required to redeem and discharge the outstanding Prior Bonds and (ii) paying the costs of issuing the Series 2004 Bonds. See "SOURCES AND USES OF FUNDS."

From the proceeds of the Series 2004 Bonds and other funds of the Authority, there will be deposited in the debt service fund established under the trust indenture for the Prior Bonds, an amount sufficient to redeem and discharge the Prior Bonds. The amount so deposited will be held by the trustee for the Prior Bonds and invested in direct obligations of or obligations guaranteed by the United States of America, with such amount applied solely for payment or redemption of the Prior Bonds on November 1, 2004.

DESCRIPTION OF THE SERIES 2004 BONDS

Dates and Interest Rates

The Series 2004 Bonds will be dated the date of their delivery and will bear interest at the rates and mature in the amounts and on the dates set forth on the cover page of this Official Statement. The Series 2004 Bonds will be issued as fully registered bonds in denominations of \$5,000 or any integral multiple thereof. Interest on the Bonds will be payable semi-annually on May 1 and November 1 of each year, commencing May 1, 2005.

Book-Entry-Only System

The Series 2004 Bonds initially will be issued solely in book-entry form to be held in the book-entry-only system maintained by The Depository Trust Company ("DTC"), New York, New York. So long as such book-entry-only system is used, only DTC will receive or have the right to receive physical delivery of Bonds and, except as otherwise provided herein with respect to tenders by beneficial owners of beneficial ownership interests, beneficial owners will not be or be considered to be, and will not have any rights as, owners or holders of the Series 2004 Bonds under the Trust Indenture. For additional information about DTC and the book-entry-only system see "Appendix D – Book-Entry-Only System."

Redemption Provisions

The Series 2004 Bonds are not subject to redemption prior to maturity.

SOURCES AND USES OF FUNDS

The following table sets forth the application of the proceeds of the Series 2004 Bonds:

SOURCES OF FUNDS:	
Par Amount of Bonds	\$21,670,000.00
Net Original Issue Premium	1,681,788.55
Prior Bonds Debt Service and Debt Service Reserve Funds	<u>9,554,583.23</u>
TOTAL SOURCES	\$32,906,371.78
USES OF FUNDS:	
Deposit to Prior Bond Fund	\$30,239,860.00
Deposit to Debt Service Reserve	2,335,178.86
Costs of Issuance ¹	<u>331,332.92</u>
TOTAL USES	\$32,906,371.78

¹Includes bond insurance premium and Underwriters' Discount.

SECURITY FOR THE SERIES 2004 BONDS

The Series 2004 Bonds are special and limited obligations of the Authority, secured by and payable from the specific revenues, funds and properties pledged, therefor as described herein. The Series 2004 Bonds do not constitute a debt of the Commonwealth or any political subdivision thereof. The payment of the principal of and interest on the Series 2004 Bonds is not secured by a pledge of the faith and credit or the taxing power of the Commonwealth or any political subdivision thereof. The Authority has no taxing power.

The Series 2004 Bonds are special and limited obligations of the Authority and except to the extent payable from the proceeds of such Series 2004 Bonds or other monies pledged therefor under the Trust Indenture, the Series 2004 Bonds will be payable from the Pledged Receipts as described below.

THE ONLY SECURITY WHICH IS PLEDGED FOR THE SERIES 2004 BONDS IS THE INDEPENDENT REVENUES AND ASSETS DESCRIBED UNDER THIS HEADING. THE GENERAL ASSEMBLY DOES NOT INTEND TO APPROPRIATE ANY STATE FUNDS TO FULFILL THE FINANCIAL OBLIGATIONS REPRESENTED BY THE SERIES 2004 BONDS.

Bond Insurance Policy

The scheduled payment of the principal of and interest on the Series 2004 Bonds, when due, will be guaranteed under a financial guaranty insurance policy to be issued concurrently with the delivery of the Series 2004 Bonds by MBIA Insurance Corporation. (See "BOND INSURANCE" herein and APPENDIX F).

Pledged Receipts-Court Costs

Pledged Receipts include all monies collected and deposited in the State Treasury for the benefit of the Authority as Court Costs pursuant to KRS 24A.175(1), 24A.180(5) and KRS 42.320(2)(b).

The Court Costs received by the Authority are derived from certain criminal cases, excluding parking violations, adjudicated by the district courts of the Commonwealth resulting in a finding or admission of guilt whereby the offenders, pursuant to KRS 24A.175(1), are assessed court costs of \$100 per case. Those court costs are assessed automatically upon a conviction and are not subject to the

discretion of the court. Of the total court costs collected, 10.8%, up to a maximum annual amount of \$5,400,000, is allocated to the Authority pursuant to KRS 42.320(2)(b). These funds are collected from offenders by the circuit court clerk in the county in which the district court presides. By the seventh working day of each month, the circuit court clerk remits court costs collected to the Treasurer of the Commonwealth, pursuant to KRS 24A.180(5). The Governor's Office for Local Development verifies the amount of those funds. The Finance and Administration Cabinet then transfers the aggregate amount of Court Costs for deposit with the Trustee by the end of each month.

The amounts of Court Costs received by the Authority is established by the Kentucky General Assembly, and therefor such amounts cannot be increased by the Authority without legislative approval. Moreover, the Authority cannot unilaterally prevent a decrease in such amounts if such decrease is adopted by the Kentucky General Assembly, though the Authority has covenanted to oppose, by appropriate legal action, any future legislation introduced in the Kentucky General Assembly designed to repeal, reduce or redirect the Court Costs allocated for the use and benefit of the Authority by KRS 24A.175(1), 24A.180(5) and KRS 42.320(2)(b). See APPENDIX C - "SUMMARY OF BOND DOCUMENTS -- Trust Indenture."

The pledge of Court Costs hereunder being a contractual obligation of the Authority for the benefit of the Bondholders, the Authority covenants to oppose, including, to the extent necessary, by appropriate legal action, the adoption or enforcement of any statute or regulation that would reduce the amount of aggregate annual Court Costs payable to the Authority as an impairment of such contractual obligation, if such reduction would cause the total amount of Court Costs, Rental Payments and Supplemental Rental Payments, based on reasonable projections, to be less than the Principal Installments and interest on the Bonds which are due and payable in any future fiscal year.

The annual amounts of Court Costs received by the Authority during the fiscal years from July 1, 1999 through June 30, 2004 is as follows:

Fiscal Year	Amount
2000	\$5,601,476.06
2001	5,007,727.41
2002	4,802,149.75
2003	4,848,282.46
2004	5,280,959.36

Pledged Receipts - Rental Payments Under Leases

Pledged Receipts also include the Rental Payments received by the Authority from Local Governments under the Leases in repayment of and as interest on each Local Government's Lease and Participation Agreement with respect to Projects funded or partially funded by the Authority bonds issued in 1984 and 1987 that were refunded by the Prior Bonds. The term of each Lease on a Project is one year, subject to automatic annual renewals unless a Local Government fails to exercise its option to renew. Thereafter, the Leases automatically are renewed and will continue to automatically renew on July 1 of each year for a period of one year unless the Local Government gives notice to the Authority, the Finance and Administration Cabinet and the Department of Corrections in writing not less than 60 days prior to the expiration date of the Lease of its intention not to renew. Each Lease on a Project contains a statement by the Local Government that it presently intends to renew the Lease from year to year until Bonds related to its Project are retired, however, such statement of intent cannot be construed as a present election to renew the Lease.

The participation of each Local Government in the financing plan represented by the Project Bonds and the execution by a Local Government of a Lease is subject to the approval of the State Local Debt Officer of Kentucky in accordance with the KRS 66.310, which requires that in each instance the

State Local Debt Officer render a decision indicating that the projected obligations of the Local Government under the Lease are within the anticipated revenue of the Local Government available for such purpose.

In the event a Local Government should elect not to renew its Lease, all of its rights in the Project shall be terminated, including the right to have the Project reconveyed to the Local Government upon retirement of the Bonds related to its Project. Upon a Local Government's failure to exercise its option to renew, all Rental Payments then due and unpaid for the then current Lease year shall become immediately due and payable and the Local Government is required to give immediate possession of its Project to the Authority.

Under each Lease, the Local Government has agreed that in any year the Lease remains in effect and the Local Government fails to pay the required Rental Payments, the Authority is entitled to notify the State Treasurer and/or the Department of Corrections and to request there be withheld from the delinquent lessee Local Government a sufficient portion of any undisbursed funds then held, set aside or allocated for jail purposes from State appropriations for that Local Government. This collection device, which is available only during any year in which the Lease is in effect, terminates should any Local Government elect not to renew its Lease.

In addition to such conditional assignment of each Local Government's rights with regard to State appropriations for their jail purposes, Rental Payments due under the Leases constitute general obligations of each Local Government but only to the extent of the Rental Payments due for the annual Lease term then in effect.

Pledged Receipts – Lease Amounts

The Authority has entered into Leases with Local Governments that terminate on October 1, 2014. The average annual Rental Payments payable to the Authority and the outstanding principal component of those Leases are as follows:

<u>Local Government</u>	<u>Average Annual Rental Payment</u>	<u>Outstanding Principal Component</u>
Adair County	\$33,681.09	\$243,950.10
Estill County	14,284.48	103,461.60
Franklin County	140,663.57	1,018,821.40
Fulton County	25,308.95	180,600.50
Knox County	38,148.75	276,310.10
McCreary County	23,175.59	163,264.90
Montgomery County	66,547.44	482,000.90
Powell County	19,167.67	135,202.70
Simpson County	<u>28,295.11</u>	<u>203,156.50</u>
Total:	\$389,272.65	\$2,806,768.70

Other Pledged Receipts

Pledged Receipts also include all interest earned and gains realized on Investment Obligations acquired with monies on deposit under the Trust Indenture other than the Payment, Surplus and Operating Fund. Interest and gains derived from investment of monies or the Leases and the Revenue Bond Account will become Pledged Receipts.

Pledged Receipts include any gifts or grants received from any agency of government both federal and State, to the extent not required to be otherwise applied, as well as any and all appropriations made to the Authority by the General Assembly of the Commonwealth to the extent not otherwise

committed during any fiscal period of the Authority. To date, the Authority has received no such gifts, grants or appropriations constituting Pledged Receipts.

Transfer of Surplus Funds

The Trust Indenture provides that moneys in the Payment, Surplus and Operating Fund may be withdrawn and paid out by the Trustee to or at the direction of the Authority for any lawful purpose of the Authority. In addition to lawful purposes of the Authority currently set forth in the Act, the Act may be amended or the General Assembly may expand the lawful purposes of the Authority in future budget acts. In the budget act for the period from July 1, 2002 to June 30, 2004, a provision was included that stated "funds in the amount of \$15,000,000 shall be expended from the Kentucky Local Correctional Facilities Construction Authority for local correctional facility and operational support." Those funds were withdrawn from the Payment, Surplus and Operating Fund in May of 2003. The combined balance in the Revenue Fund and the Payment, Surplus and Operating Fund on September 1, 2004 was \$3,381,397. The General Assembly has not yet adopted a budget for the period from July 1, 2004 to June 30, 2006. Neither the executive order under which governmental expenditures are currently authorized, nor any budget proposed for the current biennium that is being considered by the General Assembly, authorizes additional withdrawals from the Payment, Surplus and Operating Fund.

Title to Leased Projects and Terms of Leases

Title to each Project which is subject to a Lease between the Authority and a Local Government is vested in the Authority. Under the Trust Indenture, the Authority grants the Trustee an assignment of the Leases.

Under the terms of the Leases, each of the Local Governments has agreed that if it should fail to make any Rental Payments during any then current one year Lease term, the Authority may notify the State Treasurer and/or the Department of Corrections and request there be withheld from State appropriations for the delinquent Local Government lessee a sufficient portion of any undisbursed funds then held, set aside or allocated for such Local Government for jail purposes. Any such withheld amounts would be paid directly to the Authority from the State Treasurer or Department of Corrections, as the case may be. Local Governments have agreed that such direct collections may only be in the amount of any such deficiency; and any amounts so collected by the Authority are required to be immediately remitted to the Trustee to be deposited in the Debt Service Fund for the benefit of the Bondholders. This direct collection device is available only during any year in which the Lease is in effect and terminates should any Local Government elect not to renew its Lease. Notwithstanding the Local Governments' agreement to permit such direct collections, no representation or assurance can be made that the future revenues of each Local Government will be sufficient to meet all of its obligations under its Lease.

The Leases will expire on June 30, 2005, but will be subject to automatic renewals for each ensuing one year period, unless a Local Government elects not to renew and notifies the Authority of such election, in writing, at least 60 days prior to the expiration date of its Lease. Each Lease contains a statement by the Local Government that it presently intends to renew the Lease from year to year until the Bonds attributable thereto have been paid, satisfied and discharged; however, such statement of present intent cannot be construed as a present election to so renew. A Local Government's obligations under a Lease, including the obligation to make Rental Payments, are subject to and dependent upon the Local Government's annual appropriations. In the event a Local Government elects not to renew its Lease, all of its rights in the Project shall be terminated, including the Local Government's right to receive reconveyance of the Project after all Rental Payments have been made. Although a Local Government with a Participation in the Bonds has conveyed title to its Project to the Authority, the Bondholders will not have a security interest in the Project. If a Local Government should default under or fail to renew its Lease, the Bondholders will have no rights in the Project, nor will they have the right to require that such Local Government appropriate any monies for the payment of the Rental Payments.

Upon such a default under or a failure to renew a Lease, the Authority will be entitled to take possession of the Project and may make the facility available for federal, State or county prisoners on a per diem basis. However, there can be no assurance given that the Authority will follow this course of action, nor can there be any assurance that the per diem charges in such circumstances would be equal to the Rental Payments which would have been paid under the Lease.

Debt Service Reserve

Pursuant to the terms of the Trust Indenture and the Series 2004 Resolution, the Authority is required to maintain a Debt Service Reserve in an amount equal to the least of (i) 10% of the stated aggregate principal amount of the Outstanding Bonds, (ii) the maximum Annual Debt Service Requirement in the current or any succeeding Bond Fiscal Year with respect to all Outstanding Bonds and (iii) 125% of the average Annual Debt Service Requirement with respect to all Outstanding Bonds (the "Aggregate Debt Service Reserve Requirement"). In any year in which the Court Costs, Rental Payments (including Supplemental Rental Payments) and Investment Earnings are not sufficient to meet principal and interest requirements on the Bonds, the Trust Indenture requires that a sufficient portion of the Debt Service Reserve be transferred to the Debt Service Fund in order to meet such requirements. Pursuant to the Series 2004 Resolution, upon delivery of the Series 2004 Bonds the amount on deposit in the Debt Service Reserve will equal the Aggregate Debt Service Reserve Requirement.

Additional Parity Bonds

The Trust Indenture provides that the Authority will not issue additional bonds ranking on a basis of parity as to security and sources of payment with the Series 2004 Bonds unless and until the following requirements are met:

(i) To the extent required by the applicable Series Resolution, there is on deposit in the Debt Service Reserve an amount equal to the Aggregate Debt Service Reserve Requirement; and

(ii) except in the case of an issue of Refunding Bonds, a certificate of an Authorized Officer of the Authority is delivered to the Trustee stating, in effect, that annual Court Costs receipts plus annual Rental Payments from all Leases made and to be made with Local Governments shall be projected to be at least equal to 1.20 times the maximum Annual Debt Service Requirement of the Outstanding Bonds and the Series of Bonds then proposed to be issued. In the event that the additional Series of Bonds proposed to be issued are to bear a variable or periodically adjustable interest rate, the calculations of maximum Annual Debt Service Requirement shall be made with the assumption that the interest rate on the Bonds is the 30-year Revenue Bond Index as published in The Bond Buyer as of the week preceding the week in which the interest rate on such additional Series of Bonds is to be determined (or similar index if same is no longer published).

One or more Series of Refunding Bonds may be authenticated and delivered upon original issuance to refund all Outstanding Bonds or any Series of Outstanding Bonds or any part of one or more Series of Outstanding Bonds without compliance with (ii) above, so long as the maximum Annual Debt Service Requirement, assuming issuance of such Refunding Bonds, is no greater than the maximum Annual Debt Service Requirement prior to such issuance.

BOND INSURANCE

The following information has been furnished by MBIA Insurance Corporation for use in this Official Statement. Reference is made to APPENDIX F for a specimen of the Bond Insurer's policy.

The Bond Insurance Policy

The Bond Insurer's policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the Authority to the Trustee and Paying Agent or its successor of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Series 2004 Bonds as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the Bond Insurer's policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner of the Series 2004 Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law (a "Preference").

The Bond Insurer's policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Series 2004 Bonds. The Bond Insurer's policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be made on an accelerated basis; (iii) payments of the purchase price of Series 2004 Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. The Bond Insurer's policy also does not insure against nonpayment of principal of or interest on the Series 2004 Bonds resulting from the insolvency, negligence or any other act or omission of the Paying Agent or any other paying agent for the Series 2004 Bonds.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Bond Insurer from the Paying Agent or any owner of a Series 2004 Bond the payment of an insured amount for which is then due, that such required payment has not been made, the Bond Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such Series 2004 Bonds or presentment of such other proof of ownership of the Series 2004 Bonds, together with any appropriate instruments of assignment to evidence the assignment of the insured amounts due on the Series 2004 Bonds as are paid by the Bond Insurer, and appropriate instruments to effect the appointment of the Bond Insurer as agent for such owners of the Series 2004 Bonds in any legal proceeding related to payment of insured amounts on the Series 2004 Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Paying Agent payment of the insured amounts due on such Series 2004 Bonds, less any amount held by the Paying Agent for the payment of such insured amounts and legally available therefore.

The Bond Insurer

The Bond Insurer is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the "Company"). The Company is not obligated to pay the debts of or claims against the Bond Insurer. The Bond Insurer is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. The Bond Insurer has three branches, one in the Republic of France, one in the Republic of Singapore and one in the Kingdom of Spain. New York has laws prescribing minimum capital requirements, limiting classes and concentrations of investments and requiring the approval of policy rates and forms. State laws also regulate the amount of both the

aggregate and individual risks that may be insured, the payment of dividends by the Bond Insurer, changes in control and transactions among affiliates. Additionally, the Bond Insurer is required to maintain contingency reserves on its liabilities in certain amounts and for certain periods of time.

The Bond Insurer does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding the policy and the Bond Insurer set forth under the heading "BOND INSURANCE" and "APPENDIX F - FORM OF FINANCIAL GUARANTY INSURANCE POLICY." Additionally, the Bond Insurer makes no representation regarding the Series 2004 Bonds or the advisability of investing in the Series 2004 Bonds.

The Financial Guarantee Insurance Policies are not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

Information Regarding the Bond Insurer

The following documents filed by the Company with the Securities and Exchange Commission (the "SEC") are incorporated herein by reference:

- (1) The Company's Annual Report on Form 10-K for the year ended December 31, 2003; and
- (2) The Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004.

Any documents filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act of 1934, as amended, after the date of this Official Statement and prior to the termination of the offering of the Series 2004 Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2003, and (2) the Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 2004 and June 30, 2004) are available (i) over the Internet at the SEC's web site at <http://www.sec.gov>; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at <http://www.mbia.com>; and (iv) at no cost, upon request to MBIA Insurance Corporation, 113 King Street, Armonk, New York 10504. The telephone number of MBIA is (914) 273-4545.

As of December 31, 2003, the Bond Insurer had admitted assets of \$9.9 billion (audited), total liabilities of \$6.2 billion (audited), and total capital and surplus of \$3.7 billion (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of June 30, 2004 the Bond Insurer had admitted assets of \$10.5 billion (unaudited), total liabilities of \$6.7 billion (unaudited), and total capital and surplus of \$3.8 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

Financial Strength Ratings of the Bond Insurer

Moody's Investors Service, Inc. rates the financial strength of the Bond Insurer "Aaa."

Standard & Poor's, a Division of The McGraw-Hill Companies, Inc. rates the financial strength of the Bond Insurer "AAA."

Fitch Ratings rates the financial strength of the Bond Insurer "AAA."

Each rating of the Bond Insurer should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of the Bond Insurer and its ability to pay claims on its policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Series 2004 Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Series 2004 Bonds. The Bond Insurer does not guaranty the market price of the Series 2004 Bonds nor does it guaranty that the ratings on the Series 2004 Bonds will not be revised or withdrawn.

THE AUTHORITY

The Authority is a body corporate and public and an agency and instrumentality of the Commonwealth created and existing under the Act. The general purpose of the Authority is to provide an additional and alternative method of constructing, reconstructing, improving or repairing and financing jails, correctional facilities and appurtenant facilities for any county or urban county in the Commonwealth.

The activities of the Authority are related to the Department of Corrections, a department of the Justice and Public Safety Cabinet, that exercises all functions of the Commonwealth in relation to management of penal, reform, and correctional institutions; supervision of probation and parole; the giving of assistance to other departments, agencies and institutions of the state and federal government and the administration, enforcement and development of jail standards, training of jailers and jail personnel, and jail planning and construction.

Authority Membership

The Act provides that the powers of the Authority are exercised by ten members who, serve without compensation but are entitled to reimbursement for all reasonable expenses necessary and proper to the performance of their duties and functions as members of the Authority.

The Authority is composed of the Secretary of the Finance and Administration Cabinet of the Commonwealth (who is Chairman of the Authority), the President of the Kentucky Jailers Association, the President of the Kentucky County Judge/Executives Association, the President of the Kentucky Association of Counties, the President of the Kentucky Magistrates and Commissioners Association, two citizen members appointed by the Governor and two members of the General Assembly appointed by the Governor. Each of the ex officio members serves for the term of their respective office. Citizen members are appointed for a term of four years. The legislative members serve at the pleasure of the Governor. Any six members of the Authority shall constitute a quorum. The Office of Financial Management of the Finance and Administration Cabinet serves as the staff for the Authority,

The present members and officers of the Authority and their offices, terms of office and affiliations are as follows:

<u>Name</u>	<u>Term Expires</u>	<u>Affiliation</u>
R. B. Rudolph, Jr., Chairman	Ex-officio	Secretary, Finance and Administration Cabinet
Hon. Adrian Arnold, Vice Chairman	August 1, 2007	Representative, General Assembly
John D. Rees, Secretary	Ex-officio	Commissioner, Department of Corrections
Hon. Jim Townsend	Ex-officio	President, Kentucky Association of Counties
Hon. Tommy Turner	Ex-officio	President, Kentucky County Judge/Executives Association
Hon. James Kemper	Ex-officio	President, Kentucky Jailer's Association
Hon. Hugh McCormick	Ex-officio	President, Kentucky Magistrates and Commissioners Association
Christy Lynn Campbell	August 1, 2007	Citizen Member
Vacant		Citizen Member
Vacant		Senator, General Assembly

Powers of the Authority

Under the terms of the Act, the Authority has, among other powers, the power: (i) to construct, reconstruct, improve or repair any jail and appurtenant facilities in any Local Government in the State; (ii) to acquire and to convey real estate and any improvements, buildings and facilities located thereon, for which a Project is undertaken, and in such manner and under such terms as may be provided by agreement; (iii) to issue revenue bonds and revenue bond anticipation notes payable solely from the revenues, rentals and other funds pledged for their payment, for the purpose of paying any part of the cost of any one or more Projects, and to refund any of its bonds; (iv) to combine for financing purposes any two or more Projects; (v) to lease as lessor any Project to any Local Government as lessee, pursuant to the terms and provisions of a Lease; (vi) to employ consulting engineers, attorneys, accountants, construction and financial experts, managers and other employees and agents as may be necessary in the judgment of the Authority, and to fix their compensation; (vii) to make and enter into such contracts and agreements with other parties as may be necessary and incidental to the performance of its duties and execution of its powers under the Act; (viii) to establish and enforce rules, regulations and specifications in respect to any Project undertaken by the Authority, except during any period when such powers are assigned to a lessee pursuant to a Lease, provided that such rules, regulations and specifications shall be consistent with State laws and regulations pertaining to jails; (ix) to receive, accept and expend funds or other contributions from any source, both public and private, for or in aid of any Project undertaken by the Authority; (x) to make grants to Local Governments from funds determined by it to be available to it for such purposes, upon such terms and according to such criteria as the Authority shall in its discretion determine; and (xi) to do all things and perform all acts desirable, necessary and proper to carry out and implement the powers expressly granted to it by the Act.

Regional and Local Facilities Bond Programs

The Department of Corrections of the Commonwealth was established by Executive Order 92-511 and KRS Chapter 195. The Department of Corrections is directed by a Commissioner. Programs within the Department of Corrections include corrections management, adult institutions and community services.

By Executive Order 81-1026, a Jail Standards Commission, composed of representatives of State and local governments, special interest groups, all segments of the criminal justice system and private citizens, was created to develop minimum jail standards. The standards developed include health and safety conditions, fire safety and custody, care and treatment of prisoners (the "Kentucky Jail Standards").

Pursuant to KRS 441.055 through 441.095, the Department of Corrections is responsible for enforcement of the Kentucky Jail Standards, which the Department of Corrections has now promulgated into administrative regulations, Title 501, Chapter 3 of the Kentucky Administrative Regulations. The Department of Corrections employs personnel to inspect jails twice a year. If, as a result of such inspections, the Department of Corrections finds a violation of the Kentucky Jail Standards, the Commissioner of Corrections may order the jail or portions thereof to be vacated and closed until the violation is corrected.

Since the responsibility for the operation of jail facilities lies with the counties, the Department of Corrections recognizes that the maintenance of separate county jails complying with the Kentucky Jail Standards imposes a significant financial burden on the counties. In light of that reality, the Department of Corrections has endorsed the concept of regional jails and assisted in the determination of priorities for the Authority's bond program.

Under the Act, the Authority is charged with the responsibility of providing an additional and alternate method of constructing, reconstructing, improving or repairing and financing county jails. As a result of this mandate and the Kentucky Jail Standards, the Authority has recognized that an adequate statewide system of county jails would require the construction or renovation of full service and holdover jail facilities whether on a single county or regional basis. Consequently, the Authority has established its Regional and Local Facilities Bond Program. All counties in the Commonwealth are eligible to make an application to participate and receive funding from the Authority's Bond Program.

Investment Policy

All Authority funds are invested in accordance with the requirements of the Trust Indenture. See APPENDIX C.

TAX MATTERS

General

In the opinion of Kutak Rock LLP, Bond Counsel, to be delivered at the time of original issuance of the Series 2004 Bonds, under existing laws, regulations, rulings and judicial decisions, interest on the Series 2004 Bonds (a) is excluded from gross income for federal income tax purposes and (b) is not a specific item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the Series 2004 Bonds, however, will be included in the "adjusted current earnings" (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Internal Revenue Code of 1986, as amended (the "Code")) of certain corporations and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings over its alternative

minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The Authority has covenanted to comply with all requirements that must be satisfied in order for the interest on the Series 2004 Bonds to be excludible from gross income for federal tax purposes. The opinions set forth above are subject to continuing compliance by the Authority and others with such covenants. Failure to comply with such covenants could cause interest on the Series 2004 Bonds to be included in gross income retroactive to the date of issue of the Series 2004 Bonds.

The accrual or receipt of interest on the Series 2004 Bonds may otherwise affect the federal income tax liability of certain recipients such as banks, thrift institutions, property and casualty insurance companies, corporations (including S corporations and foreign corporations operating branches in the United States), Social Security or Railroad Retirement benefit recipients, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, among others. The extent of these other tax consequences will depend upon the recipients' particular tax status or other items of income or deduction. Bond Counsel expresses no opinion regarding any such consequences and investors should consult their own tax advisors regarding the tax consequences of purchasing or holding the Series 2004 Bonds.

In Bond Counsel's further opinion, under the existing laws of the Commonwealth, interest on the Series 2004 Bonds is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Series 2004 Bonds are exempt from ad valorem taxes by the Commonwealth and all political subdivisions thereof.

Future Legislation or Regulation

From time to time, there are legislative proposals in Congress that, if enacted, could alter or amend the federal tax matters referred to above or adversely affect the market value of the Series 2004 Bonds. It cannot be predicted whether or in what form any such proposal might be enacted or whether if enacted, it would apply to Series 2004 Bonds issued prior to enactment. Each purchaser of the Series 2004 Bonds should consult his or her own tax advisor regarding any pending or proposed federal tax legislation. Bond Counsel expresses no opinion regarding any pending or proposed federal tax legislation.

Tax Treatment of Bond Premium

The Series 2004 Bonds that have an original yield below their interest rate, as shown on the cover, are being sold at a premium (collectively, the "Premium Obligations"). An amount equal to the excess of the issue price of a Premium Obligation over its stated redemption price at maturity constitutes premium on such Premium Obligation. An initial purchaser of such Premium Obligation must amortize any premium over such Premium Obligation's term using constant yield principles, based on the purchaser's yield to maturity (or, in the case of Premium Obligations callable prior to their maturity, by amortizing the premium to the call date, based upon the purchaser's yield to the call date and giving effect to any call premium). As premium is amortized, it offsets the interest allocable to the corresponding payment period and the purchaser's basis in such Premium Obligation is reduced by a corresponding amount resulting in an increase in the gain (or decrease in the loss) to be recognized for federal income tax purposes upon a sale or disposition of such Premium Obligation prior to its maturity. Even though the purchaser's basis may be reduced, no federal income tax deduction is allowed. The same treatment is afforded to Series 2004 Bonds purchased at a premium in the secondary market. Purchasers of Premium Obligations should consult with their own tax advisors with respect to the determination and treatment of amortizable premium for federal income tax purposes and with respect to the state and local tax consequences of owning a Discounted Obligation.

APPROVAL OF LEGAL PROCEEDINGS

Legal matters incident to the authorization and issuance of the Series 2004 Bonds are subject to the approving legal opinion of Kutak Rock LLP, Omaha, Nebraska, Bond Counsel, who has been retained by, and acts as Bond Counsel, to the Authority. The form of the approving legal opinion of Bond Counsel is attached hereto as Appendix E. Certain legal matters will be passed upon for the Underwriter by its counsel, Peck, Shaffer & Williams LLP, Covington, Kentucky.

LITIGATION

There is no controversy or litigation of any nature now pending or, to the knowledge of the Authority, threatened, restraining or enjoining the issuance, sale, execution or delivery of the Series 2004 Bonds or in any way contesting or affecting the validity of such Series 2004 Bonds, or any proceedings of the Authority taken with respect to the issuance or sale thereof, or the pledge or application of any monies or security provided for the payment of such Series 2004 Bonds, or the due existence or powers of the Authority.

CONTINUING DISCLOSURE

In order to assist the Underwriters in complying with Securities and Exchange Commission Rule 15c2-12 (the "Rule"), the Authority has entered into a Continuing Disclosure Agreement dated as of October 1, 2004 with the Trustee (the "Agreement"). The Agreement constitutes an undertaking for the benefit of the beneficial owners of the Series 2004 Bonds and requires the Authority to provide to each NRMSIR (defined below) and to the state information depository ("SID"), if any, (i) annual financial information with respect to the Series 2004 Bonds, including annual debt service payments with respect to the Series 2004 Bonds, annual Rental Payments made by the Local Governments that have entered into Lease and Participation Agreements with the Authority and the Authority's audited financial statements, by no later than nine months after the end of each fiscal year of the Authority, and (ii) notice of the occurrence of any "material event" identified in the Rule (e.g., any principal and interest payment delinquency and other material events), in a timely manner.

Additionally, the Agreement requires the Authority to notify any Local Government that provides 10% or more of the annual debt service payments with respect to the Bonds that compliance by such Local Government with the requirements of the Rule is required, including providing the following information to each NRMSIR and SID, if any: (i) annual financial information or operating data with respect to such Local Government, for each fiscal year of the Local Government, by no later than nine months after the end of such fiscal year, (ii) annual financial statements, if any, of the Local Government, audited by such auditor as shall then be required or permitted by state law, no later than 15 business days after the final publication date of such audited financial statements and (iii) notice of the occurrence of any "material event" identified in the Rule (e.g., any principal and interest payment delinquency and other material events) with respect to the Local Government, in a timely manner. The Lease and Participation Agreements entered into between the Authority and each Local Government reiterate the continuing disclosure obligations of the Local Governments. At present, no Local Government provides 10% or more of the annual debt service payments with respect to the Bonds.

"NRMSIR" means, at any time, a then existing nationally recognized municipal securities information repository, as recognized from time to time by the SEC for the purposes referred to in the Rule. The NRMSIRs as of the date of this Official Statement are:

- (i) Bloomberg Municipal Repository
100 Business Park Drive
Skillman, New Jersey 08558
Tel: (609) 279-3225
Fax: (609) 279-5962
Website: <http://www.bloomberg.com/markets/rates/municontacts.html>
E-mail: munis@bloomberg.com

- (ii) DPC Data Inc.
One Executive Drive
Fort Lee, New Jersey 07024
Tel: (201) 346-0701
Fax: (201) 947-0107
Website: <http://www.dpcdata.com>
E-mail: nrmsir@dpcdata.com

- (iii) FT Interactive Data
Attn: NRMSIR
100 William Street
New York, New York 10038
Tel: (212) 771 -6999
Fax: (212) 771-7390 (Secondary Market Information)
(212) 771-7391 (Primary Market Information)
Website: <http://www.interactivedata.com>
E-mail: nrmsir@ftid.com

- (iv) Standard & Poor's Securities Evaluations, Inc.
55 Water Street, 45th Floor
New York, New York 10041
Tel: (212) 438-4595
Fax: (212) 438-3975
Website: www.jjkenny.com/jjkenny/pser_descrip_data_rep.html
E-mail: nrmsir.repository@sandp.com

As of the date of this Official Statement, no SID has been established in the Commonwealth. Copies of the Agreement and the Kentucky Comprehensive Annual Financial Report can be obtained from the Authority, c/o Office of Financial Management, 702 Capitol Avenue, Suite 261, Frankfort, Kentucky 40601, (502) 564-2924.

The Authority has not failed in any material way to comply with any previous undertaking to provide disclosure information pursuant to Rule 15c2-12.

RATINGS

Moody's Investors Service, Inc. ("Moody's") and Standard & Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc. ("S&P") have given the Series 2004 Bonds the ratings of "Aaa" and "AAA," respectively, with the understanding that upon delivery of the Series 2004 Bonds, the Bond Insurance Policy will be issued by the MBIA Insurance Corporation.

Such ratings reflect only the views of the respective rating agencies. An explanation of the significance of the ratings given by Moody's may be obtained from Moody's Investors Service, Inc. at 99 Church Street, New York, New York 10007, (212) 553-0300 and an explanation of the ratings given by S&P may be obtained from Standard & Poor's Ratings Services at 55 Water Street, New York, New York 10041, (212) 438-2124. There is no assurance that ratings will continue for any given period of time or that ratings will not be revised downward or withdrawn entirely if, in the judgment of the Rating Service, circumstances so warrant. Any such downward revision or withdrawal of the ratings may have an adverse effect on the market price of the Series 2004 Bonds.

UNDERWRITING

The Series 2004 Bonds are to be purchased by a syndicate managed by Morgan Stanley & Co. Incorporated as representative of the managing underwriters identified on the cover hereof and on behalf of itself (the managers and any other syndicate members collectively, the "Underwriters"). The Underwriters have agreed, subject to certain conditions, to purchase the Series 2004 Bonds at an aggregate purchase price of \$23,240,818.80 (which is equal to the principal amount of the Bonds plus net original issue premium of \$1,681,788.55 and less underwriting discount of \$110,969.75). The Underwriters will be obligated to purchase all of the Series 2004 Bonds if any are purchased. The Underwriters have advised the Authority that they intend to make a public offering of the Series 2004 Bonds at the yields set forth on the cover page hereof.

The Underwriters may offer and sell the Series 2004 Bonds to certain dealers (including dealers depositing such Series 2004 Bonds into investment trusts) and others at prices lower than the initial public offering prices stated on the cover page hereof. The initial public offering prices may be changed from time to time by the Underwriters.

APPROVAL OF ISSUANCE OF SERIES 2004 BONDS

Issuance of the Series 2004 Bonds by the Authority and the terms thereof have been approved by the Office of Financial Management of the Finance and Administration Cabinet of the Commonwealth, the State Property and Buildings Commission of the Commonwealth and the Capital Projects and Bond Oversight Committee of the General Assembly.

Pursuant to the KRS 65.944(b), the State Local Debt Officer of the Commonwealth has approved the obligations of the Local Governments evidenced by the Leases.

MISCELLANEOUS

All references to the Trust Indenture, Series 2004 Resolution, Leases and other documents mentioned herein and in the accompanying Appendices, including any summaries thereof, are qualified in their entirety by reference to such documents. Neither this Official Statement nor any statement which may have been made verbally or in writing is to be construed as a contract with the holders of the Series 2004 Bonds.

The information in the foregoing pages is presented for the guidance of prospective purchasers of the Series 2004 Bonds described therein. The information has been compiled from official and other sources and, while not guaranteed by the Authority, is believed to be correct. So far as any statements made in this Official Statement and the Appendices attached hereto involve matters of opinion or estimates, whether or not so expressly stated, they are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized.

The attached Appendices are integral parts of the Official Statement and must be read in their entirety together with all of the foregoing information.

The Authority has duly authorized the execution and delivery of this Official Statement by its Chairman.

**KENTUCKY LOCAL CORRECTIONAL
FACILITIES CONSTRUCTION AUTHORITY**

By: R. B. Rudolph, Jr.
Chairman

Attest:

By: Melissa Johnson
Treasurer

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APPENDIX A
FINANCIAL STATEMENTS OF THE AUTHORITY

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**KENTUCKY LOCAL CORRECTIONAL
FACILITIES CONSTRUCTION AUTHORITY
FRANKFORT, KENTUCKY**

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORT**

June 30, 2004 and 2003



**KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
FRANKFORT, KENTUCKY**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Kentucky Local Correctional
Facilities Construction Authority
Frankfort, Kentucky

We have audited the accompanying financial statements of the Kentucky Local Correctional Facilities Construction Authority (the Authority), a component unit of the Commonwealth of Kentucky, as of and for the years ended June 30, 2004 and 2003, as listed in the table of contents. These financial statements are the responsibility of the Authority'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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Kentucky Local Correctional Facilities Construction Authority as of June 30, 2004 and 2003, and the changes in its financial position and its cash flows 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 financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 24, 2004 on our consideration of the Kentucky Local Correctional Facilities Construction Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Moore Stephens Potter, LLP

MOORE STEPHENS POTTER, LLP
August 24, 2004

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Kentucky Local Correctional Facilities Construction Authority (the Authority), a component unit of the Commonwealth of Kentucky, we offer the readers of the Authority's financial statements this narrative overview and analysis of the financial performance of the Authority for the fiscal years ended June 30, 2004 and 2003. We encourage readers to read it in conjunction with the Authority's financial statements and the accompanying notes.

FINANCIAL HIGHLIGHTS

- Cash and cash equivalents increased \$916,295 (16.5%)
- Lease agreement receivables (net of premium on leases) decreased \$312,952 (5.2%)
- Revenue bonds payable and other liabilities decreased \$2,019,648 (6.5%)
- The Authority's accumulated net deficit decreased \$2,613,560 (14.3%)
- Operating revenues increased \$406,858 (7.5%)
- Operating expenses decreased \$97,802 (3.0%)
- Income from operations increased \$504,660 (24.0%)
- Income from investments decreased \$79,050 (93.2%)

OVERVIEW OF THE FINANCIAL STATEMENTS

This financial report consists of three parts: Management's Discussion and Analysis (this section), the basic financial statements, and the accompanying notes to the financial statements. The Kentucky Local Correctional Facilities Construction Authority is a self-supporting entity and follows enterprise fund reporting; accordingly, the financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Enterprise fund statements offer short and long-term financial information about the activities and operations of the Authority. These statements are presented in a manner similar to those of a private business.

The statement of net assets presents information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The statement of revenues, expenses, and changes in net assets presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The statement of cash flows provides relevant information about the cash receipts and cash payments of the Authority during the fiscal year. The statement should help users assess the Authority's ability to generate future net cash flows, meet future obligations as they become due, the Authority's need for future external financing, the reasons for differences in operating and related cash receipts and cash payments, and the effects on financial position of cash and non-cash investing, capital, non-capital, and financing activities.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements can be found on pages 11-19.

FINANCIAL ANALYSIS OF THE AUTHORITY

Condensed Financial Information (in thousands)

Statement of Net Assets

As of June 30

	2004	Percentage Increase (Decrease)	2003	Percentage Increase (Decrease)	2002
Current assets	\$ 3,949	28.5%	\$ 3,073	-82.3%	\$ 17,338
Non-current assets	9,287	-2.9%	9,569	-3.8%	9,949
Total assets	<u>13,236</u>	4.7%	<u>12,642</u>	-53.7%	<u>27,287</u>
Current liabilities	2,291	-0.5%	2,303	5.1%	2,191
Non-current liabilities	26,662	-7.0%	28,670	-6.3%	30,587
Total liabilities	<u>28,953</u>	-6.5%	<u>30,973</u>	-5.5%	<u>32,778</u>
Accumulated net deficit	<u>\$ (15,717)</u>	-14.3%	<u>\$ (18,331)</u>	233.8%	<u>\$ (5,491)</u>

Current assets consist primarily of the operating and program cash and cash equivalents and the current portion of lease agreement receivables.

Non-current assets consist primarily of debt service reserve cash and cash equivalents and investments and the non-current portion of lease agreement receivables.

Current liabilities consist primarily of the current portion of the revenue bonds payable due annually on November 1.

Non-current liabilities represent the non-current portion of the revenue bonds payable.

In providing funds for the construction and improvement of correctional facilities, the Authority obtains its funding through the issuance of revenue bonds and the receipt of court costs remittances. When revenue bonds are issued, the Authority incurs long-term obligations that are repaid by revenue received from annual court costs receipts. When construction grants are awarded to local governments, the disbursements are immediately reflected as operating expenses. Due to the timing of these transactions, the Authority periodically incurs losses from operations. In addition, during 2003 House Bill No. 269 authorized the one-time non-reciprocal payment to the Commonwealth in the amount of \$15,000,000 (as discussed on page 5), which has been reported as a non-operating expense in the 2003 financial statements. As a result of these transactions, the Authority has accumulated a **net deficit** as of June 30, 2004.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

**Condensed Financial Information (in thousands)
Statement of Revenues, Expenses, and Changes in Net Assets
For the Fiscal Year Ended June 30**

	<u>2004</u>	Percentage Increase (Decrease)	<u>2003</u>	Percentage Increase (Decrease)	<u>2002</u>
Operating revenues:					
Court costs receipts	\$ 5,281	8.9%	\$ 4,848	1.0%	\$ 4,802
Interest income-leases	434	-5.7%	460	-5.0%	484
Other	96	0.0%	96	0.0%	96
Total operating revenues	<u>5,811</u>	7.5%	<u>5,404</u>	0.4%	<u>5,382</u>
Operating expenses:					
Construction grants	1,522	0.0%	1,522	0.0%	1,522
Interest expense	1,585	-5.5%	1,677	-4.9%	1,763
Other	96	-5.9%	102	9.7%	93
Total operating expenses	<u>3,203</u>	-3.0%	<u>3,301</u>	-2.3%	<u>3,378</u>
Income from operations	<u>2,608</u>	24.0%	<u>2,103</u>	4.9%	<u>2,004</u>
Non-operating revenues (expenses)	<u>6</u>	100.0%	<u>(14,943)</u>	-5436.8%	<u>280</u>
Change in net assets	2,614	120.4%	(12,840)	-662.2%	2,284
Accumulated net deficit, beginning of year	<u>(18,331)</u>	233.8%	<u>(5,491)</u>	-29.4%	<u>(7,775)</u>
Accumulated net deficit, end of year	<u><u>\$ (15,717)</u></u>	-14.3%	<u><u>\$ (18,331)</u></u>	233.8%	<u><u>\$ (5,491)</u></u>

Court costs receipts represent 10.8% or \$10.80 of each \$100.00 court cost, up to \$5,400,000 each fiscal year, taxed against a defendant upon conviction in each case tried in a state Circuit or District Court. The court costs are collected by all circuit clerks in Kentucky and are submitted on a monthly basis. Any receipts collected above the \$5,400,000 each fiscal year are paid into the Commonwealth's general fund.

Interest income-leases represents the portion of the rental payments received by the Authority under the leases from Local Governments in repayment of and as interest on a Local Government's agreed participation.

Other operating revenues consist of the amortization of the premium on leases.

Construction grants represent the annual installments of funding for construction and improvement of correctional facilities in ten counties throughout the state of Kentucky.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

Interest expense represents the interest due semi-annually each May 1 and November 1 on the revenue bonds payable.

Other operating expenses are primarily representative of the amounts due to the Office of Financial Management (OFM) to reimburse OFM for expenses incurred on behalf of the Authority and the amortization of the bond discount and the debt issuance costs.

Non-operating revenues (expenses) typically consist primarily of income from investments, which declined approximately \$79,000 (93.2%) from 2003 due to the significant reduction in the Authority's average deposits attributable to the \$15,000,000 non-reciprocal payment to the Commonwealth (included within non-operating expenses on the accompanying 2003 financial statements) during May 2003 (see below), as well as the continued general decline in interest rates during the fiscal year. Income from investments for the year ended June 30, 2003 declined approximately \$224,000 (72.5%) from 2002. Income from investments for the year ended June 30, 2002 declined approximately \$469,000 (60.3%) from 2001.

During its 2003 Regular Session the General Assembly of the Commonwealth of Kentucky passed House Bill No. 269 which contained a provision that, notwithstanding KRS 441.605 to 441.695 for fiscal year ended June 30, 2003, funds in the amount of \$15,000,000 shall be expended from the Kentucky Local Correctional Facilities Construction Authority for local correctional facility and operational support consistent with contractual covenants in accordance with bond indentures of the Authority. Accordingly, the statement of revenues, expenses, and changes in net assets for the year ended June 30, 2003 includes a non-reciprocal payment to the Commonwealth in the amount of \$15,000,000.

Condensed Financial Information (in thousands)

Statement of Cash Flows

For the Fiscal Year Ended June 30

	<u>2004</u>	Percentage Increase (Decrease)	<u>2003</u>	Percentage Increase (Decrease)	<u>2002</u>
Net cash provided by (used in):					
Operating activities	\$ 4,449	6.5%	\$ 4,179	1.8%	\$ 4,106
Non-capital financing activities	0	100.0%	(15,000)	-100.0%	0
Capital and related financing activities	(3,541)	0.1%	(3,536)	-0.1%	(3,541)
Investing activities	<u>8</u>	-99.4%	<u>1,293</u>	281.4%	<u>339</u>
Net change in cash and cash equivalents	916	107.0%	(13,064)	-1545.1%	904
Cash and cash equivalents, beginning of year	<u>5,558</u>	-70.2%	<u>18,622</u>	5.1%	<u>17,718</u>
Cash and cash equivalents, end of year	<u><u>\$ 6,474</u></u>	16.5%	<u><u>\$ 5,558</u></u>	-70.2%	<u><u>\$ 18,622</u></u>

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

The **net change in cash and cash equivalents** totaled \$916,295 at June 30, 2004 primarily due to the \$449,381 increase in the cash received from court costs during 2004. The **net change in cash and cash equivalents** totaled (\$13,064,508) at June 30, 2003 primarily due to the \$15,000,000 payment to the Commonwealth and the \$1,292,900 net cash provided by investing activities attributable primarily to the \$1,190,000 in proceeds from the sale of investments during 2003. The **net change in cash and cash equivalents** totaled (\$903,907) at June 30, 2002 primarily due to the \$273,336 decline in the cash received from court costs and the \$877,503 decline in the net cash provided by investing activities attributable largely to the decline in investment income received.

DEBT ADMINISTRATION

At year-end, the Authority had \$28,925,000 in revenue bonds principal outstanding (a decrease of 6.3% as shown below). More detailed information about the Authority's debt is presented in Note 4 to the financial statements.

The following summarizes the changes (in thousands) in the Authority's debt resulting from the regularly scheduled principal and interest payments between fiscal years ended June 30, 2004, 2003, and 2002.

	<u>2004</u>	Percentage Increase (Decrease)	<u>2003</u>	Percentage Increase (Decrease)	<u>2002</u>
Revenue bonds payable	\$ 28,925	-6.3%	\$ 30,865	-5.6%	\$ 32,710
Unamortized discount	<u>(233)</u>	-8.6%	<u>(255)</u>	-8.3%	<u>(278)</u>
Revenue bonds payable, net	<u>\$ 28,692</u>	-6.3%	<u>\$ 30,610</u>	-5.6%	<u>\$ 32,432</u>

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

As presented in Note 5 to the financial statements, as of June 30, 2004, the Authority has no further obligations under the Phase 1 Grants (a total obligation of \$784,338 a year since October 1994).

The outstanding 1994 Series Multi-County Correctional Facilities Revenue Refunding Bonds are callable on November 1, 2004 at 102%.

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the Authority's finances for all of those with an interest. If you have any questions concerning the information provided in this report or need additional financial information, contact the Office of Financial Management, Finance & Administration Cabinet, Commonwealth of Kentucky, Room 261, Capitol Annex, Frankfort, Kentucky, 40601.



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
STATEMENTS OF NET ASSETS
June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 2,882,135	\$ 2,062,613
Court costs receivable	524,517	485,836
Accrued interest receivable-investments	705	2,707
Accrued interest receivable-leases	106,795	113,349
Lease agreement receivables	435,178	408,963
Total current assets	<u>3,949,330</u>	<u>3,073,468</u>
Non-current assets:		
Cash and cash equivalents-debt service reserve	3,591,752	3,494,979
Lease agreement receivables	5,286,397	5,625,564
Debt issuance costs, net of accumulated amortization of \$408,744 in 2004 and \$369,188 in 2003	408,744	448,300
Total non-current assets	<u>9,286,893</u>	<u>9,568,843</u>
Total assets	<u>13,236,223</u>	<u>12,642,311</u>
<u>LIABILITIES</u>		
Current liabilities:		
Revenue bonds payable	2,030,000	1,940,000
Accounts payable	1,333	87,775
Accrued interest payable	259,693	275,419
Total current liabilities	<u>2,291,026</u>	<u>2,303,194</u>
Non-current liabilities:		
Revenue bonds payable	<u>26,662,289</u>	<u>28,669,769</u>
Total liabilities	<u>28,953,315</u>	<u>30,972,963</u>
<u>NET ASSETS</u>		
Accumulated net deficit	<u>\$ (15,717,092)</u>	<u>\$ (18,330,652)</u>



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
Years Ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Operating revenues:		
Court costs receipts	\$ 5,280,959	\$ 4,848,283
Interest income-leases	433,735	459,553
Amortization of premium on leases	96,011	96,011
Total operating revenues	<u>5,810,705</u>	<u>5,403,847</u>
Operating expenses:		
Construction grants	1,522,233	1,522,233
Interest expense	1,585,220	1,677,163
Revenue bonds payable:		
Amortization of bond discount	22,520	22,520
Amortization of debt issuance costs	39,556	39,556
Other expenses	33,366	39,225
Total operating expenses	<u>3,202,895</u>	<u>3,300,697</u>
Income from operations	<u>2,607,810</u>	<u>2,103,150</u>
Non-operating revenues (expenses):		
Income from investments	5,750	84,800
Realized loss on the sale of investments	0	(27,525)
Payment to the Commonwealth	0	(15,000,000)
Total non-operating revenues (expenses)	<u>5,750</u>	<u>(14,942,725)</u>
Change in net assets	2,613,560	(12,839,575)
Accumulated net deficit, beginning of year	<u>(18,330,652)</u>	<u>(5,491,077)</u>
Accumulated net deficit, end of year	<u>\$ (15,717,092)</u>	<u>\$ (18,330,652)</u>



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Cash flows from operating activities:		
Cash received from court costs	\$ 5,242,279	\$ 4,792,898
Lease payments collected, including interest	849,251	916,237
Cash payments on construction grants	(1,522,233)	(1,522,233)
Cash payments for services	(119,809)	(7,500)
Net cash provided by operating activities	<u>4,449,488</u>	<u>4,179,402</u>
Cash flows from non-capital financing activities:		
Payment to the Commonwealth	<u>0</u>	<u>(15,000,000)</u>
Cash flows from capital and related financing activities:		
Principal paid on revenue bonds	(1,940,000)	(1,845,000)
Interest paid on revenue bonds	(1,600,945)	(1,691,809)
Net cash used in capital and related financing activities	<u>(3,540,945)</u>	<u>(3,536,809)</u>
Cash flows from investing activities:		
Investment income received	7,752	102,900
Proceeds from the sale of investments	0	1,190,000
Net cash provided by investing activities	<u>7,752</u>	<u>1,292,900</u>
Net change in cash and cash equivalents	916,295	(13,064,507)
Cash and cash equivalents, beginning of year	<u>5,557,592</u>	<u>18,622,099</u>
Cash and cash equivalents, end of year	\$ <u><u>6,473,887</u></u>	\$ <u><u>5,557,592</u></u>
Reconciliation of cash and cash equivalents to the statements of net assets:		
Current cash and cash equivalents	\$ 2,882,135	\$ 2,062,613
Non-current cash and cash equivalents-debt service reserve	<u>3,591,752</u>	<u>3,494,979</u>
Total cash and cash equivalents per the statements of net assets	\$ <u><u>6,473,887</u></u>	\$ <u><u>5,557,592</u></u>



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
STATEMENTS OF CASH FLOWS (CONTINUED)
Years Ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Reconciliation of income from operations to net cash flows from operating activities:		
Income from operations	\$ 2,607,810	\$ 2,103,150
Interest paid on revenue bonds	1,600,945	1,691,809
Amortization of premium on leases	(96,011)	(96,011)
Amortization of bond discount	22,520	22,520
Amortization of debt issuance costs	39,556	39,556
(Increase) decrease in assets:		
Court costs receivable	(38,681)	(55,386)
Accrued interest receivable-leases	6,554	72,352
Lease agreement receivables	408,963	384,333
Increase (decrease) in liabilities:		
Accounts payable	(86,442)	31,725
Accrued interest payable	(15,726)	(14,646)
Net cash provided by operating activities	<u>\$ 4,449,488</u>	<u>\$ 4,179,402</u>



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of the Kentucky Local Correctional Facilities Construction Authority (the Authority) is presented to assist in understanding the Authority's financial statements. The financial statements and notes are representations of the Authority's management who is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

Nature of Organization:

The Kentucky Local Correctional Facilities Construction Authority is a public corporation and governmental agency of the Commonwealth of Kentucky created in 1982 by an Act of the Kentucky General Assembly. The purpose of the Authority is to provide up to 75 percent of the cost of construction, improvement or repair of any jails operated by Kentucky local governments.

The Authority is a component unit of the Commonwealth of Kentucky and is included in the Commonwealth's Comprehensive Annual Financial Report as a discretely presented component unit.

Basis of Presentation:

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The activities of the Authority are accounted for as an enterprise fund on the accrual basis of accounting. Accordingly, revenues are recognized when they are earned and expenses are recognized when they are incurred.

The Authority applies all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB pronouncements prevail. The Authority has further elected not to apply FASB pronouncements issued after November 30, 1989, in accordance with GASB Statement No. 20.

In June 1999, the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34, "*Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments.*" Accordingly, the financial statements include a Management's Discussion and Analysis (MD&A) section providing an analysis of the Authority's overall financial position and results of operations.

Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents:

For purposes of the statements of cash flows, the Authority considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Net Assets:

Net assets are displayed in three components:

- a. Invested in capital assets, net of related debt - Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- b. Restricted net assets - Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c. Unrestricted net assets - All other net assets that do not meet the definition of "invested in capital assets, net of related debt" or "restricted."

Amortization of Premium on Lease Agreement Receivables:

Premiums on lease receivables are amortized on the straight-line method over the life of the related receivable. The results of this method do not materially differ from those that would be obtained by applying the effective interest method.

Amortization of Bond Discount and Debt Issuance Costs:

Bond discount and debt issuance costs are amortized on the straight-line method over the life of the bond issue. The results of this method do not materially differ from those that would be obtained by applying the effective interest method.

Operating Revenues and Expenses:

Operating revenues and expenses for enterprise funds are those that result from providing services. It also includes all revenues and expenses not related to capital and related financing, non-capital financing, or investing activities.

NOTE 2 - CASH AND CASH EQUIVALENTS

Pursuant to the issue of the Multi-County Correctional Facilities Revenue Refunding Bonds, Series 1994 (see Note 4), the Authority entered into a Trust Indenture Agreement with Star Bank of Cincinnati, Ohio. The Trust Indenture provides for the issuance of the bonds and the establishment of the following special accounts with the trustee.



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 2 - CASH AND CASH EQUIVALENTS (CONTINUED)

Cost of Issuance Account:

Established from Bond proceeds for the purpose of paying the cost of issuing such Bonds.

Operating Account:

Designated for the operating costs of the Authority.

Construction Account:

Established from Bond proceeds, available funds of the Authority and cash contributions of Local Governments not financed through the Authority (the "Local Government Contributions" or "County Contributions") or other sources as determined by series resolution, to be applied to the acquisition, construction, reconstruction and equipping of the Projects designated and the necessary expenses incidental thereto. No disbursements shall be made from the Construction Account unless the Trustee receives a Requisition for Funds approved by the Authority.

Debt Service Fund:

Interest Account:

Established to receive interest on delivery of bonds and transfer of capitalized interest from the Construction Account for Local Governments so requesting. Subsequently, transfers from the Revenue Fund shall be made for payments of the interest becoming due on the Bonds.

Principal Account:

To receive transfers from the Revenue Fund for principal becoming due on the Bonds.

Debt Service Reserve Fund:

Funded from Bond proceeds and funds of the Authority available upon delivery of Bonds in an amount equal to the maximum annual principal and interest requirements on all Bonds issued under the Trust Indenture (the "Aggregate Debt Service Reserve Requirement").

Revenue Fund:

All of the pledged receipts of the Authority, including court costs, investments earnings, rental payments and supplemental rental payments, shall be deposited in the Revenue Fund and disbursed for payment of interest and principal which will come due on the Bonds on said Interest and Principal Payment Dates.

Payment, Surplus, and Operating Fund:

There shall be paid into the Payment, Surplus, and Operating Fund the amounts required to be so paid by the provision of the Trust Indenture, and there may be paid into the Payment, Surplus, and Operating Fund any monies received by the Authority from any other source, including legislative appropriations of the State unless required to be otherwise applied as provided by the Trust Indenture.



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 2 - CASH AND CASH EQUIVALENTS (CONTINUED)

At June 30, 2004 and 2003 the components of the Revenue Bond accounts are as follows:

	<u>2004</u>	<u>2003</u>
Operating account	\$ 5,336	\$ 5,329
Debt service reserve fund	3,591,752	3,494,979
Revenue fund	2,832,986	1,057,310
Payment, surplus, and operating fund	<u>43,813</u>	<u>999,974</u>
Total cash and cash equivalents	6,473,887	5,557,592
Less non-current debt service reserve	<u>(3,591,752)</u>	<u>(3,494,979)</u>
	<u>\$ 2,882,135</u>	<u>\$ 2,062,613</u>

The carrying amounts and market values of cash and cash equivalents by credit risk category are summarized as follows:

	<u>Category</u> <u>1</u>	<u>Category</u> <u>2</u>	<u>Category</u> <u>3</u>	<u>Carrying</u> <u>Amount</u>	<u>Original</u> <u>Cost</u>
<u>June 30, 2004</u>					
U.S. Treasury Reserve Fund	\$ <u>0</u>	\$ <u>0</u>	\$ <u>6,473,887</u>	\$ <u>6,473,887</u>	\$ <u>6,473,887</u>
<u>June 30, 2003</u>					
U.S. Treasury Reserve Fund	\$ <u>0</u>	\$ <u>0</u>	\$ <u>5,557,592</u>	\$ <u>5,557,592</u>	\$ <u>5,557,592</u>

The above schedule classifies the carrying amounts of cash and cash equivalents as to credit risk by the three categories described below:

- Category 1 - Amounts covered by federal depository insurance or collateralized with securities held by the Authority or the Authority's agent in the Authority's name.
- Category 2 - Amounts collateralized with securities held by the pledging financial institution's trust department or agent in the Authority's name.
- Category 3 - Amounts which are uninsured and uncollateralized or which are collateralized, but the securities are held by the financial institution's trust department or agent in the institution's name.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 3 - LEASE AGREEMENT RECEIVABLES

Lease agreement receivables represent the participating counties' agreed amount of bond principal required to finance the counties' share of project costs funded through the bond issue. The counties and their respective amounts are as follows:

	<u>2004</u>	<u>2003</u>
Adair	\$ 291,224	\$ 309,190
Estill	123,510	131,130
Franklin	1,216,192	1,291,221
Fulton	215,521	228,572
Johnson	652,694	692,282
Kenton	2,656,341	2,820,214
Knox	329,839	350,187
McCreary	194,556	206,142
Montgomery	575,376	610,872
Powell	161,121	170,731
Simpson	<u>242,407</u>	<u>257,203</u>
	6,658,781	7,067,744
Less premium on leases	<u>(937,206)</u>	<u>(1,033,217)</u>
Net lease agreement receivables	5,721,575	6,034,527
Less current maturities	<u>(435,178)</u>	<u>(408,963)</u>
Non-current lease agreement receivables	<u>\$ 5,286,397</u>	<u>\$ 5,625,564</u>

Premium on leases represents the difference between the amount of bond principal assigned and bond proceeds allocated to the participating counties, which reflects the counties' share of bond issuance costs.

Future minimum lease payments required under the lease agreement receivables at June 30, 2004 are as follows:

<u>Year Ending June 30</u>	
2005	\$ 435,178
2006	463,075
2007	492,765
2008	524,361
2009	557,990
Thereafter	<u>4,185,412</u>
	<u>\$ 6,658,781</u>



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 4 - REVENUE BONDS PAYABLE

At June 30, 2004, revenue bonds payable (Multi-County Correctional Facilities Revenue Refunding Bonds-Series 1994) consist of the following:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Amounts Due Within One Year</u>
Serial bonds (a)	\$ 13,175,000	\$	\$ 1,940,000	\$ 11,235,000	\$ 2,030,000
Term bonds (b)	<u>17,690,000</u>	<u> </u>	<u> </u>	<u>17,690,000</u>	<u> </u>
	30,865,000	0	1,940,000	28,925,000	2,030,000
Unamortized discount	<u>(255,231)</u>	<u> </u>	<u>(22,520)</u>	<u>(232,711)</u>	<u> </u>
	<u>\$ 30,609,769</u>	<u>\$ 0</u>	<u>\$ 1,917,480</u>	<u>\$ 28,692,289</u>	<u>\$ 2,030,000</u>

(a) Serial bonds, 4.95% to 5.40% due annually on November 1 in amounts ranging from \$2,030,000 to \$2,475,000.

(b) Term bonds, 5.50% due November 1, 2014.

At June 30, 2003, revenue bonds payable (Multi-County Correctional Facilities Revenue Refunding Bonds-Series 1994) consist of the following:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Amounts Due Within One Year</u>
Serial bonds	\$ 15,020,000	\$	\$ 1,845,000	\$ 13,175,000	\$ 1,940,000
Term bonds	<u>17,690,000</u>	<u> </u>	<u> </u>	<u>17,690,000</u>	<u> </u>
	32,710,000	0	1,845,000	30,865,000	1,940,000
Unamortized discount	<u>(277,751)</u>	<u> </u>	<u>(22,520)</u>	<u>(255,231)</u>	<u> </u>
	<u>\$ 32,432,249</u>	<u>\$ 0</u>	<u>\$ 1,822,480</u>	<u>\$ 30,609,769</u>	<u>\$ 1,940,000</u>

The term bonds are subject to redemption by operation of the Debt Service Fund through mandatory sinking fund installments. The redemption price will be 100% of the principal redeemed plus accrued interest, if any, to the redemption date.

The serial and term bonds maturing on or after November 1, 2005 shall be subject to redemption prior to their stated maturity at the option of the Authority in whole at any time or in part on any interest payment date on or after November 1, 2004, at redemption prices ranging from 100% to 102% of the principal amount redeemed. Such redemption price, plus accrued interest, if any, is payable on the date of redemption.



KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 4 - REVENUE BONDS PAYABLE (CONTINUED)

The Series 1994 Bonds are also subject to extraordinary redemption, without premium, to the extent of casualty insurance proceeds, condemnation awards, and monies received from a Local Government electing to purchase its Project.

Payments of principal and interest are fully guaranteed by Financial Security Assurance, Inc. All cash and investments of the Authority held by the trustee bank are pledged as collateral for the bond indebtedness.

The bonds are special obligations of the Authority and, except to the extent payable from the proceeds of such bonds or other monies pledged under the Trust Indenture, are payable from the pledged receipts as described below, to the extent such sources exist.

1. The Authority is entitled to 10.8% or \$10.80 of each \$100.00 court cost, up to \$5,400,000 each fiscal year, taxed against a defendant upon conviction in each case tried in a state Circuit or District Court. The court costs are collected by all circuit clerks in Kentucky and are submitted on a monthly basis. Any receipts collected above the \$5,400,000 each fiscal year are paid into the Commonwealth's general fund.
2. Rental payments received by the Authority under the leases from Local Governments in repayment of and as interest on a Local Government's agreed participation.
3. All interest earned and gains realized on investment obligations unless the Trust Indenture or Series 1994 Resolution specifically requires such interest earned or gains realized to be credited to the account of the Authority or a Local Government.
4. Any gifts or grants received from any agency of government, both federal and state, to the extent not otherwise required to be applied.
5. Any and all appropriations made to the Authority by the General Assembly of the Commonwealth to the extent not otherwise committed during any fiscal period of the Authority.

Debt service requirements at June 30, 2004 are as follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>
2005	\$ 2,030,000	\$ 1,503,658
2006	2,135,000	1,399,506
2007	2,240,000	1,287,917
2008	2,355,000	1,168,419
2009	2,475,000	1,039,775
2010-2014	14,455,000	2,686,612
2015	<u>3,235,000</u>	<u>346,363</u>
	\$ <u>28,925,000</u>	\$ <u>9,432,250</u>

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 5 - CONSTRUCTION GRANTS

On September 9, 1994, the Authority adopted a resolution for the funding of regional jails in the counties of Bourbon, Boyd, Hardin, Marshall, and Rockcastle. These awards are to be paid in ten equal annual installments beginning in October 1994. The Authority's total participation in these projects (Phase 1 Grants) is \$7,843,379. As of June 30, 2004, the Authority has no further obligations under the Phase 1 Grants.

On June 10, 1997, the Authority adopted a resolution for the funding of regional jails in the counties of Ballard, Boyle, Calloway, Henderson and Letcher. These awards are to be paid in ten equal annual installments beginning in October 1997. The Authority's total participation in these additional projects (Phase 2 Grants) is \$7,378,954.

Disbursements on these projects through June 30, 2004 and the remaining obligations are as follows:

	<u>Grant Amount</u>	<u>Cumulative Disbursed by Year Ended June 30, 2002</u>	<u>Disbursed Year Ended June 30, 2003</u>	<u>Disbursed Year Ended June 30, 2004</u>	<u>Obligation Remaining at June 30, 2004</u>
<u>Phase 1 Grants</u>					
Bourbon	\$ 1,150,000	\$ 920,000	\$ 115,000	\$ 115,000	\$ 0
Boyd	700,000	560,000	70,000	70,000	0
Hardin	4,259,185	3,407,347	425,919	425,919	0
Marshall	1,612,194	1,289,756	161,219	161,219	0
Rockcastle	122,000	97,600	12,200	12,200	0
<u>Phase 2 Grants</u>					
Ballard	183,442	91,720	18,344	18,344	55,034
Boyle	2,146,589	1,073,295	214,659	214,659	643,976
Calloway	1,530,650	765,325	153,065	153,065	459,195
Henderson	2,974,273	1,487,135	297,427	297,427	892,284
Letcher	<u>544,000</u>	<u>272,000</u>	<u>54,400</u>	<u>54,400</u>	<u>163,200</u>
	<u>\$ 15,222,333</u>	<u>\$ 9,964,178</u>	<u>\$ 1,522,233</u>	<u>\$ 1,522,233</u>	<u>\$ 2,213,689</u>

NOTE 6 - PAYMENT TO THE COMMONWEALTH

During its 2003 Regular Session the General Assembly of the Commonwealth of Kentucky passed House Bill No. 269 which contained a provision that, notwithstanding KRS 441.605 to 441.695, for fiscal year ended June 30, 2003, funds in the amount of \$15,000,000 shall be expended from the Kentucky Local Correctional Facilities Construction Authority for local correctional facility and operational support consistent with contractual covenants in accordance with bond indentures of the Authority. Accordingly, the statement of revenues, expenses, and changes in net assets for the year ended June 30, 2003 includes a non-reciprocal payment to the Commonwealth in the amount of \$15,000,000.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2004 and 2003

NOTE 7 - ACCUMULATED NET DEFICIT

In providing funds for the construction and improvement of correctional facilities, the Authority obtains its funding through the issuance of revenue bonds and the receipt of court costs remittances. When revenue bonds are issued, the Authority incurs long-term obligations that are repaid by revenue received from annual court costs receipts. When construction grants are awarded to local governments the disbursements are immediately reflected as operating expenses. Due to the timing of these transactions, the Authority periodically incurs losses from operations. In addition, during 2003 House Bill No. 269 authorized the one-time non-reciprocal payment to the Commonwealth in the amount of \$15,000,000 (see Note 6), which has been reported as a non-operating expense in the accompanying 2003 financial statements. As a result of these transactions, the Authority has accumulated a net deficit as of June 30, 2004 in the amount of \$15,717,092.

NOTE 8 - RELATED PARTY TRANSACTIONS

The Authority receives the benefit of accounting and administrative services from the Office of Financial Management (OFM). OFM serves as staff to the Authority and is reimbursed for the costs of salaries, fringe benefits, personnel costs, etc. in the amount of \$25,000 per year. During 2004, the Authority reimbursed OFM \$25,000 for these costs.

Additionally during 2004, the Authority reimbursed OFM \$7,034 for professional services it had paid on behalf of the Authority.

At June 30, 2003, the Authority owed the Office of Financial Management \$87,775 (included within accounts payable on the accompanying June 30, 2003 statement of net assets). As of June 30, 2003, OFM was due \$25,000 per year for three years (a total of \$75,000). Additionally, since 2002 OFM had paid on behalf of the Authority a total of \$12,775 for professional services. In July 2003, the Authority paid the \$87,775 due to OFM.



MOORE STEPHENS POTTER LLP

CERTIFIED PUBLIC ACCOUNTANTS • BUSINESS ADVISORS

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

To the Board of Directors
Kentucky Local Correctional
Facilities Construction Authority
Frankfort, Kentucky

We have audited the financial statements of the Kentucky Local Correctional Facilities Construction Authority as of and for the year ended June 30, 2004, and have issued our report thereon dated August 24, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Kentucky Local Correctional Facilities Construction Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky Local Correctional Facilities Construction Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management, the Board of Directors, and the Auditor of Public Accounts of the Commonwealth of Kentucky, and is not intended to be and should not be used by anyone other than these specified parties.

Moore Stephens Potter, LLP

MOORE STEPHENS POTTER, LLP

August 24, 2004

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members in principal cities throughout the world*

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
SCHEDULE OF FINDINGS
Year Ended June 30, 2004

Schedule of auditor's results

We have issued an unqualified opinion dated August 24, 2004 on the financial statements of the Kentucky Local Correctional Facilities Construction Authority as of and for the year ended June 30, 2004.

Our audit disclosed no instances of noncompliance which are material to the Authority's financial statements.

Findings relating to the financial statements

Our audit disclosed no findings that are required to be reported in accordance with *Government Auditing Standards*.

KENTUCKY LOCAL CORRECTIONAL FACILITIES CONSTRUCTION AUTHORITY
SCHEDULE OF PRIOR AUDIT FINDINGS AND THEIR RESOLUTION
Year Ended June 30, 2004

The audit as of and for the year ended June 30, 2003 disclosed no findings that are required to be reported in accordance with *Government Auditing Standards*.

APPENDIX B

DEBT SERVICE REQUIREMENTS

The following table sets forth the Annual Debt Service Requirements of the Series 2004 Bonds:

Bond Year Ending <u>November 1</u>	<u>Principal</u>	<u>Interest</u>	Total Debt <u>Service</u>
2005	\$1,845,000	\$944,370	\$2,789,370
2006	1,940,000	844,050	2,784,050
2007	1,995,000	785,850	2,780,850
2008	2,040,000	740,963	2,780,963
2009	2,105,000	679,763	2,784,763
2010	2,170,000	616,613	2,786,613
2011	2,280,000	502,688	2,782,688
2012	2,400,000	382,988	2,782,988
2013	2,530,000	256,988	2,786,988
2014	2,365,000	124,163	2,489,163

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APPENDIX C

SUMMARY OF BOND DOCUMENTS

The following is a general summary of the Trust Indenture, the Leases, the Participation Agreements and the Series 2004 Resolution. Such summary does not purport to be complete and accordingly is qualified by reference to the full text of such documents, copies of which may be obtained from the Trustee upon written request. The summary herein of the Series 2004 Resolution includes certain provisions that supersede or modify the corresponding provisions of the Trust Indenture while the Bond Insurance Policy is in effect.

Definitions

"*Aggregate Debt Service Reserve Requirement*" shall mean an amount equal to the lesser of (a) 10% of the stated aggregate principal amount of the Bonds, (b) the maximum Annual Debt Service Requirement in the current or any succeeding Bond Fiscal Year with respect to all Outstanding Bonds and (c) 125% of the average Annual Debt Service Requirement with respect to all Outstanding Bonds; provided that the Authority may satisfy said Aggregate Debt Service Reserve Requirement by either or both (x) depositing moneys to the credit of the Debt Service Reserve and (y) procuring for the Debt Service Reserve a surety bond (or other credit facility), in each case in the manner and in the amount required by the Trust Indenture and as may be specified by the Series Resolution authorizing such Bonds.

"*Annual Budget*" shall mean the annual budget, as amended or supplemented, for a particular Bond Fiscal Year adopted by the Authority under the Indenture and filed with the Trustee.

"*Annual Debt Service Requirement*" shall mean, for any Bond Fiscal Year, the interest on all Outstanding Bonds which shall be due and payable November 1 and May 1 of each such Bond Fiscal Year and the principal of all Outstanding Bonds which shall be due and payable on November 1 in each such Bond Fiscal Year; including Serial Bond principal requirements and Mandatory Sinking Fund Installments for Term Bonds.

"*Authority's Agreed Financial Participation*" or "*Authority's Participation*" shall mean the financial obligation of the Authority to pay and retire as the same become due the Authority's pro rata portion of the principal and interest requirements of Bonds allocated to a particular Project.

"*Authorized Officer*" shall mean the Chairman, Vice Chairman, Secretary or Treasurer of the Authority, and any other of its members, officers, agents or employees duly authorized by Resolution of the Authority to perform the act or sign the document in question.

"*Bond Fiscal Year*" shall mean each annual period which begins on July 1 in any calendar year and ends on June 30 in the following calendar year.

"*Bond Insurance Policy*" shall mean the municipal bond insurance policy issued by the Bond Insurer guaranteeing the scheduled payment of principal of and interest on the Series 2004 Bonds.

"*Bond Insurer*" shall mean MBIA Insurance Corporation, or any successor thereto.

"*Bond Proceeds Fund*" shall mean the Fund so designated which is established and created by the Trust Indenture.

"*Capitalized Interest*" shall mean that portion of the proceeds of the Bonds of a particular Series designated by the Authority or a Local Government as interest on its Agreed Financial Participation prior to and during the construction period of a particular Project as set forth in a Series Resolution.

"*Certificate*" shall mean a document signed by an Authorized Officer attesting to or acknowledging the circumstances or other matters therein stated.

"*Code*" shall mean the Internal Revenue Code of 1986, as amended.

"*Construction*" shall mean and shall include, inter alia, (a) preliminary planning to determine the feasibility of any Project; the engineering, architectural, legal, fiscal and economic investigations and studies necessary thereto; and surveys, designs, plans, working drawings, specifications, procedures and other actions necessary to the construction of any Project; (b) the erection, building, acquisition, alteration, remodeling, improvement or extension of any Project; (c) the inspection and supervision of the construction of any Project, and all costs incidental to the construction and financing of same; and such term shall also relate to and mean any other physical devices or appurtenances in connection with, or reasonably attendant to, any Project; and (d) any and all other acts performed in connection with the planning, implementation, acquisition, financing or construction of any Project.

"*Construction Account*" shall mean, for each Series of Bonds, the account so designated which is established and created pursuant to the Trust Indenture.

"*Construction Completion Loan*" shall mean a loan made by the Authority to a Local Government from the Construction Account for the purpose of completing a particular Project in the event moneys on deposit in the Construction Account are not sufficient for such purpose.

"*Continuing Disclosure Agreement*" shall mean the Continuing Disclosure Agreement between the Authority and the Trustee relating to the Bonds of a particular Series.

"*Costs of Issuance*" shall mean the costs of issuing a Series of Bonds as approved by an Authorized Officer.

"*Costs of Issuance Account*" shall mean, for each Series of Bonds, the Account so designated which is established and created pursuant to the Trust Indenture.

"*Court Costs*" shall mean those court costs authorized to be imposed by KRS 24A.175(1), as amended, and required to be paid over to the State Treasury by Circuit Clerks for the benefit and use of the Authority pursuant to KRS 24A.180(5), KRS 42.320(2)(b) and KRS 441.685(1)(d).

"*Debt Service Fund*" shall mean the Fund so designated which is established and created by the Trust Indenture.

"*Debt Service Reserve*" shall mean, with respect to the Bonds of a particular Series, the Fund so designated which is established and created by the Trust Indenture as a reserve for the payment of principal of, interest on, and Mandatory Sinking Fund Installments, if any, in respect of the Bonds of such Series.

"*Defeasance Obligations*" shall mean:

(a) direct obligations of, or obligations the payment of the principal and interest on which are unconditionally guaranteed by (including in each case obligations issued or held in book entry form), the United States of America or a United States government agency; and

(b) pre-funded municipal obligations defined as follows:

Any bonds or other obligations of any state of the United States of America or of an agency, instrumentality or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on

the date specified in such instructions; and which are rated, based on the related escrow, rated "AAA" and "Aaa," respectively, by S&P and Moody's.

"*Funds and Accounts*" shall mean the funds and accounts created under the Trust Indenture or any Series Resolution.

"*Interim Financing Escrow Account*" shall mean, for each Series of Bonds, the Account so designated which is established and created pursuant to the Trust Indenture.

"*Justice Cabinet*" shall mean the Justice and Public Safety Cabinet of the Commonwealth.

"*KRS*" shall mean the Kentucky Revised Statutes, as amended.

"*Lease and Participation Agreement*" or "*Lease*" shall mean the agreement, as amended or supplemented from time to time, made and entered into by and between a Local Government and the Authority, as authorized by the Act, providing for the lease of a particular Project by the Authority to the Local Government from year to year and establishing the Authority's Agreed Financial Participation in financing the cost of the particular Project in substantially the same form as set forth in Exhibit B to the Indenture.

"*Local Government*" shall mean any county or urban-county government having entered into a Lease and Participation Agreement or Participation Agreement with the Authority relating to the construction and operation of a particular Project.

"*Local Government's Agreed Financial Participation*" or "*County's Participation*" shall mean the financial obligation of a Local Government to pay Rental Payments under a Lease for application to the payment and retirement as the same become due of its pro rata portion of the principal and interest requirements of Bonds allocated to a particular Project.

"*Mandatory Sinking Fund Installment*" shall mean the annual installment of principal established for Term Bonds by a Series Resolution.

"*Moody's*" shall mean Moody's Investors Service, Inc., a Delaware corporation, its successors and assigns.

"*Operating Costs*" shall mean, as of any particular date, the Authority's operating expenses, if any, of carrying out and administering its statutory functions and its duties under the Trust Indenture and shall include, without limiting the generality of the foregoing, salaries, supplies, utilities, mailing, labor, materials, office rent, maintenance, furnishings, equipment machinery and apparatus, insurance premiums, legal, accounting, management, consulting and banking services and expenses, the fees and expenses of the Trustee, Fiduciaries and Paying Agents, including Costs of Issuance, if any, other than Costs of Issuance paid from proceeds of Bonds.

"*Outstanding*" when used with reference to Bonds shall mean, as of any date, all Bonds, theretofore or then being authenticated and delivered under the Trust Indenture except:

- (a) Any Bonds cancelled by the Trustee on or prior to such date;
- (b) Bonds in lieu of or in substitution for which other Bonds shall have been authenticated and delivered pursuant to the Trust Indenture; and
- (c) Bonds deemed to have been paid under the Trust Indenture.

"*Parity Bonds*" shall mean Bonds issued pursuant to a Series Resolution of the Authority in accordance with the terms and provisions of the Trust Indenture ranking on the basis of parity as to security and source of payment with previously issued Bonds.

"*Participation Agreement*" shall mean the agreement made and entered into by and between a Local Government and the Authority, as authorized by the Act, providing for the operation, maintenance and insurance of a particular Project and establishing the Authority's Agreed Financial Participation in financing part of the cost of the particular Project.

"*Paying Agent*" shall mean any bank or trust company designated, and its successor or successors hereafter appointed as paying agent for the Bonds of any Series in the manner provided in the Trust Indenture.

"*Payment, Surplus and Operating Fund*" shall mean, the Fund so designated which is established and created by the Trust Indenture.

"*Permitted Investments*" shall mean any investment authorized by KRS Section 42.500, as amended

"*Pledged Receipts*"

(i) shall include the Rental Payments received by the Authority under the Leases from Local Governments;

(ii) shall include Supplemental Rental Payments received by the Authority under Supplemental Leases from Local Governments in repayment and as interest on Construction Completion Loans;

(iii) shall include all moneys collected and deposited in the State Treasury for the benefit of the Authority as Court Costs pursuant to KRS 24A.175(1), KRS 24A.180(5) and KRS 42.320(2)(b);

(iv) shall include all interest earned and gains realized on Permitted Investments unless the Trust Indenture or Series Resolution specifically requires such interest earned or gains realized to be credited to the Rebate Fund or a construction account of a Local Government;

(v) shall include any gifts or grants received from any agency of government, both federal and State, to the extent not otherwise required to be applied; and

(vi) shall include any and all appropriations made to the Authority by the General Assembly of the Commonwealth of Kentucky to the extent not otherwise committed and budgeted by the Authority during any fiscal period of the Authority.

"*Principal Installment*" for any Bond Fiscal Year shall mean, as of any date of calculation and with respect to any Series so long as any Bonds thereof are outstanding:

(i) the principal amount of the Outstanding Bonds of said Series which mature in such Bond Fiscal Year, reduced by the aggregate principal amount of such Bonds which would before such Bond Fiscal Year be retired by reason of the payment when due and application in accordance with the Trust Indenture of Mandatory Sinking Fund Installments for the retirement of such Bonds; plus

(ii) the unsatisfied balance of the Mandatory Sinking Fund Installments, if any, due during such Bond Fiscal Year for the Bonds of such Series.

"*Principal Installment Date*" shall mean, for each Series of Bonds, the date upon which each Principal Installment on the Bonds of such Series shall be payable, which shall be a November 1.

"*Project*" shall mean the jail building or buildings and related detention facilities determined by Resolution of the Authority to qualify for financial assistance from the Authority pursuant to the Act and Resolutions of the Authority.

"*Project Bonds*" shall mean the Bonds allocable to a Local Government under its Lease.

"*Redemption Account*" shall mean, with respect to the Bonds of a particular Series, the Account so designated which is established and created pursuant to the Trust Indenture.

"*Redemption Date*" shall mean the date set forth in a Series Resolution on which Bonds of the Series authorized by such Series Resolution may be called for redemption.

"*Redemption Price*" shall mean, with respect to any Bond, the principal amount thereof plus the applicable premium, if any, payable upon redemption thereof pursuant to the Trust Indenture and the Series Resolution pursuant to which the same was issued.

"*Redemption Ratio*" shall mean the amount of Bonds redeemed or purchased (other than by Mandatory Sinking Fund Installment or pursuant to the issuance of Refunding Bonds) divided by the total principal amount of the Outstanding Bonds subject to Mandatory Sinking Fund Redemption immediately preceding such redemption or purchase.

"*Refunding Bonds*" shall mean all Bonds, whether issued in one or more Series, authenticated and delivered on original issuance for the purpose of refunding Bonds theretofore issued pursuant to the Trust Indenture.

"*Rental Payments*" shall mean the total amount due each year as rent from Local Governments to the Authority under a Lease and Participation Agreement.

"*Revenue Fund*" shall mean the Kentucky Local Correctional Facilities Construction Authority Fund identified by KRS 441.685, which is established and created by the Trust Indenture.

"*Series*" shall mean all of the Bonds authenticated and delivered on original issuance in a simultaneous transaction, and any Bonds thereafter authenticated and delivered in lieu of or in substitution for such Bonds pursuant to the Trust Indenture, regardless of variations in maturity, interest rate, Sinking Fund Installments or other provisions.

"*Series of Bonds*" or "*Bonds of a Series*" or words of similar import shall mean the Series authorized by a Series Resolution.

"*Series Resolution*" shall mean a Resolution of the Authority authorizing the issuance of a Series of Bonds in accordance with the terms and provisions of the Trust Indenture, adopted by the Authority and incorporated by reference within the Indenture.

"*State*" shall mean the Commonwealth of Kentucky.

"*Supplemental Lease*" shall mean an amendment to a Lease and Participation Agreement containing provisions for additional rental payments by a Local Government to the Authority in order to provide for principal and interest requirements on Construction Completion Loans.

"*Supplemental Trust Indenture*" shall mean any trust indenture supplemental to or amendatory of the Trust Indenture adopted by the Authority in accordance with the Trust Indenture.

"Term Bonds" shall mean those Bonds designated by Series Resolution as requiring Mandatory Sinking Fund Installments.

Trust Indenture

The Trustee Indenture provides for the issuance of the Authority's Bonds and the establishment of the following special accounts with the Trustee:

Bond Proceeds Fund. To the extent any deposit is required to be made therein pursuant to a Series Resolution, the Trustee shall establish and create within the Bond Proceeds Fund a separate Costs of Issuance Account, a separate Construction Account, a separate Interim Financing Escrow Account and a separate Redemption Account for such Series of Bonds, and shall identify each such separate Account by inserting in the designation therefor the year, letter or other designation of the Bonds of such Series.

Costs of Issuance Account. (a) There shall be deposited from time to time in the Costs of Issuance Account established for each Series the amount of moneys necessary to pay the Costs of Issuance of such Series from either:

(i) the proceeds of the Bonds of such Series as specified and determined in the Series Resolution authorizing the issuance of such Series, or

(ii) moneys from time to time received by the Authority from any other source, including Court Costs and legislative appropriations by the State, and determined by the Authority to be deposited in such Account, unless required to be otherwise applied as provided by the Trust Indenture.

(b) The Trustee shall from time to time pay out, or permit the withdrawal of, moneys credited to any Costs of Issuance Account, free and clear of any lien or pledge or assignment, for the purpose of paying Costs of Issuance of the Bonds of the Series for which such Account was established, upon receipt by said Trustee of the following:

(i) a written requisition of the Authority signed by an Authorized Officer stating with respect to each payment to be made:

(A) the item for which payment is to be made;

(B) the name of the person or party to whom the payment is to be made;

(C) the amount to be paid; and

(ii) a Certificate signed by an Authorized Officer stating that the amount to be paid from such Account pursuant to such requisition is a proper charge thereon. Upon receipt of each such requisition, the Trustee shall deliver to the Authority or designated payee a check or draft drawn upon the applicable Costs of Issuance Account for the payment of each item.

(c) Upon receipt of a Certificate signed by an Authorized Officer of the Authority to the effect that all Costs of Issuance of the applicable Series of Bonds have been paid, the Trustee shall transfer any moneys remaining in said Costs of Issuance Account to the Construction Account or Redemption Account, as the case may be, established for such Series.

(d) Upon the deposit of the proceeds of the Bonds of a Series or other moneys in the manner hereinabove described in any Costs of Issuance Account, the Authority shall furnish the Trustee with a schedule of dates on which it is estimated by the Authority that such moneys in said Account will be required to be expended. The Authority may from time to time amend the schedule so furnished. Upon

receipt of such schedule or amended schedule by the Trustee, the Authority may direct the Trustee to, or in the absence of direction the Trustee shall, invest and reinvest the moneys in said identified Account in Permitted Investments, so that the maturity date or date of redemption at the option of the holder of such Permitted Investments shall coincide as nearly as practicable with the times at which moneys are needed by the Authority to be so expended. The Trustee shall sell or present for redemption any obligations purchased by it as an investment whenever it shall be necessary in order to provide moneys to meet any payment from the Costs of Issuance Account.

Construction Account. (a) There shall be deposited into the applicable Construction Account (i) such amount of the proceeds of the Bonds of any Series required to be deposited therein as shall be specified and determined by the Series Resolution authorizing such Series of Bonds, in accordance with the Trust Indenture, (ii) amounts to be transferred from the Costs of Issuance Account and (iii) amounts to be transferred from the Interim Financing Escrow Account.

(b) In accordance with each Series Resolution, upon the written direction of the Authority signed by an Authorized Officer, the Trustee shall allocate for accounting purposes the Estimated Construction Cost for each Project; or such lesser amount which will generate said Estimated Construction Cost from earnings on Permitted Investments over the estimated construction period as may be specified in a Series Resolution.

(c) Except as may be limited by the purposes for which a Series of Bonds is issued as set forth in the Series Resolution, amounts in any Construction Account shall be expended and applied by the Trustee upon written direction of the Authority signed by an Authorized Officer from time to time as hereinafter described, only for the making of reimbursements to the Local Government or for the making of disbursements directly to contractors, architects or engineers, or suppliers of the particular Project in accordance with the Local Government's Construction Contract pursuant to the terms of a Lease and Participation Agreement or Participation Agreement between the Authority and the Local Government and the Trust Indenture.

The Trustee shall keep and maintain records with respect to the Construction Account, which shall include a separate accounting, through the establishment of subaccounts for each Project, with respect to funds and moneys in said Construction Account held for the use and benefit of each individual Local Government which has entered into a Lease and Participation Agreement or Participation Agreement with the Authority and pursuant to the terms and provisions of which the Authority is to participate in financing the cost of the acquisition and construction of that respective Project.

At or prior to the delivery of any Series of Bonds, the Trustee shall be furnished with executed copies or duly authenticated counterparts of all Lease and Participation Agreements and Participation Agreements between the Authority and Local Governments to which said Series of Bonds relates, or in lieu thereof, shall be furnished by the Authority, with a duly certified list of all such Lease and Participation Agreements and Participation Agreements containing all pertinent data in respect thereto, together with summaries thereof.

(d) Upon the deposit of the proceeds of Bonds or other moneys in the manner hereinabove described in the subaccounts of the Construction Account, the Authority shall furnish the Trustee with a schedule of dates on which it is estimated by each Local Government that such moneys in such subaccount will be required to be expended. The Authority, upon advice of a Local Government, may from time to time amend the schedule so furnished as further data and information respecting the construction of that particular Project become available. After such schedule or amended schedule has been furnished to the Trustee, the Authority may direct the Trustee to, or in the absence of direction the Trustee shall, invest and reinvest the moneys in such subaccounts (and in the aggregate for the Construction Account) in Permitted Investments so that the maturity date or date of redemption at the option of the holder of such Permitted Investments shall coincide as nearly as practicable with the times at

which moneys are required by the Authority to be so expended on account of the particular Project. The Trustee shall sell or present for redemption any Permitted Investments purchased by it as an investment whenever it shall be necessary in order to provide moneys to meet any authorized payment from such Construction Account.

(e) The Trustee shall from time to time pay out or permit the withdrawal of moneys from the applicable subaccount of the Construction Account, upon receipt by the Trustee of a written Requisition for Funds of the Local Government approved by an Authorized Officer of the Authority containing the following with respect to each payment or disbursement to be made:

(i) the name of the person or parties to whom the payment or disbursement is to be made;

(ii) the amount to be paid to such person or party;

(iii) the applicable Lease and Participation Agreement or Participation Agreement in respect of which the payment or disbursement is to be made;

(iv) that with respect to such requested payment or disbursement there has not been filed with or served upon the Authority notice of any lien or attachment upon, or claim affecting the right to receive, payment of any of the amounts requisitioned and payable to any of the persons, firms or corporations named in such requisition which has not been released or will not be released simultaneously with such payment.

(v) that such Requisition for Funds contains no item representing payment on account of any retained percentages of the cost of Construction which the Local Government is at the date of such requisition entitled to retain;

(vi) that in connection with such Requisition for Funds the Authority has received such proofs executed by the Architects for the Local Government and officials of the Local Government which has entered into the specified Lease and Participation Agreement or Participation Agreement as are properly required by Authority, to the effect that a payment and performance bond for the Project has been posted and that each obligation set forth in said requisition has been (1) properly incurred, (2) is then due and unpaid; and (3) that insofar as such obligation was incurred for work, services, materials, equipment or supplies, such work or services was actually performed, or such materials, equipment or supplies were actually installed in furtherance of the Construction of the particular Project, or were delivered at the site of the Project for such purposes, all in accordance with the Lease and Participation Agreement or Participation Agreement specifically identified in such Requisition for Funds; and

(vii) that all of the requirements of the Department of Corrections through the date of said Requisition for Funds have been met.

(f) All such written Requisitions for Funds of Local Governments approved by an Authorized Officer of the Authority and conforming to the Trust Indenture received by the Trustee may be relied upon by and shall be retained in the possession of the Trustee.

Notwithstanding the foregoing requirements for written requisitions for funds, the Trustee shall transfer from the appropriate subaccounts of the Construction Account to the Debt Service Fund such amounts as a Series Resolution or Lease and Participation Agreement may designate as Capitalized Interest without further direction of the Authority or a Local Government.

(g) At such time as all moneys due to be disbursed from a subaccount of the Construction Account in respect of a Lease and Participation Agreement or Participation Agreement have been so

disbursed and paid, and the Trustee has received a Certificate executed by the Chairman of the Authority stating that completion of the particular Project authorized by the specified Series of Bonds has occurred, which Certificate shall be accompanied by an opinion of legal counsel stating that there are no uncanceled mechanics', laborers', contractors' or materialmen's liens on file in any public office where the same should be filed in order to be valid liens against any part of any Project, and that in the opinion of said legal counsel the time within which such liens can be filed has expired, that part of the balance in said subaccount shall be transferred by the Trustee in accordance with (h) below.

(h) In those instances in which the Local Government has entered into a Lease and Participation Agreement, that portion of the surplus, if any, in the applicable subaccount of the Construction Account determined from the Local Government's Participation shall be transferred by the Trustee to the Debt Service Fund and the Local Government shall receive a credit against its Rental Payment then due under its Lease in the amount so determined. In those instances in which the Local Government has entered into a Participation Agreement, the Local Government shall receive a rebate in cash in an amount determined by applying the same percentage as the Local Government's contribution, if any, to the applicable subaccount of the Construction Account from funds other than the proceeds of the related Bonds.

Any (A) such surplus amounts representing the Authority's Participation in any subaccount of the Construction Account and (B) amounts in a subaccount for a Project for which construction has not commenced within the time required under a Participation Agreement shall be transferred by the Trustee at the direction of the Authority to a separate subaccount of the Construction Account and used for the purpose of making Construction Completion Loans or providing increased funding under a Participation Agreement. In such event, amounts shall be transferred to the Project subaccount related to the applicable Project and, in the case of a Construction Completion Loan, the Authority and applicable Local Government shall enter into a Supplemental Lease and Participation Agreement providing for increased Rental Payments in an amount adequate to pay the proportionate amount of debt service on the Bonds applicable to such Construction Completion Loan. Amounts that are not required for Construction Completion Loans or for additional funding to complete Projects subject to a Participation Agreement may be transferred to subaccounts for additional Projects, upon the order of an Authorized Officer.

In the event any Local Government fails to initiate the construction of its Project in accordance with the terms of the Lease and Participation Agreement, the Trustee, upon written direction of the Authority, shall transfer that portion of the Construction Account allocated to the Local Government's share of said Project to the Debt Service Fund and shall apply the amount so transferred to the extraordinary redemption of Bonds in accordance with the provisions of the Trust Indenture.

Interim Financing Escrow Account. (a) There shall be deposited in the Interim Financing Escrow Account such amount of the proceeds of the Bonds of any Series required to be deposited therein as shall be specified and determined by the Series Resolution to be sufficient to either:

(i) fund the Authority's Agreed Financial Participation in a Project the Construction of which has been completed (or substantially completed) prior to the delivery of such Bonds and for which there is no Agreed Financial Participation by the Local Government, or

(ii) provide for the retirement of interim financing debt obligations incurred by Local Governments in the Construction of Projects when the Authority's Participation and/or the Local Government's Participation related to such Bonds are to be used to retire said interim debt obligations.

(b) The Trustee shall from time to time pay out, or permit the withdrawal of, moneys credited to any Interim Financing Escrow Account, free and clear of any lien or pledge or assignment, for the purpose of effecting cash payments to Local Governments or retiring existing obligations of Local

Governments in accordance with the Series Resolution, upon receipt by the Trustee of a written requisition of the Authority signed by an Authorized Officer stating (i) the item for which the payment is to be made, (ii) the name of the person or party to whom the payment is to be made, and (iii) the amount to be paid.

(c) Upon the receipt of a Certificate signed by an Authorized Officer of the Authority to the effect that all disbursements from the Interim Financing Escrow Account contemplated by the applicable Series Resolution have been paid, the Trustee shall transfer any moneys remaining in said Account to the Construction Account.

(d) Moneys on deposit in the Interim Financing Escrow Account may be invested in Permitted Investments until expended in the same manner as moneys on deposit in the Costs of Issuance Account.

Redemption Account. (a) There shall be deposited in the Redemption Account such amount of the proceeds of the Bonds of any Series required to be deposited therein as shall be specified and determined by the Series Resolution to be sufficient to provide for the payment of the principal or Redemption Price of and interest on the Outstanding Series of Bonds or Prior Bonds, or portion thereof, designated by the Series Resolution for redemption or, if applicable, defeasance.

(b) The Trustee shall transfer or pay out moneys credited to the Redemption Account to the person or persons, at the times and in the amounts as the Series Resolution shall provide.

(c) The moneys credited to the Redemption Account, together with investment earnings thereon, shall be free and clear of any lien or pledge or assignment in trust created by the Trust Indenture.

(d) Moneys on deposit in the Redemption Account shall be invested in Defeasance Obligations until applied as provided by the Series Resolution.

(e) The Trustee shall transfer to the Debt Service Fund any amounts remaining in the Redemption Account upon the final payment of the principal and Redemption Price of and interest on the Bonds or Prior Bonds designated by the Series Resolution for payment or redemption.

Revenue Fund.

(1) The Authority shall cause all moneys received as Rental Payments pursuant to Lease and Participation Agreements, and Supplemental Rental Payments pursuant to Supplemental Leases to be deposited promptly with the Trustee, to the credit of the Revenue Fund.

(2) The Authority shall transfer all moneys received as Court Costs pursuant to KRS 24A.175(1), KRS 24A.180(5) and KRS 42.320(2)(b), together with all investment earnings therefrom, to the Trustee to the credit of the Revenue Fund on or before the last business day of each month. At any time the Authority holds moneys representing Court Costs pending the deposit required as described in this paragraph, the Authority shall keep said Court Costs segregated from all other State moneys for accounting purposes.

(3) The Trustee shall transfer moneys from the Revenue Fund to the following Accounts and Funds at the times and in the amounts hereinafter stated in the following sequence:

(a) There shall be transferred to the Interest Account, on the last business day of each month preceding an Interest Payment Date, an amount equal to the interest which will come due on the Bonds on said Interest Payment Date and all unpaid amounts of past due interest.

(b) There shall be transferred to the Principal Account, on the last business day of each month preceding an Interest Payment Date, an amount equal to the 50% of the Principal Installment which will come due on the Bonds on the next Principal Installment Date and all unpaid amounts of past due principal.

(c) There shall be transferred to the Debt Service Reserve such amount as will cause the amount on deposit therein to equal the Aggregate Debt Service Reserve Requirement, including for this purpose the reimbursement of an insurer or issuer of a credit facility for any moneys advanced pursuant to a surety bond or such credit facility procured by the Authority to meet the Aggregate Debt Service Reserve Requirement.

(d) There shall be transferred to the Bond Insurer amounts owed to it and not paid pursuant to (i) and (ii) above.

(e) Subject to the priority transfers enumerated in (3)(a) through (d) above, such transfers as are set forth in a Series Resolution.

(f) As required, but subject to the priority of the transfers enumerated in (3)(a) through (e) above, the amount remaining in the Revenue Fund on each May 1 and November 1 may be transferred to the Payment, Surplus and Operating Fund.

(4) Moneys on deposit in the Revenue Fund may be invested in Permitted Investments maturing or subject to redemption at the option of the holder thereof no later than the date for any required disbursement from the Revenue Fund.

Payment, Surplus and Operating Fund.

(1) There shall be deposited into the Payment, Surplus and Operating Fund the amounts transferred from the Revenue Fund.

(2) Moneys in the Payment, Surplus and Operating Fund shall be withdrawn and paid out from time to time for the purpose of (a) depositing funds to the Debt Service Fund to the extent amounts on deposit therein are not adequate to pay Interest and Principal Installments which are due and payable, (b) depositing funds in the Debt Service Reserve to the extent amounts in the Revenue Fund are not adequate to maintain therein the Aggregate Debt Service Reserve Requirement, (c) paying amounts due and payable to a Local Government under a Participation Agreement and (d) at the direction of an Authorized Officer, paying reasonable or necessary Operating Costs and when amounts permitted by clauses (c) and (d) are so withdrawn and paid out, such moneys shall be free and clear of any lien, pledge or assignment in trust created by the Trust Indenture.

(3) Notwithstanding anything in the Trust Indenture to the contrary, moneys in the Payment, Surplus and Operating Fund may be withdrawn and paid out by the Trustee to or at the direction of the Authority for any lawful purpose of the Authority, including, but not being limited to, (i) transfers to other Funds or Accounts created by the Trust Indenture, including the Debt Service Fund or (ii) for the purpose of carrying out the duties and responsibilities of the Authority set forth in the Act, including making grants to Local Governments.

(4) Amounts in the Payment, Surplus and Operating Fund may, in the discretion of the Authority, be invested in Permitted Investments maturing in such amounts and at such times as may be necessary to provide funds when needed. The Trustee may, and to the extent required for payments from the Payment, Surplus and Operating Fund shall, sell or duly present for redemption, any such Permitted Investments at any time, and the proceeds of such sale and of all payments at maturity and upon redemption of such Permitted Investments shall be held in the Payment, Surplus and Operating Fund unless otherwise transferred or expended pursuant to the provisions described above.

Debt Service Fund.

(1) There shall be deposited to the appropriate accounts of the Debt Service Fund (i) the amounts required to be transferred thereto from the Revenue Fund and (ii) accrued interest received upon the delivery of any Series of Bonds.

(2) The Trustee shall pay from the Interest Account to the Paying Agent for any of the Bonds (i) on the business day preceding each Interest Payment Date, the amounts required for the payment of interest on the Outstanding Bonds due on such date and (ii) on the day preceding the Redemption Date or date of purchase of any Bonds, the amounts required for the payment of accrued interest on Bonds redeemed or purchased for retirement unless the payment of such accrued interest shall be otherwise provided for, and in each such case, such amounts shall be applied by the Paying Agent to such payments.

(3) The Authority may direct the Trustee to, or in the absence of direction the Trustee shall, invest the moneys in the Interest Account in Permitted Investments so that the maturity date or date of redemption at the option of the holder shall be before the Interest Payment Date next succeeding the date upon which such investment is made and if such amounts are not disbursed on such Interest Payment Date, then in Permitted Investments that are redeemable at the option of the holder thereof at their purchase price.

(4) The Trustee shall pay from moneys credited to the Principal Account to the Paying Agent on the business day preceding each Principal Installment Date for any of the Outstanding Bonds, the amounts required for the payment of principal due on such date and such amounts shall be applied by the Paying Agent to such payments.

(5) The amount accumulated in the Principal Account for each Mandatory Sinking Fund Installment may, and if so directed by the Authority shall, be applied (together with amounts accumulated in the Interest Account with respect to interest on the Bonds for which such Mandatory Sinking Fund Installment was established) by the Trustee prior to the forty-fifth (45th) day preceding the due date of such Mandatory Sinking Fund Installment as follows:

(a) to the purchase of Bonds of the Series and maturity for which such Mandatory Sinking Fund Installment was established, at prices (including any brokerage and other charges) not exceeding the Redemption Price payable from Mandatory Sinking Fund Installments for such Bonds when such Bonds are redeemable by application of said Mandatory Sinking Fund Installments plus unpaid interest accrued to the date of purchase, such purchases to be made in such manner as the Trustee shall determine, or

(b) to the redemption, pursuant to the terms of the Trust Indenture, if such Bonds if then redeemable by their terms at the Redemption Price referred to in clause (a) above.

As soon as practicable after the forty-fifth (45th) day preceding the due date of any such Mandatory Sinking Fund Installment, the Trustee shall proceed to call for redemption on such due date, Bonds of the Series and maturity for which such Mandatory Sinking Fund Installment was established in such amount (after taking into account Bonds purchased pursuant to (i) above) as shall be necessary to complete the retirement of the principal amount specified for such Mandatory Sinking Fund Installment of the Bonds of such Series and maturity. The Trustee shall pay out of such Principal Account to the Paying Agent, on the business day preceding each such Redemption Date, the amount required for the redemption of the Bonds so called for redemption, and such amount shall be applied by said Paying Agent to such redemption.

(6) The Authority may direct the Trustee to, or in the absence of direction, the Trustee shall, invest the moneys in the Principal Account in Permitted Investments so that the maturity date or date of

redemption at the option of the holder shall be on or before the Principal Installment Date next succeeding the date when such investment is made and if such amounts are not disbursed on such Principal Installment Date, then in Permitted Investments that are redeemable at the option of the holder thereof at their purchase price.

(7) Upon any purchase or redemption of Term Bonds of any Series and maturity, other than by Mandatory Sinking Fund Installments, by use of moneys deposited in the Debt Service Fund from a source other than the Revenue Fund, the amount of future Mandatory Sinking Fund Installments for such Term Bonds shall be reduced (subject to \$5,000 rounding) by multiplying the amount of each applicable future Mandatory Sinking Fund Installment by the Redemption Ratio. The portion of any such Mandatory Sinking Fund Installment remaining after the deduction of any such amounts so credited (or the original amount of any such Mandatory Sinking Fund Installment if no such amounts shall have been credited) shall constitute the unsatisfied balance of such Mandatory Sinking Fund Installment for the purpose of the calculation of Principal Installments due on a such date.

Debt Service Reserve.

(1) There shall be deposited to the credit of the Debt Service Reserve (i) any proceeds of Bonds or a surety bond (or other credit facility) so provided to be deposited by any Series Resolution, (ii) any Pledged Receipts from the Revenue Fund required to be deposited therein and (iii) any moneys received on account of or in connection with Permitted Investments credited to the Debt Service Reserve.

(2) The Trustee shall use amounts on deposit in the Debt Service Reserve or amounts drawn under a surety bond (or other credit facility) held for the credit of the Debt Service Reserve for the payment of Principal Installments of, or interest on, any outstanding Bond, but only to the extent amounts in the Debt Service Fund and the Revenue Fund are not adequate for such purpose. If the Authority satisfies the entire Aggregate Debt Service Reserve Requirement with a surety bond or other credit facility, the Trustee shall only draw upon such surety bond or other credit facility to pay the Principal Installments of or interest on the Bonds. If the Authority satisfies the Aggregate Debt Service Reserve Requirement both by a deposit of moneys and a surety bond (or other credit facility), the Trustee shall draw pro rata from such moneys and upon such surety bond or other credit facility to make such payments. The Trustee is authorized and directed to draw upon such surety bond or other credit facility in order to meet any such deficiency in the Debt Service Fund.

(3) Any interest earned or sums realized as a result of investment of moneys in the Debt Service Reserve shall accrue to, and be a part of, the Debt Service Reserve, provided that any such interest earned or sums realized which cause the amount in the Debt Service Reserve to exceed the Aggregate Debt Service Reserve Requirement shall be transferred to the Revenue Fund.

(4) The value of amounts on deposit in the Debt Service Reserve and of each surety bond (or other credit facility) shall be determined as of each May 1 and November 1 prior to making any disbursements described in (3)(d), (e) and (f) under Revenue Fund above, as described in (2)(c) and (d) under Payment, Surplus and Operating Fund above and upon any draw thereon as provided in (2) above.

Investment of Funds.

(1) Except as otherwise provided for in the Trust Indenture:

(a) Investment obligations purchased as an investment of moneys in any Fund or Account held by the Authority or the Trustee under the provisions of the Trust Indenture shall be deemed at all times to be a part of such Fund or Account and the income or interest earned, gains realized or losses suffered by a Fund or Account due to the investment thereof shall be retained in, credited or charged thereto as the case may be;

(b) In computing the amount in all Funds, including the Accounts thereof, Permitted Investments purchased as an investment of moneys therein shall be valued at the lower of the market value or amortized cost thereof; provided that the value of a surety bond (or other credit facility) on deposit in the Debt Service Reserve shall be the face value thereof. Valuation as of any date of computation shall include the amount of interest or gain realized to such date; and

(c) The Trustee shall sell or present for redemption or exchange, any Permitted Investments purchased by it as an investment pursuant to the Trust Indenture whenever it shall be necessary in order to provide moneys to meet any payment or transfer from the Fund or Account for which such investment was made. The Trustee shall provide periodic statements to the Authority in writing, relating to the Permitted Investments held for the credit of each Fund or Account in its custody under the provisions of the Trust Indenture as of the end of the preceding month.

(2) It shall not be necessary for the Paying Agent to give security for the deposit of any moneys with it held in trust for the payment of principal of or Redemption Price, if any, or interest on any Bonds.

Conditions Precedent to Authentication and Delivery of Bonds. The Trustee shall authenticate and deliver, to or upon the order of the Authority, any of the Bonds authorized to be issued pursuant to the Trust Indenture and a Series Resolution only upon receipt by the Trustee of:

(1) A copy of the Trust Indenture and the applicable Series Resolution, each certified by an Authorized Officer of the Authority;

(2) The written order of the Authority as to the delivery of such Bonds signed by an Authorized Officer describing such Bonds to be authenticated and delivered, designating the purchaser or purchasers to whom such Bonds are to be delivered, and stating the purchase price of such Bonds;

(3) Except in the case of an issue of Refunding Bonds, an Accountant's Certificate stating in effect that annual Court Costs receipts plus annual Rental Payments from all Leases made and to be made with Local Governments shall be projected to be at least equal to 1.20 times maximum Annual Debt Service Requirement of the Outstanding Bonds and the Series of Bonds then proposed to be issued.

In the event the additional Series of Bonds proposed to be issued are to bear a variable or periodically adjustable interest rate, the calculations of maximum Annual Debt Service Requirement shall be made with the assumption the interest rate on the Bonds is the 30-year Revenue Bond Index as published in *The Bond Buyer* as of the month preceding the month in which the additional Series of Bonds are to be delivered (or similar index if same is no longer published). In the event any Outstanding Bonds have previously been issued on a variable rate basis, the calculation of maximum Annual Debt Service Requirement shall be made utilizing the greater of either (A) the highest interest rate on said variable rate Outstanding Bonds during the preceding 24 months; or (B) 10%.

(4) An opinion of Bond Counsel stating the opinion that the Trust Indenture and the applicable Series Resolution authorizing the Series of Bonds have been duly and lawfully adopted by the Authority; that the Trust Indenture and the applicable Series Resolution are in full force and effect and are valid and binding upon the Authority and enforceable in accordance with their terms; that the Trust Indenture creates a valid pledge of the Pledged Receipts and any other funds, assets and revenues of the Authority pledged for the payment of such Bonds; that upon the execution, authentication and delivery thereof, the Bonds of such Series will be duly and validly issued and will constitute valid and binding obligations of the Authority entitled to the benefits of the Trust Indenture and such applicable Series Resolution; and, to the extent the Series of Bonds are to be issued as "tax-exempt" Bonds, that at the time

of their delivery the receipt of interest on said Bonds will be excludable from the gross income of the recipients thereof for State and federal income tax purposes;

(5) A written order of the Authority signed by an Authorized Officer directing the deposit in the Debt Service Reserve of so much of the proceeds of the Bonds to be issued, or other funds of the Authority, upon their issuance, sale and delivery, as is required, after giving effect to the face value of any surety bonds (or other credit facilities) on deposit or procured for deposit in the Debt Service Reserve, to increase the aggregate amount then held by the Trustee in said Debt Service Reserve to the Aggregate Debt Service Reserve Requirement, assuming for such purposes that the proposed Bonds have been issued;

(6) Except in the case of an issue of Refunding Bonds, a certificate of an Authorized Officer of the Authority stating that the Authority is not in default in the performance of any of the covenants, conditions, agreements or provisions contained in the Trust Indenture;

(7) To the extent any Lease and Participation Agreements are to be entered into with respect to the issuance of such additional Bonds, an opinion of counsel that each such Lease and Participation Agreement has been duly authorized, executed and delivered by, and is a legally binding enforceable obligation of, the applicable Local Government;

(8) An executed counterpart of the Continuing Disclosure Agreement; and

(9) Such further documents, moneys and securities as are required by the provisions of the Trust Indenture or any Supplemental Trust Indenture.

Provisions for Refunding Issue. One or more Series of Refunding Bonds may be authenticated and delivered upon original issuance to refund all Outstanding Bonds or any Series of outstanding Bonds or any part of one or more Series of Outstanding Bonds without compliance with the requirements of (3) and (6) above so long as the maximum Annual Debt Service Requirement assuming issuance of such Refunding Bonds is no greater than the maximum Annual Debt Service Requirement prior to such issuance. Bonds of the Series of Refunding Bonds shall be issued in a principal amount sufficient, together with other moneys available therefor, to accomplish such refunding and to make such deposits required by the provisions of the Act, the Indenture and of the Series Resolution authorizing said Series of Refunding Bonds.

Tax Covenant. The Authority shall at all times do and perform all acts and things permitted by law and necessary or desirable in order to assure that interest paid by the Authority on the Bonds shall, for the purposes of Federal income taxation, be excludable from gross income under any valid provision of law. The establishment of a Rebate Fund is required in to which the Authority is required to deposit excess investment earnings for transfer to the federal government of the United States.

Budgets. The Treasurer of the Authority shall, at least 60 days prior to the close of each Bond Fiscal Year, prepare on behalf of the Authority, a preliminary budget covering its fiscal operations for all of the Authority's activities, including the Regional and Local Facilities Bond Programs, and file the same with the Trustee and with such officials of the State as may be required by the Act, as then amended. The Annual Budget shall at least set forth for such Bond fiscal Year the estimated Pledged Receipts, Principal Installments and interest due and payable or estimated to become due and payable during such Bond Fiscal Year and estimated Operating Costs.

Personnel and Servicing of Program. The Authority shall at all times appoint, retain and employ competent personnel for the purpose of carrying out its activities and shall establish and enforce reasonable rules, regulations, tests and standards governing the employment of such personnel at

reasonable compensation, salaries, fees and charges and all persons employed by the Authority shall be qualified for their respective positions.

General Covenant to Collect Rental Payments. The Authority generally covenants and agrees to take all actions and perform all rights of the Authority as set forth in the Lease and Participation Agreements and Supplemental Leases in a timely fashion and the Authority specifically assigns to the Trustee its right under each Lease to collect from the State Treasurer or Department or Corrections those amounts to which a Local Government which is delinquent in its Rental Payments would be entitled under the provisions of KRS 441.206, or such other then existing provision of law, from State Appropriations, to the extent of said delinquencies.

Revenue Covenant. If, during any fiscal year, the total amount received in Court Costs, Rental Payments and Supplemental Rental Payments is less than the Principal Installments and interest on the Bonds due and payable in such fiscal year, the Authority will request that the Governor of the Commonwealth of Kentucky request that the General Assembly of the Commonwealth of Kentucky amend KRS 24A.175(1), KRS 24A.180, KRS 42.320 or any other applicable law to provide that the amount of Court Costs payable to the Authority be increased so that the total amount received as Court Costs, Rental Payments and Supplemental Rental Payments will be, based on reasonable projections, no less than the Principal Installments and interest on the Bonds which will be due and payable in any future fiscal year.

Non-Impairment. The pledge of Court Costs under the Trust Indenture being a contractual obligation of the Authority for the benefit of the Bondholders, the Authority covenants to oppose, including, to the extent necessary, by appropriate legal action, the adoption or enforcement of any statute or regulation that would reduce the amount of aggregate annual Court Costs payable to the Authority as an impairment of such contractual obligation, if such reduction would cause the total amount of Court Costs, Rental Payments and Supplemental Rental Payments, based on reasonable projections, to be less than the Principal Installments and interest on the Bonds which are due and payable in any future fiscal year.

Trustee to Exercise Powers of Statutory Trustee. The Trustee is vested with all of the rights, powers and duties of a trustee permitted to be secured pursuant to the Act.

Events of Default. Each of the following events is an "Event of Default"; that is to say if:

(1) the Authority shall default in the payment of any Principal Installment of or Redemption Price, if any, on any Bond when and as the same shall become due, whether at maturity or upon call for redemption or otherwise; or

(2) payment of any installment of interest on any of the Bonds shall not be made when and as the same shall become due; or

(3) the Authority shall fail or refuse to comply with the provisions of the Act, or shall default in the performance or observance of any other of the covenants, agreements or conditions on its part contained in the Trust Indenture, any Series Resolution, any Supplemental Trust Indenture or the Bonds, and such failure, refusal or default shall continue for a period of 45 days after written notice thereof by the Trustee, provided that if the failure stated in such notice cannot be corrected within such period, such failure shall not constitute an event of default so long as corrective action is commenced and diligently pursued until such failure is corrected.

Remedies. Upon the happening and continuance of any Event Default specified in (1) and (2) above, the Trustee shall proceed, or upon the happening and continuance of any Event of Default specified in (3) above the Trustee may proceed, and upon the written request of the Registered Owners of

not less than 25% in principal amount of the Outstanding Bonds shall proceed, in its own name, subject to the provisions described under this heading, to protect and enforce its rights and the rights of the Registered Owners by such of the following remedies as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce such rights:

(1) by mandamus or other suit, action or proceeding at law or in equity, to enforce all rights of the Registered Owners, including the right to require the Authority to enforce, collect and receive Rental Payments required by Lease and Participation Agreements and Supplemental Leases adequate to carry out the covenants and agreements as to, and pledge of, the Pledged Receipts, and to require the Authority to carry out any and all other covenants or agreements with Registered Owners and to perform its duties under the Act;

(2) by bringing suit upon the Bonds;

(3) by action or suit in equity, require the Authority to account as if it were the trustee of an express trust for the Registered Owners of the Bonds;

(4) by action or suit in equity, enjoin any acts or things which may be unlawful or in violation of the rights of the Registered Owners of the Bonds;

(5) by declaring all Bonds due and payable and, if all defaults shall be made good, then, with the written consent of the Registered Owners of not less than 25% in principal amount of the Outstanding Bonds, by annulling such declaration and its consequences;

(6) in the event that all Bonds are declared due and payable, by selling Permitted Investments and all other assets of the Authority (to the extent not theretofore set aside for redemption of Bonds for which call has been made), and enforcing all Lease and Participation Agreements and Supplemental Leases to the fullest legal extent in the name of the Authority for the use and benefit of the Registered Owners of Bonds; or

(7) by action or suit for any and all other relief, including the appointment of a receiver to enforce the rights of the Registered Owners.

In the enforcement of any rights and remedies under the Trust Indenture, the Trustee shall be entitled to collect its expenses incident to the enforcement from funds of the Authority pledged under the Trust Indenture and shall have a lien upon all moneys held under the Trust Indenture for such purpose, and shall be entitled to sue for, enforce payment on and receive any and all amounts then or during any default becoming, and at any time remaining, due from the Authority for principal, Redemption Price, interest or otherwise, under any provision of the Trust Indenture or a Series Resolution or of the Bonds, and unpaid, with interest on overdue payments at the rate or rates of interest specified in such Bonds, together with any and all costs and expenses of collection and of all proceedings under the Trust Indenture and under such Bonds, without prejudice to any other right or remedy of the Trustee or of the Registered Owners, and to recover and enforce a judgment or decree against the Authority or Local Governments for any portion of such amounts remaining unpaid, with interest, costs and expenses, and to collect from any moneys available for such purpose, in any manner provided by law, the moneys adjudged or decreed to be payable.

Priority of Payments After Default. In the event that upon the happening and continuance of any Event of Default the funds held by the Trustee and the Paying Agent shall be insufficient for the payment of principal or Redemption Price, if any, and interest then due on the Bonds, such funds (other than funds held for the payment or redemption of particular Bonds which have theretofore become due at maturity or by call for redemption) and any other moneys received or collected by the Trustee acting pursuant to the Act and the Trust Indenture, after making provision for the payment of any expenses necessary in the

opinion of the Trustee to protect the interests of the Registered Owners of the Bonds, and for the payment of the charges and expenses and liabilities incurred and advances made by the Trustee, the Bond Registrar or any Paying Agent in the performance of their respective duties under the Trust Indenture, shall be applied as follows:

Unless the principal of all of the Bonds shall have become or have been declared due and payable:

FIRST, to the payment to the persons entitled thereto of all installments of interest then due in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installment, then to the payment thereof ratably, according to the amounts due on such installment, to the persons entitled thereto, without any discrimination or preference; and

SECOND, to the payment to the persons entitled thereto of the unpaid principal or Redemption Price of any Bonds which shall have become due, whether at maturity or by call for redemption, in the order of their due dates and, if the amounts available shall not be sufficient to pay in full all the Bonds due on any date, then to the payment thereof ratably, according to the amounts of principal or Redemption Price, if any, due on such date, to the persons entitled thereto, without any discrimination or preference.

If the principal of all of the Bonds shall have become or have been declared due and payable, to the payment of the principal and interest then due and unpaid upon the Bonds without preference or priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, or of any Bond over any other Bond, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or preference except as to any difference in the respective rates of interest specified in the Bonds.

Whenever moneys are to be applied by the Trustee pursuant to the provisions described above, such moneys shall be applied by the Trustee at such times, and from time to time, as the Trustee in its sole discretion shall determine, having due regard to the amount of such moneys available for application and the likelihood of additional money becoming available for such application in the future. The deposit of such moneys with the Paying Agent, or otherwise setting aside such moneys in trust for the proper purpose, shall constitute proper application by the Trustee, and the Trustee shall incur no liability whatsoever to the Authority, to any Registered Owner or to any other person for any delay in applying any such moneys, so long as the Trustee acts with reasonable diligence, having due regard for the circumstances, and ultimately applies the same in accordance with such provisions of the Trust Indenture as may be applicable at the time of application by the Trustee. Whenever the Trustee shall exercise such discretion in applying such moneys, it shall fix the date (which shall be an Interest Payment Date unless the Trustee shall deem another date more suitable) upon which such application is to be made and upon such date interest on the amounts of principal to be paid on such date shall cease to accrue. The Trustee shall give such notice as it may deem appropriate for the fixing of any such date.

Termination of Proceedings. In case any proceedings taken by the Trustee on account of any Event of Default shall have been discontinued or abandoned for any reason, then in every such case the Authority, the Trustee and the Registered Owners shall be restored to their former positions and rights under the Trust Indenture, respectively, and all rights, remedies, powers and duties of the Trustee shall continue as though no such proceeding had been taken.

Registered Owners' Direction of Proceedings. Anything in the Trust Indenture to the contrary notwithstanding, the Registered Owners of the majority in principal amount of the Bonds then Outstanding shall have the right by an instrument or concurrent instruments in writing executed and delivered to the Trustee, and upon indemnification of the Trustee, to direct the method of conducting all

remedial proceedings to be taken by the Trustee under the Trust Indenture, provided that such direction shall not be otherwise than in accordance with law or the provisions of the Trust Indenture, and that the Trustee shall have the right to decline to follow any such direction which in the opinion of the Trustee would be unjustly prejudicial to Registered Owners not parties to such direction.

Limitation on Rights of Registered Owners. No Registered Owner of any Bond shall have any right to institute any suit, action, mandamus or other proceeding in equity or at law under the Trust Indenture, or for the protection or enforcement of any right under the Trust Indenture or any right under law, unless such Registered Owner shall have given to the Trustee written notice of the Event of Default or breach of duty on account of which such suit, action or proceeding is to be taken, and unless the Registered Owners of not less than 25% in principal amount of the Bonds then Outstanding shall have made written request of the Trustee after the right to exercise such powers or right of action, as the case may be, shall have occurred, and shall have afforded the Trustee a reasonable opportunity either to proceed to exercise the powers granted in the Trust Indenture or granted under the law or to institute such action, suit or proceeding in its name and unless, also, there shall have been offered to the Trustee reasonable security and indemnity against the costs, expenses and liabilities to be incurred therein or thereby, and the Trustee shall have refused or neglected to comply with such request within a reasonable time; such notification, request and offer of indemnity are declared in every such case, at the option of the Trustee, to be conditions precedent to the execution of the powers under the Trust Indenture or for any other remedy under the Trust Indenture or under law. It is understood and intended that no one or more Registered Owners of the Bonds secured by the Trust Indenture shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Trust Indenture, or to enforce any right under the Trust Indenture or under law with respect to the Bonds or the Trust Indenture, except in the manner provided in the Trust Indenture, and that all proceedings at law or in equity shall be instituted, had and maintained in the manner provided in the Trust Indenture and for the benefit of all Registered Owners of the Outstanding Bonds. Nothing in the Trust Indenture contained shall affect or impair the right of any Registered Owner to the payment of the principal of and interest on his Bonds, or the obligation of the Authority to pay the principal of and interest on each Bond to the Registered Owner thereof at the time and place provided in said Bond.

Anything to the contrary notwithstanding contained in the Trust Indenture, each Registered Owner of any Bond by his acceptance thereof shall be deemed to have agreed that any court in its discretion may require, in any suit for the enforcement of any right or remedy under the Trust Indenture or any Series Resolution, or in any suit against the Trustee for any action taken or of an undertaking to pay the reasonable costs of such suit, and that such court may in its discretion assess reasonable costs, having due regard to the merits and good faith of the claims or defenses made by such party litigant, but the provisions of this paragraph shall not apply to any suit instituted by the Trustee, to any suit instituted by any Registered Owner, or group of Registered Owners, holding at least 25% in principal amount of Bonds Outstanding or to any suit instituted by any Registered Owner for the enforcement of the payment of the principal or Redemption Price of or interest on any Bond on or after the respective due date thereof expressed in such Bond.

Remedies Not Exclusive. No remedy conferred upon or reserved to the Trustee or to the Registered Owners of the Bonds is intended to be exclusive of any other remedy or remedies, and each and every such remedy shall be cumulative and shall be in addition to any other remedy given under the Trust Indenture or now or hereafter existing at law or in equity or by statute.

No Waiver of Default. No delay or omission of the Trustee or of any Registered Owner of the Bonds to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver of any such default or an acquiescence therein, and every power and remedy given by the Trust Indenture to the Trustee and the Registered Owners of the Bonds, respectively, may be exercised from time to time and as often as may be deemed expedient.

Notice of Event of Default. The Trustee shall give to the Registered Owners notice of each Event of Default under the Trust Indenture known to the Trustee within 30 days after knowledge of the occurrence thereof, unless such Event of Default shall have been remedied or cured before the giving of such notice, provided that, except in the case of default in the payment of the principal of or Redemption Price, if any, or interest on any of the Bonds, or in the making of any payment required to be made into the Bond Proceeds Fund, the Trustee shall be protected in withholding such notice if and so long as the Authority, its Executive Committee or a trust committee of members or responsible officers of the Trustee in good faith determines that the withholding of such notice is in the interests of the Registered Owners. Each such notice of Event of Default shall be given by the Trustee by mailing written notice thereof to all Registered Owners by regular United States Mail.

Lease Agreements

Conveyance of Title to Project. Each Local Government which has entered into a Lease has conveyed its Project to the Authority.

The Authority agrees to reconvey the Project to the Local Government upon the payment by the Local Government of all Rental Payments provided for under the Lease.

Lease of Project to Local Government. Each Project subject to a Lease is leased by the Authority to the Local Government for a current period ending June 30, 2005 for a Rental Payment equal to the total interest requirements becoming due on the Project Bonds during that Bond Fiscal Year. Each Lease has automatically renewed and shall continue to be automatically renewed on July 1 of each year for a period of one year at a time unless the Local Government shall give notice to the Authority and others not less than 60 days prior to a July 1.

In each year that the Lease is in effect, the Authority agrees that so long as the Local Government is current in its obligations under the Lease, the Authority shall contribute the Authority Participation toward the Rental Payments due under the Lease.

Each year's Rental Payments under the Lease are equal to the annual principal and interest requirements to become due on the Project Bonds, subject to the credit in favor of the Local Government for the payment of the Authority Participation. In addition, each Local Government will be obligated to pay the costs of operating, maintaining and insuring its Project.

Rental Payments As Annual Obligations of Local Government. Nothing contained in the Lease binds the Local Government to a renewal or the payment of Rental Payments for any but the current period unless the Local Government shall exercise its option to renew, in which event the Local Government obligates itself to make Rental Payments for such one-year renewal Lease Term. The Local Government's option to renew its Lease is deemed to have been exercised unless the required notice of termination is given. Each Local Government's governing body has declared that each Project constitutes a public project and has formally expressed its present intention to renew the Lease.

Local Government's Assignment of Interest in State Appropriations. Under the Lease the Local Government agrees that in the event it is delinquent in a Rental Payment for any period during which the Lease has been renewed, and said delinquency continues for a period of 30 days beyond the due date, then the Authority, or the Trustee acting on behalf of the Authority, may without further demand collect from the State Treasurer or the Department of Corrections, to the extent of the delinquent amount, those amounts to which the Local Government might be entitled under the provisions of KRS 441.007 or such other provisions of Kentucky law then existing relating to the appropriation of State funds to counties for correctional facilities. The Lease specifically states that nothing should be construed as an assignment of the Local Government's rights in appropriations for any period following a termination of the Lease by the Local Government.

Termination of Lease on Local Government's Failure to Renew. In the event the Local Government fails to renew the Lease in any year, then the Lease shall immediately terminate and all Rental Payments for the current year shall be due and collectible and the Local Government shall give immediate possession of the Project to the Authority.

Application of Insurance Proceeds. In the event any of the Project buildings are destroyed by hazards covered by casualty insurance, the Authority shall have the right to expend the proceeds to restore the property and if said proceeds are not so expended then same shall be applied to the redemption of outstanding Project Bonds. In the event of partial destruction, the proceeds of such insurance shall be applied solely for the purpose of making the necessary repairs and replacements.

Local Government's Option to Purchase Project. The Local Government shall have the right at any time to purchase from the Authority and secure the reconveyance of the Project upon the payment of the price equal to the principal amount of all Project Bonds then due and outstanding, together with a sum equal to the interest due or to become due on said Project Bonds until the retirement thereof, plus the redemption premium, if any. If provisions are made for the payment of all Project Bonds from County funds, then the Local Government's obligations under the Lease are terminated.

General Covenants of Local Government. The Local Government agrees that it will each year file with the appropriate agency of the State its proposed annual budget which shall contain an adequate allocation to provide for the payment of Rental Payments due under the Lease for any year in which the Lease is renewed and for the expenses of operating, maintaining and insuring the Project. In addition, the Local Government agrees that in the event it exercises its right not to renew its Lease, unless such non-renewal is precipitated by the purchase of its Project by the Local Government, the Local Government will not purchase, lease or rent any other facilities for the purpose of performing the functions or providing the services for which the Project was to be constructed until the complete payment and retirement of all of the Project Bonds.

The Local Government agrees to the Authority's assignment of all rights of the Authority under the Lease to the Trustees as additional security for the Project Bonds.

Participation Agreements

Those Participating Counties which are not utilizing the Authority as issuing agency and for whose Projects no Project Bonds have been issued have entered or will enter into Participation Agreements with the Authority under which the Local Government, in consideration of the Authority's grant of financial assistance for its Project, covenants and agrees to operate, maintain and insure the Project so long as the Authority's Bonds remain outstanding. Title to Projects which are the subject of Participation Agreements remains vested in the Local Government.

Series 2004 Resolution

Municipal Bond Insurance. The Series 2004 Resolution authorizes the Authorized Officers of the Authority to obtain the issuance of the Bond Insurance Policy pertaining to the Series 2004 Bonds.

While the Bond Insurance Policy is in effect, the following provisions, among others, shall apply instead of or in addition to the corresponding provisions of the Trust Indenture: (i) Any amendment of or supplement to the Trust Indenture requiring Bondholder consent shall also require the prior written consent of the Bond Insurer; (ii) the Bond Insurer, acting alone, shall have the right to direct all remedies upon the happening and continuance of an Event of Default, and there shall be no acceleration of the principal of the Series 2004 Bonds without the prior written consent of the Bond Insurer; (iii) in addition to the Events of Default listed in the Trust Indenture, a declaration of bankruptcy by the Authority shall be an Event of Default; and (iv) in the cases of defaults, other than payment defaults, the continuation of

such a default for a period of 30 days after the Trustee has given notice of the occurrence of such default shall be an Event of Default.

Series 2004 Resolution is a Contract. The provisions of the Series 2004 Resolution shall constitute a contract between the Authority, the Bond Insurer and the Bondholders, and after the issuance of any of the Series 2004 Bonds no change or alteration of any kind in the provisions of the Series 2004 Resolution may be made, except as provided the Series 2004 Resolution or as provided in the Trust Indenture for entering into Supplemental Trust Indentures.

APPENDIX D

BOOK-ENTRY-ONLY SYSTEM

The Series 2004 Bonds initially will be issued solely in book-entry form to be held in the book-entry only system maintained by The Depository Trust Company ("DTC"), New York, New York. So long as such book-entry system is used, only DTC will receive or have the right to receive physical delivery of Series 2004 Bonds and, except as otherwise provided herein with respect to tenders by beneficial owners of beneficial ownership interests, beneficial owners will not be or be considered to be, and will not have any rights as, owners or holders of the Series 2004 Bonds under the Trust Indenture.

The following information about the book-entry only system applicable to the Series 2004 Bonds has been supplied by DTC. Neither the Authority nor the Trustee makes any representations, warranties or guarantees with respect to its accuracy or completeness.

DTC will act as securities depository for the Series 2004 Bonds. The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Series 2004 Bond certificate will be issued for in the aggregate principal amount of the Series 2004 Bonds and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, FICC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of Series 2004 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2004 Bonds on DTC's records. The ownership interest of each actual purchaser of each Series 2004 Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial owners will not receive written confirmation from DTC of their purchase. Beneficial owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series 2004 Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of beneficial owners. Beneficial owners will not receive

certificates representing their ownership interests in Series 2004 Bonds, except in the event that use of the book-entry system for the Series 2004 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2004 Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Series 2004 Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual beneficial owners of the Series 2004 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series 2004 Bonds are credited, which may or may not be the beneficial owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to beneficial owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial owners of Series 2004 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series 2004 Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Series 2004 Bond documents. For example, beneficial owners of Series 2004 Bonds may wish to ascertain that the nominee holding the Series 2004 Bonds for their benefit has agreed to obtain and transmit notices to beneficial owners. In the alternative, beneficial owners may wish to provide their names and addresses to the Trustee and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Series 2004 Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Series 2004 Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Series 2004 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions, and interest payments on the Series 2004 Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Authority or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to beneficial owners will be governed by standing instructions and customary practices, as is the case with Series 2004 Bonds held for the accounts of customers in bearer form or registered in "street name" and will be the responsibility of such Participant and not of DTC or its nominee, the Trustee or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the beneficial owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Series 2004 Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, Series 2004 Bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series 2004 Bond certificates will be printed and delivered.

NEITHER THE AUTHORITY NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATION TO ANY DIRECT PARTICIPANT, INDIRECT PARTICIPANT OR ANY BENEFICIAL OWNER OR ANY OTHER PERSON NOT SHOWN ON THE REGISTRATION BOOKS OF THE TRUSTEE AS BEING A HOLDER WITH RESPECT TO: (1) THE SERIES 2004 BONDS; (2) THE ACCURACY OF ANY RECORDS MAINTAINED BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT; (3) THE PAYMENT BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY AMOUNT DUE TO ANY BENEFICIAL OWNER IN RESPECT OF THE PURCHASE PRICE OF TENDERED SERIES 2004 BONDS OR THE PRINCIPAL OR REDEMPTION PRICE OF OR INTEREST ON THE SERIES 2004 BONDS; (4) THE DELIVERY BY ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY NOTICE TO ANY BENEFICIAL OWNER WHICH IS REQUIRED OR PERMITTED UNDER THE TERMS OF THE INDENTURE TO BE GIVEN TO HOLDERS; (5) THE SELECTION OF THE BENEFICIAL OWNERS TO RECEIVE PAYMENT IN THE EVENT OF ANY PARTIAL REDEMPTION OF THE SERIES 2004 BONDS; OR (6) ANY CONSENT GIVEN OR OTHER ACTION TAKEN BY DTC AS HOLDER.

Each Beneficial Owner for whom a Direct Participant or Indirect Participant acquires an interest in the Series 2004 Bonds, as nominee, may desire to make arrangements with such Direct Participant or Indirect Participant to receive a credit balance in the records of such Direct Participant or Indirect Participant, to have all notices of redemption, elections to tender Series 2004 Bonds or other communications to or by DTC which may affect such Beneficial Owner forwarded in writing by such Direct Participant or Indirect Participant, and to have notification made of all debt service payments.

Beneficial owners may be charged a sum sufficient to cover any tax, fee, or other governmental charge that may be imposed in relation to any transfer or exchange of their interests in the Series 2004 Bonds.

The Authority cannot and does not give any assurances that DTC, Direct Participants, Indirect Participants or others will distribute payments of debt service on the Series 2004 Bonds made to DTC or its nominee as the registered owner, or any redemption or other notices, to the beneficial owners, or that they will do so on a timely basis, or that DTC, Direct Participants or Indirect Participants will serve and act in the manner described in this Official Statement.

The information in this Appendix D concerning DTC and DTC's book-entry system has been obtained from sources that the Authority believes to be reliable, but the Authority takes no responsibility for the accuracy thereof.

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APPENDIX E

FORM OF BOND COUNSEL OPINION FOR THE BONDS

[Date of delivery]

Kentucky Local Correctional Facilities
Construction Authority
Frankfort, KY 40601

Re: \$21,670,000 Kentucky Local Correctional Facilities Construction Authority
Multi-County Correctional Facilities Revenue Refunding Bonds, Series 2004

Ladies and Gentlemen:

We have acted as Bond Counsel in connection with the issuance and sale by the Kentucky Local Correctional Facilities Construction Authority (the "Authority"), of \$21,670,000 aggregate principal amount of Multi-County Correctional Facilities Revenue Refunding Bonds, Series 2004 (the "Bonds"). The Bonds are issuable as fully registered Bonds without coupons dated as of their date of delivery in the denomination of \$5,000 or any integral multiple thereof, bearing interest payable semiannually on May 1 and November 1 of each year commencing on May 1, 2005, at the rates per annum set forth in the schedule below and maturing on November 1, in each of the years and in the principal amounts as follows:

Maturity Year	Principal Amount	Interest Rate	Maturity Year	Principal Amount	Interest Rate
2005	\$1,845,000	3.00%	2010	\$2,170,000	5.25%
2006	1,940,000	3.00	2011	2,280,000	5.25
2007	1,995,000	2.25	2012	2,400,000	5.25
2008	2,040,000	3.00	2013	2,530,000	5.25
2009	2,105,000	3.00	2014	2,365,000	5.25

The Bonds are not subject to redemption prior to their maturity.

The Bonds have been authorized and issued by the Authority, pursuant to the Constitution and laws of the Commonwealth of Kentucky (the "Commonwealth"), including particularly Sections 441.605 to 441.695, inclusive, of the Kentucky Revised Statutes, as supplemented and amended (the "Act"), a Trust Indenture dated as of October 1, 2004 (the "Indenture") between the Authority and U.S. Bank National Association, as Trustee (the "Trustee"), and a series resolution adopted by the Authority on September 15, 2004 (the "Bond Resolution") for the purpose of providing funds (a) to refund the Authority's outstanding Multi-County Correctional Facilities Revenue Refunding Bonds, Series 1994 (the "Prior Bonds"), the proceeds of which were used to refund two earlier series of the Authority's revenue bonds, the proceeds of which were used in turn to pay the cost, in participation with certain counties of the Commonwealth, of constructing, acquiring, installing and equipping various local correctional facilities (collectively, the "Project") and (b) to pay the costs of issuance of the Bonds.

The Authority has covenanted in the Indenture to at all times do and perform all acts and things permitted by law and necessary or desirable in order to assure that the interest paid by the Authority on the Bonds shall, for purposes of federal income taxation, be excludable from the gross income of the recipient under any valid provision of law.

We have examined the laws of the Commonwealth, the Act, a certified copy of the Bond Resolution, an executed counterpart of the Indenture and of each Lease (as defined in the Indenture), certified copies of proceedings of the Authority authorizing the issuance of the Bonds, a copy of an executed bond of said issue and such other documents, records, certificates and opinions as we have deemed relevant and necessary in rendering this opinion.

From such examination, we are of the opinion that:

1. The Authority is an authority constituting an agency and instrumentality of the Commonwealth, duly organized and validly existing under the laws of the Commonwealth. The Authority has the legal right and authority to issue the Bonds.

2. The Bonds have been authorized and issued in accordance with the laws of the Commonwealth and constitute valid and binding special and limited obligations of the Authority, payable as to principal and interest solely and only from the Pledged Receipts, as defined in the Indenture. The Bonds do not pledge the general credit or taxing power, if any, of the Commonwealth, the Authority or any other agency or political subdivision of the Commonwealth.

3. The Indenture has been duly authorized, executed and delivered by the Authority and the Bond Resolution has been duly adopted by the Authority, and each constitutes a valid and binding obligation of the Authority, enforceable against the Authority in accordance with their respective terms.

4. Each Lease has been duly authorized, executed and delivered by the Authority, and represents a valid and binding agreement of the Authority, enforceable in accordance with its terms.

5. Assuming compliance by the Authority with certain covenants, including the covenant referred to in the fourth paragraph of this letter, under existing laws, regulations, rulings and judicial decisions, interest on the Bonds (including any original issue discount properly allocable to the owners thereof) is excluded from gross income for federal income tax purposes and is not a special preference item for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the Bonds, however, must be included in the "adjusted current earnings" of certain corporations (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Code) and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings (which includes tax-exempt interest) over its alternative minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The accrual or receipt of interest on the Bonds may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend upon the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences. Purchasers of the Bonds, particularly purchasers that are corporations (including S corporations and foreign corporations operating branches in the United States), property or casualty insurance companies, banks, thrifts or other financial institutions or certain recipients of Social Security or Railroad Retirement benefits, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred (or continued) indebtedness to purchase or carry tax-exempt obligations are advised to consult their tax advisors as to the tax consequences of purchasing or holding the Bonds.

6. Under the existing laws of the Commonwealth, interest on the Bonds is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Bonds are exempt from ad valorem taxation by the Commonwealth and all political subdivisions thereof.

The obligations of the Authority, and the enforceability thereof, with respect to the Bonds and the other documents described above are subject, in part, to the provisions of the bankruptcy laws of the United States of America and to other applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting creditors' rights generally, now or hereafter in effect. Certain of such obligations, and enforcement thereof, are also subject to general equity principles, which may limit the specific enforcement of certain remedies but which do not affect the validity of such documents.

We express no opinion as to the title to the Project, or the sufficiency in the Indenture, Leases, Bond Resolution or otherwise of the description of the Project, or the priority of any liens, charges or encumbrances on the Project.

Very truly yours,

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APPENDIX F

FORM OF MUNICIPAL BOND INSURANCE POLICY

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FINANCIAL GUARANTY INSURANCE POLICY
MBIA Insurance Corporation
Armonk, New York 10504

Policy No. [NUMBER]

MBIA Insurance Corporation (the "Insurer"), in consideration of the payment of the premium and subject to the terms of this policy, hereby unconditionally and irrevocably guarantees to any owner, as hereinafter defined, of the following described obligations, the full and complete payment required to be made by or on behalf of the Issuer to [PAYING AGENT/TRUSTEE] or its successor (the "Paying Agent") of an amount equal to (i) the principal of (either at the stated maturity or by any advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Obligations (as that term is defined below) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed hereby shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law. The amounts referred to in clauses (i) and (ii) of the preceding sentence shall be referred to herein collectively as the "Insured Amounts." "Obligations" shall mean:

[PAR]
[LEGAL NAME OF ISSUE]

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Insurer from the Paying Agent or any owner of an Obligation the payment of an Insured Amount for which is then due, that such required payment has not been made, the Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such Insured Amounts which are then due. Upon presentment and surrender of such Obligations or presentment of such other proof of ownership of the Obligations, together with any appropriate instruments of assignment to evidence the assignment of the Insured Amounts due on the Obligations as are paid by the Insurer, and appropriate instruments to effect the appointment of the Insurer as agent for such owners of the Obligations in any legal proceeding related to payment of Insured Amounts on the Obligations, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners, or the Paying Agent payment of the Insured Amounts due on such Obligations, less any amount held by the Paying Agent for the payment of such Insured Amounts and legally available therefore. This policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Obligation.

As used herein, the term "owner" shall mean the registered owner of any Obligation as indicated in the books maintained by the Paying Agent, the Issuer, or any designee of the Issuer for such purpose. The term owner shall not include the Issuer or any party whose agreement with the Issuer constitutes the underlying security for the Obligations.

Any service of process on the Insurer may be made to the Insurer at its offices located at 113 King Street, Armonk, New York 10504 and such service of process shall be valid and binding.

This policy is non-cancellable for any reason. The premium on this policy is not refundable for any reason including the payment prior to maturity of the Obligations.

IN WITNESS WHEREOF, the Insurer has caused this policy to be executed in facsimile on its behalf by its duly authorized officers, this [DAY] day of [MONTH, YEAR].

MBIA Insurance Corporation

President

Attest:

Assistant Secretary

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