KENTUCKY PRIVATE ACTIVITY BOND ALLOCATION COMMITTEE
MINUTES
February 16, 2006

The Kentucky Private Activity Bond Allocation Committee (the "Committee") meeting was called to order by Chairman John Farris, proxy for Robbie Rudolph, Secretary, Finance and Administration Cabinet, on Thursday, February 16, 2006 at 10:10 a.m. in Room 386 of the Capitol Annex, Frankfort, Kentucky. Other members present were: Katie Smith, proxy for Marvin E. Strong, Jr., Secretary, Cabinet for Economic Development; Allen Holt, proxy for Brad Cowgill, State Budget Director; and Edgar C. Ross, Controller, Finance and Administration Cabinet.

Chairman Farris declared that a quorum was present and verified that the press had been notified of the meeting.

The first item on the agenda was the approval of the January 5, 2006 minutes. A motion was made by Mr. Allen Holt and seconded by Mr. Edgar Ross to approve the minutes. **Motion CARRIED.**

Mr. F. Thomas Howard, Executive Director, Office of Financial Management, stated that under KRS 103.286, not less than 60 percent of the state volume cap is awarded annually to state issuers and 40 percent to the local issuers. Mr. Howard indicated that right now there is $333,872,400 of volume cap available. He stated that 60 percent of that, or $200,323,400, would be allocated to the state issuers. Mr. Rob Ramsey, Financial Analyst, Office of Financial Management stated that Kentucky Housing Corporation ("KHC") requested $160,258,720 and Kentucky Higher Education Student Loan Corporation ("KHESLC") requested $40,064,680. Mr. Howard indicated that the table under Attachment A was historical information of the allocation of volume cap to state issuers from 1990 through 2005. Mr. Howard stated a summary of key ratios and financial statement figures from KHC and KHESLC were also included in Attachment A to give a sense of their respective financial situations. Mr. Howard indicated that Mr. Walter Clare, Acting Chief Financial Officer, KHC, and Ms. Cathy Shipp, KHESLC, would present brief overviews of their programs and financial needs.

Ms. Shipp stated that KHESLC has had tremendous growth issuing $400,000,000 in bonds last year with plans to issue $500,000,000 in 2006. Ms. Shipp indicated that as of December 31, 2005, KHESLC had $1,443,737,422 in total assets and as of January 31, 2006 had a little over $1,400,000,000.

Mr. Clare stated that this was the fourth year that KHC and KHESLC have worked together to divide the state issuer pool. He went on to say that this was a very amiable way to divide the available cap that was not practiced in the past. Mr. Clare indicated that in 2005, KHC issued over $350,000,000 in single family mortgages, most of those being first time home buyers. He stated that calendar year 2005 was the biggest year for KHC to date. Mr. Clare indicated that in 2006 KHC hopes to fund around $500,000,000 in loans. Mr. Clare stated that KHC was blending taxable borrowings with its tax-exempt resources to meet demand.

He stated that at this time KHC is able to keep the mortgage rates on target but wants to utilize every bit of tax exempt authority available to help keep mortgage rates and costs down for the borrowers and KHC. Mr. Clare indicated that any refunding resources from past bond deals would be recycled from the same program. Mr. Clare stated that KHC was hoping for the biggest year to date for 2006.

Chairman Farris stated he would like to publicly thank both state issuers for working together and coming to an agreement on dividing volume cap. Mr. Clare stated that credit should be given to Mr. Charles Robinson, who recently resigned as CFO of KHESLC. Mr. Clare stated that Mr. Jim Ackinson and Mr. Charles Robinson came to the agreement for both state issuers. Chairman Farris stated with the absence of Mr. Robinson and Mr. Ackinson, hopefully KHC and KHESLC can still work together to benefit both state issuers.

Ms. Shipp stated that she is just filling in right now for KHESLC until a replacement for Mr. Robinson can be found.

With no further discussion a motion was made by Mr. Holt and seconded by Mr. Ross to approve KHC's request for $160,258,720 and KHESLC's request for $40,064,680 from the state issuer pool. **Motion CARRIED.**

Chairman Farris stated the next item on the agenda is proposed regulation changes. Mr. Howard stated that staff has been working closely with KHC and KHESLC to determine what the percentage allocation for the state and local issuers should be. Mr. Howard again indicated that in 2006 each state issuer is anticipating to fund $500,000,000 in loans. Mr. Howard reiterated that the statute states not less than 60 percent of the volume cap be allocated to the state issuers and that the administrative regulations allocate 60 percent for the state issuers and 40 percent for the local issuers. Mr. Howard stated with the increased demand of the state issuers and the decreased level of usage from the local issuer pool, staff has filed an administrative regulation change that would allocate 80 percent to the state issuers and 20 percent to local issuers. Mr. Howard also stated that the multi-family housing projects of the local issuer pool would be transferred to KHC and issued under their cap. Mr. Howard indicated that KHC has over $30,000,000 set aside to meet the demands of multi-family housing projects and they can use an additional allocation from their current cap to help meet the strategic needs in the Commonwealth. Mr. Howard stated that this would reduce the competition in the local issuer pool and move the focus to manufacturing and solid waste projects. Mr. Howard pointed out that manufacturing and solid waste projects who previously received allocation cap will drop to the bottom of the list and may not receive any allocation. He indicated that the graphs in Attachment D show the increase in allocation of cap to housing projects compared to manufacturing and solid waste projects. Mr. Howard indicated that the change in the administrative regulation was necessary to meet the demand of the state issuers and housing projects while fairly dispersing the local issuer pool among manufacturing and solid waste projects. Mr. Howard stated that a public hearing would be held on Friday, February 24, 2006 at 10:00 a.m. in Room 386 of the Capitol Annex to hear any concerns that may be raised by the community regarding changes in the regulations. Mr. Howard stated that any comments received from that public hearing would be considered when making amendments to the regulation that would be necessary to gain approval of the changes. Mr. Howard stated the regulation changes would be heard in March and if approved, would become effective in April. Mr. Howard stated that the Committee would then meet to allocate the local issuer pool and the balance that would be available to the state issuers so they would have continuity in managing their demand. Mr. Howard pointed out that both KHC and KHESLC have to blend taxable and tax exempt yield trends to prevent an imbalance in their net interest margins and spreads.

Mr. Ramsey stated the first chart shows the unused local issuer pool portion of the cap for the regular cycle and cap that was not applied for during the second cycle. Mr. Ramsey indicated from 1995 to date more volume cap is going unused. Mr. Ramsey stated the five year average for unused local cap in the first cycle is approximately $55,000,000. He indicated in 2004 and 2005 there was over $60,000,000 unused from the first and second cycle. Mr. Ramsey stated the second graph illustrates this better because it actually looks at percentages. He indicated the five year average for the regular cycle is approximately 45 percent, which is about half of the designation for the local issuers that is not being used. Mr. Ramsey indicated that it was even higher in last couple of years and this was the basis from which staff decided to raise the state issuer pool percentage from 60 percent to 80 percent. Mr. Ramsey stated the next chart reflects the increase in housing over time and the decrease in manufacturing and solid waste. Mr. Ramsey indicated manufacturing and solid waste had been receiving less cap as housing projects had been growing and utilizing the available volume cap. Mr. Ramsey stated this is another reason staff felt the state issuer pool percentage should be increased. Mr. Ramsey indicated the next graph reflects what would occur if the state and local issuer pools were split 80/20. Mr. Ramsey stated an 80/20 percent split starting in 2002 would be the primal allocation as there is never a point above 100 percent. He indicated the local issuers have been averaging about 20 percent usage over the past five years. Mr. Ramsey stated he also looked at other states and how volume cap was allocated. Mr. Ramsey indicated from 1993 to date the Kentucky average has been decreased for local issuer demand while housing has been increasing steadily. He stated Kentucky has outpaced the nation in decreased demand for local projects while outpacing the nation in increased demand for housing projects as is shown by the graph entitled "Kentucky Demand vs National Demand" in Attachment D. Mr. Ramsey stated the final attachment compares total available volume cap to local volume cap by housing, solid waste and manufacturing projects. He indicated from 1995 local cap has been decreasing in demand while housing has been outpacing everything. Mr. Ramsey stated for all these reasons, staff recommends raising the state issuer pool to 80 percent and decreasing the local issuer pool to 20 percent.

Mr. Holt asked what the statute states regarding exact percentages in regards to volume cap allocation. Mr. Howard indicated that the statute states that "... no less than 60 percent of private activity cap be reserved for state bond issuance authorities." Mr. Howard further stated that the actual regulation clearly defines the percentage amounts for the separate pools and that the regulations can be changed without changing the statutes. Mr. Howard indicated that in the future, if the housing market decreases substantially and manufacturing grows, the regulations could be amended to reflect the change in demand at that time.

A motion was made by Mr. Holt and seconded by Mr. Ross to support the proposed regulation changes. **Motion CARRIED.**

Mr. Howard stated there are two bills that have been filed that relate to this Committee. Mr. Howard indicated the first one was House Bill 42, which is related to non-cap projects dealing with urban renewal that the Committee has reviewed in recent years. He indicated the primary purpose of the bill is to restrict and provide additional requirements for the recording and approval process. Mr. Howard indicated the project approval would move to the State Local Finance Officer to hear instead of this Committee. Mr. Howard stated this is advantageous because they understand the impact on the local school and library tax districts, whereas this Committee is at a disadvantage in that regard. Mr. Howard indicated that staff does support House Bill 42. Mr. Howard stated that Senate Bill 28 directly relates to multi-family housing projects and the regulation changes that are being proposed would address that. Mr. Howard stated staff wanted to make sure the Committee was aware of these bills in case they were asked to take a look at them.

Chairman Farris asked if there was any other business. With no further business before the Committee, a motion was made by Mr. Ross and seconded by Ms. Smith to adjourn the meeting. **Motion CARRIED.**

Respectfully submitted,

F. Thomas Howard
Secretary