

**Kentucky Asset/Liability Commission
Minutes**

June 11, 2002

The Kentucky Asset/Liability Commission ("ALCo") meeting was called to order by Chairman T. Kevin Flanery in Room 264 of the Capitol Annex Building, Frankfort, Kentucky, on Tuesday, June 11, 2002, at 2:00 p.m.

Members present included: T. Kevin Flanery, Secretary, Finance and Administration Cabinet; Cindy James, proxy for Ben Chandler, Attorney General; Eugene Harrell, proxy for State Treasurer Jonathan Miller; Beth Jurek, proxy for James R. Ramsey, State Budget Director; and Alex Rose, proxy for Dana Mayton, Secretary, Revenue Cabinet. Kevin Mason, Legislative Research Commission, was also present at the meeting.

Secretary Flanery called for a motion to approve the minutes of the February 14, 2002 meeting. A motion to approve the minutes of the February 14, 2002 meeting was made by Mr. Rose and seconded by Mr. Harrell. Motion CARRIED.

Before introducing Resolution 2002-02, Secretary Flanery indicated to the Commission members that staff of the Office of Financial Management would be discussing proposed financings that will directly impact the steps the Commonwealth is taking to eliminate some of the uncertainty that exists without an enacted budget. Secretary Flanery explained that the Standard & Poors and Moody's Investors Service have placed the Commonwealth on CreditWatch and Watchlist, respectively. The actions were due to the current lack of an enacted budget, but he was hopeful that the Resolutions presented today for approval would give the ratings agencies some level of comfort in regard to the current state of the Commonwealth.

Secretary Flanery introduced Resolution 2002-02:

A RESOLUTION PROVIDING FOR THE AUTHORIZATION, ISSUANCE, SALE AND DELIVERY OF PROJECT NOTES, 2002 GENERAL FUND SERIES OF THE KENTUCKY ASSET/LIABILITY COMMISSION IN AN AGGREGATE PRINCIPAL AMOUNT NOT TO EXCEED \$15,000,000 FOR THE PURPOSE OF PROVIDING INTERIM FINANCING FOR AUTHORIZED PROJECTS IN ANTICIPATION OF THE ISSUANCE OF BONDS BY THE STATE PROPERTY AND BUILDINGS

COMMISSION; AND AUTHORIZING A TRUST INDENTURE, FINANCING AGREEMENT, NOTE PURCHASE AGREEMENT, PRELIMINARY OFFICIAL STATEMENT, OFFICIAL STATEMENT AND OTHER AGREEMENTS THAT MAY BE ENTERED INTO, ALL RELATED TO SUCH NOTES.

Gordon L. Mullis, Executive Director of the Office of Financial Management, informed the Commission that Resolution 2002-02 is similar to previous resolutions adopted by the Commission to issue Project Notes. The Resolution includes authorized but unissued projects for the Economic Development Bond Pool in an amount not to exceed \$15,000,000. All of the projects have been approved by KEDFA. Two remaining projects will be approved by the State Property and Buildings Commission meeting on June 11, 2002 and will formally complete the funding for these projects. Mr. Mullis indicated that UBS PaineWebber is the underwriter for this transaction. The Notes will be sold the week of June 24, 2002.

The issue will be closed and funds deposited in the bank prior to June 30, 2002. Mr. Mullis indicated this was an important issue because without an enacted budget any cash to be raised must be deposited or issues must be closed by the end of the fiscal year. Mr. Mullis indicated that if approved, this transaction would be presented to the Capital Projects and Bond Oversight Committee on June 18, 2002.

Alex Rose, proxy for Dana Mayton, Secretary of the Revenue Cabinet, asked if the Legislature had approved a budget would this Resolution be necessary. Mr. Mullis indicated that it would not be necessary to adopt the Resolution at this time. Mr. Mullis further indicated that ALCo normally would not issue notes for economic development bond projects. The lack of a budget creates a tremendous amount of uncertainty. Mr. Mullis continued that the Secretary of Finance, Secretary of Economic Development, State Budget Director and Governor Patton all desire that staff take advantage of the opportunity that the Resolutions afford. This action is consistent with what has been done in the past.

Secretary Flanery asked if there were any questions from the Commission members regarding the Resolution 2002-02. There were no questions. A motion was made by Mr. Rose and seconded by Ms. James. The motion carried and Resolution 2002-02 was **ADOPTED.**

Secretary Flanery introduced the second item on the agenda that was Resolution 2002-03:

A RESOLUTION PROVIDING FOR THE AUTHORIZATION, ISSUANCE, SALE AND DELIVERY OF PROJECT NOTES, 2002 AGENCY FUND SERIES OF THE KENTUCKY ASSET/LIABILITY COMMISSION IN AN AGGREGATE PRINCIPAL AMOUNT NOT TO EXCEED \$70,000,000 FOR THE PURPOSE OF PROVIDING INTERIM FINANCING FOR AUTHORIZED PROJECTS IN ANTICIPATION OF THE ISSUANCE OF BONDS BY THE STATE PROPERTY AND BUILDINGS COMMISSION OR A STATE AGENCY; AND AUTHORIZING A TRUST INDENTURE, FINANCING AGREEMENTS, NOTE PURCHASE AGREEMENT, PRELIMINARY OFFICIAL STATEMENT, OFFICIAL STATEMENT AND OTHER AGREEMENTS THAT MAY BE ENTERED INTO, ALL RELATED TO SUCH NOTES.

Mr. Mullis stated that much of the discussion regarding the General Fund Project Notes also applies to the Agency Fund Project Notes. The notable difference in the Resolutions is the number of projects that are being funded and the total amount of the Notes issued. The Resolution provides for an authorization of up to \$70 million that will fund the projects in Attachment B. These projects were either specific line item projects or part of the agency bond pool program that were previously approved but the projects had not required funding. For that reason, the authorization is being captured under the existing budget. However, only \$8 -10 million is being raised at this time. Mr. Mullis indicated that the cash would be raised and deposited in the bank by June 30, 2002. He indicated that all the projects for the University of Kentucky, except the Biomedical Sciences Research Building, would be funded at this time. Capitalized interest will be included to give assurance to the marketplace that payment will be received on the Notes at maturity. The Notes will be unsupported and will have a one-year fixed rate. Structuring of both of these Note programs has not been finalized. UBS PaineWebber will serve as underwriter and Peck Shaffer & Williams will serve as bond counsel for this issue. The Notes will be sold the week of June 24, 2002, and the issue will be closed and funds deposited in the bank prior to June 30, 2002.

Mr. Rose asked about the legality of the proposed Resolutions.

Secretary Flanery stated the Resolutions did not authorize unusual transactions, but because of the lack of a budget, the timing is crucial. Before the Asset/Liability Commission was formed, the Commonwealth raised cash before the funds were actually needed. Secretary Flanery indicated the actual transactions are fairly straightforward; and the Resolutions, if adopted, would allow for actions to be taken that would eliminate any issues that might arise regarding authorization.

Mr. Mullis stated that Peck, Shaffer & Williams has reviewed the Resolutions, the law surrounding the Commonwealth's authority to issue, this Commission's capacity to approve the issuance of the Notes, and the State Property and Buildings Commission's subsequent capacity to issue permanent bonds at some point in the future. Bond Counsel is very comfortable that as long as action is taken during an enacted budget period, the Commission is acting on the highest and safest ground. Mr. Mullis continued that a written opinion that indicates these transactions are a valid and true debt of the Commonwealth would be forthcoming from Peck, Shaffer & Williams. Mr. Mullis indicated that the Finance and Administration Cabinet General Counsel would also review and issue an opinion that the transactions meet the criteria of the law.

Secretary Flanery asked if there were any other comments or questions. There were no questions or comments. A motion was made by Mr. Rose and seconded by Mr. Harrell to adopt Resolution 2002-03. The motion carried and the Resolution was **ADOPTED**.

Secretary Flanery asked staff for a summary of the 2001 TRAN in Attachment C.

Terri Fugate, Financial Analyst, Office of Financial Management, indicated that the Commonwealth has \$650 million outstanding in General Fund Tax and Revenue Anticipation Notes. The maturity date for the Notes is June 26, 2002, and debt service will be paid on that date. The General Fund cash has been lower this year than in the past years. A low was reached in September when the expenditure target was met and again in November and April. Ms. Fugate informed the Commission that the Series B Notes saved the Commonwealth \$5 million in interest because they were variable rate notes and the Index Rate has dropped since selling the TRAN, which made the average interest rate approximately 1.6 percent. It is anticipated that the interest earned on

the TRAN proceeds will break even with the debt service that is to be paid on the TRAN.

Secretary Flanery indicated that the chart in Attachment C illustrates the spread between the Series A and Series B TRANs compared to the Short Term Pool and how the Series B TRAN was operating below the Short Term Pool. Secretary Flanery informed the Commission that the reason for this borrowing is that if funds were not borrowed through the TRAN at a tax-exempt rate, funds would have to be borrowed from funds like the Road Fund at taxable rates. Secretary Flanery asked if the TRAN would make a profit this year.

Mr. Mullis stated that it is expected the TRAN would meet its interest expense, but sufficient funds will not be available to make a deposit to the General Fund as has been done in previous fiscal years.

Mr. Mullis asked if Tom Howard would give the Commission a briefing on the 2002 TRAN.

Tom Howard, Deputy Executive Director of the Office of Financial Management, informed the Commission that staff met with various rating agencies and asked for guidance with respect to the 2002 TRAN. Mr. Howard stated that it was the general consensus of the rating agencies that no decisions should be made until the present fiscal year closed. It was suggested that the cash balance, steps to be taken to balance the budget through end of fiscal year, expenditure expectations and revenue receipts should be reviewed in mid-July and a decision on how to proceed with the TRAN would be made at that time. Mr. Howard indicated that the earliest possible date to enter the market would be early August 2002.

Secretary Flanery stated that the TRAN is not debt in the traditional sense because the cash is being borrowed and paid back all in the same fiscal year. Secretary Flanery pointed out that the General Fund is depleted of cash in August, and it is anticipated that the Commonwealth will lose the investment earnings the Commonwealth has had in the past.

Mr. Howard stated the possibility of having a larger amount of variable rate debt was discussed with the rating agencies because if rates go up or down, the Commonwealth should earn somewhat of a guaranteed spread.

Mr. Mullis stated that the cash flow problem would be exacerbated even more next fiscal year with the loss of all the Budget Reserve Trust Fund and the virtual lack of any fund balances of any note. There will be little or no funds in reserve and no borrowed money to deposit in the bank to replace the cash that is spent. Mr. Mullis indicated that staff would continue to analyze the proposed transaction to ensure that it is an appropriate one for the Commonwealth, and will keep the Commission informed of the progress of the transaction.

Secretary Flanery expressed his gratitude to the staff of the Office of Financial Management for their recommendation last year to structure transactions with fixed and variable rate Notes. If staff had not done this, the Commonwealth would have paid \$5 million more in interest expense.

Secretary Flanery asked if there was any further business to be brought before the Commission. With no further business before the Commission, a motion to adjourn was made by Mr. Rose and seconded by Mr. Harrell. Motion **CARRIED** and the meeting adjourned at 2:40 p.m.

Respectfully submitted,

Gordon L. Mullis, Secretary