

KENTUCKY PRIVATE ACTIVITY BOND ALLOCATION COMMITTEE
MINUTES
June 30, 2009

The Kentucky Private Activity Bond Allocation Committee (the "Committee") meeting was called to order by Chairman Lori Flanery, Deputy Secretary, and proxy for Jonathan Miller, Secretary, Finance and Administration Cabinet, on Tuesday, June 30, 2009 at 2:00 p.m. in Room 386 of the Capitol Annex, Frankfort, Kentucky. Other members present were Katie Smith, proxy for Larry Hayes, Interim Secretary, Cabinet for Economic Development, Ryan Green, proxy for Larry Hayes, Secretary, Governor's Executive Cabinet, Ed Ross, Controller, Finance and Administration Cabinet and Mary Lassiter, State Budget Director.

Other guests present were Tom Howard, Executive Director of the Office of Financial Management and Secretary to the Committee, Rob Ramsey, Tom Midkiff and Marcia Adams, staff from OFM, Travis Powell, Finance Legal Department, Kristi Culpepper from LRC, Rick McQuady from Kentucky Housing Corporation (KHC), Jim Ackinson from Kentucky Higher Education Student Loan Corporation (KHESLC), Bill Skees, Jr. Frost, Brown, Todd and David Mast from Utilities Dynamics, Paducah, KY.

Chairman Flanery verified with staff that a quorum was present and that the press had been notified of the meeting.

The first item on the agenda was the approval of the March 26, 2009 minutes. A motion was made by Mr. Ed Ross and the motion was seconded by Mr. Ryan Green to approve the minutes. **Motion CARRIED.**

2009 Available Volume Cap - Rob Ramsey stated that there was \$108,302,820 available for the local issuer Volume Cap Lottery. With only one application for \$26 million dollars by the Kentucky American Water Company for the County of Owen, staff recommends they receive that Volume Cap allocation. With that allocation, \$82,302,820 would remain, which would carryforward to be split amongst the State issuers, Kentucky Housing Corporation (KHC) and the Kentucky Higher Education Student Loan Corporation (KHESLC), as well as any of the \$26 million that may not be issued. Mr. Tom Howard stated that Kentucky American did receive an allocation in the original local issuer's pool and did issue the full amount of \$45,390,000. Mr. Ramsey added that the handout details the lottery results and the summary of the 2009 Volume Cap. A motion was made by Ms. Mary Lassiter to approve the awarding of the \$26 million Cap to Kentucky American Water that was seconded by Ms. Katie Smith. **Motion CARRIED.**

Mr. Howard added that the Committee would return at a later date and award any carryforward left unissued from the \$26 million from Kentucky American Water.

2009 State Issuer Pool – Mr. Ramsey pointed out applications from KHC and KHESLC and noted the two agencies had come to a prearranged agreement to split the Cap approximately 50/50, with KHC taking an additional \$539,230. Representatives from both organizations were present to answer any questions for the Committee. Ms. Lassiter asked what happens to the \$82.3 million carryforward. Mr. Ramsey and Mr. Howard confirmed that it must remain as local issuer Cap or pre-allocated carryforward until December 15,

2009. Mr. Jim Ackinson from KHESLC confirmed that neither agency with a need could request from this pool until that December period. Mr. Howard confirmed that to be the case. A motion was made by Ms. Mary Lassiter to approve the applications for the State Issuers Pool that was seconded by Mr. Ross. **Motion CARRIED.**

2008 Allocation Revisions – Mr. Ramsey stated that in 2008, two projects, V.G. Reed & Sons, Inc. and Neff Packaging Solutions, Inc. (items #10 & 11), failed to provide notices of issuance. With OFM unaware of those bonds being issued, we rolled the amount back into the KHC carryforward pool. These funds have been reallocated to the two projects with the consent of KHC and under bond counsel recommendation. We are going to revise the carryforward amount that KHC will be rolling forward from 2008 to 2009. That amount is \$103,430,785 as opposed to the original amount of \$109,648,793.

Mr. Howard informed the Committee that this is the first time for this type of occurrence and the current regulations have no penalty. Staff is entertaining discussions now or later to consider repercussions for not filing a notice of issuance. In this case, we had ample carryforward. Had it been used, the bonds would have been declared taxable. The owner of the bonds (the buyer) would be penalized and would have a claim against their bond counsel. This committee would not have any liability if we had not been notified that the bonds had been validly issued. Mr. Ross asked if we had a signed document that is used when these funds are allocated. Mr. Howard answered that there is a form on the website regarding notice of issuance and is part of the bond Cap allocation and they are required to return this within dates supplied by the committee in regard to lottery results and carryforward. Even though this is exceptionally rare, we may want to consider a penalty or sanction related to a future action that can be applied going forward. Ms. Lassiter questioned who the sanction would be against, the issuer or the bond counsel. Mr. Howard responded that depending on the situation and the project size, there may need to be a monetary penalty or fee to the project or barring the bond counsel or issuer for a period of time from submitting applications. These are all general ideas and nothing specific. Mr. Ackinson suggested an affidavit required by bond counsel of their initial allocation responding in the affirmative or negative that the bonds were issued. Mr. Howard reiterated that this information is supplied to counsel when Cap is awarded as well as NOI form and the additional notice would add another layer of security and responsibility by staff. We are not recommending anything at this time, welcome suggestions, and can follow up at a subsequent meeting. Deputy Flanery, reminded the proxies to share this information with their representatives and discuss with Mr. Howard their thoughts on this issue. A motion was made by Ms. Smith to approve the reallocations of CAP that was seconded by Ms. Lassiter. **Motion CARRIED**

2009 QECB Allocations - Mr. Ramsey continued to the summary of the Qualified Energy Conservation Bonds (QECB). Kentucky's QECB allocation for 2009 is \$44,291,000 and is based on population and a caveat which requires large, local governments (populations larger than 100,000) receive their proportionate share of the state allocation. This would be Lexington and Louisville Metro, due to their populations, Louisville Metro's \$5.8 million and Lexington's \$2.9 million dollars leave the state portion at \$35.6 million dollars. Mr. Howard added that the population estimates are based on different years. Staff verified the computations with Finance legal in that the regulation stated how the formulas were

intended to work. These are tax credit bonds with the purpose to reduce energy consumption in publicly owned buildings, and other provisions for developing Green Community programs, renewable resources, expenditures for different types of research for alternative fuels, mass commuting facilities, non-fossil fuel technology, and public campaigns to reduce energy consumption. These bonds are not a 100% tax credit; it is only 70% of the Treasury's posted tax credit rate. Meaning, the issuer will have to pay the 30% as interest and the remaining 70% would be treated as an above-the-line taxable item on the purchaser's income tax form but a dollar-for-dollar reduction once the tax liability is computed. This is an offshoot of what was originally the Q-ZAB program for school bonds, which has been refreshed and made more user friendly to eliminate the need for the issuance of tax credit bonds written at a discount or that carry supplemental interest payments. Effectively, you have a market-clearing rate of tax credits and here they are only providing a portion of the subsidy. It is complicated but a strong tool if the issuers can find investors with a tax liability for the tax credits.

Ms. Lassiter asked if this was a one-time allocation as part of the stimulus bill or an ongoing program and this committee will be asked to allocate these types of tax credit bonds every year. Mr. Howard answered that the Clean Renewable Energy Bond program is an ongoing authorization. This 2009 QECB has to be issued by December 31, 2010. Depending on the success of the program, it may be reauthorized under a different subsidy level rather than a 70% credit. At this time, we don't know if we will have to do this in the future. We are the only committee that deals with Volume Cap, we did not know of any other place that could properly allocate these authorizations to the local governments and the State. We may want to create a temporary emergency regulation with the criteria relating to what we are about to do. The state portion will not be issued without an appropriation to support the repayment of those obligations. Lexington & Louisville can move on this if they want but are not immediately prepared to do so.

Ms. Lassiter asked if the state portion is restricted only for state governmental purposes or is there some intention the state would sub-allocate to communities with populations smaller than 100,000. Mr. Howard continued that the restriction is related to governmental use so that could be local governmental use as well as state governmental use. That is something for the committee to consider when we talk more about the Recovery Zone aspects. As we develop policies, we would like to bring to the committee a proposal, that when necessary, we can file an appropriate regulation when in a position to issue these bonds. Mr. Ross asked if this would be a single issue or combined with something else. Mr. Howard answered that as an example where Lexington has only received 2.9 million dollars, they might waive their allocation and allow it to come back to the state with the understanding the state would loan them the money to take advantage of a larger issuance. Trying to find purchasers of tax-credit bonds is a new market that still has to be developed. The larger the issue, the more effective it will be for a corporate entity that needs to purchase the credits.

Ms. Smith asked if Louisville or Lexington wanted more, like \$6 million, would they have to give their \$5.7 million back to the State and ask for a loan. Mr. Howard responded that Louisville could issue their allocated amount immediately on their own or we would want to have discussions with them. The policy related to this reduction in public facilities hasn't been thoroughly vetted or discussed so I would hate to give someone a larger loan than they

may have received an allocation for. As of yet, we don't have a specific application as to how they are to be treated.

Deputy Flanery stated that we are approving the allocation, the actual numbers we have received for the metro areas of Louisville and Lexington and the state, according to the I.R.S. regulation. Mr. Howard added that we will come back with a state allocation with a specific program or application as it is developed and the locals can move forward immediately. Ms. Lassiter asked that if they did not issue by a certain date, would it revert back. Mr. Howard continued that his understanding was Congress has delegated specifically carved out allocations not only here but in the Recovery Zone publications as they intend for the locals to make those determinations. If the locals did not waive and return their allocation, I do not believe that the state will require them to return it. Deputy Flanery asked that at a future date, we ask the locals about their issuance and if they have not used it, would they be willing to give it to the state for the greater good. Mr. Howard agreed that would be the appropriate approach. Mr. Green asked if this is only for a year, there would be no carryforward unless the government decided to continue the program. Mr. Howard responded affirmatively. A motion was made by Ms. Lassiter that was seconded by Ms. Smith. **Motion CARRIED.**

2009 Recovery Zone Allocations – Mr. Ramsey reported to the Committee that attachment D shows a summary of the Recovery Zone bonds showing two types under this authorization, Recovery Zone Economic Development Bonds (RZEDB) as well as Recovery Zone Facility Bonds (RZFB) . Kentucky's RZEDB allocation is \$97,120,000 and the RZFB allocation is \$145,681,000. A detail list is also provided and the Federal Government has given guidance for the local distributions and breakdowns of both the Economic Development Bonds and the Facility Bonds. This is an informational item and with the guidance provided by the IRS, we believe no action is required but we do ask that the Committee be involved in the event of Cap waivers.

Mr. Howard described the difference between the two programs. Recovery Zone Bonds are a subset of Build America Bonds (BABs). This effectively makes four types of BAB's available, 1) the direct reimbursement program, which SPBC just issued, that receives a 35% direct subsidy from the United States Treasury. This program is specifically for new construction projects. 2) The 35% tax credit program is more lenient, meaning you can use it to refund your existing obligations or to fund working capital needs. 3) The Recovery Zone aspect of BABs are the Economic Development Bond programs consisting of \$10 billion allocated nationally which Kentucky received approximately \$95 million and the Facilities Bonds which were \$15 billion nationally and Kentucky's portion was approximately \$145 million. ED Bonds have to be issued by a governmental issuer and provide a 45% direct subsidy in your interest cost versus the 35% subsidy in the regular BABs. The difference is these have to be in an economically distressed area for specific projects but can even be used for job training targeted to spur recovery in depressed areas. 4) The Facilities Bonds are essentially Private Activity Bonds that would normally come under our traditional Volume Cap allocation process that are now exempt from the AMT. These need to be in depressed areas and spur economic development and to fund hard dollar costs for equipment, buildings etc. The RZFB is more like a conduit issue versus the State Property issue or local government issue for the direct subsidy. With the allocations being made directly to local

governments they have greater control over how those funds are used. The question becomes, what happens regarding a potential transfer and/or waiver of their Volume Cap allocation. There are a number of these that have very small allocations, \$16,000 and \$25,000 of which no one will issue bonds for that amount. Then the issue of waiver and transfer becomes paramount.

Mr. Howard continued that in reading the regulation there are two conclusions, one is that local governments may have the ability to transfer these directly without state involvement, which we need to confirm if this is permissible and does the Committee want to pursue this. Secondly, as it relates to a waiver, what action do we want to validate a waiver? What proof would we want - a metro council meeting or a county judge executive alone to say they are waiving their IRS allocation and giving it back to the state. If the authorization does come back, how would we set parameters to allocate it to projects in the state. Do we want to maintain similar characteristics to what we have for the other programs or given the broad nature of the program, do we want to more finely tune it. There are many things to consider in how we develop the appropriate parameters in appropriating any waiver of Volume Cap. Record keeping is imperative. With respect to notices of issuance or transfer; can we require them even though we don't allocate so we know if it has been used or not? Can we remind them of their responsibility to waive or transfer their allocation with a certain timeframe? The staff would like the Committee's and any outside input as to what might be the appropriate parameters for allocation of waived Volume Cap aside of the issues of transfers. Several issues are involved and not addressed in the regulations and given the discretion we have been provided by Congress, I believe we can mold this in limited application to the things the Committee would like. I would like permission to reach out to Economic Development, the Governor's Office of Economic Analysis and others who would like to be involved, to put together a preliminary recommendation for handling this. Also, to discuss rolling this piece into the regulation or at least an emergency regulation, because whatever we produce, needs to have public comment and adequate notice and hearing. The regulation process is the best way to do this and we know what we have agreed to and the extent this program may be extended as well, we would have a guideline for a subsequent allocation.

Mr. Ross asked if it was 45% on both these allocations. Mr. Howard answered it was 45% for RZEDB Governmental issues and the other is the relief from the AMT. It is a tremendous subsidy, 45% almost half your interest. For example, the 35% subsidy from the State Property and Buildings Commission issue was a net benefit to the Commonwealth of over \$25 million on a \$209 million dollar transaction over 20 years versus issuing traditional tax-exempt bonds. Ms. Lassiter asked if we knew how other states are dealing with this issue. Mr. Howard replied that his counterparts in other states are asking what everyone else was doing. Georgia is going through the same thought process that we are and wondered if we would share what we do today. Our intent is to establish on the Office of Financial Management (OFM) website a link for Recovery Zone and Energy Bonds so you can look at the regulations, the allocations, any associated forms and whatever criteria has been adopted and link to those. Mr. Howard asked a local bond counsel, Bill Skees, if he knew if anyone has done anything yet. Mr. Skees replied it was all too new and they are all trying to absorb it and figure out the nuances and regulations. There are some areas that are not clear at all, like the issue of transfer and he still did not know the answer.

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Mr. Ramsey pointed out the bonds must be issued by December 31, 2010. There is no specific action required at this time but this is a notification that these allocations have been made by the IRS. The communities are free to issue these bonds without State approval and we will come back to you with specific recommendations at a later date.


2009 Summary of HATA Cap – Mr. Ramsey noted that Kentucky still has its full \$132,810,201 of HATA Cap available, which will expire at the end of 2011.

Deputy Flanery asked if there were any questions from the Committee or the guests. Mr. Rick McQuady from KHC asked if an opportunity comes up and KHC needs additional bond Cap or if KHESLC (Jim Ackinson) needs additional bond Cap, can we negotiate where he can take part of my \$115 million in October if he needs it and I can take part of his if I need that. Mr. Howard responded that his view was that we would have the flexibility to reallocate the state pool but the committee would need to convene and acknowledge the reallocation of the additional Cap.

Mr. Ramsey added normally the Committee would not reconvene until time to allocate carryforward from the local issuer pool lottery in December. Mr. Howard added that with the allocation of state Volume Cap, that likely one of the two state issuers may not be able to use it but we could reallocate to the other one, if needed. We are willing on short notice to accommodate a request that the agencies would have given how market conditions move rapidly.

With no further business before the Committee, a motion was made by Mr. Green to adjourn the meeting and seconded by Ms. Smith. The meeting stands adjourned.

Respectfully submitted,



F. Thomas Howard
Secretary