Book- Entry-Only **Ratings: See "RATINGS" herein**

NEW ISSUE

Subject to compliance by the Commission, the Cabinet, the State Agency and others with certain covenants, in the opinion of Chapman and Cutler LLP, Bond Counsel, under present law, interest on the Series 2008 Bonds is excludible from gross income of the owners thereof for federal income tax purposes, and is not included as an item of tax preference in computing the federal alternative minimum tax for individuals and corporations, but such interest is taken into account in computing an adjustment used in determining the federal alternative minimum tax for certain corporations. It is also the opinion of Bond Counsel that under the laws of the Commonwealth of Kentucky, as presently enacted and construed, that the interest on the Series 2008 Bonds is exempt from the income tax imposed by the Commonwealth of Kentucky, and the Series 2008 Bonds are exempt from ad valorem taxation by the Commonwealth of Kentucky and all of its political subdivisions and taxing authorities. See "TAX MATTERS" herein for a more complete discussion.

$15,720,000
COMMONWEALTH OF KENTUCKY
State Property and Buildings Commission
Agency Fund Revenue Bonds, Project No. 91

Dated: Date of delivery **Due: April 1, as shown on inside cover**

The Agency Fund Revenue Bonds, Project No. 91 (the "Series 2008 Bonds") will be issued only as fully registered Bonds, and when issued, will be 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 2008 Bonds. Purchasers will not receive certificates representing their ownership interest in the Series 2008 Bonds purchased. So long as DTC or its nominee is the registered owner of the Series 2008 Bonds, payments of the principal of and interest due on the Series 2008 Bonds will be made directly to DTC. The Series 2008 Bonds will be issued in denominations of $5,000 or any integral multiple thereof, and will bear interest payable on each April 1 and October 1, commencing on April 1, 2009. Principal of, redemption premium, if any, and interest on the Series 2008 Bonds will be paid directly to DTC by U.S. Bank National Association, as Trustee and Paying Agent.

AMOUNTS, MATURITIES, INTEREST RATES, YIELDS AND CUSIP NUMBERS ON INSIDE COVER.

The Series 2008 Bonds are subject to redemption prior to maturity as described herein.

The Series 2008 Bonds are being issued by the State Property and Buildings Commission (the "Commission"), an independent agency of the Commonwealth of Kentucky (the "Commonwealth"), at the request of the Finance and Administration Cabinet of the Commonwealth (the "Cabinet") and the Kentucky River Authority (the "State Agency") pursuant to a Bond Resolution adopted by the Commission on September 15, 2008, as supplemented and amended on October 3, 2008 to (i) finance and refinance the Project described herein and refund the outstanding Project Notes, 2005 Agency Fund Second Series A-5 issued by the Kentucky Asset/Liability Commission, (ii) make the required deposit into the Reserve Fund (as described and defined herein) and (iii) pay costs of issuing the Series 2008 Bonds.

THE SERIES 2008 BONDS ARE SPECIAL AND LIMITED OBLIGATIONS OF THE COMMISSION. THE SERIES 2008 BONDS DO NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE COMMONWEALTH, OR A PLEDGE OF THE FULL FAITH AND CREDIT OR TAXING POWER OF THE COMMONWEALTH, BUT ARE PAYABLE SOLELY FROM AMOUNTS DEPOSITED IN CERTAIN FUNDS AND ACCOUNTS CREATED BY THE RESOLUTION AND FROM RENTAL INCOME DERIVED FROM THE BIENNIALLY RENEWABLE LEASE (ALL AS DESCRIBED AND DEFINED HEREIN) WITH THE CABINET AND THE STATE AGENCY, THE RENT FROM WHICH IS SUBJECT TO APPROPRIATION BY THE GENERAL ASSEMBLY OF THE COMMONWEALTH ON A BIENNIAL BASIS. THE SERIES 2008 BONDHOLDERS HAVE NO SECURITY INTEREST IN ANY PROPERTIES CONSTITUTING THE PROJECT OR ANY AMOUNTS DERIVED THEREFROM. See "SECURITY FOR THE SERIES 2008 BONDS" herein.

The Series 2008 Bonds are offered when, as and if issued and accepted by the Underwriters, subject to the approving legal opinion of Chapman and Cutler LLP, Bond Counsel. Certain legal matters will be passed on for the Underwriters by their counsel, Perkins Coie LLP. It is expected that delivery of the Series 2008 Bonds will be made on or about October 21, 2008, through the facilities of DTC, against payment therefor.

Morgan Stanley

Citi

J.J.B. Hilliard, W.L. Lyons, LLC	**NatCity Investments, Inc.**	**Morgan Keegan & Co., Inc.**
JP Morgan	**Wachovia Bank, N.A.**	**Edward D. Jones & Co., L.P.**
First Kentucky Securities Corp.	**Ross, Sinclaire & Associates, LLC**	**Merrill Lynch & Co.**

Dated: October 8, 2008

$15,720,000
COMMONWEALTH OF KENTUCKY
State Property and Buildings Commission
Agency Fund Revenue Bonds, Project No. 91

The Series 2008 Bonds mature on the dates, in the principal amounts, bear interest at the rate per annum and have yields as follows:

Maturity (April 1)	Principal Amount	Interest Rate	Yield	CUSIP†	Maturity (April 1)	Principal Amount	Interest Rate	Yield	CUSIP†
2010	$490,000	3.400%	3.400%	49151EV26	2015	$590,000	4.500%	4.600%	49151EV75
2011	505,000	3.750	3.750	49151EV34	2016	620,000	4.750	4.800	49151EV83
2012	525,000	4.000	4.050	49151EV42	2017	645,000	5.000	5.000	49151EV91
2013	545,000	4.000	4.150	49151EV59	2018	680,000	5.125	5.200	49151EW25
2014	565,000	4.250	4.400	49151EV67					

$4,955,000 5.750% Term Bonds due April 1, 2024 Yield 5.820% CUSIP No. 49151EW33
$5,600,000 5.750% Term Bonds due April 1, 2029 Yield 5.950% CUSIP No. 49151EW41

† Copyright 2008, American Bankers Association, CUSIP data herein are provided by Standard & Poor's, CUSIP Service Bureau, a Division of The McGraw-Hill Companies, Inc. The CUSIP numbers listed are being provided solely for the convenience of the Series 2008 Bondholders only at the time of issuance of the Series 2008 Bonds and the Commission does not make any representation with respect to such numbers or undertake any responsibility for their accuracy now or at any time in the future. The CUSIP number for a specific maturity is subject to being changed after the issuance of the Series 2008 Bonds as a result of various subsequent actions, including, but not limited to, a refunding in whole or in part of such maturity or as a result of the procurement of secondary market portfolio insurance or other similar enhancement by investors that is applicable to all or a portion of certain maturities of the Series 2008 Bonds.

COMMONWEALTH OF KENTUCKY
STATE PROPERTY AND BUILDINGS COMMISSION

Members

STEVEN L. BESHEAR
Governor
(Chairman of the Commission)

DANIEL MONGIARDO
Lieutenant Governor

JACK CONWAY
Attorney General

JONATHAN MILLER
Secretary
Finance and Administration Cabinet
(Executive Director of the Commission)

LARRY M. HAYES
Interim Secretary
Cabinet for Economic Development

MARY E. LASSITER
State Budget Director

EDGAR C. ROSS
State Controller

F. THOMAS HOWARD
Executive Director
Office of Financial Management
(Secretary to the Commission)

This Official Statement does not constitute an offer to sell the Series 2008 Bonds to any person, or the solicitation of an offer from any person to buy the Series 2008 Bonds, in any jurisdiction where such offer or such solicitation of an offer to buy would be unlawful. The information set forth herein is provided by the Commonwealth of Kentucky from 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 of the Underwriters. No dealer, salesman or any other person has been authorized to give any information or to make any representation, other than those contained in this Official Statement, in connection with the offering contained herein, and, if given or made, such information or representation must not be relied upon as having been authorized by the Commonwealth of Kentucky or the Underwriters. The information and expressions of opinion contained herein are subject to change without notice, and neither the delivery of this Official Statement nor the sale of any Series 2008 Bonds shall, under any circumstances, create any implication that there has been no change in the matters described herein since the date hereof. This Official Statement is submitted in connection with the issuance of the Series 2008 Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION OR AUTHORITY, NOR HAS SUCH FEDERAL OR ANY STATE SECURITIES COMMISSION OR AUTHORITY PASSED UPON THE ACCURACY OR ADEQUACY OF THIS OFFICIAL STATEMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH TEND TO STABILIZE OR MAINTAIN THE MARKET PRICE FOR THE SERIES 2008 BONDS ABOVE THE LEVELS WHICH WOULD OTHERWISE PREVAIL. SUCH ACTIVITIES, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

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(continued)

SUMMARY

The following information is furnished solely to provide limited introductory information regarding the Commission and the Series 2008 Bonds and does not purport to be comprehensive. Such information is qualified in its entirety by reference to the more detailed information and descriptions appearing elsewhere in this Official Statement and should be read together therewith. The terms used in this Summary and not otherwise defined shall have the respective meanings assigned to them elsewhere in this Official Statement. The offering of the Series 2008 Bonds is made only by means of the entire Official Statement, including the cover hereof and the Exhibits hereto. No person is authorized to make offers to sell, or solicit offers to buy, the Series 2008 Bonds unless the entire Official Statement is delivered in connection therewith.

The Commission	The State Property and Buildings Commission (the "Commission") is an independent agency of the Commonwealth of Kentucky (the "Commonwealth"). See "THE STATE PROPERTY AND BUILDINGS COMMISSION".
The Offering	The Commission is offering its $15,720,000 Agency Fund Revenue Bonds, Project No. 91 (the "Series 2008 Bonds").
Authority	The Series 2008 Bonds are being issued pursuant to the provisions of the Constitution and laws of the Commonwealth, including particularly Chapters 56 and 58 of the Kentucky Revised Statutes ("KRS") and a bond resolution (the "Resolution") adopted by the Commission on September 15, 2008, as supplemented and amended on October 3, 2008 (i) authorizing the issuance of the Series 2008 Bonds and (ii) approving a Lease dated as of October 1, 2008 (the "Lease") by and among the Commission, as lessor, and the Finance and Administration Cabinet of the Commonwealth (the "Cabinet") and the Kentucky River Authority (the "State Agency" and collectively with the Cabinet, the "Lessee").
Use of Proceeds	The Series 2008 Bonds are being issued to provide funds with which to (i) finance and refinance the Project described herein and refund the outstanding Project Notes, 2005 Agency Fund Second Series A-5 issued by the Kentucky Asset/Liability Commission (the "Project Notes"), (ii) make the required deposit into the Reserve Fund (as described and defined herein) and (iii) pay costs of issuing the Series 2008 Bonds.
Security	The Series 2008 Bonds and any Additional Bonds (as defined herein) issued under the Resolution (the Series 2008 Bonds and any such Additional Bonds being referred to collectively as the "Bonds") and the interest thereon are payable solely from the Revenues to be derived from the rental payments of the Cabinet and the State Agency to the Commission under the Lease. See "SECURITY FOR THE SERIES 2008 BONDS" and "SUMMARIES OF THE PRINCIPAL DOCUMENTS – The Lease".

The primary source for the payments due under the Lease will be rental payments made by the State Agency. The State Agency will make its rental payments due under the Lease from collections of certain fees paid by entities that withdraw water from the Kentucky River Basin. See "THE STATE AGENCY – Water-user Fees" and " – Tier II Fee Payers – Fiscal Year 2008."

The Bonds are further secured by amounts on deposit in the various funds and accounts established by the Resolution, including a debt service reserve fund (the "Reserve Fund") which is required to be maintained at a level equal to the maximum annual debt service requirement on the Bonds then outstanding (the "Reserve Fund Requirement"). The Commission will deposit, from proceeds of the Series 2008 Bonds, an amount equal to the initial Reserve Fund Requirement. See "SECURITY FOR THE SERIES 2008 BONDS – Debt Service Reserve Fund.

The Bonds are not secured by a lien on any of the properties constituting the Project (defined in the Resolution as the Project and any other public project included from time to time in the Lease) or any amounts derived therefrom.

THE SERIES 2008 BONDS ARE SPECIAL AND LIMITED OBLIGATIONS OF THE COMMISSION. THE SERIES 2008 BONDS DO NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE COMMONWEALTH, OR A PLEDGE OF THE FULL FAITH AND CREDIT OR TAXING POWER OF THE COMMONWEALTH, BUT ARE PAYABLE SOLELY FROM AMOUNTS DEPOSITED IN CERTAIN FUNDS AND ACCOUNTS CREATED BY THE RESOLUTION AND FROM RENTAL INCOME DERIVED FROM A BIENNIALLY RENEWABLE LEASE AGREEMENT WITH THE CABINET AND THE STATE AGENCY, THE RENTS FROM WHICH ARE SUBJECT TO APPROPRIATION BY THE GENERAL ASSEMBLY OF THE COMMONWEALTH ON A BIENNIAL BASIS. THE SERIES 2008 BONDHOLDERS HAVE NO SECURITY INTEREST IN ANY PROPERTIES CONSTITUTING THE PROJECT OR ANY AMOUNTS DERIVED THEREFROM.

Additional Bonds

The Resolution authorizes the issuance of obligations having a pledge on the Revenues on a parity with the lien of the Series 2008 Bonds (the "Additional Bonds") subject to the conditions set forth therein. See "ADDITIONAL BONDS".

Features of Series 2008 Bonds

The Series 2008 Bonds are being offered in the authorized denominations of $5,000 or any integral multiple thereof, with the principal maturities and at the interest rates and yields set forth on the inside cover hereof. The Series 2008 Bonds, when issued, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York, which will act as securities depository for the Series 2008 Bonds. Purchasers will not receive certificates representing their ownership interest in the Series 2008 Bonds purchased. So long as DTC or its nominee is the registered owner of the Series 2008 Bonds, payments of the principal of, premium, if any, and interest due on the Series 2008 Bonds will be made directly to DTC.

The Series 2008 Bonds will bear interest payable on each April 1 and October 1, commencing on April 1, 2009. Principal of, premium, if any, and interest on the Series 2008 Bonds will be paid directly to DTC by U.S. Bank National Association, as Trustee and Paying Agent (the "Trustee").

Optional Redemption The Series 2008 Bonds maturing on and after April 1, 2019, are subject to redemption at the option of the Commission on any date on or after April 1, 2018, in whole or in part, at a redemption price equal to 100% of the principal amount of the Series 2008 Bonds to be redeemed, plus accrued interest to the date fixed for redemption. See "THE SERIES 2008 BONDS – Redemption Provisions – *Optional Redemption*."

Mandatory Sinking Fund Redemption The Series 2008 Bonds maturing on April 1, 2024 and April 1, 2029 are subject to mandatory sinking fund redemption prior to maturity at a redemption price equal to 100% of the principal amount thereof being redeemed, plus accrued interest to the date fixed for redemption on April 1 of the years 2019 to 2024 and 2025 to 2029, respectively, and in each case, inclusive. See "THE SERIES 2008 BONDS – Redemption Provisions – *Mandatory Sinking Fund Redemption*."

It is expected that delivery of the Series 2008 Bonds will be made on or about October 21, 2008, against payment therefor.

Tax Status Subject to compliance by the Commission, the Cabinet, the State Agency and others with certain covenants, in the opinion of Chapman and Cutler LLP, Bond Counsel, under present law, interest on the Series 2008 Bonds is excludible from gross income of the owners thereof for federal income tax purposes, and is not included as an item of tax preference in computing the federal alternative minimum tax for individuals and corporations, but such interest is taken into account in computing an adjustment used in determining the federal alternative minimum tax for certain corporations. It is also the opinion of Bond Counsel, under the laws of the Commonwealth of Kentucky, as presently enacted and construed, that the interest on the Series 2008 Bonds is exempt from the income tax imposed by the Commonwealth of Kentucky, and the Series 2008 Bonds are exempt from ad valorem taxation by the Commonwealth of Kentucky and all of its political subdivisions and taxing authorities. See "TAX MATTERS" herein for a more complete discussion and EXHIBIT D – "FORM OF BOND COUNSEL OPINION FOR THE SERIES 2008 BONDS."

Continuing Disclosure The Series 2008 Bonds are subject to Rule 15c2-12 under the Securities and Exchange Act of 1934, as amended. In general, the Rule prohibits an underwriter from purchasing or selling municipal securities in an initial offering unless it has determined that the issuer of such securities has committed to provide annually, certain information, including audited financial information, and notice of various events described in the Rule, if material. In order to enable the purchaser to comply with the provisions of the Rule, the Commission will enter into a Continuing Disclosure Agreement (the "Disclosure Agreement") with the Trustee.

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 2008 Bonds is available by contacting the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601, (502) 564-2924; or, during the initial offering period, by contacting the representative of the Underwriters, Morgan Stanley & Co. Incorporated, 1585 Broadway, New York, New York 10036, (212) 761-1554.

OFFICIAL STATEMENT
Relating to

$15,720,000
COMMONWEALTH OF KENTUCKY
State Property and Buildings Commission
Agency Fund Revenue Bonds, Project No. 91

INTRODUCTION

This Official Statement, including the cover page and the exhibits attached hereto, provides information in connection with the issuance and sale by the State Property and Buildings Commission (the "Commission"), an independent agency of the Commonwealth of Kentucky (the "Commonwealth"), of its $15,720,000 Agency Fund Revenue Bonds, Project No. 91 (the "Series 2008 Bonds") issued at the request of the Finance and Administration Cabinet of the Commonwealth (the "Cabinet") and the Kentucky River Authority (the "State Agency") to provide funds with which to (i) finance and refinance the Project described herein and refund the outstanding Project Notes, 2005 Agency Fund Second Series A-5 issued by the Kentucky Asset/Liability Commission (the "Project Notes"), (ii) make the required deposit into the Reserve Fund (as described and defined herein) and (iii) pay costs of issuing the Series 2008 Bonds.

The Series 2008 Bonds have been authorized and issued pursuant to the Constitution and laws of the Commonwealth, including particularly Chapters 56 and 58 of the Kentucky Revised Statutes ("KRS"). The Commission has adopted a Bond Resolution on September 15, 2008, as supplemented and amended on October 3, 2008 (the "Resolution") authorizing the issuance of the Series 2008 Bonds and the execution and delivery of the Lease hereinafter described.

The Cabinet and the State Agency, jointly as lessee, have entered into a Lease dated as of October 1, 2008, with the Commission, as lessor (the "Lease"), to provide the Commission with amounts to pay the principal of and interest on the Series 2008 Bonds as they become due. The rentals payable under the Lease include amounts necessary to restore any deficiency in the Reserve Fund described herein and to pay certain fees and expenses. The primary source for the payments due under the Lease will be payments made by the State Agency from collections of certain fees paid by entities that withdraw water from the Kentucky River Basin. See "THE STATE AGENCY – Water-user Fees" and " – Tier II Fee Payers – Fiscal Year 2008." No assurance can be given that the State Agency will collect sufficient fees from water users to permit the Cabinet and the State Agency to make the rental payments due under the Lease.

The initial term of the Lease ends June 30, 2010, and the Lease renews automatically (unless terminated in writing by the last business day of the preceding May by the Cabinet or the State Agency) for successive biennial periods to and including the biennial period which includes the final maturity of the Series 2008 Bonds. The Lease requires the State Agency, for each biennial period of the Lease beginning July 1, 2010, to request legislative appropriations of "Agency Funds" in amounts sufficient to permit the State Agency to make rental payments to the Commission which amounts are designed to be sufficient to pay principal of and interest on the Series 2008 Bonds. The Cabinet agrees under the Lease that if a deficiency exists in the Reserve Fund or if the State Agency fails to make a request for an appropriation as described above, then the Cabinet will request a General Fund appropriation in an amount sufficient to allow the Cabinet to maintain the Reserve Fund Requirement in the Reserve Fund as required by the Resolution.

THE KENTUCKY GENERAL ASSEMBLY HAS NOT APPROPRIATED ANY AMOUNTS TO THE CABINET TO MAKE THE RENT PAYMENTS UNDER THE LEASE. THE ONLY

SOURCE OF PAYMENT OF PRINCIPAL OF AND INTEREST ON THE SERIES 2008 BONDS IS THE RENTAL INCOME DERIVED FROM THE LEASE.

The Commission has pledged to the payment of its obligations under the Resolution, payments to be received by the Commission from the Cabinet and the State Agency under the Lease. The Kentucky General Assembly has adopted a budget for the State Agency having amounts projected to be sufficient to pay required rent under the Lease. The required rent payments are designed to be sufficient to meet principal and interest requirements on the Bonds through June 30, 2010.

Under the provisions of the Constitution of the Commonwealth, the Cabinet and the State Agency are prohibited from entering into financing obligations extending beyond the biennial budget. The proposed budgets for the Cabinet and the State Agency are submitted to the General Assembly of the Commonwealth every two years and are subject to the discretion and approval of each successive regular or extraordinary session of the General Assembly of the Commonwealth. There can be no assurance (i) that the Cabinet or the State Agency will include rent payments in future budgets submitted to the General Assembly, (ii) that the General Assembly will appropriate amounts sufficient to enable the Cabinet or the State Agency to make rent payments under the Lease or (iii) that the Governor, in the performance of his or her obligation to balance the Commonwealth's annual budget, will not reduce or eliminate any such appropriations.

The appropriations to the State Agency, from which payment of the principal of and interest on the Series 2008 Bonds are derived, are "Agency Fund" appropriations and not "General Fund" appropriations. See "THE STATE AGENCY – Agency Fund Appropriations" for a discussion of the difference between Agency Fund appropriations and General Fund appropriations.

In addition to amounts to be received by the Commission as rent under the Lease, a debt service reserve fund (the "Reserve Fund") has been established under the Resolution as further security for the Series 2008 Bonds. The Commission is required to maintain an amount equal to the maximum annual debt service requirement from time to time on the outstanding Bonds (the "Reserve Fund Requirement") on deposit in the Reserve Fund. If amounts on deposit in the Reserve Fund are less than the Reserve Fund Requirement, the Cabinet and the State Agency are required to pay Additional Rent under the Lease until the amount in the Reserve Fund equals the Reserve Fund Requirement. The Cabinet has covenanted to seek a General Fund appropriation at each future session of the General Assembly, if there is a deficiency in the Reserve Fund or if the State Agency fails to make a request for an appropriation as described above, sufficient to remedy such deficiency. Proceeds of the Series 2008 Bonds in an amount equal to the initial Reserve Fund Requirement will be deposited in the Reserve Fund.

THE GENERAL ASSEMBLY OF THE COMMONWEALTH IS UNDER NO OBLIGATION TO MAKE APPROPRIATIONS FOR RENTAL PAYMENTS TO THE CABINET OR THE STATE AGENCY NOR IS THE CABINET OR THE STATE AGENCY UNDER ANY OBLIGATION TO RENEW THE LEASE. THE BONDS ARE PAYABLE SOLELY FROM AND SECURED BY AMOUNTS DEPOSITED IN CERTAIN FUNDS AND ACCOUNTS CREATED BY THE RESOLUTION AND FROM A PLEDGE OF RENTAL PAYMENTS UNDER THE LEASE AND ARE NOT SECURED BY ANY LIEN ON, OR INTEREST IN, THE PROPERTIES CONSTITUTING THE PROJECT OR ANY AMOUNTS DERIVED THEREFROM.

Brief descriptions of the Commonwealth, the Commission, the Resolution, the Series 2008 Bonds, the Lease, the Project, the Cabinet and the State Agency are included in this Official Statement. Capitalized terms not otherwise defined herein have the meanings assigned to them in the Resolution. All summaries of documents and agreements in this Official Statement are qualified in their entirety by reference to such documents and agreements, copies of which are available at the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601 (502) 564-2924.

THE SERIES 2008 BONDS

General

The Series 2008 Bonds are issuable only as fully registered Bonds. The Series 2008 Bonds will be issuable in the denominations of $5,000 or integral multiples thereof, will be dated the date of their delivery, and will bear interest payable on each April 1 and October 1, commencing on April 1, 2009, at the interest rates set forth on the inside cover of this Official Statement. U.S. Bank National Association is the trustee for the Series 2008 Bonds (the "Trustee").

Book-Entry-Only System

The Series 2008 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 2008 Bonds and Beneficial Owners will not be or be considered to be, and will not have any rights as, owners or holders of the Series 2008 Bonds under the Resolution. For additional information about DTC and the book-entry-only system see "EXHIBIT C – Book-Entry-Only System."

Redemption Provisions

Optional Redemption. The Series 2008 Bonds maturing before April 1, 2019, are not subject to optional redemption prior to maturity. The Series 2008 Bonds maturing on and after April 1, 2019, are subject to redemption at the option of the Commission on any date on or after April 1, 2018, in whole or in part, at a redemption price equal to 100% of the principal amount of the Series 2008 Bonds to be redeemed, plus accrued interest to the date fixed for redemption.

Mandatory Sinking Fund Redemption. The Series 2008 Bonds maturing on April 1, 2024 and April 1, 2029 (collectively, the "Term Bonds") are subject to mandatory sinking fund redemption prior to maturity at a redemption price equal to 100% of the principal amount thereof being redeemed, plus accrued interest to the date fixed for redemption on April 1 of the years and in the amounts set forth in the tables below:

Series 2008 Bonds Maturing on April 1, 2024

YEAR	PRINCIPAL AMOUNT
2019	$715,000
2020	755,000
2021	800,000
2022	845,000
2023	895,000
2024*	945,000

* Final Maturity

Bonds Maturing on April 1, 2029

YEAR	PRINCIPAL AMOUNT
2025	$1,000,000
2026	1,055,000
2027	1,115,000
2028	1,180,000
2029*	1,250,000

* Final Maturity

In lieu of mandatory sinking fund redemption, the Commission, or the Trustee on behalf of the Commission, may purchase Term Bonds at the most advantageous price obtainable, not to exceed the principal amount thereof plus accrued interest to the date of purchase. The purchase of such Series 2008 Bonds will be used to reduce the amount of Series 2008 Bonds of such maturity to be called by the Trustee on the next succeeding mandatory sinking fund redemption date. In the event that any of the Term Bonds are redeemed, the principal amount of the Term Bonds so redeemed shall be credited against mandatory sinking fund installments in such order as the Commission shall determine.

Notice of Redemption. At least thirty (30) days but not more than sixty (60) days before the date fixed for redemption of any Series 2008 Bonds, the Trustee shall cause a notice of redemption to be mailed, by regular United States first class mail, postage prepaid, to all owners of Series 2008 Bonds to be redeemed in whole or in part at their registered addresses. Failure to mail any notice or any defect therein in respect of any Series 2008 Bond shall not affect the validity of the redemption of any other Series 2008 Bond. Such redemption notice shall set forth the details with respect to the redemption. Any owner owning at least $1,000,000 in aggregate principal amount of the Series 2008 Bonds may request that a second copy of the notice of redemption be sent to a second address provided to the Trustee in writing. The notice of redemption shall set forth the complete title of the Series 2008 Bonds, the CUSIP numbers, the date of the issue, the serial numbers, the interest rate, the maturity date, the date fixed for redemption, the redemption price to be paid and, if less than all of the Series 2008 Bonds of any one maturity then Outstanding shall be called for redemption, the distinctive numbers and letters of such Series 2008 Bonds to be redeemed and, in the case of Series 2008 Bonds to be redeemed in part only, the portion of the principal amount thereof to be redeemed, and the place or places of redemption, including the name, address and phone number of a contact person. With respect to an optional redemption of any Series 2008 Bonds, unless moneys sufficient to pay the principal of and interest on the Series 2008 Bonds to be redeemed shall have been received by the Trustee prior to the giving of such notice of redemption, such notice may, at the option of the Commission, state that said redemption shall be conditional upon the receipt of such moneys by the Trustee on or prior to the date fixed for redemption. The notice of redemption shall also state that on the date fixed for redemption the redemption price will become due and payable upon each Series 2008 Bond or portion thereof so called for redemption prior to maturity, and that interest thereon shall cease to accrue from and after said date.

The Trustee also shall send a copy of such notice by registered or certified mail, overnight delivery service or electronic means for receipt not less than thirty-two (32) days before such redemption date to DTC, and at least two (2) national information services that disseminate notices of redemption of obligations such as the Series 2008 Bonds; provided, however, that such mailing shall not be a condition precedent to such redemption and failure to mail any such notice shall not affect the validity of any proceedings for the redemption of Series 2008 Bonds.

A second notice of redemption shall be given within sixty (60) days after the date fixed for redemption in the manner required above to the registered owners of redeemed Series 2008 Bonds which have not been presented for payment within thirty (30) days after the date fixed for redemption.

Any notice mailed as provided above, shall be conclusively presumed to have been duly given upon mailing, whether or not the owner of such Series 2008 Bonds receives the notice. Upon the giving of notice and the deposit of funds for redemption, interest on the Series 2008 Bonds so called for redemption shall cease to accrue after the date fixed for redemption.

SECURITY FOR THE SERIES 2008 BONDS

The Commission has pledged to the payment of its obligations under the Resolution payments to be received by the Commission from the Cabinet and the State Agency pursuant to the Lease. The primary source for the payments due under the Lease will be payments made by the State Agency from collections of certain fees paid by entities that withdraw water from the Kentucky River Basin. See "THE STATE AGENCY – Water-user Fees" and " – Tier II Fee Payers – Fiscal Year 2008." No assurance can be given that the State Agency will collect sufficient fees from water users to make the rental payments due under the Lease.

The Kentucky General Assembly has adopted a budget for the State Agency having amounts projected to be sufficient to pay required rent under the Lease through June 30, 2010. No funds have been appropriated directly to the Cabinet to enable the Cabinet to pay rent under the Lease. The required rent payments are designed to be sufficient to meet principal and interest requirements on the Series 2008 Bonds through June 30, 2010. The Lease will be automatically renewed unless a written notice of the election of the Cabinet or the State Agency not to renew, signed by the Secretary of the Cabinet and/or the Chairman of the State Agency, respectively, shall have been delivered to the Commission before the close of business on the last business day in May, immediately preceding the beginning of such succeeding renewal term.

The proposed budgets for the Cabinet and the State Agency are submitted to the General Assembly of the Commonwealth every two years and are subject to the discretion and approval of each successive regular or extraordinary session of the General Assembly of the Commonwealth. There can be no assurance (i) that the Cabinet or the State Agency will include rent payments in future budgets submitted to the General Assembly, (ii) that the General Assembly will appropriate amounts sufficient to enable the Cabinet or the State Agency to make rent payments under the Lease or (iii) that the Governor, in the performance of his or her obligation to balance the Commonwealth's annual budget, will not reduce or eliminate any such appropriations. The only source of funds for payment of rent under the Lease is rent received by the Commission from the State Agency under the Lease.

The appropriations to the State Agency, from which payment of the principal of and interest on the Bonds are derived, are "Agency Fund" appropriations and not "General Fund" appropriations. See "THE STATE AGENCY – Agency Fund Appropriation" for a discussion of the difference between Agency Fund appropriations and General Fund appropriations.

The Bonds are also secured by certain other funds and accounts pledged therefor and described in the Resolution, including the Reserve Fund. Except as described below, the Commission is required to maintain (i) an amount equal to the Reserve Fund Requirement on deposit in the Reserve Fund or (ii) a Reserve Fund Facility in an amount equal to the Reserve Fund Requirement, as described under "SUMMARIES OF THE PRINCIPAL DOCUMENTS – The Resolution" herein. If amounts on deposit in the Reserve Fund are less than the Reserve Fund Requirement, the Cabinet and the State Agency are required to pay Additional Rent under the Lease until the amount in the Reserve Fund equals the Reserve Fund Requirement. Although no funds have been appropriated from the General Fund to the Cabinet for the payment of rent or Additional Rent under the Lease, the Cabinet has covenanted in the Lease that it will seek a General Fund appropriation to replenish any deficiency in the Reserve Fund if such a deficiency exists or if the State Agency fails to make a request for an appropriation as described above. Proceeds of the Series 2008 Bonds in an amount equal to the initial Reserve Fund Requirement will be deposited in the Reserve Fund.

THE SERIES 2008 BONDS ARE SPECIAL AND LIMITED OBLIGATIONS OF THE COMMISSION AND ARE PAYABLE SOLELY FROM THE REVENUES AND FUNDS SPECIFICALLY PLEDGED FOR THE PAYMENT OF THE PRINCIPAL OF, PREMIUM, IF ANY, AND INTEREST ON THE SERIES 2008 BONDS.

At the time of issuance, the Series 2008 Bonds will be the only Bonds outstanding payable from the Revenues.

The Commission had outstanding bonds in the aggregate principal amount of $2,459,325,000 as of October 1, 2008. The Commission has further committed to issue its Revenue and Revenue Refunding Bonds, Project No. 90 in the amount of $375,000,000 (the "General Fund Bonds") and its Taxable Agency Fund Revenue Bonds, Project No. 92 in the amount of $4,975,000 for the Kentucky Department of Military Affairs (the "DMA Bonds"), which are expected to be issued simultaneously with the delivery of the 2008 Bonds. The DMA Bonds are payable from "Agency Fund" appropriations of the Department of Military Affairs. Upon the issuance of the 2008 Bonds, the General Fund Bonds and the DMA Bonds, the Commission will have a total of $2,812,775,000 aggregate principal amount of bonds outstanding.

ADDITIONAL BONDS

In the Resolution, the Commission reserves the right to issue bonds or obligations having a pledge on the Revenues (as hereinafter defined) which is on a parity with the lien of the Series 2008 Bonds (the "Additional Bonds") for the purpose of constructing or acquiring public projects of the State Agency to be included in the Lease, or for the purpose of refunding any of the Outstanding Bonds of the Commission, or for any combination of such purposes, but only provided the Commission shall have complied with the following requirements:

(i) The amounts required to have been credited to the respective funds and accounts in the Resolution, up to the date of authorization of said Additional Bonds shall have been credited to said respective funds and accounts; and

(ii) The Revenues Available for Debt Service for the immediately preceding Fiscal Year (for which audited financial statements are available), or the adjusted Revenues Available for Debt Service for said immediately preceding Fiscal Year, if such revenues are adjusted as provided in the Resolution, have been equal to not less than one hundred fifteen per cent (115%) of the maximum combined principal and interest requirements for any succeeding Fiscal Year during the life of the then Outstanding Bonds, of:

(A) all Outstanding Bonds,

(B) the Additional Bonds then proposed to be issued, and

(C) any other obligations payable from the Revenues Available for Debt Service.

For purposes of the application of this test, Revenues Available for Debt Service are to be evidenced by a certificate of an authorized officer of the State Agency.

In the event there shall have been a change in the rates charged by the State Agency that create Revenues Available for Debt Service from the rates in effect for the next preceding Fiscal Year (for which audited financial statements are available), which change is in effect at the time of the issuance of any such Additional Bonds, then the Revenues Available for Debt Service as described in this subparagraph (ii) shall be adjusted to reflect the Revenues Available for Debt Service for said next preceding Fiscal Year as they would have been had said then existing rates been in effect during all of said Fiscal Year. Any such adjusted Revenues Available for Debt Service shall be evidenced by a certificate of an authorized officer of the State Agency, which certificate shall be approved by the Commission prior to the issuance of the Additional Bonds and filed with the Secretary of the Commission upon its approval.

In addition, the Commission further reserves the right in the Resolution to issue Additional Bonds: (i) to refund any of the Outstanding Bonds, provided that the debt service on the Additional Bonds in each following Fiscal Year is no greater than the debt service on the Bonds being refunded; and (ii) to refund any of the Outstanding Bonds, provided such Additional Bonds are issued to refund bonds due within ninety (90) days of the date of the refunding, and for the payment of which no other funds are or will be available at the maturity thereof.

As a condition precedent to the issuance of Additional Bonds in all cases, the Commission, the Cabinet and the State Agency shall enter into an amendment of or a supplement to the Lease, providing for rentals sufficient to provide Revenues to pay the principal of, premium, if any, and interest on all of the Outstanding Bonds, to make up any deficiencies in the Reserve Fund and to pay all other costs under this Resolution.

See "SUMMARIES OF THE PRINCIPAL DOCUMENTS – The Lease – Additional Obligations" for a description of the terms under which the State Agency is authorized to incur obligations on a parity with its obligations to make rental payments under the Lease in connection with the Series 2008 Bonds.

PLAN OF FINANCE

The proceeds of the Series 2008 Bonds will be used by the Commission, the Cabinet and the State Agency to (i) finance and refinance the Project and refund the Project Notes, (ii) make the required deposit in the Reserve Fund and (iii) pay costs of issuing the Series 2008 Bonds. See "SOURCES AND USES OF FUNDS FOR THE SERIES 2008 BONDS" and "SUMMARIES OF THE PRINCIPAL DOCUMENTS" herein.

The proceeds of the Series 2008 Bonds required to refund the Project Notes will be deposited in the note payment fund maintained by the trustee for the Project Notes (the "Prior Trustee") and applied to the payment of the Project Notes on the next available call date for the Project Notes, which is December 4, 2008. Any amounts on deposit in the project fund created by the trust indenture for the Project Notes relating to the Project will be transferred to the Construction Fund created by the Resolution.

SOURCES AND USES OF FUNDS FOR THE SERIES 2008 BONDS

The following table sets forth the estimated sources and uses of the application of the funds related to the Series 2008 Bonds.

SOURCES OF FUNDS:	
Par Amount of Series 2008 Bonds	$15,720,000.00
Original Issue Discount	(184,184.05)
Equity Contribution	335,000.00
TOTAL SOURCES	$15,870,815.95
USES OF FUNDS:	
Refunding of the Project Notes	$14,025,000.00
Deposit to Reserve Fund	1,323,462.50
Deposit to Stabilization Fund	335,000.00
Costs of Issuance*	187,353.45
TOTAL USES	$15,870,815.95

* Includes underwriters' discount, legal fees, printing and miscellaneous costs.

THE PROJECT

The Project financed and refinanced with the proceeds of the Series 2008 Bonds consists of the construction of a full concrete cellular dam, to be known as Dam 9, near Lexington, Kentucky (the "Project"), which is being installed as a security measure in connection with the dam structure that is currently in place. The estimated cost of construction of the Project is approximately $14.7 million. Construction began on the Project in March, 2007 and is expected to be completed in February, 2009.

A portion of the proceeds of the Commission's Revenue and Revenue Refunding Bonds, Project No. 90, expected to be issued at approximately the same time as the Series 2008 Bonds, will be provided to the State Agency for the purpose of financing other public projects, and primarily for Dam 3, which is described for other purposes under "THE STATE AGENCY – Tier II Fee Payers – Fiscal Year 2008."

The Cabinet and the State Agency will lease the Project from the Commission under the Lease. For further information on the State Agency benefiting from the Project, see "THE STATE AGENCY" herein.

THE STATE PROPERTY AND BUILDINGS COMMISSION

General

The Commission is composed of the Governor (who is the Chairman of the Commission), the Lieutenant Governor, the Attorney General, the Secretary of the Finance and Administration Cabinet (who is the Executive Director of the Commission), the Secretary of the Cabinet for Economic Development, the State Budget Director and the State Controller. The State Budget Director and the State Controller were added to the Commission by Executive Order 2008-506 dated June 6, 2008 and effective June 16, 2008. The Office of Financial Management ("OFM") in the Finance and Administration Cabinet serves as staff to the Commission, and the Executive Director of the OFM serves as Secretary to the Commission. The Commission is an independent agency of the Commonwealth, created by KRS 56.450, with power, subject to approval by and in cooperation with the Cabinet, to finance the acquisition of real estate and the construction and equipping of building projects and other public projects for any agency of the Commonwealth.

KRS 56.450(4) authorizes the Commission, on application of any state agency of the Commonwealth, to issue revenue bonds in the Commission's name in accordance with the provisions of KRS Chapters 56 and 58, secured by and payable solely from all or any part of the revenues derived from the leasing of the project financed to such state agency. The Commission is authorized to execute lease agreements with those state agencies requesting the Commission to issue revenue bonds, which leases provide for the payment of lease rentals to the Commission in order to make principal and interest payments on the revenue bonds issued in the name of the Commission. The Cabinet has applied to the Commission to issue the Series 2008 Bonds secured by revenues from the Lease.

Future Financings

The 2005 General Assembly enacted a State Budget for the biennium ending June 30, 2006, which authorized $2.056 billion of bond funded capital projects. The General Fund authorization was $1,204 million; the Road Fund authorization was $450 million; Agency Funds were authorized at $251.7 million; and $150 million was authorized to be supported by the Federal Highway Trust Funds. The Road Fund and Federal Highway Trust Fund authorizations have been issued. A significant portion of the Agency Fund and General Fund projects have been permanently funded.

The 2006 General Assembly adopted a State Budget for the biennium ending June 30, 2008 which authorized an additional $2.3 billion of capital projects to be funded with debt. The General Fund authorization is $1,392.9 million; the Agency Fund authorizations total $267.5 million; while the Road Fund and Federal Highway Trust Fund authorizations are $350 million and $290 million, respectively. The Federal Highway Trust Fund and a portion of the Agency Fund, Road Fund and General Fund projects have been permanently funded.

The 2008 General Assembly adopted a State Budget for the biennium ending June 30, 2010 which authorized debt financing for projects totaling $1.659 billion to support various capital initiatives of the Commonwealth. Of the total authorization, $650.3 million is General Fund supported, $643.2 million is Agency Restricted Fund supported, $135 million is Road Fund supported and $231 million is Federal Highway Trust Fund supported bonds (Grant Anticipation Revenue Vehicle Bonds) designated for the Louisville-Southern Indiana Ohio River Bridges Project. This authorization is in addition to the authority to issue refunding bonds to refund outstanding issues. The proposed budget also includes $50 million of debt restructuring for fiscal relief in each of Fiscal Years 2009 and 2010.

The Kentucky General Assembly may authorize debt financing to support various capital initiatives of the Commonwealth in future sessions. Bonds may also be issued to refund outstanding Commission bonds.

THE FINANCE AND ADMINISTRATION CABINET

General. The Cabinet, created and governed by the provisions of KRS 12.020 and KRS 42.011, is a statutory administrative organization of the Commonwealth headed by the Secretary of the Cabinet, who is appointed by the Governor. The Secretary of the Cabinet is the chief financial officer of the Commonwealth.

Senate Bill 49 of the 2005 General Assembly reorganized the Finance and Administration Cabinet to assume the responsibilities of the former Revenue Cabinet and the Governor's Office of Technology. In addition to these responsibilities, Cabinet functions include, (1) coordination and supervision of the fiscal affairs and fiscal procedures of the Commonwealth; (2) accounting, fiscal reporting and auditing of Commonwealth accounts; (3) purchasing, storekeeping and control of property and stores; (4) the construction, maintenance and operation of public buildings, except those provided for the exclusive use of certain agencies; (5) providing administrative services of a financial nature to other agencies of state government; (6) the investment and management of all Commonwealth funds other than pension funds; and (7) oversight of the issuance and management of all debt incurred in the name of the Commonwealth or any agency thereof.

Department of Facilities and Support Services. The Department of Facilities and Support Services is responsible for the Commonwealth's capital construction program; real property acquisition, disposition and leasing services; the daily operation and maintenance of state-owned office properties and surplus property services.

Department of Revenue. The Department of Revenue is responsible for the administration and enforcement of all state revenue laws and for the assessment and collection of state taxes. The Department of Revenue bills and collects the tax revenue necessary to support the state services provided by the Commonwealth.

THE STATE AGENCY

General Information

The Kentucky River Authority was first established by the Kentucky General Assembly in 1986 to take over operation of the Kentucky River Locks and Dams 5 through 14 from the United States Army Corps of Engineers. The State Agency is now responsible for maintaining the 14 lock and dam structures on the Kentucky River. These structures were constructed by the United States Army Corps of Engineers for navigation purposes, but are now only used for recreational boating and water supply.

Following the drought of 1988, the State Agency was given a mission to protect and improve the waters of the Kentucky River through environmental management of the entire watershed. This was the first effort by the Commonwealth of Kentucky to protect a major water resource through watershed management. Watershed management recognizes that the focus of the river should not just be on the water flowing through it, but also including human activities throughout the basin that affect the amount and quality of water that flows through the basin.

The State Agency is charged with developing comprehensive plans for the management of the Kentucky River Basin (the "Basin"), including long range water supply, drought response and ground water protection plans. It is charged to adopt regulations to improve and coordinate water resource activities within the basin among state agencies. It is also charged to develop recreational areas within the Basin.

The State Agency is supported by water-user fees collected from facilities which withdraw water from the Basin. Exemptions are given to facilities using water for agricultural purposes. These fees are then passed on to the citizens in the Basin who purchase water or the product manufactured by use of the water resources.

The elements of the Authority's Mission Statement include (i) the maintenance and management of the water resources of the Basin; (ii) providing a clean water supply for the citizens of the Basin; (iii) providing leadership and a common forum for all stakeholders of the Basin and (iv) the promotion of the highest and best recreational uses of the water resources of the Basin.

The Board of the State Agency consists of 12 members, including the Secretary of the Energy and Environment Cabinet, the Secretary of the Finance and Administration Cabinet and ten members appointed by the Governor of the Commonwealth, representing citizens residing in the Basin, local government officials and engineers and other professionals in the area of water quality and management. The current Board members of the State Agency and their terms and background are as follows:

KENTUCKY RIVER AUTHORITY
BOARD MEMBERS

Member	Term Expires	Position
Mr. Robert Ware (Chairman) Lawrenceburg, Kentucky	September 18, 2009	A member residing in a county adjacent to the main stem of the Kentucky River
Mr. Randall Christopher (Vice-Chairman) Irvine, Kentucky	September 18, 2009	A member residing in a county adjacent to the main stem of the Kentucky River
Mr. Donald C. Haney Richmond, Kentucky	September 18, 2011	A member representing an expert in water quality
Mr. Warner J. Caines (Treasurer) Frankfort, Kentucky	September 18, 2008	A member representing registered engineers
The Honorable Michael D. Miller Mayor of Jackson, Kentucky	September 18, 2009	A member representing mayors from counties which obtain the major portion of their water supply from the Kentucky River
Mr. Daryl E. Newby Frankfort, Kentucky	September 18, 2009	A member residing in a county adjacent to Locks and Dams 1-4 of the Kentucky River
Mr. Randall C. Day Whitesburg, Kentucky	September 18, 2009	A member residing in a county to either the north, middle, or south forks of the Kentucky River
Mr. Rex Morgan Campbellsburg, Kentucky	September 18, 2008	A member residing in a county adjacent to the main stem of the Kentucky River
Mr. Ted Collins Franklin Co. Judge Executive Frankfort, Kentucky	September 18, 2009	A member representing a county judge executive from counties which obtain the major portion of their water supply from the Kentucky River
Mr. Tim Hazlette Nicholasville, Kentucky	September 18, 2011	A member residing in a county adjacent to the main stem of the Kentucky River
Mr. Jonathan Miller Secretary, Finance and Administration Cabinet Frankfort, Kentucky	*Ex Officio*	Secretary of Finance and Administration Cabinet

KENTUCKY RIVER AUTHORITY
BOARD MEMBERS

Member	Term Expires	Position
Mr. Len Peters Secretary, Energy and Environment Cabinet Frankfort, Kentucky	*Ex Officio*	Secretary of Energy and Environment Cabinet

The audited financial statements of the State Agency for Fiscal Years 2006 and 2007 are set forth in EXHIBIT A to this Official Statement.

Water-user Fees

The operations of the State Agency are supported by the collection of water-user fees (the "Fees") from entities that withdraw water from the Basin. There are two categories of Fees: Tier I fees, which are paid by all users for the benefit of the entire watershed (the "Tier I Fees") and Tier II fees, which are an additional charge on water withdrawn from the "Main Stem" of the Kentucky River, and are reserved for the maintenance and replacement of the Locks and Dams on the Kentucky River (the "Tier II Fees"). Tier I water fees are currently $.022 per thousand gallons of water withdrawn from any source within the boundaries of the Basin. The Tier II fee was increased on April 1, 2008 to its current rate of $.06 per thousand gallons of water from its prior rate of $.016 per thousand gallons of water.

The Fee rates are initially set for each year of the biennium to carry out the functions, projects and expenses authorized by the General Assembly. Fee rates may be amended as necessary to fund projects budgeted by the State Agency. Fees are collected quarterly and are deposited into a fund within the State Treasury.

The primary source for the payments due under the Lease will be payments made by the State Agency from collections of Tier II Fees.

Tier II Fee Payers – Fiscal Year 2008

In fiscal year 2008, 20 entities used 28,163,726,000 gallons of water and accounted for 100% of all Tier II Fees collected in that year. The following chart identifies the 10 largest water users and payers of Tier II Fees in fiscal year 2008:

Kentucky River Authority
Tier II Fee Payers
Fiscal Year 2008

	Water Usage (Gallons)	Tier II Fees per 1000 gal $0.016	% of Total Tier II Fees
Kentucky-American Water Co.	13,997,455,000	$373,976	49.4330%
Frankfort Electric and Water Plant Board	3,165,570,369	84,509	11.1706%
Richmond Water, Gas, and Sewage	2,318,243,904	62,401	8.2483%
Winchester Municipal Utilities	1,437,564,806	42,695	5.6435%
Nicholasville Water Works	1,424,945,800	38,737	5.1203%
Versailles Municipal Water Works	1,236,645,600	33,198	4.3882%
Harrodsburg Municipal Water Works	1,025,044,430	27,458	3.6295%
East Kentucky Power Cooperative	918,966,842	23,849	3.1524%
Lawrenceburg Municipal Water Works	780,179,000	21,686	2.8665%
Lancaster Municipal Water Works	519,637,000	13,825	1.8275%
Total	26,824,252,751	$722,334	95.4798%

One of the principal Tier II Fee payers has commenced construction of an additional water treatment plant adjacent to Dam 3 on the Kentucky River north of Frankfurt, near the border of Owen and Franklin Counties.

Historical Pro Forma Debt Service Coverage

The following table sets out the historical pro forma debt service coverage for the ten year period ending June 30, 2008, assuming the current Tier II Fee rate of $0.06 per 1,000 gallons of water used and the maximum annual debt service on the Series 2008 Bonds:

Kentucky River Authority
Tier II
Historical Pro Forma Debt Service Coverage

Period Ended June 30	Annual Water Usage (Gallons)	Tier II Fees per 1000 gal $0.060	Maximum Annual DS	Coverage
1999	27,268,420,572	$1,636,105	$1,323,463	1.24x
2000	27,917,803,909	1,675,068	1,323,463	1.27x
2001	28,143,364,251	1,688,602	1,323,463	1.28x
2002	28,244,065,261	1,694,644	1,323,463	1.28x
2003	29,432,587,408	1,765,955	1,323,463	1.33x
2004	28,594,670,180	1,715,680	1,323,463	1.30x
2005	25,483,457,513	1,529,007	1,323,463	1.16x
2006	28,487,932,629	1,709,276	1,323,463	1.29x
2007	27,881,340,169	1,672,880	1,323,463	1.26x
2008	28,131,180,185	1,687,871	1,323,463	1.28x

The State Agency expects revenues generated from Tier II Fees in subsequent fiscal years to be no less than the average of the most recent five fiscal years set forth above.

Agency Fund Appropriations

The budget of the Commonwealth is required to include all fund sources, which include General Funds, Road Funds, Federal Funds, Agency Funds and Tobacco Funds. The State Agency is required to develop and submit a balanced budget for consideration by the General Assembly during its regular session, which begins in January of each even-numbered year. Agency Funds of the State Agency are described in its financial statements included in EXHIBIT A.

The State Agency has agreed to include an amount sufficient for rent under the Lease in each budget request. Payments of rent related to the Series 2008 Bonds may only be made from Agency Funds available to the State Agency from Tier II Fees.

The Kentucky General Assembly has adopted the budget for the State Agency having amounts projected to be sufficient to enable the State Agency to pay required rents through June 30, 2010. The required rent payments are designed to be sufficient to meet principal and interest requirements on the Series 2008 Bonds through June 30, 2010.

Under the provisions of the Constitution of the Commonwealth, the State Agency is prohibited from entering into financing obligations extending beyond the biennial budget. The proposed budget for the State Agency is submitted to the General Assembly of the Commonwealth every two years, and is subject to the discretion and approval of each successive regular or extraordinary session of the General Assembly of the Commonwealth. There can be no assurance (i) that the State Agency will include rent payments in future budgets submitted to the General Assembly, (ii) that the General Assembly will appropriate amounts sufficient to enable the State Agency to make rent payments or (iii) that the Governor, in the performance of his or her obligation to balance the Commonwealth's annual budget, will not reduce or eliminate such appropriations.

THE COMMONWEALTH

The Commonwealth of Kentucky, nicknamed the Bluegrass State, was the first state west of the Alleghenies to be settled by pioneers. Kentucky is bounded by the Ohio River to the north and the Mississippi River to the west, and is bordered by the States of Illinois, Indiana, Ohio, West Virginia, Tennessee, Missouri and the Commonwealth of Virginia.

The Commonwealth's economy in many ways resembles a scaled-down version of the U.S. economy in its diversity. The Kentucky economy, once dominated by coal, horses, bourbon and tobacco has become a diversified modern economy illustrated by the fact that Kentucky's manufacturing employment concentration as a percentage of non-farm employment is now higher than the national average. In addition, Kentucky's nonmanufacturing industries have grown considerably in recent years, with strong gains in air transportation, health and business services, and retail trade. The Commonwealth's parks, horse breeding and racing industry, symbolized by the Kentucky Derby, play an important role in expanding the tourism industry in the Commonwealth.

Financial Information Regarding the Commonwealth

Information regarding debt issuing authorities of the Commonwealth is included in EXHIBIT A attached hereto.

The Commonwealth annually publishes *The Kentucky Comprehensive Annual Financial Report* with respect to the Fiscal Year of the Commonwealth most recently ended. *The Kentucky Comprehensive Annual Financial Report* includes certain financial statements of the Commonwealth as well as general financial information pertaining to the Accounting System and Budgetary Controls, Debt Administration, Cash Management, Risk Management, General Fund Budgetary Basis and Governmental Funds GAAP Basis. In addition, the Notes to Financial Statements as set forth in *The Kentucky Comprehensive Annual Financial Report* contain information regarding the basis of preparation of the Commonwealth's financial statements, Funds and Pension Plans. The "Statistical Section" of The *Kentucky Comprehensive Annual Financial Report* includes information on Commonwealth revenue sources, Commonwealth expenditures by function, taxes and tax sources, taxable property, assessed and estimated values, property tax, levies and collections, demographic statistics (population, per capita income and unemployment rate), construction and bank deposits, sources of personal income and largest Commonwealth manufacturers.

Certain Financial Information Incorporated by Reference;
Availability from NRMSIRs and the Commonwealth

The Kentucky Comprehensive Annual Financial Report for Fiscal Year 2007 is incorporated herein by reference. The Commonwealth has filed *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2007 with the following Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs") in accordance with SEC Rule 15c2-12:

(i) Bloomberg Municipal Repository
100 Business Park Drive
Skillman, New Jersey 08558
E-mail: munis@bloomberg.com
Tel: (609) 279-3225
Fax: (609) 279-5962

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

(iii) Interactive Data Pricing and Reference Data, Inc.
Attn: NRMSIR
100 William Street, 15th Floor
New York, New York 10038
E-mail: nrmsir@interactivedata.com
Tel: (212) 771-6999; 800-689-8466
Fax: (212) 771-7390

(iv) Standard & Poor's Securities Evaluations, Inc.
55 Water Street, 45th Floor
New York, New York 10041
E-mail: nrmsir_repository@sandp.com
Tel: (212) 438-4595
Fax: (212) 438-3975

A copy of *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2007 may be obtained from the NRMSIRs or from the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601, (502) 564-2924. Additionally, *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2007 and certain other fiscal years may be found on the Internet at:

http://finance.ky.gov/ourcabinet/caboff/ooc/ofm/debt/cafr.htm

Only information contained on the Internet web page identified above is incorporated herein and no additional information that may be reached from such page by linking to any other page should be considered to be incorporated herein.

The Commission will enter into a Continuing Disclosure Agreement in order to enable the purchaser of the Series 2008 Bonds to comply with the provisions of SEC Rule 15c2-12. See "CONTINUING DISCLOSURE AGREEMENT" herein. In addition, ongoing financial disclosure regarding the Commonwealth will be available through the filing by the Commonwealth of two documents entitled *The Kentucky Comprehensive Annual Financial Report* and *Supplementary Information to the Kentucky Comprehensive Annual Financial Report* (or successor reports) with the NRMSIRs as required under SEC Rule 15c2-12.

Budgetary Process in the Commonwealth

The General Assembly is required by the Kentucky Constitution to adopt measures providing for the state's revenues and appropriations for each fiscal year. The Governor is required by law to submit a biennial State Budget (the "State Budget") to the General Assembly during the legislative session held in each even numbered year. State Budgets have generally been adopted by the General Assembly during those legislative sessions, which end in mid-April, to be effective upon the Governor's signature for appropriations commencing for a two-year period beginning the following July 1.

In the two even numbered years prior to 2006, the regular legislative session of the General Assembly adjourned without adoption of a State Budget. On both occasions, the Governor signed Executive Orders authorizing the Secretary of the Finance and Administration Cabinet to issue warrants for the payment of all claims made by the Executive Branch of government in accordance with a Public Services Continuation Plan providing for the continued operation of state government in the absence of a legislatively adopted State Budget (the "Continuation Plan"). The Continuation Plans provided full spending authority for the total debt service payments. In both cases, the Kentucky General Assembly enacted a State Budget in November of the following odd numbered year, which incorporated the Continuation Plans and appropriated funds for the remainder of the biennium.

Fiscal Year 2006

The *Government-Wide Financial Statements* provide a broad view of the Commonwealth's operations in a manner similar to a private-sector business. The Commonwealth's combined net assets (governmental and business-type activities) totaled $17.9 billion at the end of 2006, as compared to $17.4 billion at the end of the previous year.

At $17.9 billion, the largest portion of the Commonwealth's net assets is invested in capital assets (e.g., land, infrastructures, buildings and improvements and machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The Commonwealth uses these capital assets to provide services to its citizens; therefore, these assets are not available for future spending.

The second largest portion of the Commonwealth's net assets, totaling $1.77 billion, is restricted and represents resources that are subject to either external restrictions or legislative restrictions on how they may be used. The remaining balance is unrestricted net assets. The unrestricted net assets, which if positive could be used at the Commonwealth's discretion, showed a negative balance of $1.80 billion. Therefore, no funds were available for discretionary purposes. A contributing factor to the negative balance is that liabilities are recognized on the government-wide statement of net assets when the obligation is incurred. Accordingly, the Commonwealth recognizes long-term liabilities (such as general bonded debt, compensated absences, unfunded employer pension cost, and contingent liabilities) on the statement of net assets.

The Commonwealth received program revenues of $8.7 billion and general revenues (including transfers) of $10.0 billion for total revenues of $18.7 billion during Fiscal Year 2006. Expenses for the Commonwealth during Fiscal Year 2006 were $18 billion, which resulted in a total increase of the Commonwealth's net assets in the amount of $662 million, net of contributions, transfers and special items.

As a result of the improving economy during the fiscal year, the net assets of governmental activities increased by $431 million or 2.47 percent. Approximately 56 percent of the governmental activities' total revenue came from taxes, while 34 percent resulted from grants and contributions (including federal aid). Overall, program revenues were insufficient to cover program expenses for governmental activities. Therefore, the net program expenses of these governmental activities were supported by general revenues, mainly taxes. As of the end of Fiscal Year 2006, the Commonwealth's governmental funds reported combined ending fund balances of $3.14 billion, an increase of $527 million in comparison with the prior year. The unreserved portion of fund balance ($2.36 billion), which is the portion of fund balance available for spending in the coming year, has increased to 75 percent of the total fund balance. The remainder of fund balance is reserved to indicate that it is not available for new spending.

The General Fund is the chief operating fund of the Commonwealth. At the end of Fiscal Year 2006, total fund balance reached $897 million, with an unreserved balance of $713 million. This compares to a General Fund unreserved Fund Balance of $593 million as of June 30, 2005. An unreserved fund balance represents the excess of the assets of the General Fund over its liabilities and reserved fund balance accounts. Reservations of fund balances of governmental funds represent amounts that are not available for appropriation. Examples of fund balance reservations reported include reserves for encumbrances, inventories and capital outlay.

The fund balance, of the Commonwealth's general fund, increased by $226 million during Fiscal Year 2006. This is a 33.8 percent increase in fund balance from the prior year. The contributing factors to this increase were continuing spending reduction efforts, an improving economy and tax reform.

The major special revenue funds had moderate increases in revenues and slight fluctuations in expenditures with no significant changes in fund balance. The major contributing factors include an increase in motor fuels tax receipts, in the Transportation Fund, increased benefit payments in the Federal Fund, and increased spending in the Transportation function in the Agency Revenue Fund.

The Commonwealth of Kentucky's bonded debt increased by $310 million to $3,546,468,000, a 9.57 percent increase during Fiscal Year 2006. No general obligation bonds were authorized or outstanding at June 30, 2006. The key factor in this increase was the issuance of new debt during fiscal year 2006.

Fiscal Year 2007

The Commonwealth's combined net assets (governmental and business-type activities) totaled $17.4 billion at the end of 2007, as compared to $17.9 billion at the end of the previous year.

The largest portion of the Commonwealth's net assets, $18.2 billion, is invested in capital assets (e.g., land, infrastructures, buildings and improvements and machinery and equipment), and minus any related debt, which is still outstanding and used to acquire those assets. The Commonwealth uses these capital assets to provide services to its citizens; therefore, these assets are not available for future spending.

The second largest portion of the Commonwealth's net assets, totaling $1.6 billion, is restricted and represents resources that are subject to either external restrictions or legislative restrictions on how they may be used. The remaining balance is unrestricted net assets. The unrestricted net assets, if they have a positive value, could be used at the Commonwealth's discretion. However, the unrestricted balance is a negative $2.4 billion; therefore funds are not available for discretionary purposes. A contributing factor to the negative balance is that liabilities are recognized on the government-wide statement of net assets when the obligation is incurred. Accordingly, the Commonwealth recognizes long-term liabilities (such as general bonded debt, compensated absences, unfunded employer pension cost, and contingent liabilities) on the statement of net assets.

The Commonwealth received program revenues of $9.5 billion and general revenues (including transfers) of $10.2 billion for total revenues of $19.7 billion during Fiscal Year 2007. Expenses for the Commonwealth during Fiscal Year 2007 were $20.2 billion, which resulted in a total decrease of the Commonwealth's net assets in the amount of $(507) million, net of contributions, transfers and special items.

The slowing economy, during Fiscal Year 2007, caused revenues to decline resulting in the decrease in net assets of governmental activities by $(466) million or 2.6 percent. Approximately 56 percent of the governmental activities' total revenue came from taxes, while 34 percent resulted from grants and contributions (including federal aid). Overall, program revenues were insufficient to cover program expenses for governmental activities. Therefore, the net program expenses of these governmental activities were supported by general revenues, mainly taxes.

As of the end of Fiscal Year 2007, the Commonwealth's governmental funds reported combined ending fund balances of $2.86 billion, a decrease of $(280) million in comparison with the prior year. The unreserved portion of fund balance ($1.86 billion), which is the portion of fund balance available for spending in the coming year, has increased to 65 percent of the total fund balance. The remainder of fund balance is reserved to indicate that it is not available for new spending.

The General Fund is the chief operating fund of the Commonwealth. At the end of Fiscal Year 2007, total fund balance reached $813 million, with an unreserved balance of $517 million. This compares to a General Fund unreserved Fund Balance of $713 million as of June 30, 2006. An unreserved fund balance represents the excess of the assets of the General Fund over its liabilities and reserved fund balance accounts. Reservations of fund balances of governmental funds represent amounts that are not available for appropriation. Examples of fund balance reservations reported include reserves for encumbrances, inventories and capital outlay.

The Commonwealth's general fund balance, after several years of growth, has decreased by $81 million during Fiscal Year 2007, which represents a decline of 9 percent, of the prior year balance. The slow economy which reduced tax revenues is the major factor for this decline.

The major special revenue funds had no significant changes in fund balances, however, some changes in a fund's revenues and/or expenditures, might be considered significant. These changes include an increase in motor fuels tax receipts, in the Transportation Fund; increased benefit payments in the Federal Fund, and increased spending in the Transportation function of the Agency Revenue Fund.

The Commonwealth of Kentucky's bonded debt decreased by $104 million to $3.4 billion, a 2.93 percent decrease during Fiscal Year 2007. The major factor in this decrease was the maturity of bonds outstanding and the issuance of notes for interim financing, rather than bonds. No general obligation bonds were authorized or outstanding at June 30, 2007.

Fiscal Year 2008 (Unaudited)

Fiscal Year 2008 General Fund revenues totaled $8,664.3 million versus $8,573.8 million for the prior fiscal year, which represents an increase of 1.1 percent. Actual revenues for Fiscal Year 2008 were $28 million above the official revised revenue estimate rendered in January 2008 by the Consensus Forecasting Group ("CFG") as modified by the 2008 General Assembly, which projected revenue growth of 0.7 percent. Tobacco tax receipts rose by 0.6 percent compared to the previous fiscal year. Reduced revenue estimates in December 2007 and January 2008 resulted in a budget reduction during Fiscal Year 2008.

Individual income tax receipts grew by 14.5 percent in FY 2008 compared to the previous fiscal year, due largely to a shift in the reporting requirement for limited liability pass-through entities. Sales and use tax receipts grew 2.1 percent, as the national housing slump and higher energy prices cut into consumers' ability to make other taxable purchases. Corporate income tax collections declined 56.0 percent due primarily to the offsetting factor affecting individual income tax receipts. The limited liability pass-through shift was the main contributor to the decline. Coal severance taxes increased by 5.0 percent in FY 2008 reflecting both increased volume and prices. Property tax receipts increased by 1.7 percent from the previous fiscal year. Meanwhile, Lottery receipts rose by 0.4 percent.

Fiscal Year 2009 (Unaudited)

On January 16, 2008, the CFG revised the official General Fund revenue estimate for Fiscal Year 2009 to $8,823.6 million; which is the estimated levels upon which the Fiscal Year 2009 budget was enacted. The official forecast reflects a 1.8 percent increase in General Fund receipts for Fiscal Year 2009 when compared to Fiscal Year 2008 actual receipts. The estimate excludes Phase I Tobacco Master Settlement Agreement ("MSA") payments, which are estimated by CFG to be $119.69 million in Fiscal Year 2009.

Fiscal Year 2009 General Fund actual revenues total $2,084.9 million through September 2008, an increase of 0.9 percent over the same period in Fiscal Year 2008. Based on year-to-date receipts, a 3.1 percent rate of growth is required in the final nine months of Fiscal Year 2009 to meet the revised official estimate.

General Fund revenues for September 2008 were $804.6 million, a decrease of 4.6 percent compared to September 2007. During September 2008, sales and use tax revenues dropped by 0.8 percent compared to the previous year. Individual income tax receipts rose 3.2 percent. Corporation income tax receipts fell 45.2 percent, more than offsetting the modest gains in the individual income tax. Property taxes fell 10.3 percent due to a reversal of the timing in the public service property account that inflated August collections. Coal severance tax receipts grew by 45.3 percent in September and are up 36.0 percent for the first quarter of Fiscal Year 2009. The Kentucky Lottery Corporation dividend payment for September 2008 was $15.5 million, up from $14.5 million last September.

Investment Policy

The Commonwealth's investments are governed by KRS 42.500 et seq. and KAR Title 200 Chapter 14. The State Investment Commission, comprised of the Governor, the Treasurer, Secretary of the Finance and Administration Cabinet and gubernatorial appointees of the Kentucky Banker's Association, is charged with the oversight of the Commonwealth's investment activities. The Commission is required to meet at least quarterly, and delegates day to-day investment management to the Office of Financial Management.

At August 31, 2008, the Commonwealth's operating portfolio was approximately $3.4 billion in cash and securities. The composition of investments was as follows: U.S. treasury securities (15%); securities issued by agencies and instrumentalities of the United States Government (24%); mortgage backed securities and collateralized mortgage obligations (16%); repurchase agreements collateralized by the aforementioned (14%); municipal securities (9%); and corporate and asset backed securities, including money market securities (22%). The portfolio had a current yield of 4.63% and an effective duration of 1.03 years.

The Commonwealth's investments are currently categorized into three investment pools: Short-term, Intermediate-term and Bond Proceeds Pools. The purpose of these pools is to provide economies of scale that enhance yield, ease administration and increase accountability and control. The Short-term Pool consists primarily of General Fund and related accounts and provides liquidity to the remaining pools. The Intermediate-term Pool represents Agency Fund investments, state held component unit funds and fiduciary fund accounts held for the benefit of others by the Commonwealth. The Bond Proceeds Pool is where bond proceeds for capital construction projects are deposited until expended for their intended purpose.

The Commonwealth engages in selective derivative transactions. These transactions are entered into only with an abundance of caution and for specific hedge applications to minimize yield volatility in the portfolio. The State Investment Commission expressly prohibits the use of margin or other leveraging techniques. The Commonwealth executes a variety of transactions which may be considered derivative transactions, which include: the securities lending program, over-the-counter treasury options, interest rate swaps, mortgage backed securities, collateralized mortgage obligations and asset backed securities.

The Commonwealth has used over-the-counter treasury options since the mid-1980s to hedge and add value to the portfolio of treasury securities. These transactions involve the purchase and sale of put and call options on a covered basis, holding either cash or securities sufficient to meet the obligation should it be exercised. The State Investment Commission limits the total option commitment to no more than twenty percent of the total portfolio of treasury and agency securities. Historically, actual commitments have been less than ten percent of the portfolio. The Commonwealth currently has no options positions outstanding.

The Commonwealth has had a securities lending program since the mid-1980s. The Commonwealth is able to enter into either a principal relationship or an agent relationship. In a principal relationship the Commonwealth reverses its treasury and agency securities in exchange for 102% of eligible collateral, marked to market daily. Eligible Collateral is defined as securities authorized for purchase pursuant to KRS 42.500. In an agent program the agent lends the Commonwealth's treasuries and agencies, takes the cash received from the loan and invests it in securities authorized for purchase pursuant to KRS 42.500. The income generated by these transactions is split among the agent, Credit Suisse, and the Commonwealth. At the present time the Commonwealth has entered into an agent agreement that has a guarantee of 10 basis points of the average market value of securities in the program. Through the re-investment of loan proceeds, the Commonwealth owns a $25 million par medium-term note issued by Lehman Brothers Holdings Inc. This bond is currently in default. Additionally, the Commonwealth owns a $25 million Senior Bank Note issued by Washington Mutual which is also in default.

On June 20, 2003, the State Investment Commission adopted Resolution 03-03, which amended the Commonwealth's investment policy concerning asset-based interest rate swaps. The change modifies the exposure limits from a $200,000,000 notional amount to a net market value approach, the absolute value of which cannot exceed $50,000,000 for all counterparties. The Commonwealth engages in asset-based interest rate swaps to better manage its duration and to stabilize the volatility of interest income. The Commonwealth currently has no asset-based interest rate swaps outstanding.

House Bill 5 of the First Extraordinary Session of 1997 was enacted on May 30, 1997. The Bill amended KRS 42.500 to authorize the purchase of additional investment securities with excess funds available for investment. The new classes of investment securities include: United States dollar denominated corporate securities, issued by foreign and domestic issuers, including sovereign and supranational governments, rated in one of the three highest categories by a nationally recognized rating agency, and asset backed securities rated in the highest category by a nationally recognized rating agency. The Commonwealth currently holds several asset backed securities that have been downgraded from the highest rating category. All of these positions are rated investment grade. Additionally, the Commonwealth holds a $5 million par medium-term note issued by Lehman brothers Holdings Inc. This note is currently in default.

KAR Title 200 Chapter 14 provides, among other things that: corporate securities, inclusive of Commercial Paper, Banker's Acceptances and Certificates of Deposit are limited to twenty-five million per issuer and a stated final maturity of five years or less. Money market securities rated A1-P1 or higher are limited to 20% of any investment pool and when combined with corporate and asset backed securities (ABS) must not exceed 25% of any investment pool. United States Agency Mortgage Backed Securities (MBS) and Collateralized Mortgage Obligations (CMO) are also limited to a maximum of 25% of any investment portfolio. ABS, MBS and CMO must have a weighted-average-life of four years or less at time of purchase.

State Retirement Systems

Following is information about the state's retirement system, including pension plans and other post employment benefits. Capitalized terms used under this heading and not otherwise defined shall have the respective meanings given by the CAFRs, as herein defined.

Pension Plans. Eligible state employees participate in one of two multi-employer defined benefit plans, the Kentucky Retirement Systems and the Kentucky Teacher's Retirement System ("KTRS"). The Kentucky Retirement Systems is comprised of four retirement plans, Employees Non-Hazardous and Employees Hazardous, County Employees and State Police. Each retirement plan is state supported, except for the County Employees, which has been excluded from the Kentucky Retirement Systems information provided herein. The Kentucky Retirement Systems and KTRS (collectively, the "Pension Plans") provide both pension and Other Post Employment Benefits ("OPEB") to state employees and teachers based upon their years of service and retirement dates. The Pension Plans are component units of the Commonwealth of Kentucky for financial reporting purposes and are included in *The Kentucky Comprehensive Annual Financial Report*. For a brief description of the Pension Plans and of the Pension Plans' assets and liabilities, see *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2007, Note 8 beginning on page 76. Additional information regarding the Kentucky Retirement Systems and KTRS can be found in their respective web sites at http://www.kyret.com and http://www.ktrs.ky.gov, including their respective Comprehensive Annual Financial Reports (collectively, the "CAFRs") and the accompanying actuarial studies, described under "Other Post-Employment Benefits." Only information contained on the Internet web page identified above is incorporated herein and no additional information that may be reached from such page by linking to any other page should be considered to be incorporated herein.

Pension Funding. Based upon the assumptions employed in the Pension Plans' June 30, 2007 actuarial valuation reports used in preparing the associated Pension Plans' 2007 CAFRs, the Kentucky Retirement Systems had a state supported pension Unfunded Actuarial Accrued Liability (the "UAAL") of $4,380 million, while KTRS had a UAAL of $5,970 million. The state supported portion of the

Pension Plans for Fiscal Year 2007 had funding percentages of 58.7 percent for the Kentucky Retirement Systems and 71.9 percent for KTRS. The Kentucky Retirement Systems state supported Annual Required Contribution for Fiscal Year 2007 pension benefits was $214.2 million versus the Actual Contribution of $107.6 million. The KTRS state supported Annual Required Contribution for Fiscal Year 2007 was $494.6 million, of which $421.6 million was contributed.

Other Post Employment Benefits. The Governmental Accounting Standards Board has promulgated Statement 45 ("Accounting and Financial Reporting by Employers for Post-employment Benefits other than Pensions"). The State is required to adopt the standards after the Fiscal Year ending June 30, 2008.

The State is obligated to provide healthcare benefits to certain retired state employees and teachers. The Pension Plans administer two multi-employer defined benefit healthcare plans (collectively, the "Health Plans") for which the state pays a portion of the cost of the benefits of the retired employees. As of January 1, 2006, the State commenced self-funding of healthcare benefits for state employees. The Kentucky Retirement Systems also adopted, on January 1, 2006, a self funding health care plan for Medicare Eligible Retirees. KTRS became self-insured for post retirement healthcare costs for Medicare Eligible Retirees on July 1, 1991. Beginning January 1, 1997, KTRS offered non-Medicare Eligible Employees insurance through the state health insurance program, which has since become self insured.

The Pension Plans have commissioned actuarial studies which have provided results for consideration, under certain actuarial funding methods and sets of assumptions. A five year experience study was completed for the period ending June 30, 2006 for the Kentucky Retirement Systems and the next scheduled experience study period will be prepared in January, 2011. KTRS' last five-year experience study was for the period ending June 30, 2005, the next five year experience study will be for the period ending June 30, 2010. Pursuant to their respective actuarial studies, the OPEB UAAL as of June 30, 2007 has been estimated to not exceed $5,151 million for the Kentucky Retirement Systems and $5,788 million for KTRS. These estimates represent the amount of healthcare benefits under the respective Health Plans, payable for the ensuing 30-year period and allocated by the actuarial cost method, as of June 30, 2007. The actuarial estimates for the Kentucky Retirement Systems OPEB liabilities substantially decreased from the $8,089.5 million previously reported in the Kentucky Retirement Systems' 2006 CAFR, primarily due to the Board's policy of incrementally increasing employer contributions to the funds in order to reach full entry age normal cost by 2016. The actuarial estimates for KTRS actually increased from $4,210.3 million due to health care costs escalating at a much faster rate than revenue growth in the Medical Insurance Plan.

The Kentucky Retirement Systems state supported Annual Required Contribution for Fiscal Year 2007 healthcare benefits was $146.3 million versus the Actual Contribution of $101.2 million. The KTRS state supported Annual Required Contribution for Fiscal Year 2007 was $231.5 million, of which $123.6 million was contributed. The Commonwealth's Fiscal Year 2008-2010 biennial budget contemplates $125 million of direct transfers from the KTRS Guarantee Fund to the Medical Insurance Stabilization Fund. Previously, the General Assembly directed transfers of $73.0 million in Fiscal Year 2007, $62.3 million in Fiscal Year 2006 and $29.1 million in Fiscal Year 2005. These amounts are to be repaid from the State General Fund over a 10-year period corresponding with each transfer. The state supported portion of the Health Plans for Fiscal Year 2007 had funding percentages of 16.1 percent for the Kentucky Retirement Systems and 2.4 percent for KTRS.

The Commonwealth's 2008-2010 biennial budget increased employer contribution rates by 37 percent for the Kentucky Retirement Systems' non-hazardous duty retirement system. The increase for the State Police Retirement System is 18 percent.

Changes to State Retirement Systems. During the 2008 Regular Session, Governor Steve Beshear presented the Kentucky Public Pension Protection and Modernization Act to address the long-term financial stability of the Commonwealth's pension systems. While there was significant discussion and debate between both the House and the Senate resulting in different versions of the pension legislation being considered, ultimately both sides of the General Assembly failed to reach an agreement.

On May 29, 2008, Governor Beshear issued an executive order creating the Kentucky Public Pension Working Group and urged both the House and Senate to work together toward an agreement for a special session. Governor Beshear's May 29th executive order created a working group composed of senior executive branch officials, pension fund directors, employee representatives, and private sector investment experts. The working group is conducting an operational and governance review of the state retirement systems and is also studying the issues in dispute during the 2008 regular legislative session that had not been recommended by the prior administration's Blue Ribbon Commission, to determine their viability and cost. To accomplish these tasks, the workgroup has been divided into six subcommittees including: best practices in investments; future funding strategies; a County Employees Retirement System ("CERS") and Local Government Employees Retirement System ("LGERS") committee that is tasked to study the transfer of classified school employees to a new retirement system, and the potential for a new local government employees retirement system; a committee to consider defined contribution options; a group that will evaluate healthcare costs and strategies; and a committee to evaluate and ensure best practices in securities litigation. The working group will provide its final report to the Governor by November 1, 2008 and will also offer to provide testimony to the Interim State Government Committee, allowing the General Assembly to address these issues in the 2009 regular legislative session.

In June 2008, Governor Beshear called a special session of the General Assembly after both the House and Senate reached an agreement on pension reform, which ultimately became House Bill 1. The final agreement accomplished several things, including: a schedule to improve state funding by reaching the full actuarially required contribution ("ARC") by 2025; proposed a new benefit tier for future hires that would require workers to stay longer and place more money into their own retirement over time in order to reach their full retirement benefit; established a floor for annual cost of living adjustments ("COLA") equal to 1.5% of the Consumer Price Index with the potential for future increases if the COLA is pre-funded; closed several loopholes; and created increased legislative oversight of the pension funds in future years.

As a result of the passage of House Bill 1, the growth in the state's unfunded liability is expected to be slowed. These results are expected to be augmented by proposed changes in the Commonwealth's investment strategies and allocations to bring the retirement systems closer to their peer group performance levels over time. By using the dual combination of the best practices and findings of the Kentucky Public Pension Working Group and by following the schedule of payments included in House Bill 1 the state expects to see reductions in the liabilities that have accrued over time.

SUMMARIES OF THE PRINCIPAL DOCUMENTS

The following statements are brief summaries of certain provisions of the Resolution and the Lease. Such statements do not purport to be complete and reference is made to the Resolution and the Lease, copies of which are available for examination at the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601.

The Resolution

Certain Definitions. Under the Resolution "Revenues" means, with respect to the Lease, all of the rental payments and other payments to be made by the State Agency to the Commission pursuant to the Lease, or any other amounts received by the Commission for the use or occupancy of the Project and any other payments or deposits to be made to the Bond Service Fund, including proceeds from the disposition of any portion of the Project pursuant to the Resolution.

"Revenues Available for Debt Service" means the aggregate of all of the revenues of the State Agency for a Fiscal Year, excluding (i) the proceeds of any Bonds or other obligations payable from the Revenues Available for Debt Service and (ii) amounts required by law (excluding appropriations law) to be used for purposes other than for debt service on the Bonds and any other obligation payable from the Revenues Available for Debt Service (which, as of the date of the Resolution, included revenues derived from Tier I rates and charges of the State Agency), all determined in accordance with generally accepted accounting principles. As of the date of the Resolution, revenues derived from Tier II rates and charges of the State Agency constitute Revenues Available for Debt Service.

Funds and Accounts. The following funds and accounts have been established under the Resolution. In addition to the deposit to the funds described under "PLAN OF FINANCE" above, deposits of the proceeds of the Series 2008 Bonds and Revenues will be made as described below.

1. Bond Service Fund. The Resolution creates a Bond Service Fund with respect to the Bonds (the "Bond Fund"), to be held and maintained by the Trustee. There will be deposited into the Bond Service Fund all or such portion of the Revenues as will be sufficient to pay when due the principal of, premium, if any, and interest on all Bonds Outstanding under the Resolution at or before their maturity. Accrued interest on the Bonds, if any, will be deposited to the Bond Service Fund. The Resolution requires the Commission to deposit or cause to be deposited on or before any April 1 or October 1 and any date set for redemption of Bonds prior to maturity (each a "Payment Date") with the Trustee all amounts required for the payment of the principal of, premium, if any, and interest on the Bonds due on such Payment Date.

No further payments are required to be made to the Bond Fund when, and so long as, the aggregate amount therein is sufficient to retire all of the Bonds that are then Outstanding, plus interest due and to become due together with redemption premium, if any. In the event that the amount on deposit in the Bond Service Fund is insufficient to pay the principal of, premium, if any, and interest on the Bonds on any Payment Date, the Trustee shall transfer moneys from the Reserve Fund in an amount sufficient to pay the principal of, premium, if any, and interest on the Bonds on such Payment Date.

2. Cost of Issuance Fund. The Resolution creates a Cost of Issuance Fund for the Bonds to be held and maintained by the Trustee. From the proceeds of the Bonds and other available moneys, if any, deposited by the Commission at the time of delivery of the Bonds, there will be deposited therein an amount sufficient to pay certain expenses in connection with the issuance of the Bonds. The proceeds of Additional Bonds may be deposited in the Cost of Issuance Fund to pay the costs of issuance of such Additional Bonds.

3. Construction Fund. The Resolution creates a Construction Fund, to be held by the Treasurer of the Commonwealth. Until disbursed as authorized by the Resolution, the Construction Fund constitutes a trust fund for the benefit of the owners. The Construction Fund will be used solely for the financing of the Project which is to be financed with the proceeds of Additional Bonds. The Commission will, at the delivery of such Additional Bonds, cause to be deposited into the Construction Fund from the Additional Bond proceeds the sum set forth in the related Supplemental Resolution. Any moneys remaining in the Construction Fund after the Project is completed in full will be transferred to the Trustee to be held, in trust, in the Bond Service Fund, unless otherwise provided in the Supplemental Resolution.

4. Reserve Fund. The Resolution creates the Project No. 91 Reserve Fund, which shall be maintained by the Trustee as a separate trust fund, and separate account statements with respect thereto shall at all times be kept and maintained.

On the date of issuance of the Series 2008 Bonds, an initial deposit to the credit of the Reserve Fund is to be made in an amount which is equal to the Reserve Fund Requirement with respect to the Series 2008 Bonds. Moneys in the Reserve Fund shall at all times be maintained in an amount not less than the Reserve Fund Requirement. If on any date the amount on deposit in the Reserve Fund is less than the Reserve Fund Requirement, the Trustee shall promptly notify the Commission, the Cabinet and the State Agency in writing of such deficiency, and the Trustee shall deposit in the Reserve Fund any payments made by the Commission, the Cabinet or the State Agency to replenish the Reserve Fund, pursuant to the Lease. The Commission shall cause the State Agency and the Cabinet to seek appropriations to remedy any deficiency in the Reserve Fund, as provided in the Lease.

Moneys on deposit in the Reserve Fund on any Payment Date in excess of the Reserve Fund Requirement shall be transferred to the Bond Service Fund. Except for such excess amounts, moneys on deposit in the Reserve Fund shall be used to make up any deficiencies in the Bond Service Fund to pay the interest on and the principal of the Bonds (in the order listed). Upon any such transfer from the Reserve Fund to the Bond Service Fund, the Trustee shall promptly notify the Commission, the Cabinet and the State Agency of such transfer and the amount of such transfer. Investment Obligations in the Reserve Fund shall be valued by the Trustee on each Payment Date on the basis of the amortized cost of such Investment Obligations, exclusive of accrued interest thereon.

The procurement and deposit of a Reserve Fund Facility shall be treated as a proper deposit in lieu of cash to the credit of the Reserve Fund to the stated amount of such Reserve Fund Facility then in force and available to draw upon. In the event that such a Reserve Fund Facility is to be delivered to the Trustee to satisfy the Reserve Fund Requirement in whole or in part, an insurance agreement (which is authorized by the Resolution to be executed and delivered) may specify the manner in which draws shall be made upon the Reserve Fund Facility, and may specify subrogation rights of the Reserve Fund Facility Provider and provisions regarding reimbursement to the Reserve Fund Facility Provider; provided, that the Reserve Fund Facility Provider shall receive no payment of the principal of or the interest on the Bonds it is deemed to own until all of the principal of, interest on and past due interest on the Bonds have been paid to the other owners of the Bonds (other than the Reserve Fund Facility Provider).

In the event that a Reserve Fund Facility is delivered to the Trustee in lieu of cash, a corresponding amount of money on deposit in the Reserve Fund shall be transferred to a separate, segregated account in the Bond Service Fund. All moneys in any such separate, segregated account in the Bond Service Fund shall be invested in Investment Obligations with a yield no greater than the respective yields on the related Tax-Exempt Bonds, and, if applicable, used to pay the principal of and interest on the Bonds as the same becomes due or to redeem Bonds prior to maturity on the next optional redemption date permitted with respect to the Bonds; provided, that such moneys may be otherwise used or invested if the Commission delivers to the Trustee an opinion of nationally recognized bond counsel to the effect that such other use or investment does not adversely affect the tax status of the interest on the Series 2008 Bonds and any Tax Exempt Additional Bonds for federal income tax purposes.

As used above:

"Reserve Fund Facility" means a surety bond, insurance policy, guaranty, letter of credit or other credit facility issued to guarantee or assure timely payment of the principal of or interest on, or both, of some or all of the outstanding Bonds, subject only to notification that there are insufficient funds for such payment. A Reserve Fund Facility shall be in a stated amount which, when added to the funds deposited in the Reserve Fund and the stated amounts of all other Reserve Fund Facilities, will equal 100% of the

Reserve Fund Requirement computed on a basis which includes all outstanding Bonds. A Reserve Fund Facility must be unconditional and irrevocable so long as any Bonds secured thereby are outstanding. This definition shall also include any related covenants or agreements contained in an agreement with the related Reserve Fund Facility Provider. If more than one Reserve Fund Facility is held in the Reserve Fund at any time, references shall be to the related Reserve Fund Facility.

"Reserve Fund Facility Provider" means an insurance company, bank, savings and loan association, savings bank, thrift institution, credit union, trust company, surety company or other institution, which is, at the time of the issuance of a Reserve Fund Facility, of sufficient credit quality to entitle debt backed by its Reserve Fund Facility to be rated in the two (2) highest rating categories by at least two (2) nationally recognized rating agencies.

Federal Tax Covenants of the Commission. The Commission has covenanted to do and perform all acts and things permitted by law and necessary or desirable in order to assure that the interest paid on the tax-exempt Bonds by the Commission shall be excludible from the gross income of the owners of the tax-exempt Bonds (the "Holders") for the purposes of federal income taxation and not permit the tax-exempt Bonds to be or become "arbitrage bonds" as defined in the Code.

Investment of Funds. Moneys in any Fund or Account established under the Resolution will be invested in obligations permitted by Kentucky law as specified in the Resolution.

Events of Default. The Resolution defines "Events of Default" as follows:

(a) Default in the due and punctual payment of the interest on any Bond;

(b) Default in the due and punctual payment of the principal of, or premium, if any, on any Bond at maturity or upon redemption prior to maturity; or

(c) Default in the performance or observance of any other of the covenants, agreements or conditions on the part of the Commission in the Resolution or in the Bonds contained, and the continuation thereof for a period of 30 days after written notice given by the Trustee to the Commission or by the owners of not less than 25% in aggregate principal amount of Bonds Outstanding, to the Commission and the Trustee; *provided*, *however*, that if such event of default can, in the opinion of the Trustee, be corrected but not within such period, it shall not constitute an event of default under the Resolution if corrective action is instituted by the Commission within such period and diligently pursued until the event of default no longer exists.

Upon the happening and continuation of any event of default described in clause (a) or (b) above, unless the principal of all the Bonds has already become due and payable, either the Trustee (by notice in writing to the Commission) or the owners of not less than 25% of the aggregate principal amount of Bonds Outstanding (by notice in writing to the Commission and the Trustee) may declare the principal of all the Bonds then Outstanding and the interest accrued thereon to be due and payable immediately, and upon any such declaration the same will become and be immediately due and payable, anything in the Resolution or in any of the Bonds contained to the contrary notwithstanding. The right of the Trustee or of the owners of not less than 25% of the aggregate principal amount of Bonds then Outstanding to make any such declaration as aforesaid, however, is subject to the condition that if, at any time after such declaration, all overdue installments of interest on such Bonds and the principal of all Bonds which will have matured by their terms, together with the reasonable and proper charges, expenses and liabilities of the Trustee, are either paid by or for the account of the Commission or provision satisfactory to the Trustee is made for such payment, then and in every such case any such default and its consequences will *ipso facto* be deemed to be annulled, but no such annulment will extend to or affect any subsequent default or impair or exhaust any right or power consequent thereon.

The Resolution provides that upon the occurrence and continuation of any event of default under the Resolution, the Trustee may proceed, and upon the written request of the owners of not less than 25% in aggregate principal amount of Bonds then Outstanding must proceed, to protect and enforce its rights and the rights of the owners under the pertinent Kentucky Revised Statutes and under the Resolution forthwith by such suits, actions, or by special proceedings in equity or at law, or by proceedings in the office of any board or officer having jurisdiction, whether for the specific performance of any covenant or agreement contained in the Resolution or in aid of the execution of any power granted therein or in the Kentucky Revised Statutes or for the enforcement of any legal or equitable rights or remedies as the Trustee, being advised by counsel, deems most effectual to protect and enforce such rights or to perform any of its duties under the Resolution.

The Resolution provides that the Trustee is entitled to sue for, enforce payment on, and receive any or all amounts then or during the continuation of any event of default becoming, and at any time remaining, due from the Commission, for principal, interest or otherwise under any of the provisions of the Resolution or of the Bonds, and unpaid, with interest on overdue payments at the rate or rates of interest borne by the Bonds then Outstanding, to the extent permitted by law together with any and all costs and expenses of collection and of all proceedings under the Resolution and under the Bonds, without prejudice to any other right or remedy of the Trustee or of the owners, and to recover and enforce judgment or decree against the Commission, but solely as provided in the Resolution and in the Bonds, for any portion of such amounts remaining unpaid, with interest, costs, and expenses, and to collect (but solely from the moneys in the funds and accounts established by the Resolution other than the Rebate Fund and the Stabilization Fund) in any manner provided by law, the moneys adjudged or decreed to be payable.

The Resolution provides that, regardless of the happening of an event of default, the Trustee, if requested in writing to take any action under the Resolution or the Bonds by the owners of not less than 25% of the aggregate principal amount of Bonds Outstanding, has no duty to act until it is furnished with indemnification satisfactory to it. The Trustee may institute and maintain such suits and proceedings as it may be advised are necessary or expedient to prevent any impairment of the security under the Resolution or the Bonds by any acts which may be unlawful or in violation of the Resolution and such suits and proceedings as the Trustee may be advised are necessary or expedient to preserve or protect its interest and the interest of the owners of the Bonds, provided that such request will not be otherwise than in accordance with the provisions of law and of the Resolution and will not be unduly prejudicial to the interest of the owners of the Bonds not making such request.

Individual Holder Action Restricted. No owner of Bonds has any right to institute any suit, action, or proceeding in equity or at law for the enforcement of the Resolution or for the execution of any trust thereof or for the appointment of a receiver or the enforcement of any other right under the Kentucky Revised Statutes, unless such owner has given to the Trustee written notice of the event of default or breach of trust or duty on account of which such suit, action, or proceeding is to be taken and unless the owners of not less than 25% in aggregate principal amount of Bonds Outstanding have made written request accompanied by indemnity and security satisfactory to the Trustee and have offered it reasonable opportunity either to proceed to exercise the powers granted by the Resolution or to institute such action, suit, or proceeding in its own name, and the Trustee thereafter fails or refuses to exercise the powers granted by the Resolution or to institute such action, suit or proceeding in its, his or their own name or names. It is understood and intended that no one or more owners of Bonds have any right in any manner whatsoever to affect, disturb or prejudice the security of the Resolution by its, his or their action or to enforce any right thereunder except in the manner therein provided, and that all proceedings at law or in equity will be instituted and maintained in the manner therein provided and for the equal benefit of the owners of all of such Bonds then Outstanding. Nothing contained in the Resolution or in the Bonds affects or impairs the right of any owner of any Bond to payment of the principal of or interest on such Bond at and after the maturity thereof, or the obligation of the Commission to pay the principal of, premium, if any, and interest on the Bonds to the respective owners thereof at the time and place, from the source and in the manner therein provided and in the Bonds expressed.

Amendments to the Resolution. If it appears desirable and to the advantage of both the Commission and the owners of the Bonds, the Commission will adopt resolutions supplemental to the Resolution, altering or amending the Resolution, but each such supplemental resolution will not become effective unless and until it has been approved as provided in the Resolution by the owners of 66-⅔% of the aggregate principal amount of Bonds Outstanding and unless and until the opinion of counsel required by the Resolution has been delivered. Notwithstanding the foregoing, no such modifications, alterations or amendments will be made which permit an extension of the time of payment at maturity of the principal of, premium, if any, or interest on any Bond, or a reduction in the amount of principal or premium, if any, or the rate of interest thereon without the written consent of the owner thereof, or which would reduce the percentage of owners of Bonds whose approval is required by the Resolution for adoption of any supplemental resolution as described above.

In addition to the foregoing, the Commission and the Trustee may, without regard to the provisions described above, make any amendment or change to the Resolution (i) to cure any formal defect or ambiguity, if in the opinion of the Trustee such amendment or change is not adverse to the interest of the owners of the Bonds, (ii) to grant to or confer on the Trustee for the benefit of the owners of the Bonds any additional rights, remedies, powers, authority or security which may lawfully be granted or conferred and which are not contrary to or inconsistent with the Resolution as theretofore in effect, (iii) to permit the Trustee to comply with any obligations imposed on it by law, (iv) to achieve compliance of the Resolution with any federal tax law, (v) to maintain or improve any rating on the Bonds, (vi) to provide for a Reserve Fund Facility, (vii) to issue Additional Bonds in accordance with the terms of the Resolution; or (viii) which in the opinion of nationally recognized Bond Counsel will not materially adversely affect the rights of owners of the Bonds, and the Commission may adopt such supplemental resolution to accomplish the foregoing.

Change, Substitution or Other Modification of Project. The Commission covenants that, as long as the Bonds shall be Outstanding, it will not sell, mortgage or make any other disposition or permit or cause the sale, mortgage or other disposition of all or any part of the Project, except to the extent the Commission shall determine the same to be no longer useful, or to have become inefficient by reason of depreciation or obsolescence, in any of which events the Commission shall cause substitute facilities to be provided as a part of the Project in such manner as to preserve the usefulness and operating efficiency of the Project at all times. In the event the Commission shall determine that properties constituting part of the Project are no longer useful, and need not be replaced, any proceeds derived from the sale or other disposition thereof shall be applied as in the case of other moneys in the Bond Service Fund

Anything in the Resolution or the Lease notwithstanding, the Commission may, in its sole discretion, change, substitute or otherwise modify components of the Project, so long as all Bond proceeds are applied to facilities, payments or undertakings which are included in and subject to rental payments under the Lease such that rental payments thereunder will be sufficient to pay principal of, premium, if any, and interest on the Bonds; provided that any such change, substitution or modification shall not cause the Commission to be in violation of certain covenants of the Resolution.

The Trustee. The Resolution sets forth the terms and provisions regarding the responsibilities, compensation and removal of the Trustee. The Trustee is entitled to reasonable compensation from

Revenues and to the extent the Commission fails to make such payment, the Trustee may make such payment from funds in its possession (other than the Rebate Fund) and shall be entitled to a preference therefor over any Outstanding Bonds. The Trustee may be removed at any time at the written request of the Commission or a majority of owners, but such removal shall not be effective until a successor Trustee is appointed pursuant to the Resolution.

Discharge of the Resolution. If the Commission pays or causes to be paid, or there is otherwise paid, to the owners of all Bonds the total principal and interest due or to become due thereon, including premium, if applicable, at the times and in the manner stipulated therein and in the Resolution then the pledge of Revenues under the Resolution, and all covenants, agreements and other obligations of the Commission to the owners of the Bonds shall cease, terminate and become void and shall be discharged and satisfied.

Whenever there shall be held by the Trustee in the Bond Service Fund or an escrow fund established for such purpose, either (a) moneys in an amount which shall be sufficient, or (b) Defeasance Obligations (as defined below) the principal of and interest on which when due (without consideration of reinvestment income) will provide moneys which, together with other moneys, if any, then on deposit in the Bond Service Fund or such escrow fund, shall be sufficient, to pay when due the principal of, interest and redemption premium, if applicable, on the Bonds or any part thereof to and including the date upon which the Bonds or any of them will be redeemed or will mature, as the case may be, then and in any of said events all such Bonds shall be deemed to have been paid within the meaning and with the effect expressed in the defeasance provisions of the Resolution, and the Trustee will and is irrevocably instructed by the Resolution to give notice thereof to the owners.

As used herein, "Defeasance Obligations" means:

(a) non-callable direct obligations of the United States of America, non-callable and non-prepayable direct federal agency obligations the timely payment of principal of and interest on which is fully and unconditionally guaranteed by the United States of America, non-callable direct obligations of the United States of America which have been stripped by the United States Treasury itself or by any Federal Reserve Bank (not including "CATS, "TIGRS" and "TRS" unless the Commission obtains a confirmation that the Bonds defeased thereby shall be rated in the highest rating category by S&P and Moody's (as each term is hereinafter defined) with respect thereto) and the interest components of REFCORP bonds for which the underlying bond is non-callable (or non-callable before the due date of such interest component) for which separation of principal and interest is made by request of Federal Reserve Bank of New York in book-entry form, and shall exclude investments in mutual funds and unit investment trusts;

(b) non-callable obligations timely maturing and bearing interest (but only to the extent that the full faith and credit of the United States of America are pledged to the timely payment thereof), including, but not limited to, debt obligations of the Resolution Funding Corp., and U.S. Agency for International Development guaranteed notes (which must mature at least four business days before the appropriate payment date);

(c) certificates rated "AAA" by Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P"), "Aaa" by Moody's Investors Service, Inc. ("Moody's") and "AAA" by Fitch, Inc. ("Fitch") (if rated by Fitch) evidencing ownership of the right to the payment of the principal of and interest on obligations described in clause (b), provided that such obligations are held in the custody of a bank or trust company satisfactory to the Trustee, including the Trustee or any of its affiliates, in a segregated trust account in the trust department separate from the general assets of such custodian;

(d) bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state (i) 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 such bonds or obligations on the date specified in the notice, (ii) timely payment of which is fully secured by a fund consisting only of cash or obligations of the character described in clause (a), (b) or (c) which fund may be applied only to the payment when due of such bonds or other obligations, and (iii) rated “AAA” by S&P, “Aaa” by Moody’s and “AAA” by Fitch (if rated by Fitch); and

(e) non-callable senior debt obligations of U.S. government-sponsored agencies that are not backed by the full faith and credit of the U.S. government, including, but not limited to, Federal Home Loan Mortgage Corp. debt obligations, Farm Credit System consolidated systemwide bonds and notes, Federal Home Loan Banks consolidated debt obligations, Federal National Mortgage Association debt obligations, Resolution Funding Corp. debt obligations and U.S. Agency for International Development guaranteed notes (which must mature at least four business days before the appropriate payment date); provided, that, in each case, the obligations are rated “AAA” by S&P, “Aaa” by Moody’s and “AAA” by Fitch (if rated by Fitch).

The Lease

1. <u>Lease of Project by Lessee from Lessor; Term of the Lease; Payment of Rent</u>. The Commission has entered into the Lease with the Cabinet and the State Agency (collectively, the “Lessee”) whereby the Lessee will lease the Project from the Commission and will pay rentals to the Commission during biennial renewal terms which will provide funds sufficient to pay the amounts due on the Series 2008 Bonds. The rentals payable under the Lease include amounts sufficient to restore any deficiency in the Reserve Fund, as determined in accordance with the Resolution.

The Lease has an initial term ending June 30, 2010. The Commission has granted the Lessee (or the Cabinet or the State Agency) the exclusive option to renew the Lease for successive and ensuing renewal terms of two years commencing July 1 in each even-numbered year. The last renewal term for the Lease relating to the Series 2008 Bonds ends June 30, 2030 (the final maturity date permissible for any Series 2008 Bonds to be issued by the Commission for the Project being April 1, 2029) and for each such renewal term, if renewed therefor, the State Agency is obligated to pay, and agrees under the Lease that in the event of such renewal must pay or cause to be paid, to the Commission, as rent for such biennium each Debt Servicing Obligation which comes due on each payment date during the renewal term for such period, secured by amounts paid by the State Agency from Revenues Available for Debt Service; *provided,* that the State Agency shall cause such rent to be deposited on the dates and in the manner set forth in the Lease. In the event that either the Cabinet or the State Agency elects to renew the Lease for an ensuing renewal term, but not the other, then the renewing entity shall be considered to be the sole Lessee thereunder; *provided, however,* that if the State Agency elects not to renew the Lease, then the Cabinet shall have the right under the Resolution to substitute another state agency of the Commonwealth as co-Lessee under the Lease or to enter into a sublease or another agreement with any such state agency.

Payments for the rent becoming due during the term ending June 30, 2010, and for each renewal term, if the Lease shall be renewed for any such renewal term, shall be made or caused to be made by the State Agency to the Commission on each debt servicing date during each such term, in such minimum amounts as will enable the Commission, solely from such source, to pay its Debt Servicing Obligation for the Project; provided, that the Lessee shall cause such rent to be deposited on the dates and in the manner set forth in the Lease. The primary source of the payment of rent shall be from payments made by the State Agency.

Each of the successive options to renew may be exercised for the succeeding renewal term at any time after the adjournment of the Session of the General Assembly of the Commonwealth at which appropriations shall have been made for the operation of the state government for each succeeding renewal term by notifying the Commission by a writing signed by the Secretary of the Cabinet and/or the Chairman of the State Agency, respectively, delivered to the Commission; *provided, however,* that such option shall in each instance be deemed automatically exercised, and the Lease automatically renewed for the succeeding renewal term, effective on the first day thereof, unless a written notice of the election of the Lessee not to renew, signed by the Secretary of the Cabinet and/or the Chairman of the State Agency, respectively, shall have been delivered to the Commission before the close of business on the last business day in May, immediately preceding the beginning of such succeeding renewal term.

If the Lessee (or the Cabinet or the State Agency) exercises its successive renewal option, according to the automatic renewal provisions described above, then upon the first day of the biennial renewal term for which such option is exercised, the Lessee (or the Cabinet or the State Agency) shall be firmly bound for the entire amount of the rent, including the Additional Rent (hereinafter defined), becoming due and payable for such renewal term, payable from any funds of the Lessee (or the Cabinet or the State Agency), including, but not limited to, appropriations, contributions, gifts, matching funds, devises and bequests from any source, whether federal or state, and whether public or private, so long as the same are not conditioned upon any use of the Project in a manner inconsistent with law; *provided, however,* that nothing contained in the Lease may be construed as binding the Lessee (or the Cabinet or the State Agency) to pay rentals for more than one biennial renewal term at a time. Under the provisions of the Constitution of the Commonwealth, the Commission, the Cabinet and the State Agency are each prohibited from entering into lease obligations extending beyond their biennial budget period.

"Debt Servicing Obligation" means the aggregate amounts required to be paid in respect of the Bonds, on any payment date, being (i) the scheduled maturity of the principal of any Bonds maturing on such payment date; (ii) the principal of and premium, if any, on any Bonds subject to redemption on such payment date; and (iii) the interest required to be paid on the Bonds which were outstanding immediately prior to such payment date.

No rent need be paid during any period when the amount in the Bond Fund is sufficient to pay the principal and interest next payable on the Series 2008 Bonds then Outstanding, plus the amount of other costs then due on the Series 2008 Bonds.

In the Resolution, the Commission has covenanted that it will receive and apply the lease-rental payments from the Cabinet and the State Agency to pay the principal of and interest on the Series 2008 Bonds when due, and will carry out each and every duty imposed on it by the Kentucky Revised Statutes in respect thereto.

Additional Rent. The State Agency, and in the case of subsection (a) below the Cabinet, covenants and agrees to pay "Additional Rent" for the term of the Lease and during any renewal term, as follows:

(a) To the Trustee, to restore any deficiency in the Reserve Fund, as determined in accordance with the Resolution;

(b) To the Trustee, when due, all fees of the Trustee for services rendered, all fees and charges of any paying agent, the Bond Registrar, counsel, accountants and others incurred in the performance on request of the Trustee of services for which the Trustee and such other persons are entitled to payment or reimbursement; and

(c) To the Commission, upon demand, all reasonable expenses incurred by it in relation to the Project which are not otherwise required to be paid by the Commission under the terms of the Lease.

Effect of Lessee's Exercise of Its Option to Renew. If the Lessee (or the Cabinet or the State Agency) gives written notice to the Commission of the election of the Lessee (or the Cabinet or the State Agency) not to renew the Lease for any renewal term, prior to the automatic renewal described above, the Lessee (or the Cabinet or the State Agency) shall not become obligated to pay rentals beyond the last day of the then current term, and the Lessee (or the Cabinet or the State Agency) shall thereby forfeit all of its future options to renew, and shall peacefully surrender to the Commission possession of the Project on or prior to the last day of the then current term; *provided, however,* an election on the part of the Lessee (or the Cabinet or the State Agency) not to renew for a future term shall not in any manner alter or diminish any obligation of the Lessee (or the Cabinet or the State Agency) thereunder for the then current term, and shall not preclude subsequent reinstatement of the Lease for any future renewal term, if agreed to by the Commission upon the same terms and conditions as would have been applicable if the Lease had been renewed according to the provisions of the Lease, except that if such reinstatement is sought when one or more installments of rent or Additional Rent for such renewal term are overdue and unpaid, it shall be a condition of such reinstatement that such overdue rent or Additional Rent be tendered.

State Agency to Seek Appropriations. The State Agency covenants and agrees that on each and every occasion when appropriations bills are prepared for introduction in the various successive Sessions of the General Assembly of the Commonwealth, the State Agency will cause to be included in the appropriations proposed to be made for the State Agency, sufficient amounts in the aggregate (over and above all other requirements of the State Agency) to enable the State Agency to pay rent under the Lease, and thereby provide to the Commission moneys sufficient for the payment of the Debt Servicing Obligation and the other payment obligations of the State Agency under the Lease. In its statutory role as the financial agency of the Commonwealth, the Cabinet covenants to apply appropriated funds to make such rent payments to the extent such appropriations are made in each legislative and budgetary biennium of the Commonwealth.

Cabinet to Seek Appropriations. In the event of a deficiency in the Reserve Fund or in the event that the State Agency fails to make a request for an appropriation as described above, the Cabinet covenants and agrees in the Lease that on each and every occasion when appropriations bills are prepared for introduction in the various successive Sessions of the General Assembly of the Commonwealth, the Cabinet will cause to be included in the General Fund appropriations proposed to be made for the Cabinet, sufficient amounts (over and above all other requirements of the Cabinet), which will enable the Cabinet to pay the Additional Rent in an amount sufficient, on any date, to maintain the Reserve Fund Requirement in the Reserve Fund as required by the Resolution. In its statutory role as the financial agency of the Commonwealth, the Cabinet covenants to apply appropriated funds to make such Additional Rent payments to the extent such appropriations are made in each legislative and budgetary biennium of the Commonwealth.

Pledge of Revenues Available for Debt Service. Under the Lease there is pledged for the payment of the Debt Servicing Obligation and any rent payable in accordance with the terms and the provisions of the Lease, subject only to the provisions of the Lease and the Resolution permitting the application thereof for or to the purposes and on the terms and conditions set forth in the Lease and the Resolution, the Revenues Available for Debt Service.

2. Rate Covenant of State Agency. To provide funds sufficient to make all rental payments due under the Lease, the State Agency covenants to at all times establish, enforce and collect rates and charges for services rendered and facilities afforded by the works and facilities of the State Agency (the "System"); taking into account and consideration the cost and value of the System, the costs of operating and maintaining the System in a good state of repair, proper and necessary allowances for depreciation and for additions and extensions, the amounts necessary for the orderly retirement of all obligations for the repayment of money ("Obligations"), and the accumulation and maintenance of necessary reserves any amounts deposited in the Stabilization Fund established by the State Agency as described below (other than amounts received from proceeds of any obligations); and such rates and charges shall be adequate to meet all such requirements as provided in the Lease, and shall, if necessary, be adjusted from time to time in order to comply with the terms of the Lease (subject to such regulatory approvals as may be required by law); and annual Revenues Available for Debt Service from such rates and charges shall be further adequate to provide, after payment of any amounts deposited in the Stabilization Fund (other than amounts received from the proceeds of Obligations) during the applicable period, 1.15 times coverage of annual principal and interest on all Obligations (including without limitation the Bonds); provided, that, in determining such coverage, the State Agency may include as annual Revenues Available for Debt Service any amounts withdrawn from the Stabilization Fund during the applicable period, so long as the annual Revenues Available for Debt Service from such rates and charges shall provide (after such deductions) at least one (1) time coverage of such annual principal and interest; provided further, that for Interim Indebtedness (as hereinafter defined) annual principal and interest shall be calculated using (i) an assumed interest rate equal to the rate used by the Cabinet to calculate debt service appropriations for bonds newly authorized in that budget period, (ii) a final maturity date that is no later than twenty (20) years from the date the Interim Indebtedness is incurred, and (iii) approximately level debt service. The term "Interim Indebtedness" as used herein, means Obligations with respect to which the State Agency has covenanted to issue Bonds, or to request that Bonds be issued on its behalf, for the repayment thereof, at or prior to the maturity of such Obligations.

For each Fiscal Year of the budget period in its budget prepared in accordance with the terms of the Lease, the State Agency agrees that it will prepare an estimate of gross income and revenue to be derived from the operation of the System for each such Fiscal Year, and to the extent that said gross income and revenues are insufficient to meet all requirements as provided herein, the State Agency covenants and agrees that it will immediately (subject to regulatory approvals as required by law) revise its rates and charges for services rendered by the System, so that the same will be adequate to meet all of such requirements

3. Rate Stabilization Fund. The State Agency may establish a Rate Stabilization Fund (the "Stabilization Fund") which would be held by the Trustee on behalf of the State Agency as a separate, segregated account of the State Agency as provided in the Resolution. Pursuant to the terms of the Resolution, the Stabilization Fund is not pledged to the payment of the principal of, premium, if any, or interest on the Series 2008 Bonds or any other amount payable under the Resolution, and is not a part of the funds and accounts pledged to the security of the Series 2008 Bonds under the Resolution. In any applicable period, after the payment of current expenses and debt service with respect to all outstanding Obligations, the State Agency may transfer its revenues or the proceeds of any Obligations to the Stabilization Fund. The State Agency may maintain the Stabilization Fund at such funding level as it may determine. Any moneys on deposit in the Stabilization Fund may be withdrawn from the Stabilization Fund by the State Agency with a written requisition of the State Agency submitted to the Trustee, and used by the State Agency for any lawful purpose of the State Agency, including without limitation the payment of current expenses, the payment of debt service on any Obligations, deposits to

the Reserve Fund and the payment of the cost of repairs, replacements, renewals, improvements, extensions and equipment of and to the System. In complying with its rate covenant described above, the State Agency may account for moneys on deposit in the Stabilization Fund as described above.

4. Additional Obligations. Before Obligations (including without limitation any Bonds) may be incurred by the State Agency, there is required to be filed with the Trustee a certificate of the chief accounting officer of the State Agency stating, and setting forth the calculations supporting such statement, that at the date of incurring such Obligations, Revenues Available for Debt Service are at least 1.15 times Maximum Annual Debt Service.

In calculating Revenues Available for Debt Service, if there is in effect at the date of such calculation any change in the State Agency's rates and charges that produce revenues that are available to pay debt service or obligations of the State Agency, it shall be assumed that such new rates and charges were in effect at all times and the calculation of Revenues Available for Debt Service shall be adjusted to reflect the amounts which would have been credited had such rates and charges been in effect at all times.

"Maximum Annual Debt Service" as used below means the sum of all amounts required to be paid from revenues of the State Agency, during any single fiscal year commencing after the date of such calculation, or set aside during such fiscal year, for payment of debt service on all Obligations.

For the purpose of determining the Maximum Annual Debt Service, variable rate obligations will be deemed to bear interest at the maximum rate of interest applicable to such variable rate bonds; provided, however, that if such maximum rate of interest is less than the interest rate quoted in The Bond Buyer 25 Revenue Bond Index (the "Index Rate") as published in The Bond Buyer for the last week of the month preceding the date of issuance of such variable rate bonds, then the interest rate on such variable rate bonds shall be deemed to be the Index Rate. If The Bond Buyer 25 Revenue Bond Index is no longer published, an index that is deemed to be substantially equivalent by nationally recognized bond counsel may be substituted therefor. Also, for the purpose of determining the Maximum Annual Debt Service, any Obligation scheduled to be outstanding during such period that is subject to tender at the option of the holder shall be assumed to mature on the stated maturity date or mandatory sinking fund payment date thereof.

In calculating Maximum Annual Debt Service it will be assumed that the Obligations proposed to be incurred at the time of incurring such Obligations are outstanding and that the proceeds of such Obligations, if incurred to refund other Obligations, shall have been applied as provided in the proceedings in connection with the incurrence of such proposed Obligations.

Obligations incurred to refund other Obligations may be incurred without compliance with the requirements described above if there shall be filed with the Trustee a certificate of the chief accounting officer of the State Agency stating, and setting forth the calculations on which such statement is based, assuming the incurrence of such Obligations, that debt service, as calculated upon issuance of such Obligations, will not be greater than debt service, as calculated immediately prior to the proposed incurrence of such Obligations, in any future Fiscal Year.

See "ADDITIONAL BONDS" in the body of this Official Statement for a discussion of the ability of the Commission to issue Bonds having a pledge on the payments due under the Lease which is on a parity with the lien of the Series 2008 Bonds.

5. Events of Default and Remedies. Events of default under the Lease include a default in the due and punctual payment of any rent or a default in the performance of any covenants therein not remedied within 30 days (but the Lessee shall not be deemed to be in default if the Lessee commences to

remedy said defaults within said thirty (30) day period, and proceeds to and does remedy said default with due diligence).

If an event of default occurs under the Lease, the Commission, in addition to all other remedies given to the Commission at law or in equity, may by written notice to the Cabinet and the State Agency terminate the Lease or, without terminating the Lease, take possession (actually or constructively) of the Project. In such event, the Commission may sublet the Project or any portion thereof, and in the event of a reletting may apply the rent therefrom first to the payment of the Commission's expenses incurred by reason of the Lessee's default, and the expense of reletting, including but not limited to any repairs, renovation or alteration of the Project, and then to the payment of rent and all other sums due from the Lessee under the Lease. The owners have no security interest in any properties constituting the Project or any amounts derived therefrom.

RATINGS

Moody's Investors Service, Inc. ("Moody's"), Standard & Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc. ("S&P") and Fitch Ratings ("Fitch") have given the Series 2008 Bonds the ratings of "A1", "A+" and "A+", respectively.

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 7 World Trade Center at 250 Greenwich Street, New York, New York 10007, (212) 583-0300; 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; and an explanation of the rating given by Fitch may be obtained from Fitch Ratings at One State Street Plaza, New York, New York 10004, (212) 908-0500. 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 agency, circumstances so warrant. Any such downward revision or withdrawal of the ratings may have an adverse effect on the market price of the Series 2008 Bonds.

APPROVAL OF LEGAL PROCEEDINGS

Legal matters incident to the authorization and issuance of the Series 2008 Bonds are subject to the approving legal opinion of Chapman and Cutler LLP, Chicago, Illinois, Bond Counsel, who has been retained by, and acts as Bond Counsel, to the Commission. The form of the approving legal opinion of Bond Counsel is attached hereto as EXHIBIT D. Certain legal matters will be passed upon for the Underwriters by their counsel, Perkins Coie LLP, Chicago, Illinois. Certain legal matters will be passed upon for the Commission, the Cabinet and the State Agency by their respective counsel.

LITIGATION

There is no controversy or litigation of any nature now pending or threatened restraining or enjoining the issuance, sale, execution or delivery of the Series 2008 Bonds, or in any way contesting or affecting the validity of the Series 2008 Bonds or any proceedings of the Commission taken with respect to the issuance or sale thereof, or the pledge or application of any monies or security provided for the payment of the Series 2008 Bonds or the due existence or powers of the Commission.

TAX MATTERS

Federal tax law contains a number of requirements and restrictions which apply to the Series 2008 Bonds, including investment restrictions, periodic payments of arbitrage profits to the United States of America, requirements regarding the proper use of Series 2008 Bond proceeds and the facilities financed therewith, and certain other matters. The Commission, the Cabinet and the State Agency, respectively, have covenanted to comply with all requirements that must be satisfied in order for the interest on the Series 2008 Bonds to be excludible from gross income for federal income tax purposes. Failure to comply with certain of such covenants could cause the interest on the Series 2008 Bonds to become includible in gross income for federal income tax purposes retroactively to the date of the issuance of the Series 2008 Bonds.

Subject to the compliance by the Commission, the Cabinet, the State Agency and others with the above-referenced covenants, under present law, in the opinion of Chapman and Cutler LLP, Bond Counsel, interest on the Series 2008 Bonds is excludible from the gross income of the owners thereof for federal income tax purposes, and is not included as an item of tax preference in computing the federal alternative minimum tax for individuals and corporations. Interest on the Series 2008 Bonds is taken into account, however, in computing an adjustment used in determining the federal alternative minimum tax for certain corporations. The Internal Revenue Code of 1986, as amended (the "Code"), includes provisions for an alternative minimum tax ("AMT") for corporations in addition to the corporate regular tax in certain cases. The AMT, if any, depends upon the alternative minimum taxable income of the corporation ("AMTI"), which is the taxable income of the corporation with certain adjustments. One of the adjustment items used in computing the AMTI of a corporation is an amount equal to 75% of the excess of the "adjusted current earnings" of such corporation over an amount equal to its AMTI (before such adjustment item and the alternative tax net operating loss deduction). "Adjusted current earnings" would include all tax exempt interest, including interest on the Series 2008 Bonds.

In rendering its opinion, Bond Counsel will rely upon certifications of the Commission, the Cabinet and the State Agency with respect to certain material facts solely within the knowledge of the Commission, the Cabinet and the State Agency relating to the application of the proceeds of the Series 2008 Bonds. The opinion of Bond Counsel represents its legal judgment based on its review of the law and facts that it deems relevant to render such opinion, and is not a guarantee of result.

Ownership of the Series 2008 Bonds may result in collateral federal income tax consequences to certain taxpayers, including, without limitation, corporations subject to the branch profits tax, financial institutions, certain insurance companies, certain S corporations, individual recipients of Social Security or Railroad Retirement benefits and taxpayers who may be deemed to have incurred (or continued) indebtedness to purchase or carry tax-exempt obligations. Prospective purchasers of the Series 2008 Bonds should consult their tax advisors as to applicability of any such collateral consequences.

The issue price (the "Issue Price") for each maturity of the Series 2008 Bonds is the price at which a substantial amount of such maturity of the Series 2008 Bonds is first sold to the public. The Issue Price of a maturity of the Series 2008 Bonds may be different from the price set forth, or the price corresponding to the yield set forth, on the cover page of this Official Statement.

If the Issue Price of a maturity of the Series 2008 Bonds is less than the principal amount payable at maturity, the difference between the Issue Price of each such maturity, if any, of the Series 2008 Bonds (the "OID Bonds") and the principal amount payable at maturity is original issue discount.

For an investor who purchases an OID Bond in the initial public offering at the Issue Price for any such maturity and who holds such OID Bond to its stated maturity, subject to the condition that the Commission, the Cabinet, the State Agency and others comply with the covenants discussed above, (a) the full amount of original issue discount with respect to such OID Bond constitutes interest which is excludible from the gross income of the owner thereof for federal income tax purposes; (b) such owner will not realize taxable capital gain or market discount upon payment of such OID Bond at its stated maturity; (c) such original issue discount is not included as an item of tax preference in computing the alternative minimum tax for individuals and corporations under the Code, but is taken into account in computing an adjustment used in determining the alternative minimum tax for certain corporations under the Code, as described above; and (d) the accretion of original issue discount in each year may result in an alternative minimum tax liability for corporations or certain other collateral federal income tax consequences in each year even though a corresponding cash payment may not be received until a later year. Owners of OID Bonds should consult their own tax advisors with respect to the state and local tax consequences of original issue discount on such OID Bonds.

Owners of Series 2008 Bonds who dispose of Series 2008 Bonds prior to the stated maturity (whether by sale, redemption or otherwise), purchase Series 2008 Bonds in the initial public offering, but at a price different from the Issue Price or purchase Series 2008 Bonds subsequent to the initial public offering should consult their own tax advisors.

If a Series 2008 Bond is purchased at any time for a price that is less than the stated redemption price of the Series 2008 Bond at maturity or, in the case of an OID Bond, its Issue Price plus accreted original issue discount (the "Revised Issue Price"), the purchaser will be treated as having purchased a Series 2008 Bond with market discount subject to the market discount rules of the Code (unless a statutory de minimis rule applies). Accrued market discount is treated as taxable ordinary income, and is recognized when a Series 2008 Bond is disposed of (to the extent such accrued discount does not exceed gain realized) or, at the election of the purchaser, as it accrues. Such treatment would apply to any purchaser who purchases an OID Bond for a price that is less than its Revised Issue Price. The applicability of the market discount rules may adversely affect the liquidity or secondary market price of such Series 2008 Bond. Purchasers should consult their own tax advisors regarding the potential implications of market discount with respect to the Series 2008 Bonds.

An investor may purchase a Series 2008 Bond at a price in excess of its stated principal amount (a "Premium Bond"). Such excess is characterized for federal income tax purposes as "bond premium," and must be amortized by an investor on a constant yield basis over the remaining term of the Premium Bond in a manner that takes into account potential call dates and call prices. An investor in a Premium Bond cannot deduct amortized bond premium relating to such Premium Bond. The amortized bond premium is treated as a reduction in the tax-exempt interest received. As bond premium is amortized, it reduces the investor's basis in the Premium Bond. Investors who purchase a Premium Bond should consult their own tax advisors regarding the amortization of bond premium and its affect on the Premium Bond's basis for purposes of computing gain or loss in connection with the sale, exchange, redemption or early retirement of the Premium Bond.

There are or may be pending in the Congress of the United States of America legislative proposals, including some that may carry retroactive effective dates, that, if enacted, could alter or amend the federal tax matters referred to above or adversely affect the market value of the Series 2008 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 2008 Bonds issued prior to enactment. Prospective purchasers of the Series 2008 Bonds should consult their own tax advisors regarding any pending or proposed federal or local tax legislation. Bond Counsel expresses no opinion regarding any pending or proposed federal tax legislation.

Payments of the interest on, and proceeds of the sale, redemption or maturity of, tax-exempt obligations, including the Series 2008 Bonds, are in certain cases required to be reported to the Internal Revenue Service (the "Service"). Additionally, backup withholding may apply to any such payments to any Series 2008 Bond owner who fails to provide an accurate Form W-9 Request for Taxpayer Identification Number and Certification, or a substantially identical form, or to any Series 2008 Bond owner who is notified by the Service of a failure to report any interest or dividends required to be shown on federal income tax returns. The reporting and backup withholding requirements do not affect the excludability of such interest from gross income for federal tax purposes.

It is also the opinion of Bond Counsel, under the laws of the Commonwealth of Kentucky, as presently enacted and construed, that the interest on the Series 2008 Bonds is exempt from the income tax imposed by the Commonwealth of Kentucky, and the Series 2008 Bonds are exempt from ad valorem taxation by the Commonwealth of Kentucky and all of its political subdivisions and taxing authorities. Ownership of the Series 2008 Bonds may result in other state and local tax consequences to certain taxpayers. Bond Counsel expresses no opinion regarding any such collateral consequences arising with respect to the Series 2008 Bonds. Prospective purchasers of the Series 2008 Bonds should consult their tax advisors regarding the applicability of any such state and local taxes.

UNDERWRITING

The group of underwriters listed on the cover hereof, on behalf of which Morgan Stanley & Co. Incorporated is acting as representative (the "Underwriters") have agreed to purchase the Series 2008 Bonds for a purchase price of $15,379,609.45, which is an amount equal to the par amount of the Series 2008 Bonds, less an original issue discount of $184,184.05 and less an underwriters' discount of $156,206.50. The Underwriters have advised the Commission that they intend to make a public offering of the Series 2008 Bonds at the initial public offering yields set forth on the inside cover hereof, provided, however, that the Underwriters have reserved the right to make concessions to dealers and to change such initial public offering prices as the Underwriters shall deem necessary in connection with the marketing of the Series 2008 Bonds.

CONTINUING DISCLOSURE AGREEMENT

The Series 2008 Bonds are subject to the Rule. In general, the Rule prohibits an underwriter from purchasing or selling municipal securities in an initial offering unless it has determined that the issuer of such securities has committed to provide annually, certain information, including audited financial information, and notice of various events described in the Rule, if material. In order to enable the Underwriters to comply with the provisions of the Rule, the Commission will enter into a Continuing Disclosure Agreement (the "Disclosure Agreement") with the Trustee. Specifically, the Commission will covenant to provide notice in a timely manner to each nationally recognized municipal securities depository or the Municipal Securities Rulemaking Board, and the appropriate state information depository, if any, of any of the following types of events with respect to the Series 2008 Bonds, if material: (i) principal and interest payment delinquencies; (ii) non-payment related defaults; (iii) unscheduled draws on debt service reserves reflecting financial difficulties; (iv) unscheduled draws on credit enhancements reflecting financial difficulties; (v) substitution of credit or liquidity providers or their failure to perform; (vi) adverse tax opinions or events affecting the tax-exempt status of the securities; (vii) modifications to rights of security holders; (viii) Series 2008 Bond calls; (ix) defeasances; (x) release, substitution, or sale of property securing repayment of the securities; and (xi) rating changes. The Commonwealth is already providing ongoing market disclosure as required by the Rule pursuant to agreements entered into in connection with other outstanding securities, and has complied with requirements of the Rule.

OTHER MATTERS

This Official Statement has been prepared under the direction of the Executive Director of the Office of Financial Management.

The information set forth herein has been obtained from sources which are considered reliable. There is no guarantee that any of the assumptions, projections, expectations or estimates contained herein will ever be realized. All of the summaries of the statutes, documents and resolutions contained in this Official Statement are made subject to all of the provisions of such statutes, documents and resolutions. The summaries of the documents herein contained do not purport to be complete statements of such provisions and reference is made to such documents for further information. Reference is made to official documents in all respects.

This Official Statement has been approved, and its execution and delivery have been authorized, by the Commission and by the State Agency.

THE COMMONWEALTH OF KENTUCKY STATE PROPERTY AND BUILDINGS COMMISSION

By: /s/ F. Thomas Howard
F. Thomas Howard
Executive Director
Office of Financial Management
(Secretary to the Commission)

KENTUCKY RIVER AUTHORITY

By: /s/ Robert Ware
Robert Ware
Chairman

EXHIBIT A

FINANCIAL STATEMENTS OF

KENTUCKY RIVER AUTHORITY

June 30, 2006 and 2007

REPORT OF THE AUDIT OF THE KENTUCKY RIVER AUTHORITY

For The Fiscal Year Ended June 30, 2007

CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS
www.auditor.ky.gov

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TABLE OF CONTENTS

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority

Independent Auditor's Report

We have audited the accompanying financial statements of the Kentucky River Authority, a discretely presented component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2007. These financial statements are the responsibility of the Kentucky River Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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. 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 audit provides 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 River Authority as of June 30, 2007, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis is not a required part of the financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires 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 November 5, 2007, on our consideration of the Kentucky River Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of

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To the People of Kentucky
Honorable Ernie Fletcher, Governor
Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority
(Continued)

that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Respectfully submitted,

Crit Luallen
Auditor of Public Accounts

November 5, 2007

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

The following narrative and analysis is provided as an overview of the financial activities of the Kentucky River Authority (Authority), a discretely presented component unit of the Commonwealth of Kentucky, for the fiscal years ended June 30, 2007 and 2006, and to assist the reader in an assessment of the financial condition of the Authority in comparison with the prior year. Please assess this narrative and analysis in conjunction with the Authority's financial statements and the accompanying notes.

FINANCIAL HIGHLIGHTS

- The assets of the Authority exceeded its liabilities at the close of the most recent fiscal year and, accordingly, the Authority reported ending net assets totaling $20,744,907 of which $2,932,187 are classified as restricted

- Current year expenses totaled $2,689,630, an increase of $237,198 from FY 2006.

- Current year fee income totaled $1,407,756, a decrease of $5,749 from FY 2006.

- Current year State appropriations totaled $369,600, an increase of $72,316 from FY 2006.

- At June 30, 2007, balances remaining on commitments total approximately $398,068 (see Note 8).

OVERVIEW OF THE FINANCIAL STATEMENTS

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 and 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 Fund Net Assets presents information showing how the Authority's net assets changed during the 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 related cash flows. Thus, revenues and expenses are reported in the statement for some items that will only result in cash flows in future fiscal periods.

The Statement of Cash Flows presents the receipts and usage of cash and cash equivalents. Only transactions that affect the Authority's cash account typically are reported in the Statement of Cash Flows.

Notes to the Financial Statements:

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

FINANCIAL ANALYSIS OF THE AUTHORITY

Financial Analysis:

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Authority, assets exceeded liabilities by $20,744,907 at the close of the most recent fiscal year.

Condensed Financial Information (in thousands)
Statement of Net Assets As of June 30

	2007	2006	Percentage Increase (Decrease)
Current assets	$ 4,365	$ 6,426	(47.22%)
Capital assets-net	17,638	15,123	14%
Total assets	22,003	21,549	2%
Current liabilities	1,204	181	85%
Non-current liabilities	54	49	9%
Total liabilities	1,258	230	82%
Investment in capital assets, net of related debt	17,638	15,123	14%
Restricted for capital projects	2,932	5,380	(83.49%)
Unrestricted	175	816	(366.29%)
Total net assets	$ 20,745	$ 21,319	(2.77%)

Current assets consist primarily of unrestricted cash and cash equivalents (deposits of Tier I fees), cash and cash equivalents restricted for capital projects (deposits of Tier II fees), and accounts receivable from charges for services.

During FY 2007, the Authority did not purchase or dispose of any capital assets. Depreciation expense for FY 2007 totaled $821,253. During FY 2006, the Authority purchased capital assets totaling $5,788. Additionally, during FY 2006, the Authority received $12,762,110 in contributed capital assets and disposed of capital assets in the amount of $391,512.

Current liabilities consist primarily of general accounts payable. The fluctuation between years is an increase of approximately $1,023,311.

Non-current liabilities represent the non-current portion of compensated absences. The non-current portion of the Authority's compensated absences liability at year-end is based on an allocation of the annual and compensated leave hours used to the total hours remaining as of year-end. In total (both the current and non-current portions), the compensated absences liability increased approximately $4,753 during FY 2007.

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

Financial Analysis (Continued):

As of June 30, 2007, the Authority's net assets are comprised primarily of investment in capital assets, net of related debt $17,637,988. The remaining portion is comprised of the **net assets**, which are restricted for capital projects $2,932,187 and the portion that is unrestricted $174,732.

Condensed Financial Information (in thousands)
Statement of Revenues, Expenses,
And Changes In Fund Net Assets
For the Fiscal Years Ended June 30

	2007	2006	Percentage Increase (Decrease)
Operating revenues:			
Fee income	$ 1,408	$ 1,413	(0.3551%)
State appropriations	370	297	19.73%
Total operating revenues	1,778	1,710	3.82%
Operating expenses:			
Compensation and benefits	479	554	(15.6576%)
Rentals	31	19	39%
Professional fees	47	36	23%
Intergovernmental grants	93	112	(20.43%)
Other grants	122	122	0%
Repairs and engineering services	938	1,315	(40.1919%)
Administrative and other expenses	158	99	37%
Depreciation expense	821	195	76%
Total operating expenses	2,689	2,452	9%
Loss from Operations	(911)	(742)	19%
Non-Operating revenues			
Income from investments	337	140	58%
Loss on disposal of capital assets	0	(382)	
Capital contributions	0	12,762	
Total non-operating revenues	337	12,520	(3615.13%)
Change in net assets	$ (574)	$ 11,778	2152%

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

Financial Analysis (Continued):

The Authority's net assets decreased $574,830 during the current fiscal year. During FY 2006, the Authority's net assets decreased $7,215,092.

State appropriations remained relatively stable between fiscal years, an increase of approximately $72,316 from FY 2007.

Condensed Financial Information (in thousands)
Statement of Cash Flows
For the Fiscal Years Ended June 30

	2007	2006	Percentage Increase (Decrease)
Net cash provided by (used in):			
Operating activities	$ 853	$ (527)	161.8%
Capital and related financing activities	(3,336)	(5)	(100.00%)
Investing activities	337	140	58.5%
Net change in cash and cash equivalents	(2,146)	(392)	81.7%
Cash and cash equivalents, beginning of year	6,051	6,443	(6.48%)
Cash and cash equivalents, end of year	$ 3,905	$ 6,051	(54.96%)

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

CAPITAL ASSETS ADMINISTRATION

The following table summarizes the changes in capital assets between FY 2007 and 2006.

	2007	2006	Percentage Increase (Decrease)
Capital Assets Not Being Depreciated:			
Land	$ 532,293	$ 532,293	0.00%
Land improvements	0	0	
Construction in Progress-			
Dam 9	3,335,878	0	100.00%
Capital Assets Being Depreciated:			
Lock and Dams	15,408,110	15,408,110	0.0%
Equipment	181,568	181,568	0.00%
Office equipment	39,216	39,216	0.0%
Vehicles	235,489	235,489	0.0%
Accumulated depreciation	(2,094,566)	(1,273,313)	39.2%
Capital assets, net	$ 17,637,988	$ 15,123,363	14.3%

Additional information on the Authority's capital assets can be found in Note 3.

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

There have been no changes in the rate of fees charged on water use since FY 1996. Water use has generally grown at 2-3 percent per year with population growth. There are some variations in water use due to weather patterns from one year to the next and normal seasonal variations in water use during each year.

There are 14 lock and dam structures on the Kentucky River, for which the Authority is responsible for maintenance. The Authority has title to the lock and dam structures and adjoining real estate at Dams 5 through 14. Dams 1 through 4 are owned by the U.S. Army Corps of Engineers (Corps). It is anticipated that title to these facilities will be transferred to the Authority within the next three fiscal years. All these structures will require substantial renovations. Current estimates for renovations on Lock and Dam No. 10 total $24 million. The expenditures for the renovations on Lock and Dam No. 10 will be in the form of a cost share agreement.

Federal funds of $19.2 million are authorized for reconstruction of Dam 10. The Corps will manage this renovation project but at this time is awaiting additional federal appropriations to complete design work. Construction on this project is not anticipated before FY 2010-11. The Authority is currently renovating Dam 9 at an estimated construction cost of $17.5 million, all from Authority funds and primarily debt financed. Construction on Dam 9 is scheduled to be completed by December 2008. Design work on renovation of Lock and Dam 3 and Lock 4 will be complete by year-end 2007 with construction to start in FY 2008-09. This project group is estimated to cost

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS (CONTINUED)

$25 million. Currently only $20.3 million is appropriated for these projects, with $18.8 million of this amount to be debt financed. Additional appropriations will be requested in the 2008 General Assembly Session.

Eventually, major renovation of all 14 lock and dam structures on the Kentucky River will be necessary to maintain the water supply to the central and south-eastern part of the Commonwealth. This will require substantial new resources and there is no assurance of federal assistance on any renovations (other than those to Lock and Dam No. 10). Substantial increases in water use fee rates will be necessary to finance these costs. The Tier II fee rate will need to be increased in FY 2007-08 by 10 times its current rate, in order to support debt service on the currently authorized construction projects.

A bond anticipation note issue of $14.4 million for construction of Dam 9 is anticipated in FY 2008 under the current capital-financing plan. Current debt issuance authorized, totals $33.2 million.

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 Kentucky River Authority, 70 Wilkinson Boulevard, Frankfort, Kentucky, 40601.

BASIC FINANCIAL STATEMENTS

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KENTUCKY RIVER AUTHORITY
STATEMENT OF NET ASSETS
June 30, 2007

ASSETS	
Current assets:	
Cash and cash equivalents:	
Unrestricted	$ 972,915
Restricted	2,932,187
Accounts receivable	397,576
Accrued interest receivable	62,679
Total current assets	4,365,357
Capital assets-net	17,637,988
Total assets	22,003,345
LIABILITIES	
Current liabilities:	
Accounts payable	1,165,634
Accrued expenses	16,925
Compensated absences	21,866
Total current liabilities	1,204,425
Non-current liabilities:	
Compensated absences	54,013
Total liabilities	1,258,438
NET ASSETS	
Invested in capital assets, net of related debt	17,637,988
Restricted for capital projects	2,932,187
Unrestricted	174,732
Total net assets	$ 20,744,907

The accompanying notes are an integral part of the financial statements.

KENTUCKY RIVER AUTHORITY
STATEMENT OF REVENUES, EXPENSES,
AND CHANGES IN FUND NET ASSETS
For The Year Ended June 30, 2007

Operating revenues:	
Fee income	$ 1,407,756
Other income	615
State appropriations	369,600
Total operating revenues	1,777,971
Operating expenses:	
Compensation and benefits	479,065
Rentals	31,221
Professional fees	47,412
Intergovernmental grants	93,181
Other grants	121,590
Repairs and engineering services	937,652
Administrative and other expenses	158,256
Depreciation expense	821,253
Total operating expenses	2,689,630
Loss from operations	(911,659)
Non-operating revenues:	
Income from investments	336,829
Total non-operating revenues	336,829
Change in net assets	(574,830)
Net assets, beginning of year	21,319,737
Net assets, end of year	$20,744,907

KENTUCKY RIVER AUTHORITY
STATEMENT OF CASH FLOWS
For The Year Ended June 30, 2007

Cash flows from operating activities:	
Cash received from customers	$ 1,693,417
Cash payments for personnel expenses	(473,762)
Cash payments for goods and services	(366,495)
Net cash provided by operating activities	853,160
Cash flows from capital and related financing activities:	
Construction related to capital assets	(3,335,878)
Net cash used by capital and related financing activities	(3,335,878)
Cash flows from investing activities:	
Income from investments	336,829
Net cash provided by investing activities	336,829
Net decrease in cash and cash equivalents	(2,145,889)
Cash and cash equivalents, beginning of year	6,050,991
Cash and cash equivalents, end of year	$ 3,905,102

Reconciliation of income from operations to net cash flows from operating activities:	
Loss from operations	$ (911,659)
Depreciation	821,253
(Increase) decrease in operating assets:	
Accounts receivable	(84,554)
Increase (decrease) in operating liabilities:	
Accounts payable	1,022,817
Accrued expenses	550
Compensated absences	4,753
Net cash provided by operating activities	$ 853,160

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of the Kentucky River Authority (Authority) is presented to assist in understanding the Authority's financial statements. The financial statements and notes are representations of the Authority's management, which 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 Activities:

The Kentucky River Authority was created by an Act of the 1986 General Assembly of the Commonwealth of Kentucky (Commonwealth). That Act together with subsequent amendments is codified as KRS 151.700 through 151.730. These statutes empower the Authority, among other things, to collect water use fees on water withdrawn and used within the geographic boundaries of the Kentucky River Basin. Additional definitions, exemptions, and collection methods of these fees are contained in Kentucky Administrative Regulations, 420 KAR 1:010 through 1:050. The regulations separate water use fees into Tier I and Tier II fees. Tier I fees are collected on water use from all sources within the Kentucky River Basin and are applied to the operating expenses of the Authority. Tier II fees, which are collected in addition to Tier I fees on the water withdrawn and used from the main stem of the Kentucky River, are to be applied to capital projects enhancing the water supply of the main stem of the Kentucky River, as well as other capital improvements to the Kentucky River lock and dam system. The rate of water use fees may be adjusted each year of the biennium, as necessary, to carry out the functions, projects, and expenses authorized by the General Assembly in the Authority's biennial budget.

Reporting Entity:

The Authority is a component unit of the Commonwealth of Kentucky and its financial statements are included in the Commonwealth's Comprehensive Annual Financial Report as a discretely presented component unit. The Governor appoints the Authority's Board members. The Authority is attached for administrative purposes to the Commonwealth's Finance and Administration Cabinet.

Basis of Presentation:

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. 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.

As required by Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*," 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.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement Focus and Basis of Accounting:

The financial statements of the Authority have been presented using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States. Accordingly, revenues are recognized when they are earned and become measurable, and expenses are recognized at the time liabilities are incurred.

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.

Cash and Cash Equivalents:

For purposes of the statement of cash flows, the Authority considers all funds on deposit with the Commonwealth's State Treasury to be cash or cash equivalents.

Accounts Receivable:

Accounts receivable consist of revenues earned as of year-end, but not yet received. The direct write-off method is used for uncollectible fee accounts. This method is not in accordance with generally accepted accounting principles, but the departure does not have a material effect on the financial statements. Based on historical collection experience and a review of existing receivables, no fee accounts receivable were written-off during 2006.

Capital Assets:

All capital assets are valued at historical cost. Donated capital assets are recorded at their estimated fair value at the date of donation. Lock and dam structures acquired through donation are valued at estimated fair value at the date of donation. When major renovations of the locks and dams occur (projects in excess of $1 million), the engineering design cost of renovations will be expensed until a construction contract is awarded. If the nature of the renovation extends the life of the facility, both the construction costs and engineering during construction are capitalized and added to the value of the asset.

Depreciation of all exhaustible capital assets is recorded as an allocated expense. The Authority's capitalization threshold is $500. Depreciation is provided over the assets' estimated useful lives using the straight-line method of depreciation. The range of estimated useful lives by type of capital asset is as follows:

Lock and Dams	20 years
Equipment	3 - 10 years
Vehicles	5 years
Major Renovations of the Locks and Dams	50 years

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2007
(Continued)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated Absences:

Compensated absences represent the liability to employees for unused annual and compensatory leave. The liability is recorded at the employees' current rate of pay. The liability also includes employer payroll taxes (FICA) and employee benefits such as retirement. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

Financial Statements:

The Statement of Net Assets presents the Authority's non-fiduciary assets and liabilities with the difference between the two shown as net assets. Net assets are reported in three categories:

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."

Revenues:

Fee income represents the amounts collected from users who withdraw water from within the geographic boundaries of the Kentucky River Basin.

State appropriations represent the amounts allocated to the Authority by the Commonwealth of Kentucky from its general fund. These appropriations lapse at year-end as the unobligated amounts revert back to the Commonwealth of Kentucky.

Expenses:

The Authority reports expenses relating to the use of economic resources. Expenses are classified by natural or object classification in the statement of revenues, expenses, and changes in fund net assets.

Engineering Services:

Engineering service expenses during the design stage of a capital project are shown as operating expenses until a construction contract is awarded. Engineering expenses during construction are recorded as capital improvements. The level of design may vary from year to year and may contribute to a net loss for operational activities.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2007
(Continued)

NOTE 2 - CASH AND CASH EQUIVALENTS

The cash receipts of the Authority are deposited with the Commonwealth's State Treasury. The Commonwealth's Office of Financial Management is responsible for investing the funds of the Authority as a part of the Commonwealth's investment pool. See the Commonwealth's Comprehensive Annual Financial Report for disclosure of the legally authorized investments and the credit risk classifications of the investment pool.

In accordance with the applicable statutes, the Authority is to receive interest on the available balances accumulated from the collection of fees. Interest is received pro-rata, based on the average balances of the Authority.

Cash and cash equivalents consist primarily of receipts from collections of Tier II fees. Collections of Tier II fees are restricted to fund projects to improve the water supply of the main stem of the Kentucky River, as well as other capital improvements to the Kentucky River lock and dam system.

NOTE 3 - CAPITAL ASSETS

In October 1996, the United States Army Corps of Engineers deeded to the Authority Lock and Dam No. 10 on the Kentucky River, as well as the associated property on both sides of the river. The estimated value at the date of the donation was $12,880,000. During FY 2006, the Authority re-valued the lock and dam to $1,500,000.

In March 2005, the United States Army Corps of Engineers deeded to the Authority Lock and Dam No. 6 on the Kentucky River, as well as the associated property on both sides of the river. The estimated value at the date of the donation was $13,037,000. However, during FY 2006 the Authority re-valued the lock and dam to $1,500,000.

In March of 2006, the United States Army Corps of Engineers deeded to the Authority Locks and Dams No. 5, No. 7-9, and No. 11-14 on the Kentucky River, as well as the associated property. The estimated value at the date of the donation was $1,500,000 for each lock and dam.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2007
(Continued)

NOTE 3 - CAPITAL ASSETS (CONTINUED)

Capital asset activity for the year ended June 30, 2007 is as follows:

	Balance June 30, 2006	Additions	Deletions	Balance June 30, 2007
Capital assets not being depreciated:				
Land	$ 532,293	$	$	$ 532,293
Land Improvements				
Constuction In Progress - Dam #9		3,335,878		3,335,878
Total capital assets not being depreciated	532,293	3,335,878	0	3,868,171
Other capital assets:				
Lock and Dams No. 5, No. 7-9 and No. 11-14	12,000,000			12,000,000
Lock and Dam No. 6	1,500,000			1,500,000
Lock and Dam No. 10	1,500,000			1,500,000
Lock and Dam Buildings	408,110			408,110
Vehicles	235,489			235,489
Equipment	220,784			220,784
Total other capital assets	15,864,383	0	0	15,864,383
Total capital assets	16,396,676	3,335,878	0	19,732,554
Accumulated depreciation	(1,273,313)	(821,253)	0	(2,094,566)
Capital assets, net	$ 15,123,363	$ 2,514,625	$ 0	$ 17,637,988

Depreciation expense for the year ended June 30, 2007 was $821,253.

NOTE 4 - COMPENSATED ABSENCES

It is the Authority's policy to permit employees to accumulate earned but unused annual leave, compensatory leave, and sick pay benefits. The policy of the Commonwealth of Kentucky is to only record the cost of annual and compensatory leave.

Annual and Compensatory Leave:

Annual leave is accumulated at amounts ranging from 7.50 to 15.00 hours per month, determined by length of service, with maximum accumulations ranging from 30 to 60 days. The calendar year is the period used for determining accumulated leave. Compensatory leave is granted to authorized employees. At June 30, 2007, the Authority's estimated liability for accrued annual and compensatory leave was $75,879.

NOTE 4 - COMPENSATED ABSENCES (CONTINUED)

The estimated liability and change in the estimated liability for compensated absences for the Authority as of June 30, 2007 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated Absences	$ 71,126	$ 21,246	$ 16,493	$ 75,879	$ 21,866

Sick Leave:

It is the policy of the Authority to record the cost of sick leave when paid. Generally, sick leave (earned one day per month with unlimited accumulation) is paid only when an employee is absent due to illness, injury, or related family death. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits as of year-end. The estimated accumulated amount of unused sick leave as of June 30, 2007 totals approximately $143,252

NOTE 5 - INTERGOVERNMENTAL ACTIVITY

The Authority leases office space on a monthly basis from the Capital Plaza Operations agency within the Commonwealth's Commerce Cabinet. Rent expense during FY 2007 under this rental agreement totaled $12,872. The lease can be terminated on 30 days notice either by the Authority or Capital Plaza Operations.

NOTE 6 - RETIREMENT PLANS

The employees of the Authority participate in the Kentucky Employees Retirement Systems (KERS) of the Commonwealth of Kentucky, which is a cost-sharing, multiple-employer, defined benefit pension plan covering substantially all regular full-time employees. The plan provides retirement, disability, and death benefits to plan members. The KERS provides for cost-of-living adjustments at the discretion of the Kentucky legislature.

Employees who retire at or after age 65 with 48 months of credited services are entitled to a retirement benefit, payable monthly for life, equal to 2.20% of their final-average salary multiplied by their years of service. Final-average salary is the employee's average of the three fiscal years during which the employee had the highest average monthly salary. Benefits fully vest upon reaching five years of service. Vested employees may retire after 27 years of service and receive full retirement benefits or after age 55 and receive reduced retirement benefits. The KERS also provides death and disability benefits. Benefits are established by state statute.

The payroll for employees covered by the KERS for the year ended June 30, 2007 totaled approximately $348,763. The Authority's total payroll was approximately $363,255. Covered employees are required by state statute to contribute 5.00% of their salary to the KERS. The Authority is required by the same statute to contribute 7.75% of the covered employees' salaries. The contribution requirement for the year ended June 30, 2007 totaled approximately $26,772. The Authority's contributions for the years ended June 30, 2006 and 2005 totaled approximately $24,491and $23,510, respectively.

<u>NOTE 6 - RETIREMENT PLANS</u> (CONTINUED)

Ten-year historical trend information showing the KERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Employees Retirement System's Annual Financial Reports (which is a matter of public record). The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the Kentucky Employees Retirement System.

In addition to the above defined benefit pension plan, the Authority's employees are also eligible to participate in two deferred compensation plans sponsored by the Commonwealth of Kentucky. These plans are organized as a Section 457 plan and as a Section 401(k) plan under the Internal Revenue Code. Both plans permit employees to defer a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, or financial hardship. The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the deferred compensation plans.

<u>NOTE 7 - ECONOMIC DEPENDENCY</u>

The Authority collects fees from water users in the Kentucky River Drainage Basin. These fees are the primary funding source of the Authority's activities. For the year ended June 30, 2007, four customers accounted for approximately 64% of the total fees earned during the year. One of these four customers accounted for approximately 41%.

<u>NOTE 8 - COMMITMENTS</u>

Prior to year-end, the Authority had contracted to have various studies performed and certain projects initiated. The balance remaining on these commitments as of year-end totaled approximately $398,068.

The Authority leases a copier under a four-year lease agreement expiring April 2010. Monthly payments under the agreement are $292 plus additional charges per copy. Rent expense during FY 2007 under this agreement totaled $3,685.

As of year-end, the future obligations under this agreement are as follows:

Fiscal Year Ending June 30:

2008	3,499
2009	3,499
2010	2,916
	$ 9,914

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2007
(Continued)

NOTE 9 - RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; injuries to employees; natural disaster; and errors and omissions. The Authority has purchased commercial insurance for public officials' liability coverage, which covers the litigation costs relative to errors and omissions as they pertain to the Authority's Board members. Additionally, the Authority's exposure under negligent claims filed against it is limited through the Kentucky Board of Claims. The Authority also has purchased commercial insurance for liability and collision loss on Authority owned vehicles, which are less than five years old. Loss to buildings and equipment are self-insured through the Commonwealth's Fire and Tornado Fund.

NOTE 10 - PRIOR PERIOD ADJUSTMENT

A prior period adjustment in the net amount of $2,537 was made for vehicle and equipment capital asset balances.

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

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority

Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of Financial
Statements Performed In Accordance With *Government Auditing Standards*

We have audited the financial statements of the Kentucky River Authority, a discretely presented component unit of the Commonwealth of Kentucky as of and for the year ended June 30, 2007, and have issued our report thereon dated November 5, 2007. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky River Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Kentucky River Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Kentucky River Authority's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Kentucky River Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Kentucky River Authority's management, and Board of Directors and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Crit Luallen
Auditor of Public Accounts

November 5, 2007

REPORT OF THE AUDIT OF THE KENTUCKY RIVER AUTHORITY

For The Fiscal Year Ended
June 30, 2006

CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS
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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority

Independent Auditor's Report

We have audited the accompanying basic financial statements of the Kentucky River Authority, a discretely presented component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2006. These financial statements are the responsibility of the Kentucky River Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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. 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 audit provides 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 River Authority as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires 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.

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To the People of Kentucky
Honorable Ernie Fletcher, Governor
Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority
(Continued)

In accordance with Government Auditing Standards, we have also issued our report dated November 10, 2006, on our consideration of the Kentucky River Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Respectfully submitted,

Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
November 10, 2006

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

The following narrative and analysis is provided as an overview of the financial activities of the Kentucky River Authority (Authority), a discretely presented component unit of the Commonwealth of Kentucky, for the years ended June 30, 2006 and 2005, and to assist the reader in an assessment of the financial condition of the Authority in comparison with the prior year. Please assess this narrative and analysis in conjunction with the Authority's financial statements and the accompanying notes.

FINANCIAL HIGHLIGHTS

- The assets of the Authority exceeded its liabilities at the close of the most recent fiscal year and, accordingly, the Authority reported ending net assets totaling $21,319,737 of which $5,379,882 are classified as restricted
- Current year expenses totaled $2,452,430, a decrease of $407,573 from fiscal year 2005.
- Current year fee income totaled $1,413,505, an increase of $81,979 from fiscal year 2005.
- Current year State appropriations totaled $297,284, an increase of $821 from fiscal year 2005.
- At June 30, 2006, balances remaining on commitments totaled approximately $518,227 (see Note 8).

OVERVIEW OF THE FINANCIAL STATEMENTS

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 and 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 Fund Net Assets presents information showing how the Authority's net assets changed during the 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 related cash flows. Thus, revenues and expenses are reported in the statement for some items that will only result in cash flows in future fiscal periods.

The Statement of Cash Flows presents the receipts and usage of cash and cash equivalents. Only transactions that affect the Authority's cash account typically are reported in the Statement of Cash Flows.

Notes to the Financial Statements:

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

FINANCIAL ANALYSIS OF THE AUTHORITY

Financial Analysis:

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Authority, assets exceeded liabilities by $21,319,737 at the close of the most recent fiscal year.

Condensed Financial Information
Statement of Net Assets
As of June 30
(Expressed in Thousands)

	2006	2005	Percentage Increase (Decrease)
Current assets	$ 6,427	$ 6,919	(7.11%)
Capital assets-net	15,123	21,927	(31.03%)
Total assets	21,550	28,846	(25.29%)
Current liabilities	181	246	(26.42%)
Non-current liabilities	49	66	(25.76%)
Total liabilities	230	312	(26.28%)
Investment in capital assets, net of related debt	15,123	21,927	(31.03%)
Restricted for capital projects	5,380	6,082	(11.54%)
Unrestricted	817	525	55.62%
Total net assets	$ 21,320	$ 28,534	(25.28%)

Current assets consist primarily of unrestricted cash and cash equivalents (deposits of Tier I fees), cash and cash equivalents restricted for capital projects (deposits of Tier II fees), and accounts receivable from charges for services.

During fiscal year 2006, the Authority purchased capital assets totaling $5,788. Additionally during fiscal year 2006, the Authority received $12,762,110 in contributed capital assets and disposed of capital assets in the amount of $391,512. Depreciation expense for fiscal year 2006 totaled $195,348. During fiscal year 2005, the Authority purchased capital assets totaling $31,760. Depreciation expense for fiscal year 2005 totaled $559,922.

Current liabilities consist primarily of general accounts payable. The fluctuation between years is an increase of approximately $11,607.

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

FINANCIAL ANALYSIS OF THE AUTHORITY (Continued)

Financial Analysis (Continued):

Non-current liabilities represent the non-current portion of compensated absences. The non-current portion of the Authority's compensated absences liability at year-end is based on an allocation of the annual and compensated leave hours used to the total hours remaining as of year-end. In total (both the current and non-current portions), the compensated absences liability decreased approximately $20,623 during fiscal year 2006.

As of June 30, 2006, the Authority's net assets were comprised primarily of investment in capital assets, net of related debt of $15,123,363. The remaining portion was comprised of the **net assets**, which were restricted for capital projects in the amount of $5,379,882 and the portion that was unrestricted of $816,492.

Condensed Financial Information
Statement of Revenues, Expenses,
And Changes In Fund Net Assets
For the Fiscal Years Ended June 30
(Expressed in Thousands)

	2006	2005	Percentage Increase (Decrease)
Operating revenues:			
Fee income	$ 1,413	$ 1,331	6.16%
State appropriations	297	296	0.34%
Total operating revenues	1,710	1,627	5.10%
Operating expenses:			
Compensation and benefits	554	526	5.32%
Rentals	19	22	(13.64%)
Professional fees	36	24	50.00%
Intergovernmental grants	112	134	(16.42%)
Other grants	122	124	(1.61%)
Repairs and engineering services	1,315	1,300	1.15%
Administrative and other expenses	99	171	(42.11%)
Depreciation expense	195	560	(65.18%)
Total operating expenses	2,452	2,861	(14.30%)
Loss from Operations	(742)	(1,234)	(39.87%)
Non-Operating revenues			
Income from investments	140	198	(29.29%)
Loss on disposal of capital assets	(382)	0	
Capital contributions	12,762	13,037	(2.11%)
Total non-operating revenues	12,520	13,235	(5.40%)
Change in net assets	$ 11,778	$ 12,001	(1.86%)

FINANCIAL ANALYSIS OF THE AUTHORITY (Continued)

Financial Analysis (Continued):

The Authority's net assets decreased $7,215,092 during the current fiscal year. During fiscal year 2005, the Authority's net assets decreased $12,003,389.

State appropriations remained relatively stable between fiscal years, increasing approximately $30,537 from fiscal year 2005 to 2006.

Condensed Financial Information
Statement of Cash Flows
For the Fiscal Years Ended June 30
(Expressed in Thousands)

	2006	2005	Percentage Increase (Decrease)
Net cash provided by (used in):			
Operating activities	$ (527)	$ (711)	(25.88%)
Capital and related financing activities	(5)	(2)	150.00%
Investing activities	140	198	(29.29%)
Net change in cash and cash equivalents	(392)	(515)	(23.88%)
Cash and cash equivalents, beginning of year	6,443	6,959	(7.41%)
Cash and cash equivalents, end of year	$ 6,051	$ 6,444	(6.10%)

KENTUCKY RIVER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

CAPITAL ASSETS ADMINISTRATION

The following table summarizes the changes in capital assets between fiscal years 2006 and 2005.

	2006	2005	Percentage Increase (Decrease)
Land	$ 532,293	$ 478,293	11.29%
Land improvements	0	82,605	(100.00%)
Lock and Dams	15,408,110	25,880,000	(40.46%)
Equipment	181,568	175,780	3.29%
Office equipment	39,216	45,123	(13.09%)
Vehicles	235,489	235,489	0.00%
Accumulated depreciation	(1,273,313)	(4,970,672)	(74.38%)
Capital assets, net	$ 15,123,363	$ 21,926,618	(31.03%)

Additional information on the Authority's capital assets can be found in Note 3.

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

There have been no changes in the rate of fees charged on water use since fiscal year 1996. Water use has generally grown at 2-3 percent per year with population growth. There are some variations in water use due to weather patterns from one year to the next and normal seasonal variations in water use during each year.

There are 14 lock and dam structures on the Kentucky River, for which the Authority is responsible for maintenance. The Authority has title to the lock and dam structures and adjoining real estate at Dams 5 through 14. Dams 1 through 4 are owned by the U.S. Army Corps of Engineers (the Corps). It is anticipated that title to these facilities will be transferred to the Authority within the next three fiscal years. All these structures will require substantial renovations. Current estimates for renovations on Lock and Dam No. 10 total $24 million. The expenditures for the renovations on Lock and Dam No. 10 will be in the form of a cost share agreement.

Of the $24 million, it is anticipated that federal funds of $19.2 million will be provided. The Corps will manage this renovation project. The Authority is designing the renovation of Dam 9 at an estimated construction cost of $17.5 million, all from Authority funds and primarily debt financed. Construction on Dam 9 is scheduled to begin in the summer of 2007. Design work on renovation of Lock and Dam 3 and Lock 4 will start in fiscal year 2007 with construction to start in fiscal year 2008. This project group is estimated to cost $25 million. Currently only $20.3 million is appropriated for these projects, with $18.8 million of this amount to be debt financed.

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS (Continued)

Construction on Dam 10 is not anticipated to begin until 2008. Eventually, major renovation of all 14 lock and dam structures on the Kentucky River will be necessary to maintain the water supply to the central and south-eastern part of the Commonwealth. This will require substantial new resources and there is no assurance of federal assistance on any renovations (other than those to Lock and Dam No. 10). Substantial increases in water use fee rates will be necessary to finance these costs.

Debt financing of $14.4 million for construction of Dam 9 is anticipated in fiscal year 2007 under the current capital-financing plan.

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 Kentucky River Authority, 70 Wilkinson Boulevard, Frankfort, Kentucky, 40601.

BASIC FINANCIAL STATEMENTS

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KENTUCKY RIVER AUTHORITY
STATEMENT OF NET ASSETS
June 30, 2006

ASSETS	
Current assets:	
Cash and cash equivalents:	
Unrestricted	$ 671,109
Restricted	5,379,882
Accounts receivable	354,776
Accrued interest receivable	20,925
Total current assets	6,426,692
Capital assets-net	15,123,363
Total assets	21,550,055
LIABILITIES	
Current liabilities:	
Accounts payable	142,817
Accrued expenses	16,375
Compensated absences	21,921
Total current liabilities	181,113
Non-current liabilities:	
Compensated absences	49,205
Total liabilities	230,318
NET ASSETS	
Invested in capital assets, net of related debt	15,123,363
Restricted for capital projects	5,379,882
Unrestricted	816,492
Total net assets	$ 21,319,737

KENTUCKY RIVER AUTHORITY
STATEMENT OF REVENUES, EXPENSES,
AND CHANGES IN FUND NET ASSETS
For The Year Ended June 30, 2006

Operating revenues:	
Fee income	$ 1,413,079
Other income	426
State appropriations	297,284
Total operating revenues	1,710,789
Operating expenses:	
Compensation and benefits	554,102
Rentals	19,152
Professional fees	35,685
Intergovernmental grants	112,294
Other grants	121,590
Repairs and engineering services	1,314,963
Administrative and other expenses	99,296
Depreciation expense	195,348
Total operating expenses	2,452,430
Loss from operations	(741,641)
Non-operating revenues (expenses):	
Income from investments	140,244
Loss on Disposal of Capital Assets	(382,605)
Capital contributions	12,762,110
Total non-operating revenues	12,519,749
Change in net assets	11,778,108
Net assets, beginning of year, restated	9,541,629
Net assets, end of year	$ 21,319,737

The accompanying notes are an integral part of the financial statements.

KENTUCKY RIVER AUTHORITY
STATEMENT OF CASH FLOWS
For The Year Ended June 30, 2006

Cash flows from operating activities:	
Cash received from customers	$ 1,741,508
Cash payments for personnel expenses	(573,100)
Cash payments for goods and services	(1,695,464)
Net cash used by operating activities	(527,056)
Cash flows from investing activities:	
Income from investments	140,244
Cash flows from capital and related financing activities:	
Acquisition of capital assets	(5,788)
Net change in cash and cash equivalents	(392,600)
Cash and cash equivalents, beginning of year	6,443,591
Cash and cash equivalents, end of year	$ 6,050,991

Reconciliation of income from operations to net cash flows from operating activities:	
Loss from operations	$ (741,641)
Depreciation	195,348
(Increase) decrease in operating assets:	
Accounts receivable	30,719
Increase (decrease) in operating liabilities:	
Accounts payable	7,516
Accrued expenses	(3,130)
Compensated absences	(15,868)
Net cash used by operating activities	$ (527,056)

Non-cash investing, capital, and financing activities:	
Capital contributions	$ 12,762,110

The accompanying notes are an integral part of the financial statements.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of the Kentucky River Authority (Authority) is presented to assist in understanding the Authority's financial statements. The financial statements and notes are representations of the Authority's management which 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 Activities:

The Kentucky River Authority was created by an Act of the 1986 General Assembly of the Legislature of the Commonwealth of Kentucky (Commonwealth). That Act together with subsequent amendments are codified as Kentucky Revised Statutes, KRS 151.700 through 151.730. These statutes empower the Authority among other things, to collect water use fees on water withdrawn and used within the geographic boundaries of the Kentucky River Basin. Additional definitions, exemptions, and collection methods of these fees are contained in Kentucky Administrative Regulations, 420 KAR 1:010 through 1:050. The regulations separate water use fees into Tier I and Tier II fees. Tier I fees are collected on water use from all sources within the Kentucky River Basin and are applied to the operating expenses of the Authority. Tier II fees which are collected in addition to Tier I fees, on the water withdrawn and used from the main stem of the Kentucky River, are to be applied to capital projects enhancing the water supply of the main stem of the Kentucky River, as well as other capital improvements to the Kentucky River lock and dam system. The rate of water use fees may be adjusted each year of the biennium, as necessary, to carry out the functions, projects, and expenses authorized by the General Assembly in the Authority's biennial budget.

Reporting Entity:

The Authority is a component unit of the Commonwealth of Kentucky and its financial statements are included in the Commonwealth's Comprehensive Annual Financial Report as a discretely presented component unit. The Governor appoints the Authority's Board members. The Authority is attached for administrative purposes to the Commonwealth's Finance and Administration Cabinet.

Basis of Presentation:

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. 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.

As required by Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*," 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.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus and Basis of Accounting:

The financial statements of the Authority have been presented using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States. Accordingly, revenues are recognized when they are earned and become measurable, and expenses are recognized at the time liabilities are incurred.

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.

Cash and Cash Equivalents:

For purposes of the statement of cash flows, the Authority considers all funds on deposit with the Commonwealth's State Treasury to be cash or cash equivalents.

Accounts Receivable:

Accounts receivable consist of revenues earned as of year-end, but not yet received. The direct write-off method is used for uncollectible fee accounts. This method is not in accordance with generally accepted accounting principles, but the departure does not have a material effect on the financial statements. Based on historical collection experience and a review of existing receivables, no fee accounts receivable were written off during 2006.

Capital Assets:

All capital assets are valued at historical cost. Donated capital assets are recorded at their estimated fair value at the date of donation. Lock and dam structures acquired through donation are valued at estimated fair value at the date of donation.

Depreciation of all exhaustible capital assets is recorded as an allocated expense. The Authority's capitalization threshold is $500. Depreciation is provided over the assets' estimated useful lives using the straight-line method of depreciation. The range of estimated useful lives by type of capital asset is as follows:

Locks and Dams	20 years
Equipment	3 - 10 years
Vehicles	5 years

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2006
(Continued)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Compensated Absences:

Compensated absences represent the liability to employees for unused annual and compensatory leave. The liability is recorded at the employees' current rate of pay. The liability also includes employer payroll taxes (FICA) and employee benefits such as retirement. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

Financial Statements:

The Statement of Net Assets presents the Authority's non-fiduciary assets and liabilities with the difference between the two shown as net assets. Net assets are reported in three categories:

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."

Revenues:

Fee income represents the amounts collected from users who withdraw water from within the geographic boundaries of the Kentucky River Basin.

State appropriations represent the amounts allocated to the Authority by the Commonwealth of Kentucky from its general fund. These appropriations lapse at year-end as the unobligated amounts revert back to the Commonwealth of Kentucky.

Expenses:

The Authority reports expenses relating to the use of economic resources. Expenses are classified by natural or object classification in the statement of revenues, expenses, and changes in fund net assets.

Engineering Services:

Engineering service expenses during the design stage of a capital project are shown as operating expenses until a construction contract is awarded. Engineering expenses during construction are recorded as capital improvements. The level of design may vary from year to year and may contribute to a net loss for operational activities.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2006
(Continued)

NOTE 2 - CASH AND CASH EQUIVALENTS

The cash receipts of the Authority are deposited with the Commonwealth's State Treasury. The Commonwealth's Office of Financial Management is responsible for investing the funds of the Authority as a part of the Commonwealth's investment pool. See the Commonwealth's Comprehensive Annual Financial Report for disclosure of the legally authorized investments and the credit risk classifications of the investment pool.

In accordance with the applicable statutes, the Authority is to receive interest on the available balances accumulated from the collection of fees. Interest is received pro-rata, based on the average balances of the Authority.

Cash and cash equivalents consist primarily of receipts from collections of Tier II fees. Collections of Tier II fees are restricted to fund projects to improve the water supply of the main stem of the Kentucky River, as well as other capital improvements to the Kentucky River lock and dam system.

NOTE 3 - CAPITAL ASSETS

In October 1996, the United States Army Corps of Engineers deeded to the Authority Lock and Dam No. 10 on the Kentucky River, as well as the associated property on both sides of the river. The estimated value at the date of the donation was $12,880,000. During fiscal year 2006, the Authority re-valued the lock and dam to $1,500,000.

In March 2005, the United States Army Corps of Engineers deeded to the Authority Lock and Dam No. 6 on the Kentucky River, as well as the associated property on both sides of the river. The estimated value at the date of the donation was $13,037,000. However, during fiscal year 2006 the Authority re-valued the lock and dam to $1,500,000.

In March of 2006, the United States Army Corps of Engineers deeded to the Authority Locks and Dams No. 5, No. 7-9 and No. 11-14 on the Kentucky River, as well as the associated property. The estimated value at the date of the donation was $1,500,000 for each lock and dam.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2006
(Continued)

NOTE 3 - CAPITAL ASSETS (Continued)

Capital asset activity for the year ended June 30, 2006 was as follows:

	Balance June 30, 2005 Restated	Additions	Deletions	Balance June 30, 2006
Capital assets not being depreciated:				
Land	$ 478,293	$ 354,000	$ (300,000)	$ 532,293
Land Improvements	82,605		(82,605)	
Total capital assets not being depreciated	560,898	354,000	(382,605)	532,293
Other capital assets:				
Lock and Dams No. 5, No. 7-9 and No. 11-14	0	12,000,000		12,000,000
Lock and Dam No. 6	1,500,000			1,500,000
Lock and Dam No. 10	1,500,000			1,500,000
Lock and Dam Buildings	0	408,110		408,110
Vehicles	235,489			235,489
Equipment	220,903	5,788	(5,907)	220,784
Total other capital assets	3,456,392	12,413,898	(5,907)	15,864,383
Total capital assets	4,017,290	12,767,898	(388,512)	16,396,676
Accumulated depreciation	(1,083,872)	(195,348)	5,907	(1,273,313)
Capital assets, net	$ 2,933,418	$ 12,572,550	$ (382,605)	$ 15,123,363

Depreciation expense for the year ended June 30, 2006 was $195,348.

NOTE 4 - COMPENSATED ABSENCES

It is the Authority's policy to permit employees to accumulate earned but unused annual leave, compensatory leave, and sick pay benefits. The policy of the Commonwealth of Kentucky is to only record the cost of annual and compensatory leave.

Annual and Compensatory Leave:

Annual leave is accumulated at amounts ranging from 7.50 to 15.00 hours per month, determined by length of service, with maximum accumulations ranging from 30 to 60 days. The calendar year is the period used for determining accumulated leave. Compensatory leave is granted to authorized employees. At June 30, 2006, the Authority's estimated liability for accrued annual and compensatory leave was $71,126.

NOTE 4 - COMPENSATED ABSENCES (Continued)

Annual and Compensatory Leave: (Continued)

The estimated liability and change in the estimated liability for compensated absences for the Authority as of June 30, 2006 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated Absences	$ 91,749	$ 25,405	$ 46,028	$ 71,126	$ 21,921

Sick Leave:

It is the policy of the Authority to record the cost of sick leave when paid. Generally, sick leave (earned one day per month with unlimited accumulation) is paid only when an employee is absent due to illness, injury, or related family death. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits as of year-end. The estimated accumulated amount of unused sick leave as of June 30, 2006 totals approximately $129,731

NOTE 5 - INTERGOVERNMENTAL ACTIVITY

The Authority leases office space on a monthly basis from the Capital Plaza Operations agency within the Commonwealth's Commerce Cabinet. Rent expense during fiscal year 2006 under this rental agreement totaled $19,308. The lease can be terminated on 30 days notice either by the Authority or Capital Plaza Operations.

NOTE 6 - RETIREMENT PLANS

The employees of the Authority participate in the Kentucky Employees Retirement Systems (KERS) of the Commonwealth of Kentucky, which is a cost-sharing, multiple-employer, defined benefit pension plan covering substantially all regular full-time employees. The plan provides retirement, disability, and death benefits to plan members. The KERS provides for cost-of-living adjustments at the discretion of the Kentucky legislature.

Employees who retire at or after age 65 with 48 months of credited services are entitled to a retirement benefit, payable monthly for life, equal to 2.20% of their final-average salary multiplied by their years of service. Final-average salary is the employee's average of the three fiscal years during which the employee had the highest average monthly salary. Benefits fully vest upon reaching five years of service. Vested employees may retire after 27 years of service and receive full retirement benefits or after age 55 and receive reduced retirement benefits. The KERS also provides death and disability benefits. Benefits are established by State statute.

NOTE 6 - RETIREMENT PLANS (Continued)

The payroll for employees covered by the KERS for the year ended June 30, 2006 totals approximately $430,588. The Authority's total payroll totals approximately $449,120. Covered employees are required by State statute to contribute 5.00% of their salary to the KERS. The Authority is required by the same statute to contribute 5.89% of the covered employees' salaries. The contribution requirement for the year ended June 30, 2006 totals approximately $24,491. The Authority's contributions for the years ended June 30, 2005 and 2004 totaled approximately $23,510 and $22,800, respectively.

Ten-year historical trend information showing the KERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Employees Retirement System's Annual Financial Reports (which are a matter of public record). The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the Kentucky Employees Retirement System.

In addition to the above defined benefit pension plan, the Authority's employees are also eligible to participate in two deferred compensation plans sponsored by the Commonwealth of Kentucky. These plans are organized as a Section 457 plan and as a Section 401(k) plan under the Internal Revenue Code. Both plans permit employees to defer a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, or financial hardship. The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the deferred compensation plans.

NOTE 7 - ECONOMIC DEPENDENCY

The Authority collects fees from water users in the Kentucky River Drainage Basin. These fees are the primary funding source of the Authority's activities. For the year ended June 30, 2006, four customers accounted for approximately 68% of the total fees earned during the year. One of these four customers accounted for approximately 44%.

NOTE 8 - COMMITMENTS

Prior to year-end, the Authority had contracted to have various studies performed and certain projects initiated. The balance remaining on these commitments as of year-end totaled approximately $518,227.

The Authority leases a copier under a four-year lease agreement expiring April 2010. Monthly payments under the agreement are $292 plus additional charges per copy. Rent expense during fiscal year 2006 under this agreement totaled $4,330.

KENTUCKY RIVER AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2006
(Continued)

NOTE 8 - COMMITMENTS (Continued)

As of year-end, the future obligations under this agreement are as follows:

Fiscal Year Ending June 30:

2007	$ 3,499
2008	3,499
2009	3,499
2010	2,916
	$ 13,413

NOTE 9 - RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; injuries to employees; natural disaster; and errors and omissions. The Authority has purchased commercial insurance for public officials' liability coverage, which covers the litigation costs relative to errors and omissions as they pertain to the Authority's Board members. Additionally, the Authority's exposure under negligent claims filed against it is limited through the Kentucky Board of Claims. The Authority also has purchased commercial insurance for liability and collision loss on Authority owned vehicles, which are less than five years old. Loss to buildings and equipment are self-insured through the Commonwealth's Fire and Tornado Fund.

NOTE 10 - CHANGES IN ACCOUNTING PRINCIPLES, REPORTING PRACTICES, AND PRIOR-PERIOD ADJUSTMENTS

During fiscal year 2006 the Kentucky River Authority modified its financial statement-reporting format to merge a general fund presented in past years to account for the state appropriation into its proprietary fund. The effect of this change will increase beginning net assets by $565,218.

Net assets as previously reported have been restated to correct balances based on a re-valuation of capital assets. Beginning net assets for the Kentucky River Authority have been restated and the net effect is a decrease of $18,993,200 from fiscal year 2005.

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

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Stephen Reeder, Executive Director
Board of Directors
Kentucky River Authority

Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards

We have audited the financial statements of the Kentucky River Authority, a discretely presented component unit of the Commonwealth of Kentucky as of and for the year ended June 30, 2006, and have issued our report thereon dated November 10, 2006. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky River 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 an opinion 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 that might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud 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.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Kentucky River Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under Government Auditing Standards.

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Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards
(Continued)

This report is intended solely for the information and use of the Kentucky River Authority's management and Board of Directors and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
November 10, 2006

EXHIBIT B

DEBT INFORMATION PERTAINING TO THE COMMONWEALTH OF KENTUCKY

COMMONWEALTH DEBT MANAGEMENT

Management

The Office of Financial Management ("OFM"), Finance and Administration Cabinet, has central responsibility for the issuance, management, review and approval of all debt issued by the Commonwealth and its agencies. Table I lists active issuing entities. OFM is also responsible for the coordination and monitoring of cash needs relative to debt activity, debt service payments and the development of a comprehensive long-term debt plan. OFM serves as primary staff to the State Property and Buildings Commission, the Kentucky Asset/Liability Commission, and the Kentucky Local Correctional Facilities Construction Authority.

Structure

The Commonwealth's indebtedness is classified as either appropriation supported debt or non-appropriation supported debt.

Appropriation supported debt carries the name of the Commonwealth and is either (i) a general obligation of the State, or (ii) a lease revenue obligation of one of its debt issuing agencies created by the Kentucky General Assembly to finance various projects which is subject to state appropriation for all or a portion of the debt service on the bonds.

General obligation bonds pledge the full faith, credit and taxing power of the Commonwealth for the repayment of the debt. The Kentucky Constitution requires voter approval by general referendum prior to the issuance of general obligation bonds in amounts exceeding $500,000. Kentucky has not issued general obligation bonds since 1966. The Commonwealth has no general obligation bonds outstanding.

Project revenue notes and bonds are issued by various debt issuing authorities of the Commonwealth. The revenues produced by the projects funded by the debt are pledged as security for repayment of the debt. Project revenue debt is not a direct obligation of the Commonwealth. Project revenues are, in some cases, derived partially or solely from biennial appropriations of the General Assembly. In other cases, the direct revenues generated from the project funded constitute the entire source of payment.

The payment of debt service by the state universities is enhanced by a state intercept provision that provides that in the event of a default, the Secretary of the Finance Cabinet is required to intercept any funds appropriated to the University, but not yet disbursed, and to remit those funds to the Trustee to remedy the default.

Non-appropriation or moral obligation debt carries the name of the Commonwealth for the benefit and convenience of other entities within the state. This type of indebtedness is a special obligation of the issuer, secured and payable solely from the sources pledged for the payment thereof and does not constitute a debt, liability, obligation or a pledge of the faith and credit of the Commonwealth. The General Assembly does not intend to appropriate any funds to fulfill the financial obligations represented by these types of indebtedness. Some issues covenant that in the event of a shortfall the issuer will request from the Governor and the General Assembly sufficient amounts to pay debt service. Kentucky

Infrastructure Authority Governmental Agencies Program and certain Kentucky Higher Education Student Loan Corporation bond issues are no longer moral obligation debt.

Default Record

The Commonwealth has never defaulted in the payment of principal or interest on its general obligation indebtedness or its project revenue obligations.

TABLE I
ACTIVE DEBT ISSUING ENTITIES

ENTITY	STATUTORY AUTHORITY/ PURPOSE	DEBT LIMITATIONS	RATINGS*
State Property and Buildings Commission	**KRS 56.450** Provide financing for capital construction projects and financing programs approved by the General Assembly.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Aa3/A+/AA-
Kentucky Asset/Liability Commission	**KRS 56.860** Provide financing of capital projects and cash flow borrowings to meet working capital needs of the state.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly, exclusive of cash flow borrowings within a fiscal year.	Varies
Turnpike Authority of Kentucky	**KRS 175.410-175.990** Construct, maintain, repair, and operate Turnpike projects, resource recovery roads and economic development roads.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Aa3/AA+/AA-
The State Universities (consisting of nine)	**KRS 56.495** Construct educational buildings and housing and dining facilities.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Varies
Kentucky Housing Corporation	**KRS 198A** Make low interest mortgage loans and construction loans to increase the supply of housing for low to moderate income residents of the State.	Limited to $5.0 billion of debt outstanding.	Aaa/AAA/NR
Kentucky Infrastructure Authority	**KRS 224A** Provide financial assistance to local governments for the construction or refinancing of infrastructure facilities and to provide loans to industries for construction of pollution control facilities.	Revolving Fund programs cannot incur debt without appropriation of debt service by the General Assembly. Without legislative approval, other programs are limited to debt outstanding of $500 million.	Aa3/A+/AA-
Kentucky Higher Education Student Loan Corporation	**KRS 164A** Make guaranteed student loans to residents of the state to attend postsecondary institutions and to make loans to students attending postsecondary schools within the state.	Limited to $5.0 billion of debt outstanding.	NR/AAA/AAA (Sr. Series) NR/A/A (Subord. Series)
School Facilities Construction Commission	**KRS 157.611-157.665** Assist local school districts with the financing and construction of school buildings. Finance the construction of vocational education facilities.	Cannot incur debt without appropriation of debt service by General Assembly.	Aa3
Kentucky Economic Development Finance Authority	**KRS 154** Issue industrial revenue bonds on behalf of industries, hospitals, and commercial enterprises in the state. Provide low interest loans to developing businesses. Provide financing and tax credits to manufacturing entities expanding or locating facilities in the state.	None.	Varies
Kentucky Local Correctional Facilities Construction Authority	**KRS 441.605-441.695** Provide an alternative method of constructing, improving, repairing and financing local jails.	Limited to the level of debt service supported by court fees pledged as repayment for the bonds.	A2/AA/NR** (Insured)

*Ratings, where applicable, include Moody's, Standard & Poor's, and Fitch.
**Based on MBIA rating
Certain State Property and Buildings Commission Agency Fund Revenue bonds may have ratings different from those identified above. The Kentucky Infrastructure Authority's Governmental Agencies Program Revenue Bonds are rated "AA" by Standard & Poor's and are backed by the loans of the borrowers.

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EXHIBIT C

BOOK-ENTRY-ONLY SYSTEM

The Series 2008 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 2008 Bonds and, except as otherwise provided herein with respect to tenders by Beneficial Owners (as hereinafter defined) 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 2008 Bonds under the Resolution.

The following information about the book-entry-only system applicable to the Series 2008 Bonds has been supplied by DTC. Neither the Commission, the Trustee nor any Underwriter makes any representations, warranties or guarantees with respect to its accuracy or completeness.

DTC will act as securities depository for the Series 2008 Bonds. The Series 2008 Bonds 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 2008 Bond certificate will be issued for each maturity of the Series 2008 Bonds, in the aggregate principal amount of the Series 2008 Bonds and will be deposited with DTC.

DTC, the world's largest 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 3.5 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 is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. 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 2008 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2008 Bonds on DTC's records. The ownership interest of each actual purchaser of each Series 2008 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 2008 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 2008 Bonds, except in the event that use of the book-entry system for the Series 2008 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2008 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 2008 Bonds with DTC and their registration in the name of Cede & Co. or such other nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series 2008 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series 2008 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 2008 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series 2008 Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Series 2008 Bond documents. For example, Beneficial Owners of Series 2008 Bonds may wish to ascertain that the nominee holding the Series 2008 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 2008 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 2008 Bonds unless authorized by a Direct Participant in accordance with DTC's MNI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Commission 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 2008 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Payment of principal of, premium (if any) and interest on the Series 2008 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 Commission or the Trustee, on the 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 2008 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, the Trustee or the Commission, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal of, premium (if any) and interest on the Series 2008 Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Commission 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 2008 Bonds at any time by giving reasonable notice to the Commission or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, Series 2008 Bond certificates are required to be printed and delivered.

The Commission may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series 2008 Bond certificates will be printed and delivered.

NEITHER THE COMMISSION 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 2008 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 PRINCIPAL OR REDEMPTION PRICE OF OR INTEREST ON THE SERIES 2008 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 2008 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 2008 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 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 2008 Bonds.

The Commission cannot and does not give any assurances that DTC, Direct Participants, Indirect Participants or others will distribute payments of debt service on the Series 2008 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 EXHIBIT C concerning DTC and DTC's book-entry system has been obtained from sources that the Commission and the Underwriters believe to be reliable, but the Commission and the Underwriters take no responsibility for the accuracy thereof.

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EXHIBIT D

FORM OF BOND COUNSEL OPINION FOR THE SERIES 2008 BONDS

(To Be Dated the Date of Issuance)

Commonwealth of Kentucky
State Property and Buildings Commission
Frankfort, Kentucky

Re: State Property and Buildings Commission of the Commonwealth of Kentucky
$15,720,000 Agency Fund Revenue Bonds,
Project No. 91

We have examined a certified copy of the proceedings of the State Property and Buildings Commission of the Commonwealth of Kentucky (the *"Commission"*), authorizing the issuance by the Commission of its Agency Fund Revenue Bonds, Project No. 91 (the *"Bonds"*) in the aggregate principal amount of $15,720,000, issued for the purpose of providing funds (i) to finance and refinance a project and to refund certain outstanding notes, (ii) to fund a reserve fund with respect to the Bonds, and (iii) to pay the costs of issuance of the Bonds, all for the benefit of the state agencies identified in this opinion.

The Bonds are being issued by the Commission, pursuant to Chapter 56 and Sections 58.010 to 58.140, inclusive, of the *Kentucky Revised Statues,* as supplemented and amended (the *"Act"*), H.B. 380 of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session, as enacted and vetoed in part, as amended by H.B. 557 of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session, as enacted and vetoed in part (the *"Budget Act"*), and a resolution adopted by the Commission on September 15, 2008, as supplemented and amended on October 3, 2008 (the *"Bond Resolution"*). The project to be financed and refinanced with the proceeds of the Bonds (the *"Project"*) has been leased to the Finance and Administration Cabinet of the Commonwealth of Kentucky (the *"Cabinet"*) and the Kentucky River Authority (the *"State Agency"*), pursuant to the Lease dated as of October 1, 2008, by and among the Commission, the Cabinet and the State Agency (the *"Lease"*).

The Bonds are dated the date hereof, are issued in fully registered form in the denomination of $5,000 each and any integral multiple thereof, are lettered R and numbered 1 and upward, mature on the dates and in the principal amounts, and bear interest at the rates per annum, payable on April 1 and October 1 of each year, commencing on April 1, 2009, as follows:

Date	Principal Amount	Interest Rate	Date	Principal Amount	Interest Rate
April 1, 2010	$490,000	3.400%	April 1, 2016	$620,000	4.750%
April 1, 2011	505,000	3.750	April 1, 2017	645,000	5.000
April 1, 2012	525,000	4.000	April 1, 2018	680,000	5.125
April 1, 2013	545,000	4.000	April 1, 2024	4,955,000	5.750
April 1, 2014	565,000	4.250	April 1, 2029	5,600,000	5.750
April 1, 2015	590,000	4.500			

The Bonds are subject to optional redemption and mandatory sinking fund redemption prior to maturity as set forth therein and as set forth in the Bond Resolution.

From such examination, we are of the opinion that such proceedings show lawful authority for the issuance of the Bonds under the laws of the Commonwealth of Kentucky now in force. In that connection, we have examined (i) the Act, (ii) the Budget Act, (iii) a certified copy of the Bond Resolution, (iv) an executed counterpart of the Lease, (v) the form of Bond, and (vi) such other proceedings, documents, instruments, showings and matters of law as we have deemed necessary to render this opinion.

Based on the foregoing, and in reliance thereon, it is our opinion that the Bond Resolution has been duly adopted by the Commission, and constitutes a valid and binding obligation of the Commission, enforceable against the Commission in accordance with its terms, except to the extent that the enforcement thereof may be limited by laws relating to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting the rights and remedies of creditors and secured parties and by equitable principles, whether considered at law or in equity, including the exercise of judicial discretion. It is also our opinion that the Lease has been duly authorized, executed and delivered by the Commission, and constitutes the valid and binding obligation of the Commission, enforceable against the Commission in accordance with its terms, except to the extent that the enforcement thereof may be limited by laws relating to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting the rights and remedies of creditors and secured parties and by equitable principles, whether considered at law or in equity, including the exercise of judicial discretion.

We have also examined the form of Bond prescribed for said issue, and find the same in due form of law, and in our opinion the Bonds are valid and binding obligations of the Commission, payable as to principal and interest solely and only from the payments to be made by the State Agency pursuant to the Lease, which payments are subject to biennial appropriation by the General Assembly of the Commonwealth of Kentucky, except that the rights of the owners of the Bonds and the enforceability of the Bonds may be limited by bankruptcy, insolvency, moratorium, reorganization and other similar laws affecting the rights and remedies of creditors and secured parties and by equitable principles, whether considered at law or in equity, including the exercise of judicial discretion. The Bond Resolution authorizes the issuance of additional bonds on a parity with the Bonds.

It is also our opinion that, subject to compliance by the Commission, the Lessee, the Sublessee and others with certain covenants, under present law, the interest on the Bonds is excludible from gross income of the owners thereof for federal income tax purposes, and is not treated as an item of tax preference in computing the alternative minimum tax for individuals and corporations under the Internal Revenue Code of 1986, as amended, but is taken into account in computing an adjustment used in determining the alternative minimum tax for certain corporations. Failure to comply with certain of such covenants could cause the interest on the Bonds to be included in gross income retroactively to the date of issuance of the Bonds. Ownership of the Bonds may result in other federal tax consequences to certain taxpayers, and we express no opinion regarding any such collateral consequences arising with respect to the Bonds.

It is also our opinion, under the laws of the Commonwealth of Kentucky, as presently enacted and construed, that the interest on the Bonds is exempt from the income tax imposed by the Commonwealth of Kentucky, and the Bonds are exempt from ad valorem taxation by the Commonwealth of Kentucky and all of its political subdivisions and taxing authorities. No opinion is expressed with respect to any other taxes imposed by the Commonwealth of Kentucky or any political subdivisions thereof. Ownership of the Bonds may result in other state and local tax consequences to certain taxpayers, and we express no opinion regarding any such collateral consequences arising with respect to the Bonds.

In rendering this opinion, we have relied upon certifications of the Commission, the Cabinet and the State Agency with respect to certain material facts solely within the respective knowledge of the Commission, the Cabinet and the State Agency relating to the application of the proceeds of the Bonds. Our opinion represents our legal judgment based upon our review of the law and the facts that we deem relevant to render such opinion, and is not a guarantee of result. This opinion is given as of the date hereof, and we assume no obligation to revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention or any changes in law that may hereafter occur.

Respectfully submitted,

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