MINUTES OF THE MEETING OF THE BOARD OF DIRECTORS OF THE TEXAS PUBLIC FINANCE AUTHORITY

July 8, 2003

The Board of Directors (the "Board") of the Texas Public Finance Authority (the "Authority") convened in open meeting, notice duly posted pursuant to law (a copy of which notice is attached hereto as Exhibit "A") at 3:00 P.M.,Tuesday, July 8, 2003, Stephen F. Austin Building, Room 118, Austin, Texas. Present were: Mr. David Kelly, Chairman, Mr. Bert Mijares, Vice Chairman, Mr. Vaughn Brock, Secretary, Mr. Barry T. Smitherman, Member and Mr. Dan Serna, Member.

Representing the Authority's staff were: Ms. Kimberly Edwards, Executive Director; Ms. Paula Hatfield and Ms. Donna Richardson. Also present was Gabriela Klein.

Present in their designated capacities were the following persons: Karin Werness, Banc One Capital Markets; Keith Richard, Lehman Brothers; Tom Oppenheim, Morgan Keegan & Co., Inc.; Don Henderson, JP Morgan; Andy Bynam, Citigroup; Terry Thornton, Goldman Sachs; Ricardo D. Villasenor, AG Edwards & Sons, Inc.; Jodie Jiles, First Albany; Erlinda Cortez Dimas, Seibert Brandford & Shank; Courtney Knight, Anthony Haley, George K. Baum & Co.; Curtis V. Flowers, Loop Capital Markets; Alice Barron, Southwest Securities; Chris W. Allen, Public Financial Management; Michelle Vobach, Richard Meister, Al Rodriguez, Merrill Lynch; Mike Walker, Banc of America Securities; Bob Estrada, Estrada Hinojosa & Co., Inc.; Greg Shields, Andrews & Kurth; Nancy Hagquist, Winstead, Sechrest & Minick; Barron F. Wallace, Vinson & Elkins, LLP; Richard Donoghue, McCall, Parkhurst & Horton; Mike Bartolotta, First Southwest Company; Tim Kelley, Coastal Securities; and Kay Watson, CKW Financial Group.

Item 1. Call to order.

Mr. Kelly called the meeting to order at 3:14 P.M.

Item 1. Consider and approve a request for financing from the Texas Workforce Commission for the issuance of revenue bonds pursuant to SB 280, Acts. 78th Legislature, R.S. (2003), select a method of sale, financial advisor(s) and bond counsel, and take other necessary related action.

Ms. Edwards stated this financing request from the Texas Workforce Commission had been authorized by SB 280 and HB 3324 during the 78th Legislature, which authorized TPFA to issue revenue bonds on behalf of TWC to fund a deficit in the Unemployment Insurance Trust Fund, and authorized TWC to levy a special "obligation assessment" on employers in an amount sufficient to pay the debt service on the bonds. She informed the Board that there was a very short time frame to execute this transaction, because the TWC had requested funds by September 24.

Ms. Edwards provided a brief overview of the Unemployment Insurance program and the need for the financing. The Texas Workforce Commission ("TWC") is the state agency that administers the Unemployment Insurance program for the State of Texas. The program is a joint federal-state program. The federal program requires each state to maintain a minimum balance in the Unemployment Insurance Trust Fund. If a state falls below its minimum balance, it can obtain advances (i.e., borrow) from the Federal fund. If the advances are repaid by September 30 each year, there is no interest charged. If they are not repaid by September 30, then the state pays approximately 6% interest for the federal advances (the actual rate varies from year to year). In addition, under state law, if the Trust Fund balance is below a statutorily defined floor on October 1, a "deficit tax" will be levied the following year in order to bring the balance of the Trust Fund up above the floor. The concept behind SB 280 is that the interest rate on the bonds will be lower than the federal advance rate, and that if the bond proceeds are deposited in the fund by September 30, the deficit tax will not be levied. The obligation assessment levied to repay the bonds can be structured to minimize the impact on employers.

Ms. Edwards introduced Gene Crump, Director of Administrative Support Services and John Moore, General Counsel from the Texas Workforce Commission to answer questions. Prior to addressing questions, Mr. Crump read into the record a message from TWC Board Chair, Diane Rath who was in Washington, D.C. and could not attend the meeting (see "Exhibit A") .

Discussion ensued regarding the structure of the unemployment compensation program, tax structure and borrowing needs. Mr. Serna questioned the cash flow aspect, pointing out that TWC receives the largest infusion of their employer fundings after the first quarter, with the potential for deficit needs fluctuating on a month-to-month basis. He asked if staff had a general idea of what the optimal mix of the financing would be, including short-term variable rate, commercial paper, or long-term fixed rate or a mix or combination thereof. Mr. Crump stated TWC needed to borrow enough funds to get past the October floor test and to repay the federal advances to the Unemployment Trust Fund. That would eliminate payment of about $10 million in interest on the federal advances and allow TWC to avoid imposing a deficit tax on employers. The Comptroller's Office forecasts unemployment rates and has recently released new figures that may cause the required amount of the borrowing to increase, but it will not be above the not to exceed $1.6 billion amount that the TWC requested in its resolution.

Mr. Smitherman asked if interest was received on a positive balances why wouldn't you borrow as much as possible? Mr. Crump and Ms. Edwards explained that maximizing interest earnings was certainly one of the financing goals, but had to be accomplished within the constraints of federal tax law. Mr. Moore also provided clarification of the disposition of funds, including bond proceeds, under SB280 and the federal program. Mr. Smitherman then asked how the maximum not to exceed amount of $1.6 billion was derived. Mr. Crump advised that the statute established a not to exceed amount of $2 billion, but that TWC staff recommended the TWC request an $1.6 billion not-to-exceed amount to provide the flexibility to work with TPFA during the interim to come to exact amount of dollars. Mr. Serna asked if the transaction could be done in multiple stages, tranches of some sort. Mr. Crump agreed, stating that the real objective is being above the floor on October 1 and having enough in the Fund to pay benefits through December 31. The Department of Labor requires that if a second advance is obtained from October 1 and December 31, then the interest free loan provision that exists from January 1 through September 30 is null and void, and interest is assessed on those dollars from January 1 through September 30.

Mr. Kelly asked how large the is deficit and at what rate is it growing at the margin? Mr. Crump stated advances have been repaid as of April; TWC has borrowed an additional $70 million since then and has prepared a letter to request additional advances for the quarter August-October, 2003. TWC staff projects that they will be $300-400 million insolvent (below zero) on September 30. The 1% taxable wage base floor is about $780 million, therefore a financing in the range of $1.1 billion would be needed in order to satisfy the October 1 test. Mr. Crump indicated that increased unemployment estimates had been received from the Comptroller's Office, so the $1.1 billion will go higher, but it will be lower than the $1.6 billion, the not-to-exceed amount.

Mr. Kelly asked how often the tax rate could be changed. Mr. Crump responded once a year; the tax rate is published in December after the Commission acts on it in November. Mr. Brock asked whether the taxes cover the unemployment benefits or is it subsidized? Mr. Crump said benefits are paid only from employer taxes. He also explained that TWC is currently paying benefits of about $45 million a week. Mr. Brock inquired about the historical amount of collections, either from last year or previous any year? Ms. Edwards indicated for 2002, it was just over $1 billion. Mr. Crump said all things being equal, remittances will equal benefits paid. The tax changes actually lag behind the tax benefits being paid. The structure is set up so that it eventually equalizes benefits and remittances, but at any one time, the amounts will not match. Ms. Edwards clarified that the formula is set up so that when you are spending more than you are collecting, the higher tax rates and additional taxes kick in to bring collections back up immediately. This causes spikes in the tax rates that hit employers, often during economic downturns. Therefore, one of the policy reasons for the borrowing is that in addition to paying a lower interest rate, it also allows fine tuning of the pay back, which will lessen the impact on employers.

Mr. Smitherman asked if other states were using a program like the one proposed. Mr. Moore said that Connecticut had borrowed in the early 1990's, and Missouri and Illinois are looking at this type of structure. Mr. Smitherman asked why every state wouldn't do this. Mr. Moore said that not every state's tax structure is as low as Texas. Ms. Edwards stated that Texas' floor is set at 1%, but most other states have a 2% floor, so there is less chance they will be insolvent.

Mr. Brock asked when collections would be sufficient to pay off the amount borrowed? Mr. Crump said that theoretically if a short-term borrowing scenario was used, it would be April, but that they may still fall below the floor in October 2004. Mr. Serna stated that the bonds would amortize the deficit tax spike over a period of time and Mr. Crump confirmed this was accurate. Ms. Edwards discussed the structure of the financing explaining that if the economy does rebound it would be good to use a financing mechanism that could be prepaid without any penalty. There might be the need to use a fixed-rate component to achieve the goal of avoiding positive arbitrage. Mr. Serna said the policy standpoint would be to repay this debt as soon as the economic growth and the labor base would allow. If the objective is to smooth the impact of the employer of this deficit, then getting the financing overhead burden out as soon as possible, lowers it. Mr. Curmp agreed.

Mr. Smitherman inquired about the enforcement mechanism for an employer who doesn't pay or refuses to pay. Mr. Moore explained the Attorney General enforces collections and Ms. Edwards pointed out that the historical collection rate is very high, above 95%.

Mr. Serna inquired of staff whether TPFA would have to get separate bond ratings. Ms. Edwards said yes, that the transaction was a pure revenue bond. A significant component of the work will be rating agency presentation and possibly bond insurance and credit enhancement of some sort. The legal documents will be typical, but the disclosure document will be more substantive and will need updating more frequently. TPFA will need ongoing legal advice about whether materials produced by the TWC Public Information Division constitute speaking to the market, and on other 10(b)-5 and 15(c) 2-12 compliance issues. Ms. Edwards stated the statute did allow TPFA to recover the administrative costs of selling the bonds and administering the program, such as dealer fees and liquidity fees, from bond proceeds.

Mr. Smitherman cautioned against hiring bankers and consultants prior to finalizing fees. Being new to the Board, he inquired about the procedure so that the Board knows they are getting a market rate for the business. He commented that admittedly this work is not a commodity, but would like to know there was some mechanism to indicate the State is protected. Ms. Edwards said that typically the Authority relied on the Financial Advisors to assure that the pricing of bonds was fair; through the negotiation process, the FA's and staff look at take-down by maturities and examine every component of the spread. However, she acknowledged that this transaction is unique one and that if the Authority could introduce some competitive bidding for certain components, it certainly would be helpful. Mr. Mijares indicated that he had a similar concern. With such a short time line, he questioned what leverage the Authority had to control the fees on the transaction. Do we, for example know how much money we are going to borrow initially, do we limit that to a short amount and bid the rest? Is that up to the Financial Advisor to advise us? Ms. Edwards said there were several mechanisms that were possible, such as various auction techniques like a dutch auction. She noted that the Authority has three commercial paper dealers that are being paid very competitive fees and provide a good track record to use as a negotiating tool. Ms. Edwards explained that she did not want to get into a low bidder situation on the component that needs the skill set and commented that typically fees are lower on short-term debt, which should be a large part of this financing. She suggested that staff solicit input from the financial advisor on how to best control the transaction costs.

Mr. Serna commented one of the primary fiduciary duties of the Authority is to make sure the public finance business executed on behalf of the taxpayers of Texas is done as efficiently as

possible and that includes watching the cost. The expense side is part of the cost of what we do here. He noted that the Authority has a constant and ongoing large book of business, it is a competitive environment, and a lot of people want to do business with TPFA. He remarked that he has never seen a period of time where if somebody felt they could not offer equal or better service at a more cost effective pricing structure for TPFA, that the Board would not be so advised. Ms. Edwards acknowledged the Board's comments on the importance of controlling the fees on a transaction of this nature.

Ms. Edwards stated that in developing the staff recommendations, she had been very cognizant of policy guidelines that recognize performance, ideas and service to the Authority, as well as the statutory requirements in terms of HUB participation and the time constraints of closing the transaction prior to September 30.

Staff recommended a negotiated sale, reserving the right to structure the deal with some component of competitive bidding if appropriate. Staff recommended designating the senior-manager tier of the underwriting syndicate at this time, so that work could begin on the transaction. Once a structure had been identified, staff would make additional recommendations for the apprornpiate size, role and composition of the remainder of the underwriting syndicate. Staff recommended that Goldman Sachs, George K. Baum and Morgan Keegan, serve as co-senior managers, with Goldman Sachs being the lead manager. Mr. Smitherman moved to accept staff's recommendation. Mr. Serna seconded. The motion passed unanimously.

Staff recommended that Vinson & Elkins and Delgado, Acosta, Braden and Jones serve as co-bond counsel. Staff also recommended that Winstead Sechrest & Minick serve as disclosure counsel, to assist with the preparation of the official statement and ongoing disclosure after the transaction has closed. Mr. Kelly remarked that while cost was important, it was also important to have sufficient resources available to close the transaction on a timely basis. He requested staff to recommend additional resources if staff felt that they were necessary. Ms. Edwards indicated she believed these three firms have sufficient depth to accomplish the transaction, but would certainly advise the Board otherwise if necessary.

Staff recommended that First Southwest Company, Coastal Securities and CKW Financial Services serve as a co-financial advisor team. Ms. Edwards remarked, that in line with Mr. Kelly's comment about having sufficient resources for the legal team, this is a time when it benefits TPFA to have more than one firm to provide financial advisory services. Mr. Mijares moved to accept staff's recommendation for bond counsel and financial advisors.

Ms. Edwards noted that retaining three financial advisors is a unique structure and requested that each firm be given an opportunity to confirm whether they would be agreeable to such an engagement. Mr. Kelly, Mr. Smitherman and Mr. Serna stressed the importance of each member of the working group providing top level service on this very important transaction. Mike Bartolotta, Tim Kelley and Kay Watson each indicated they would.

Mr. Serna seconded. The motion passed unanimously.

Item 2. **Adjourn**.

The meeting adjourned at 4:33 P.M.

The foregoing minutes were approved and passed by the Board of Directors on August __, 2003.

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Vaughn Brock
Secretary, Board of Directors

ATTACHMENT: Posting Notice - Exhibit "B"