Executive Committee Meeting
Wednesday, March 16, 2005
11:00 a.m.

Hotel Roanoke & Conference Center
Pocahontas Room
Roanoke, Virginia

APPEARANCES

The Honorable Charles R. Hawkins, Chairman
Mr. Thomas W. Arthur
The Honorable Kathy J. Byron
The Honorable Allen W. Dudley
The Honorable Joseph P. Johnson
The Honorable Frank M. Ruff
The Honorable William C. Wampler, Jr.
Mr. James C. Thompson
Mr. Gary D. Walker
The Honorable Clarke N. Hogan (by phone)

Commission Staff
Carthan F. Currin, III - Executive Director
Mr. Ned Stephenson - Managing Director of Strategic Investments
Ms. Stephanie Wass - Director of Finance

Attorney General's Office
Frank S. Ferguson
Ms. Stephanie Hamlett

March 16, 2005

SENATOR HAWKINS: It's 11:00 o'clock, I'll call the meeting to order. Carthan, call role.

MR. CURRIN: Mr. Arthur?

MR. ARTHUR: Here.

MR. CURRIN: Mr. Bryant?

MR. BRYANT: (No response).

MR. CURRIN: Delegate Byron?

DELEGATE BYRON: Here.

MR. CURRIN: Delegate Dudley?
DELEGATE DUDLEY: Here.
MR. CURRIN: Delegate Hogan?
DELEGATE HOGAN: (No response)
MR. CURRIN: Delegate Johnson?
DELEGATE JOHNSON: Here.
MR. CURRIN: Senator Puckett?
SENATOR PUCKETT: (No response).
MR. CURRIN: Senator Ruff?
SENATOR RUFF: Here.
MR. CURRIN: Secretary Schewel?
SECRETARY SCHEWEL: (No response).
MR. CURRIN: Mr. Thompson?
MR. THOMPSON: Here.
MR. CURRIN: Mr. Walker?
MR. WALKER: Here.
MR. CURRIN: Senator Wampler?
SENATOR WAMPLER: Here.
MR. CURRIN: Mr. Vice-Chairman?
DELEGATE KILGORE: (No response).
MR. CURRIN: Mr. Chairman?
SENATOR HAWKINS: Here.
MR. CURRIN: You have eight members present.
SENATOR HAWKINS: Do we have a quorum?
MR. CURRIN: Yes.

SENATOR HAWKINS: Before we get started I think there is probably a couple of things I need to say before we get started in our discussion this morning. I'd like to get them on the table so we have an understanding where we're going and what we're talking about. We're back discussing the securitization program with a different sort of dynamics than we had last time. We also have a major initiative in place that we didn't have last time when we talked about securitization and particularly when talking about the telecommunications piece. There are several things that concern me. One is that out in the burley section of the state it's my understanding that Philip Morris is contracting with the flue cured area to raise burley. They're moving the burley poundage and farming operation that took place in the burley market that probably almost has ceased to exist due to Philip Morris moving to a larger farm area. If in fact that is the case, it's my understanding, it is, there's going to be a ripple effect in that economy. We need to put some things on a fast track, particularly the telecommunications piece. If we can complete that and give some sort of cushion to those economies when all this starts to hit, I think we'll be ahead of the game. Remember that our charge is to create the atmosphere for economies to grow and to do that we have to invest in infrastructure.

Another thing is the condition in Charlotte County and that certainly causes me some concern and that's based on infrastructure needs and the telecommunication piece. I wish that we'd start thinking about a couple of things if in fact we do securitize. That is fast track, if we can fast track the telecommunication piece and get that on track and done and paid for and out of the way so that we can start promoting the area to be connected by high speed connectivity, I think it would be an advantage in marketing ourselves. Also, if we get involved in any sort of discussions on the formulary, we have to also be very aware of the obligations that we have placed on some of our localities and long term expenditure such as Halifax, Pittsylvania, City of Danville on some projects that they have used their funds for to pay off debt and we can't leave them out swinging in the wind if in fact we change the formulary and there's not enough money in the pipeline to pay those obligations based on their understanding in the original agreement.

We have some difficult subjects to discuss also dealing with if in fact we do securitize how we manage these monies to make sure that there is some sort of protocol in place to guarantee that these monies are not wasted on projects that have strictly parochial interest. I think we need to start looking at more and more things that go beyond that to get all of our counties some sort of competitive advantage when it comes to attracting jobs that they need. What we're doing now will pretty much set the tone for what takes place in the Commission for the duration. I'm also concerned that we need to make sure that anything we put in place now has staying power for the next generation of the Commission in place and they'll have some guidelines to go by and also understand that these monies will not be put in harms way by someone's attitude about a condition that may be before them. Having said that, Carthan, what do you have?

MR. CURRIN: Thank you Mr. Chairman and members of the Executive Committee. Also in your packet is a one page summary spending plan for us to follow. I'm going to give a brief background on some of the issues which we faced two years ago and some status on what we're dealing with currently. Mr. Chairman, why don't we go ahead and approve the minutes.

SENATOR HAWKINS: Is there a motion that we approve the minutes of the last meeting. It's been moved and seconded that we approve the minutes of the last meeting, all in favor say aye, (ayes). Opposed (no response). The minutes are approved.

MR. CURRIN: Recent events have brought us back to a familiar subject. Because of the April Commission meeting coming up the staff felt that we needed to have this committee have a continuing dialogue on an important subject. I think you'll remember that we reviewed two years ago, two years ago you'll recall that Chapters 482-488 of the 2002 Acts of the Assembly created the TICR Endowment. It also created the Settlement Financing Corporation that was created to execute securitization. That authorizes the Governor to sell the Commission's allocation. You'll also recall that it limits the corpus invasion to ten percent annually or up to ten percent annually and by a two-thirds vote of the Commission on a given year to take up to fifteen percent.

SENATOR HAWKINS: Let me stop you there. Do you remember the last discussion we had on the vicinity of going into the corpus based on the securitization plan of 80/20, is that right?

MR. WASS: Yes, sir.

SENATOR HAWKINS: We're talking about a much less invasive securitization plan today. I believe the maximum I heard is 50/50.

MR. CURRIN: We're going to discuss the scenario with you that would suggest potentially 50/50 or 60/40 and I'll get to that in a second.

SENATOR HAWKINS: I want to make sure that you all understand the things we talked about in the last securitization discussion were based on a scenario of 80/20 securitization. We're not talking about 80/20 today so we'll have to look at this a little differently understanding the monies that we're dealing with.

MR. CURRIN: As the Chairman alluded to, we were going to securitize a hundred percent of our proceeds 80 percent tax exempt and 20 percent taxable, capital versus operating expenditures. Pricing results from tax-exempt bonds the par value $612 million, average coupon 6.4 percent, average life about 24 years. Estimated payoff was 12.2 years and I think that's in reference to the turbo section or factor in that deal. Anticipated net endowment deposit of $513 million dollars.

What's happened approximately two years ago we priced the bonds at that time March 19th and 20th, 2003 and they were scheduled to close April 3, 2003. On March 21st the Illinois State Court judgment against Philip Morris created a major tidal wave effect on our particular deal. On March 24th rating agencies put tobacco bonds on a rating watch negative. March 28th the letter from Philip Morris to the Attorney General threatening non-payment of the MSA payments. On March 31st of that month Moody's downgraded tobacco bonds and on April 1st the offer was withdrawn and on April 2nd the tobacco bonds were downgraded.

What has changed from two years ago to now as far as the market.

NOTE: At this point Delegate Hogan is now attending via the telephone.

MR. HOGAN: Have you started yet?

SENATOR HAWKINS: It's ten past eleven Clarke.

DELEGATE HOGAN: Mr. Chairman, I been trying to get through for ten minutes now and just managed it now. I'm sorry, excuse me.

SENATOR HAWKINS: We'll give you the benefit of the doubt this time.

MR. CURRIN: Mr. Chairman, counsel has advised me that Delegate Hogan may listen but may not engage on the telephone while we're proceeding on this presentation. Is that correct counsel?

MR. FERGUSON: Yes, sir. It's pretty much required that his participation be limited to that of any other member of the public.

MR. CURRIN: He could ask questions during the public participation?

DELEGATE HOGAN: Is that the Mary Sue rule?

MR. FERGUSON: Freedom of Information.

MR. CURRIN: Welcome Delegate Hogan. Let's see, currently where we are right now, there is no market as we're being advised for taxable tobacco bonds. It's largely limited to tax exempt tobacco bonds. Securitization will be a hundred percent tax exempt if we proceed. Indemnification liability limited due to federal quota buyout and that's changed dramatically from two years ago. We have the remainder of our technology projects well underway. The Commission checklist is to authorize proceeding with securitization, authorize securitization related expenses and Ms. Wass will discuss that later on. Recommend maximum percentage of MSA payments to be securitized and to approve the revised spending plan.

The tentative calendar before you that the staff has recommended for your consideration is that March 8th the RFP closes for underwriters. You'll recall at the last meeting with the Governor the general consensus of the Executive Committee was to give the Treasurer the go ahead and at least issue the RFP and that has happened as I understand it and eight underwriters responded to that RFP. As of yesterday afternoon the Treasurer notified me that an underwriter hasn't been selected to date. April 5th potential Commission meeting for final approvals. Mr. Chairman, I would suggest that we have a special Commission meeting for final approval on this subject alone which you know our next regularly scheduled meeting is on the 28th here in Roanoke. April 15th the MSA payment received for the FY05 budget will not be securitized. By early May we would anticipate securitization to be complete.

At this point Mr. Chairman I'd like to ask Mr. Stephenson to come up and give further impression of where we are and from the staff, from Ms. Wass we'll follow Mr. Stephenson.

DELEGATE JOHNSON: Mr. Chairman, this may be done later but the buyout, could you in layman's language, tell me what will happen in reference to the direction that we go.

MR. CURRIN: Delegate Johnson, since Stephanie has been intimately involved with that subject matter, I'm going to ask her to respond to that question.

MS. WASS: I believe the Commission voted at the January meeting, it wanted to spread the remaining obligation for indemnification over the next ten years. What we're taking in is the remaining obligation through 2002 losses. 2002 is when the buyout would occur and we wouldn't take losses after that. For past losses, we would take that remaining obligation over the next ten years. What's in limbo still is the final Phase II payment and that's suppose to happen in December, 2004. It's still in the courts.

DELEGATE JOHNSON: One other question. What are we going to do so far as the quote limbo is concerned?

MS. WASS: At this point we're assuming that it will be paid and if it doesn't happen, I think a decision will probably be made by this summer and we would put that into our remaining obligation.

MR. FERGUSON: Delegate Johnson, the Phase II litigation, we call it litigation over whether or not the trust payments for 2004 will be made. The reason that is in contention because the terms of the trust have created the Phase II payments. Say if there is a program whereby farmers are compensated for quota loss and that's funded through assessments of taxes against tobacco companies which the buyout is, then they would not thereafter have to phase that into Phase II. The point of contention is that because that statute was enacted in the middle of the year if you will, in October of '04, the question is whether or not they owe for '04 or not. The payments for the first three quarters of '04 are in escrow. I don't think they put the final quarter in, maybe they have but the case is being litigated in the North Carolina courts because by terms of the trust the Wake County Circuit Court in North Carolina is the proper venue and has jurisdiction to hear the matter. That court as you recall, ruled against the farmers if you will, holding that they were not required to make '04 payments. That has been appealed and it's on a fast track appeal in North Carolina, an almost unprecedented fast track. They bypassed the intermediate court of appeals and are winding up the briefing phase in the Supreme Court already. I would not be surprised if the case isn't argued within the next four weeks and you would have a decision, I would hope by the beginning of the summer and even maybe earlier. However you handicap the odds of that I think is difficult and certainly we're starting out from behind in the lower court. I think everyone agrees that whatever decision comes down from the North Carolina Supreme Court that is the end of the story because there really is not a federal issue and I don't think it will go beyond that. Then we'll determine whether or not the liability for that 27 or 28 million, the figure at issue is whether or not we will have to add that to the remaining liability with the TICR Commission has or whether that's subtracted from the overall make whole requirements for the indemnification program.

SENATOR HAWKINS: The federal buyout is based on $2 a pound and we're obligated at $4 per pound so you have a $2 per pound difference we may have to deal with at some point too. So I think it would probably be inappropriate for us to use the word finish our obligation because I don't think we'll ever finish the obligation the way it's structured. There is an ongoing obligation to deal with but we need to make sure that we have money in the track so that we can budget and make sure that we meet that obligation. If we assume that $2 extra a pound, the federal government is not paying, we have an ongoing obligation there as well. I don't think the indemnification piece is going to end by a ten year timeframe.

DELEGATE DUDLEY: Mr. Chairman, we use $12 a pound back when there was nothing in place to signify a difference. That was the goal that was there for the buyout. Now there's been an official price set in the buyout. Everyone agrees to $10 a pound. Will we revisit the difference between $12 and $10?

SENATOR HAWKINS: If I'm not mistaken, we have to go back and change the law.

MR. FERGUSON: The statute says the whole estimated value of all quota was

$1.2 billion dollars. That figure was based on $12 a pound.

SENATOR HAWKINS: We may have to go back and revisit that.

MR. FERGUSON: I would suggest that, we have to catch up with 2002 before we start worrying about that because the buyout as Stephanie indicated doesn't start until 2002. If they're not buying out everything that is of value, we're only up to the '99 crop year or the '99 quota year at this point. The losses that occurred between '99 and 2002, the Commission is still liable for those losses. Whether or not you want to put those losses at $10 versus $12 per pound and/or whether or not the Commission wants to make up the $2 difference between what the buyout is paying and what the $1.2 billion in the statute is based upon. The language in the statute is not clearly mandatory so I think this is probably something that requires some consideration by all concerned. It's strictly a legal question.

SENATOR HAWKINS: My understanding this is not the discussion for today because we've got an obligation right in front of us and that will be in the out years.

MR. FERGUSON: We've got plenty to pay right now whether it's $10 or $12 or whether it's beyond 2002 or not.

SENATOR HAWKINS: Yes, sir. Indemnification, we'll worry about that tomorrow.

MR. STEPHENSON: Thank you Mr. Chairman and good morning to everyone. Before I begin I want to offer a word of caution. Some of the material that we will place before you this morning is not yet certain and not yet known. We're dealing with unknown numbers but it's still necessary that we brief you on this because things are moving very fast and we want you to know how this thing is shaping up. And we'll know much more in the weeks to come but just that word of caution. At the conclusion of my remarks, I'm going to ask you to make some decisions that we think you need to make because time is of the essence with respect to the securitization process and you'll see those shaping up as we go through this.

At the risk of being too elementary, I want to start at the very beginning of this securitization issue and kind of go through it so we can all get kind of back up to speed because it has been a year or two. Anyone involved in bond transactions has risk and that includes us. There's three kinds of risks that we face and that is credit risk, event risk and rate risk. Credit risk being that if Philip Morris wants to pay us but they can't. Event risk is being legal issues, all kinds of things that happen that are unforeseen that could disturb these payments. Our securitization effort is really all about knocking out credit risk and event risk. You have interest rate risk and you'll always have that. You can't get around it. And that's what we're going to try to do in this securitization process. That brings us to the central question here for us in this securitization issue. Just how much we're willing to give up to knock that risk out and that's the question that has to confront this Commission. With almost everything else that you all do so well, it depends on what the issues are as to the answer to that question. To help us go through this, I want to present to you some things that I call hard facts which are irrefutably true and then we'll get into some of the soft items that are in question.

First off, we all know that securitization means less money for us. All of our committees as far as my observation are concerned has always had more applicants and more need that we have money and when we securitize that's going to be worse because we're going to have less money after we securitize because it's going to cost us a big piece to get rid of the risk. That means less money for everybody all the way around. Securitization imposes restrictions on us. I want to be clear about this because I think it's something you need to consider carefully. These are to be tax exempt bonds. You're limited in what you can do with the proceeds of the tax exempt bond. Broadly speaking, you can only use those proceeds for capital expenditure. Once the endowment is created, those funds can only be used for capital projects. You may find yourself on one of your committees with a worthy project before you that you want to do but staff or counsel or somebody's going to raise their hand and say you can't do that because its of an operating nature and these are restricted.

SENATOR HAWKINS: You've got a stream of 50 percent of the money securitized and 50 is not and you have access to the other 50 percent?

MR. STEPHENSON: That's right. We've got a split program here where you're going have some MSA payments and some endowment and we'll have to juggle which project gets funded with which kind of dollars to preserve the tax exempt status of the bonds. You're right, we'll have both but that's an additional restriction that we have not lived with before.

Securitization increases our fiduciary duties. What I want to say to you about this is that until now you could look an applicant in the eye and say we can't fund your project because I don't have the money and after you securitize, you will have the money and if you want to say no to somebody it will have to be for some other reason other than I'm out of money.

SENATOR HAWKINS: If you limit the amount of money you want to pull out of the corpus dealing with the withdrawals, are you in the same position as having not the amount of funds you need for every project that comes up?

MR. STEPHENSON: Yes, the code limits you to 15 percent of the corpus. At that point you have to stop. That's a pretty big number and you may not want to go there, you may want to restrict yourself further. You'll have to be able to say no, we cannot invade the corpus for this particular project. It's just that it's going to raise the bar on your fiduciary duties responding to these applicants. Securitization empowers you to bind future Commissions. Stephanie told me that Frank would come out of his chair when we put this on the board so maybe he can help us. I do want to speak to you briefly about the notion that once you securitize and you have an endowment it is possible for you to pledge to an applicant say a million dollars a year for ten years and that's a good thing and it might help to do that. After you've done that in a half dozen places or more for several years, though you still have your endowment, you have mortgaged it all. In other words, you have pledged it away and in future commitments and if you continue that, you could have the whole endowment pledged away and that would foreclose yourself from making further commitments.

SENATOR WAMPLER: Mr. Chairman, I would say that I would yield to the advice of the Attorney General with regard to as to whether we have the ability to bind future Commissions. I would say to the extent that we need an opinion from our counsel to advise us accordingly. I don't say that in disagreement but I think that's the magnitude that we need to understand from our lawyer how strongly he feels as to our ability to do that.

MR. FERGUSON: Let me comment now. I think it's worthy of greater research than I have off the top of my head but my initial reaction is somewhere between I think it's true that you will have greater ability to pledge than you currently have and the reason for that is that you're not restricted by future appropriations necessarily. In other words, you will not be saying we're going to give you a million dollars but remember it only means if we get appropriated from the General Assembly. You'll have that money in hand in the trust and you can make at least a moral obligation pledge to do it which you can't do. I think what Senator Wampler is referring to is absent contractual relationships and a mere grant or a mere promise to grant in the future is not enforceable. As a new Commission comes in and chooses to change that, you're not bound then in that respect. I say it's worth a little more research but I'd be surprised if I was found to be wrong on either of those points.

MR. CURRIN: If future general assemblies feel that's binding.

MR. FERGUSON: That is true but, it's true in at least one respect though going back to the, even General Assemblies are bound by their ability to get revenue in the future and you have a budget and you know the budget is pretty much dependent on revenue. Any promises they make in the future is not only contingent upon future members of the General Assembly in agreement but what funds or what revenues become available. Here we're in sort of the same situation. The future means that future members of the Commission agreeing but also being appropriated funds. Part two of that does go away with securitization because we'll have the trust with the funds in it that are sufficient to pay that pledge. It's not like we're dependent on getting an appropriation and that goes back and forth to the points that Ned made previously. We can no longer say there's no money because the money is there, at least might be there. You all know that the General Assembly may decide to turn all the MSA money over to highway construction so it is different in that regard.

SENATOR WAMPLER: Question, the fact that we securitize and capitalize in this trust. Does the office of the Attorney General have the opinion that an Appropriation Act could not override any of that legislation and secure those dollars for purposes other than use of the Tobacco Commission? Would it still remain on the books of the Commonwealth?

MR. FERGUSON: I suspect that at the end of the day that's correct.

SENATOR WAMPLER: That's the point where I was trying to go, potentially subject to the Appropriation Act.

MR. FERGUSON: It doesn't require a new appropriation.

SENATOR WAMPLER: I would agree with that Mr. Chairman and I realize it's splitting hairs but I think when it comes to binding future Commissions, we better understand.

MR. FERGUSON: You're a little more bound than you were before.

MS. HAMLETT: When Ned first said that, I really thought they were bound to the extent that it could go back to your own restriction. Once you do a tax exempt issue, you will bind them to the capitalized cost for governmental purposes.

SENATOR HAWKINS: We have a real opportunity here.

SENATOR WAMPLER: Mr. Chairman, I'd like to close on my thoughts, I just don't know that I disagree with what Ned said on this fourth bullet other than I would not want the balance of the Commission to think that those dollars are permanently on the books of the Tobacco Commission free and clear of any actions of future governors or General Assemblies.

SENATOR HAWKINS: I think your point is well taken and also we are in the same position today with allegations of money to the Commission through the administration. What I think securitization does do is that it takes it out of the budgetary process and there was a trust fund set up. It doesn't eliminate that possibility from the General Assembly. It's not always on the firing line.

MR. STEPHENSON: The next bullet, I don't need to remind you of this. The process of the securitization will cost us even without success, we found out last time when we tried. That's one of the things that we do have to face. In all of this, the unknowns that lay ahead, you can be assured that after it's all over we'll know what we should have done but we don't have the benefit of that today.

I now want to move into some things that I call soft facts also known as speculation. These are very soft facts and these are things we've been able to gather in talking to the Treasurer and among ourselves and from our knowledge last time. I'm going to give you some numbers in here that will aid us in our conversation but these numbers are not yet firm so you need to know that they can move and that might affect the way that you make these decisions. The first one is that the bond offering will be a hundred percent tax-free and we are advised that there is no market for taxable tobacco paper right now. There is a limited market for tax exempt tobacco paper and that's why this is brought to your attention.

DELEGATE DUDLEY: Technology apparently is okay to fit under the capital expenditure?

MR. STEPHENSON: We're going to speak to that in a minute, you're going to be on the spending plan that's before you and what I'd like to do is put that up and we'll talk about each one of those four but I think the short answer is yes, technology is a capital intensive effort and you can use tax exempt dollars. Under the present securitization that we are thinking about only part of the MSA payment will be sold off as Senator Hawkins was referring to. The part that is to be sold off is yet to be determined and that's one of the questions that the Committee here today has to decide how much that should be and we'll get to that in a minute.

This is obviously speculative but it is helpful for conversation purposes. Endowment earnings are estimated to be about four percent a year and obviously as time goes by it could be half of that or twice that but we have to have a proxy to talk through the issue. This is really dangerous but here it is. The endowment corpus is estimated to be $350 million a year and this is governed by a lot of factors like the market, how much you use to sell off and so forth but for discussion purposes, we're giving you the ballpark figure that we believe is in the neighborhood of what you can do.

MR. CURRIN: This is under Ned's Committee, this is a 50/50.

MR. STEPHENSON: Thank you Carthan. I'm getting ahead a little bit. One of the things that's being asked of the Commission is just how much of your payment stream do you want to sell? Half of it, 60 percent, 70 percent because the Treasurer needs to know how much she should seek. For discussion purposes today we're suggesting a number of 60 percent of your payment stream and that's how these numbers are built. It's your prerogative but that's the number that we think is a good starting point.

SENATOR HAWKINS: Are you going to start with 60 percent and then 50 percent in your discussion in Richmond?

MS. WASS: The 50 percent is actually the suggested rate from the Treasurer. They are actually looking at what we would need for working capital funds versus capital expenditures based on past expenditures of the Commission. We're looking at what the Commission would require as working capital funds taking the rest to securitize.

SENATOR HAWKINS: That includes the indemnification piece.

MS. WASS: Indemnification, education, administration and TROF and special projects and agriculture.

MR. CURRIN: Mr. Chairman, the Committee structure, we have economic development and technology could be under the securitized dollars. Everything else we would fund out of our MSA stream that would be left and that would come in as it has for the past five fiscal years.

SENATOR HAWKINS: My understanding is that if we go to the 60/40 split, the 60/40 split gives us less money for education initiatives, for special projects for those things. We're locking ourselves in even tighter with the 60/40 than 50/50. Anticipating future events is it realistic for us to put everything in tax exempt bonds 60/40 and not knowing what we'll begin with in the out years, just for a discussion for everyone involved.

MR. STEPHENSON: I think the essence of your decision on how much to sell off as to how much you're willing to restrict yourselves to capital projects. You're right, future events will tell you what we should have done. That's something to keep in mind as we narrow that level. This is a number that you're familiar with and a pretty firm number. The MSA payment I should add over the next 10 to 12 years runs between about $64 million to $89 million a year for the forecast that we're operating under now and that is the payment stream that you would be selling off half of 60 percent of whichever you might choose. Another item that is a moving target but we need a discussion on it and that is the estimated bond repayment period on or about 12 years. That number can get longer or shorter depending on what's going on in the market. For discussion purposes we need to think about 12 years and that could be structured we believe after the bonds are retired your MSA payments come back to the Commission. You really dealing with a 12 year horizon here after which the payments come back. If you believe the payments will come back to us after 12 years then we really don't need to do this and we can adjourn but therein lies the risk.

I want to give you some estimates here based on these soft facts that we talked about as to how life will be before and after securitization. Before securitization which is what we have right now today, you're receiving about $72 million dollars a year in MSA payments and you have the risk with those payments, you have no endowment and that's the way we stand today. After you securitize as we are suggesting, your MSA payments will drop from $72 down to $29 million and you still bear the same old risk with those dollars.

DELEGATE DUDLEY: Ned, is that just today's level or does that take into account projected adjustments either way?

MS. WASS: That's an average.

MR. STEPHENSON: $64 to $89 million, about that range so this is kind of in the middle. We're actually getting a little less than that now but a little more than that later on. That's your approximate payment stream.

SENATOR HAWKINS: Let's stop for a minute and realize what's driving these numbers. This is driven by domestic sales of cigarettes. The package price that's paid for the domestic market. This is also assuming you have a constant flow of growth in the market off-set by – no, it isn't.

MS. WASS: These are adjusted for all factors, the revenue that we have from treasury are adjusted for all factors in the MSA that they can project.

SENATOR HAWKINS: But declining consumption -

MS. WASS: If it's greater than what they anticipated.

SENATOR HAWKINS: That's what we have to take into consideration in these discussions is the domestic consumption and that's what we're dealing with.

MR. STEPHENSON: Right. Stephanie, isn't it also true that those estimates are now stale and if we securitize they will revise those and we'll have a fresh forecast on what's out there.

MS. WASS: Yes.

MR. STEPHENSON: If we use the number 72 so we can talk about this but it is a moving number. After securitization we drop down to 29 million MSA with the risk we've always had but in addition to that, we'll have an endowment of about $350 million dollars. That's kind of a before and after picture of this particular securitization effort.

MR. HOGAN: Is that on a 50/50 model?

MR. STEPHENSON: That's on a 60 percent securitized, 40 percent retained MSA. What I want to do on the next slide is to distill for you the essence of the difference between the before and after. As I see it, here is the essence of the difference in the securitization. You're going to give up your $43 million per year for 12 years and in exchange you're going to get $350 million cash in hand and the risk goes away. There is the heart of the securitization question.

SENATOR HAWKINS: Let's stop for a minute here. If in fact we're talking about this scenario and remember our charge from the beginning, economic development as well indemnification. This is strictly economic development. If we can take some monies and fast track some projects that we started with like the telecommunications and allow our communities to have a little competitive advantage when it comes to the marketplace and be able to attract the jobs they need and the investment that they need to stabilize the job situation in various counties. If in fact we can do that, I think we're money ahead regardless of how we deal with it because we're dealing with things that are not necessarily absolute when it comes to the marketplace and we've got to look at this a little differently than if you were an investment house looking at return. Our return is going to be on the out years on jobs and the tax base we build in our communities. I think we need to look at what we need to do for our communities and also figure out some way that when we get into these discussions we get back to those infrastructure improvements that go across community lines that are more regional in scope rather than parochial and we need to make sure all that's in front of our discussions as we get into this.

MR. CURRIN: Ned is going to talk about the staff internal spending plan for you. To cut to the chase, the next slide is going to be very helpful for that.

MR. STEPHENSON: As soon as this slide went up I saw the pencils doing the math of $43 million, 12 years that's approximately $500 million, please be careful and don't do that math because these numbers are moving around. They will not be known until the underwriters are involved and the financial advisors are involved and a fresh forecast so we can begin to solidify the numbers but this is the essence of what you're being asked to consider. I want to back up a little bit to the time before I was here. You all adopted a long range plan and part of that long range plan was a spending plan to govern your use of your endowment. Those are the pages in the plan that has some percentages and so forth, and that was the plan under the securitized world. Because we are considering securitizing only a part and retaining a part in the MSA, that plan doesn't work anymore, it doesn't mathematically fit. What's happening today, so your staff has worked to bring to you a new plan to help you govern your spending of going forward. You have that in your handouts before you. I'm going to walk through this and I'll tell you that you may be deceived a little bit by the simplicity of this plan but there are some far reaching implications in it.

SENATOR HAWKINS: Before you get into this, it's a quarter to twelve. We're going to have lunch served and we'll just make it a working lunch.

MR. STEPHENSON: Under this plan which is a draft only for you to consider, we contemplated that you can use your endowment earnings to supply the funds for your economic development committees. The two economic development committees would live off of the earnings of the endowment.

SENATOR RUFF: We have made moral commitments to Pittsylvania, Danville and Halifax for capital projects that have already begun. Would they fall inside or outside of the realm of this?

MR. STEPHENSON: They would fall inside this as we see it. Now, if the Commission wishes it can do other things that it chooses to do.

SENATOR HAWKINS: At this point we're talking about a change in the way we do things. The larger counties that we've made out year obligations to and their the ones that receive the greatest amount of money for this formulary. If in fact we change things to make it a little more accessible for everyone involved the biggest prices we pay for the larger counties and the City of Danville, therefore we could possibly have an obligation for the Commission itself assuming that responsibility for those localities which is an obligation we have as a Commission. I think it's one we need also to discuss in the out years. We can't expect the localities to pick up responsibilities when we change the rules on them. We got to understand that as well.

MS. WASS: One thing that will need some adjusting; I understand the debt service payment cannot be paid from the tax exempt proceeds so there will have to be some adjusting of funds that have come from the MSA revenues, not from securitizing.

SENATOR HAWKINS: If we could have a listing of those out year obligations that we already have assumed and have some understanding what they are and also what we're looking at for the completion of the telecommunications piece, southwest and southside Virginia and all the counties involved and see what kind of monies we're looking at to make some decisions based on hard figures.

DELEGATE DUDLEY: I'm familiar with the research center in Danville but I'm not that familiar with Halifax. You said we had an ongoing obligation that we assumed, what is that?

SENATOR HAWKINS: That's the Riverstone, Frank can probably describe that better than I can. They assumed long term debt, is that correct Frank?

SENATOR RUFF: Yes, the initial investment was $10 million dollars roughly. I'm completely confused as to whether Ned told me the right answer or Stephanie told me the right answer or whether it's a combination of the two because if that long term debt, I don't see how we could come up with this money at all.

MR. STEPHENSON: It comes out of the other side of the house so to speak.

SENATOR HAWKINS: If we assume responsibility and get rid of all the debt before and move ahead.

MS. WASS: My understanding is that you cannot use a tax exempt proceeds either endowment or earnings for debt service. We'd have to make some adjustment to the plan. Previous obligations would be taking MSA revenue, same as new projects going forward.

SENATOR HAWKINS: We've got to take into consideration all scenarios we're dealing with because we put in place obligations based on a known set of circumstances that we're dealing with, if we change the circumstances we're going to have to deal with those obligations we put in place by our own actions and it's going to require some different options. I don't think before anybody can make a decision in percentages we need to know exactly what we're looking at.

SENATOR RUFF: Mr. Chairman, since you made that statement, I have to say that in both of those cases we made a commitment. It was said and it should be in our records somewhere that those were not legal commitments. We have to be very careful not to step on someone else's toes to take care of those commitments to those communities.

SENATOR HAWKINS: If in fact we look at the commitments that they were making based on the allocation formulas in place, the counties of Pittsylvania and Halifax, the two large tobacco producers by far they receive the largest amount of money so is the City of Danville based on the jobs. If in fact we change the rules on those and change the structure of the allocation formula, the monies that they would be receiving in fairly large amounts would go into the overall structure of the allocations from the economic development side and therefore the larger counties would be paying a much larger percentage of the share.

DELEGATE BYRON: Mr. Chairman, I understand that, are we going to decide by the end of this meeting today, just so I understand what has to be done today. We've talked about some things and then you said come back with information, what is the purpose of what we're going to end up doing today?

SENATOR HAWKINS: I'm not sure we can leave here with anything other than an understanding that we got a lot of work in front of us and how we're going to deal with that and have the staff bring us up to an understanding of what, there's going to have to be some study as to what recommendations we feel we can make and be comfortable with it.

DELEGATE BYRON: As far as securitization, that is already moving forward so there is no change and we're not sitting here deciding we're going to do it.

SENATOR HAWKINS: We're looking at options for securitization. There's a series of things that has to happen.

MR. STEPHENSON: We're getting to the end of this but one of the questions I think the Committee needs to confront today is whether or not it wants to continue on the securitization path or whether it wants to stop. This is kind of a briefing on what we know today. If we want to stop we can.

MR. CURRIN: Mr. Chairman, because this is a very serious issue, because it has complexities to it, it's been two years since we discussed it, visited the subject, we thought it was important for you and we didn't have a chance to prepare for the meeting with the Governor to see kind of an updated spending plan. That's one of the things we wanted you all to do. Secondly, whether we go 50 or 60 and giving us some guidance to give to the Treasurer as to how much of this stream you want to securitize. Those are some of the questions that we felt we needed some guidance from you. Because of the Commission meeting coming up in April, it was felt not only by me but by the leadership represented on this Committee needed to be up to speed as quick possible. Unfortunately we don't have all the answers to some of the questions that we would like but we felt there was a need to at least put before you a spending plan and put forward some percentages of how this would work.

SENATOR WAMPLER: Mr. Chairman, at the direction of the vice chairman of the Commission while I cannot speak for the entire southwest portion of the Commission and with regard to the question should we move forward, I think the southwest members say that we should and we would not want to go beyond 60 percent and its probably a form of art whether you do 50 or 60 percent but 60 percent being the maximum. I would suggest at the direction of the vice chair that we revise our regional plan of how we would propose as guidelines to spend that. That would be anything from industrial access, technology parks, infrastructure, cultural heritage development that is consistent with what this committee has heard us talk about with the crooked road. What we're trying to do is develop a region as a destination. What I'm saying is that its not inconsistent with what we've done before but we've got two weeks to update that plan before we meet on the 5th of April to do so. The question that the vice chairman asked me to ask today is how do we allocate dollars and I'm not sure he knew about the spending plan in detail. If we do it for economic development, do we follow, and I understand very greatly how southside spends their money differently than southwest. I'll say that southwest will recognize the unique goals that you all have set as a region and we support those. The question is do you anticipate taking the proceeds and we allocate as we have in the past between the two regions off of the securitized proceeds?

SENATOR HAWKINS: I would certainly think that would be one of the intentions of what we're trying to do and that's a known factor we're dealing with but there again we're in a new ballgame and we need to make sure that we're making the best use of what we've got. That has been the game plan over the years. Unless there's a good reason to change it I think that's fine.

SENATOR WAMPLER: Then Mr. Chairman I would say that anticipating meeting on April 5th and that's probably the major question the southwest would want to have answered and are we going to generally follow the allocations that we have. I'm only speaking for myself now but whether we use it for southwest economic development committee and whether that's the proper way to do it in our region I don't know but I think it's consistent with what we want to do is invest in hard infrastructure. Other members can speak if I go outside of my lane but I think for our communities, we need the normal allocation we followed. If the great southside wants 66.6 percent we're glad to give that up.

SENATOR HAWKINS: I think what we're dealing with here and the bottom line to me is I think, it's what we can do to put in place the maximum benefit of the monies we have available for all the counties that come under our charge. To make sure we have money available for the hard infrastructure projects that will change the economic destiny of our counties without looking at what we have to do in order to go through the local parochial needs of an industry. If someone wants a business park or an industrial park or a shopping center we've got to get over that and move ahead and look at a picture that creates together the local communities and an overall thrust of infrastructure improvements. Southwest has to be a key part of that in the formulary and it's working so far. So I don't think anyone has a desire to change that.

SENATOR WAMPLER: The point I would make again is I'd ask staff to support us and we're going to have to have at least one meeting between now and April 5th to revise our plan accordingly. I realize that's a short schedule but we need to project this as quickly as we can.

SENATOR HAWKINS: Also dealing with all the subjects we're dealing with, we may have to advance the next meeting of the full Commission and have another executive committee to tie down some things before we move into a full Commission meeting. I don't want us to be talking and not have some answers to some very key questions that we're going to have to be accountable for. I don't think we have those answers yet.

MR. CURRIN: If I may suggest to you, we'll have Ned go over the remaining part of the presentation. I think that would be helpful to everyone and then if I may suggest, go into a full discussion. I think we've got some additional insight here that we would like to put together for you. I think that would be meaningful to the committee.

SENATOR HAWKINS: I'll just remind you lunch is on the table. You can just eat as we go through this and that would be helpful so we're not tied up.

MR. STEPHENSON: Senator Wampler, I am remiss in not stating this. I should have that inherent in this spending plan is actually in writing in what we've done is that the balance of dollars between southside and southwest would be preserved as it has been in the past and as the Commission may choose to change from time to time and that's kind of overarching. That does not change, there's nothing in the spending plan that contemplates changing the balance of dollars unless you all want to do that. That's not part of this and it will stay like it is.

SENATOR HAWKINS: Remember special projects that we're dealing with goes off the top of everything, it doesn't affect anyone's formula. There's a lot of things we've got to do.

MR. STEPHENSON: We're not going to change any formularies in this. I'm going to push through this rather quickly because I know we need to move along. We're contemplating use of the endowment earnings for economic development and the corpus for technology at a rate no more than five percent of the corpus per year. You can certainly choose that number wherever you want to put it. I'd like to flush this out for you a little bit. If you have an endowment of 350 the earnings on that are four percent. Your economic development committees will have about 13 odd million dollars to work with in the first year because that's the earnings on an amount of 350 at four percent. Five percent of the corpus that technology will work with is about 17 odd million for them to work with. Both of those numbers being reasonably consistent with what they have had in the past to work with and understanding that there's less money for everyone so it's down a little bit. I'll move along now and you stop me if you need to. This leaves the remaining MSA payments available for indemnification, education, innovation, administration and agriculture, special projects and TROF will all have to live off of the MSA side of the house and prior commitments that the Commission has made, some of these commitments into the future. A part of this plan is also that the MSA payments would not be used for technology and economic development. So technology and econ would live off the endowment and everyone else lives off of the MSA payments and that's kind of the essence of this spending plan.

I've got about six or eight slides and I'm going to burn through them really fast so if you have a question stop me. What we tried to do was contemplate how this would play out under various scenarios that we're likely to face. There's really only four scenarios either the bonds close or they don't and that might be because the market rejects them or you choose to stop but for whatever reason whether the bonds close or they don't or MSA payments continue or they don't. We've got to think about how this plan would play out for everyone under these four scenarios. The first one, if the bonds don't close and MSA payments continue, this is life as we know it now and business as usual and everything would continue. You have the most money of any scenario and you took a chance on the risk and won. That's where we are right now. The next scenario is that the bonds do not close and there's trouble with the MSA payment. In that case everything we're doing would stop and that's our worst fear and that's what we're trying to guard against. The next scenario is that we do close the bonds but MSA continues on as contemplated. Everything we're doing would continue and you're going to have less money, you're going to wish you hadn't done this. Because the MSA payments continue and you've laid off some risk and it never hurt you. That's one of the possible scenarios. The other one is that you close the bonds and there is a problem with the MSA payment and this is what we need to think about. Under this spending plan if there's trouble with the MSA payments and the technology and economic development efforts survive because they are endowed, everything else stops because they are driven off of the MSA. I say it stops or they are diminished. If that happens you look pretty wise because you ducked the risk and you won. I now want to give you a half life table. This is a concept that if you chose to invade your endowment corpus at certain speeds. For instance, if you chose to do the max permitted by code 15 percent per year in four years time half of your endowment is gone, are you with me? If you use the five percent speed that we are recommending in this plan, it takes about 13 years before you have consumed half of the endowment.

DELEGATE DUDLEY: You're assuming with that that none of the earnings are spent or part of it?

MR. STEPHENSON: The earnings are being consumed by the economic development committee every year, they're taking all of the earnings.

DELEGATE DUDLEY: Five times ten is 50.

MR. STEPHENSON: I'm not sure I'm with you, five percent.

DELEGATE DUDLEY: Five percent for ten years is 50 percent.

MR. WASS: You start with 350 million and then five percent next year is not 350 million but 350 less the five percent and that's the withdrawal amount.

SENATOR HAWKINS: Remember we're looking at figures based on an assumption that these monies will not be invested in projects that create a tax base for localities, additional jobs for localities, different sort of improvements for local economies but we have to factor that in too. There may be some other variables we have to deal with based on what the investment has created and hopefully economic development, economic conditions that have created the next wave of investments and the next jobs.

MR. STEPHENSON: Yes, the thing that I want to ask the Committee to contemplate on this slide is how fast or slow do you want to consume the endowment? There could be an argument for consuming it rapidly, leaving the money on the ground and getting the work done. There may be a conservative argument to stay slow down and preserve the endowment over time. That's kind of a philosophy question the Commission will need to answer. On this slide I'd like you to contemplate what I told you in the beginning I was going to ask you to make a decision. I've heard Senator Wampler on his views but I think there are four things you need to do today; number one is keep going or stop on securitization. That's entirely your call. Number two I'm willing to pay the cost of securitization win or lose. I'm going to suggest to you that your cost may be about a half million dollars to pursue this even though you may lose and when I say lose, I mean the bonds don't close for some reason. Thirdly, how much MSA do you want to sell? Lastly, firm up a spending plan going forward. I'm going to stop at this point Mr. Chairman for any discussion you might have. I expect the staff would try to leave here today with some direction from you on these points.

MR. CURRIN: I spoke to Secretary Schewel yesterday and asked him if the Governor's office is completely supporting it, whatever decision the Commission wants to make. If you all want to do it that's fine and if you don't, that's fine too.

SENATOR HAWKINS: I think we're on a fast track that we need to be on. We have to be cautious to things that we do when we're dealing with these monies. What I would suggest at this point is we have a long term plan to be in place. I'd like that long term committee to meet first and work with staff to make some recommendations to the Executive Committee before the next full Commission meeting. I'm also of the opinion that we probably need to advance the next full Commission meeting at least a week or so to give us some flexibility to be able to come up with an understanding of what we're dealing with her. I think 60 percent is a viable number but 50 maybe more realistic. It's important how we structure these things. As we get into a different structure of payments to localities, although we do not have a legal obligation to our localities, we do have a moral obligation to things that were put in place based on scenarios they dealt with at that time. And if we change things the way we do with localities, I think we do have a moral obligation to make sure that we live up to some sort of understanding what we put them under. We have to put that in some sort of frame. If Delegate Byron's committee can come together with that and the next full Executive Committee meeting, we'll be able to have a few more people involved in that discussion. We need more citizen input than we've got today. Most of the legislators are here as they are today. This is a critical decision we must make. I think ongoing discussion about securitization needs to continue. I think we need to know and make sure we know exactly what we're dealing with.

SENATOR RUFF: I appreciate what you said about technology and capital expenditures. I'm somewhat concerned when we talk about administration, education, and deal closings not being included. One of the things that the Long Range Planning Committee saw as an opportunity in the tobacco region was tourism and retirement and that certainly cannot be paid out of these, the part that we securitize. The prior commitments and the interest in those cannot be. I'm somewhat concerned that we may be reserving too much money for capital projects when we need to look at small things and not just the big picture but small things. I'm a little concerned with 60/40 that we're putting ourselves in a little bit of a straight jacket so that we can protect this money for capital projects. Certainly the technology is necessary. I don't know what other capital projects are out there. If there's a major manufacturer that may be an issue. We have a number of industrial parks and business parks now on the ground so we don't have the capital intensity for every county that we've had in the past. I think we need to be a little careful about that 60 percent.

SENATOR HAWKINS: There lies the rub, we have to figure these things out and this discussion is helpful because we have to start by understanding what we're dealing with because when the day is over, the decisions we make, we're going to have to live with and a lot of people are going to live with it in years to come.

SENATOR WAMPLER: I don't disagree with what Senator Ruff says but ask staff, if you have a deal closing situation before the Commission and as part of that deal closing it requires a major upgrade of water and sewer infrastructure to that industrial park, could you not use the bond proceeds as part of that deal closing?

MS. WASS: We had that discussion about whether the TROF maybe should be moved over to the endowment side because I think the majority of those grants are capital projects and we could enforce that from now on they will be for capital.

SENATOR WAMPLER: Flexibility I think is an advantage. That's the part Senator Ruff was concerned about. Cash is cash in the eyes of the prospect as long as it meets the income guidelines.

MR. STEPHENSON: You could pull the TROF deal across to the other side house if you want to. You can't pull the education piece over there.

SENATOR BYRON: You know, when you spend economic development on, what side of the flexibility line you have here. When you look at some of these figures on paper, it's hard for people to have that security. The security for the projects that we already are involved in are the ones you're going to look at in the future to see that it was or it may benefit and when you look at the figures in the long run to have that flexibility to do some other things is important.

SENATOR HAWKINS: I think that's one thing we need to have some understanding, the discussion we'll get into at the next meeting. Before the recommendations come up and before we really get into this, we need to understand that.

SENATOR WAMPLER: Question to the staff would be whom do we have, if we have this Executive Committee meeting and then a full Commission meeting, what is the outside line because I expect the Treasurer would like to go to market sooner than later.

MR. STEPHENSON: The Treasurer has asked us do you want to continue, will you pay for these costs and how much do you want to go to the market, 50 or 60.

MS. WASS: Or what is the maximum? We have to, the market may not bear 60 percent. The Treasurer may come back and say you can only do 40.

MR. CURRIN: There are other states; we don't know some things right now. Some states that may try to securitize and I can't predict and no one here can predict and whether at this juncture that would reduce the marketplace or how that would affect us. We haven't picked an underwriter yet and that's what the Treasurer's responsibility is. I understand that's in the process and we should know that. We'll have some more figures probably within a week. April 5th was a tentative timeframe to have a full Commission meeting to develop some of these issues. We were trying to coordinate around about ten members of the body would be in Richmond and we're just trying to coordinate around that time.

MS. WASS: April 5th is assuming that financial advisors and underwriters were on board and legal counsel was up to speed and assuming all of that.

MR. CURRIN: I'm sensitive to Delegate Byron's comments about why we're here and what decisions you want but we've tried to outline to the best of our ability to get into this. There are a lot of things right now that unfortunately are nothing but assumptions without having all the facts at hand at this point.

DELEGATE HOGAN: Mr. Chairman, I have a couple of thoughts about this and when it's appropriate during public comment, I'd like to add them.

MR. FERGUSON: I would assume you're speaking as an interested observer. If you get to far a field I'll tell you.

DELEGATE HOGAN: If you don't like what I'm saying you'll tell me to be quiet? Mr. Chairman, are you ready now for public comment or not.

SENATOR HAWKINS: You're the public go ahead.

DELEGATE HOGAN: We talked about as I understand it, the number we talked about before was 50 percent at $350 million dollars and that's going back to what we looked at a couple of years ago. Total sell of $700 million which to my understanding was sort of the bear minimum that we were willing to take a look at.

SENATOR HAWKINS: I think $350 million at six percent.

DELEGATE HOGAN: And now 350 is based on 60 percent and that number once the underwriters and bond houses get done with it, more likely to go down than up. I think that's a safe comment to make. I think it's important for you to realize that we're now willing to take less than we were a couple of years ago and I just put that out for people to think about.

SENATOR HAWKINS: Stephanie.

MS. WASS: The previous deal if you recall both taxable and tax exempt and securitizing the full amount and what you were basing on the $700 million gross proceeds and not net proceeds to the endowment. We're looking at net proceeds to the endowment of the tax exempt piece which was 80 percent and adjusting from there to come up with the $350 million which is probably a conservative number at 60 percent.

DELEGATE HOGAN: The other thing, when you look at the fact that what we're doing is selling risk for 150 million or it's actually not really 150 million because you've got to look at net present value. If that's worth doing and if we think the MSA is going to go away and based on what we're looking at right now in terms of court rulings, I'd say that's relatively unlikely and that's a judgment call and everybody can make their own judgment about it. If the MSA were to go away and let's talk through this. If the MSA and if the MSA stays in place and we stay like we are, most people I think would agree that what we're interested in is mitigating our risks. But if the MSA were to go away and we're sitting on a $350 million dollar endowment, what then would be the posture of the General Assembly. That MSA costs about four bucks a cartoon on cigarettes or forty cents a pack. I think it's highly unlikely that we're willing to let cigarette prices drop in Virginia forty cents a pack. What I think you would see immediately would be an effort to maintain that level of taxation with that money instead of going through the MSA going to the general fund. If we at that point are sitting on a $350 million dollar endowment, our ability to go in and say wait a minute, we just got cut out of $65 million dollars and we'd like a portion of this new cigarette tax to maintain the status quo. I think when we talk to our colleagues in the General Assembly they're looking at the $350 million dollars or whatever portion we have at that point. Our chances of making that argument are damn near zero.

SENATOR HAWKINS: Clarke, I don't follow you on the point you're trying to make. Maybe it's me but the fact you're dealing with is domestic sale of cigarettes. You got to assume that there will be at least a steady consumption rate of cigarettes rather than a declining rate. If you believe that cigarette consumption is the growth industry in this country then we don't want to securitize. You're looking at domestic consumption on a downward slide and securitization gives us some protection for the out years.

DELEGATE HOGAN: Charles, what I'm saying is not only would the MSA going away do away with the Commission dollars but it would also create a $65 or $70 million dollar hole in the budget. Your point is well taken that that may be less as the MSA declines over time but whatever it is, it's going to be substantial dollars. I think the General Assembly is going to see that drop in payments to the general fund is a negative thing. Wait a minute, cigarettes have gone down to four dollars a carton because the MSA is not there anymore and we replaced that with an excise tax to equalize things. I can't imagine we'd let that go and let cigarette prices in the Commonwealth drop forty cents a pack.

SENATOR HAWKINS: I think that assumption is based on a lot of things that's totally out of our control. The General Assembly, if you look at the MSA payments, a portion goes to the state or the Treasurer that would be absorbed fairly rapidly and a budget that's, multibillion dollar structure. If we allow the monies to continue the way they are and if anything goes downward or makes a downward turn, all of our money would be in jeopardy. Every time the General Assembly goes in session and the budget our money's in jeopardy anyway. By securitizing part of it, at least it gets it off the budget cycle and it gives us some sort of comfort knowing that it's not in the budget every year and it doesn't have to be allocated.

DELEGATE HOGAN: I would respond to that the same way Senator Wampler did which is to say that no matter what we do we're still subject to the Appropriations Act.

SENATOR HAWKINS: No question about that.

DELEGATE HOGAN: I don't want to trespass on your time but it looks to me like as we look at this thing we are mitigating a risk that at this point I'm not sure is that real and we're doing it at a substantial discount. The risk to the MSA at this point I don't believe is that great and not nearly what it was a couple of years ago. We're doing it at a substantial discount and while it makes it easier for us to manage our money and God knows it makes this technology project easier to get done. It seems to me we can work around those things and at the end of the day we'll have more money to do it. I think about all this stuff fitting together and what might happen and how would we respond if the MSA were to blow up. I don't see the securitization as a positive step. I think we're selling the risk at too high a premium. That being said, everybody has their opinion.

SENATOR HAWKINS: We're trying to figure out the best thing we can do to deal with this and everything we deal with has consequences both positive and negative. I think today we need to conclude that we either continue the process or discussion of securitization. Before we start getting into final figures, we need to have more understanding about what we're doing. I don't think anyone has a feeling that we need to go ahead and vote and commit ourselves either other than just continuing our discussion.

DELEGATE HOGAN: Other than to spend a half million dollars.

SENATOR HAWKINS: If we finish the process, that's the ultimate obligation. Any time along the way if we stop the process, the cost cuts off there. Dealing with the protection of these monies and to make sure there's some sort of economic base and the conditions we're dealing with in our area of the world, the risk I'm willing to take because I think long term stability means a great deal when we're talking about our economies and some of them are in a constant downturn. Look at your backdoor what happened in Charlotte County earlier this week. We're continuously under that pressure and without some sort of ability to react positively and in an appropriate manner to solve problems. Being less educated than the rest of the Commonwealth and less wealthy and getting older and going through life old and uneducated is no way to create an economy.

SENATOR RUFF: Ned, did you do it at 50 percent?

MR. STEPHENSON: I did.

SENATOR RUFF: Do you want to put that up there?

MR. STEPHENSON: I don't have it, I can tell you the numbers are not materially different moving from 60 to 50. Like someone said, it's a term of art but yes, we did it several ways. I think it needs to be said Senator Ruff that what the Committee can do today without trapping yourself is to send a signal to the Treasurer you contemplate securitizing not more than 60 percent and that's not saying you're going to do 60 but it's equipping her to probe the market at that level and when it comes time to cut the bait, it might be 60 or 40 or 30 when you have more information in front of you. But the signal to the Treasurer is where she should probe the market.

SENATOR HAWKINS: I think we need to inject at this point that we've been in public comment for the last ten minutes and the public has been commenting all during this process. Would anyone else like to make a comment?

DELEGATE DUDLEY: You brought up the point that Delegate Hogan brought up. What Senator Wampler brought up was a good point. The only reason we should be looking at this as I see it, at this point, is if we're scared of the General Assembly. We should not be fearing the MSA payments because in order for us to sell anything there has to be somebody out there to buy it and people that buy bonds are a whole lot more sophisticated than the people in this room and I've been in banking for 31 years.

DELEGATE HOGAN: Even on the telephone.

DELEGATE DUDLEY: Even the ones on the telephone. If there is a market and people are going to scoop these things up, they are scared of that risk. They're putting their hard cash out there. The concern of what might happen to the budget process is a valid concern and that's the only reason I can see considering selling any portion of it at this point.

SENATOR HAWKINS: The bond market, the last issuance they had of the bonds, the people had started looking at buying these bonds they were not Wall Street types but they were your next door neighbor in Rocky Mount and Chatham, Virginia because I love the people that invest in these bonds. So the sophisticated level of these bonds, the same level we are. They're average persons.

MR. WALKER: Are there steps in this process of securitization needs talking about to match the dollars that we're getting ready to spend for this half million dollars. Maybe we can take another step without spending a whole lot of money. Do we have to spend $500 thousand before we say what we want to do? What other steps do we have?

MR. CURRIN: We're not at that point yet. We'll be approaching that point very soon.

MS. WASS: Last time was the worse case scenario, you've got two days before closing and you've gone all the way down the road and priced the bonds and you are almost at the closing table and it failed. That was the worse case scenario.

MR. FERGUSON: Mr. Chairman, at the risk of speaking out of turn, the one item that we talked about, I might be able to add a little bit on is the risk in the MSA question. I think it's probably almost indisputable that there is at least a perception in the market that the litigation risk of the MSA is less now than 18 months ago otherwise there would not be any appetite for these bonds at all. To me that almost goes without saying. I'm not sure that I would agree that in the grand scheme of things the risk is substantially less than it was thirty months ago. The second point I would just raise for consideration, my sense is that a second or different risk that was not thought about or contemplated when we did this two years ago. That is not the risk that the tobacco companies are going to go bankrupt because of litigation or what other risks that we know about but there's a second risk that I think is small, not insignificant completely, is that tobacco companies are looking for ways to reduce their MSA payments to states notwithstanding the fact whether or not they remain healthy or not. We're seeing that through increased levels of challenge on enforcement of the escrow statute for example. I think we're seeing how much they're willing to fight the Phase II issue of whether or not they make the '04 payments. So while that was always in the background, it's come more to the foreground if you will, in recent times. I have every reason to believe that will continue. That's a different risk than the MSA payments, it's not a risk because of tobacco companies going belly up but it's a risk because they're looking for ways to cut costs and one way to cut costs is the MSA or they don't have to pay it as much as they been paying.

SENATOR HAWKINS: Good point.

MR. FERGUSON: I don't know how the bond rating people look at that but I don't think they're as focused on that as they are on traditional litigation, liability, reducing consumption and all these other sorts of economic and financial measures that are more conventional.

SENATOR HAWKINS: Let me see if I can sum this up where we stand right now. In the overall discussions we have more questions before us than answers. Several points have been brought up that I think we need to pursue and it's my understanding from the overall discussions that although securitization is a viable option for us, the percentage that we're dealing with is an unknown and that we probably can tell the Treasurer that we will securitize no more than 60 percent regardless of and probably less than and we're just not sure. Delegate Byron can call her committee together to come up with some answers to questions that have been raised and try to make a presentation at the next meeting of the Executive Committee which should be fairly soon before the next general meeting which will have to be postponed. We can't do this April 5th without an answer. We need this information and we can't be rushed. It'll just take more time. If it’s a little inconvenient for us to be able to do some things, that's all well and good. We're talking about the future of economic development for the entire region. We just can't rush into this.

MS. WASS: We may lose that window of opportunity and the Treasurer has indicated to us that there is a very small window here and that's why she was on the fast track. If you're going to do it, you need to do it and do it quickly.

SENATOR WAMPLER: Mr. Chairman, we need to know that date and set our work plan around it. I agree with Stephanie and Madam Treasurer wholeheartedly.

SENATOR HAWKINS: Stephanie, can you get us that date.

MS. WASS: Once the underwriters and legal counsel and the financial advisors are on board, hopefully within a week we'll know more.

SENATOR HAWKINS: If we can find out what timeframe we're dealing with so we can set Kathy's committee up so they can get into some of the details and then come back to the Executive Committee and we'll hash through it again and then we'll go to the full committee meeting. We've got to get this on track and spend some time with it. It's too complicated and too much involved and too much opportunity for mischief on all sides without due diligence on our part and we must spend the time that's necessary. If it requires a meeting within the next ten days, a full day's meeting to do it then that's fine. We all have to have an understanding of whatever we do, what we're really dealing with.

MR. CURRIN: I'll work with Delegate Byron to get her committee set up.

SENATOR HAWKINS: Does anyone have any comments or we can go around the table.

SENATOR WAMPLER: There's one thing Mr. Chairman and I'll be very brief. Some of the positive aspects of securitization is institutionalizing goals and spending plans of the Commission and whatever that amount is, it's still up for grabs and it's a function of what the market will absorb. However, I think we could say with our long range plan if we're spending a half million dollars on infrastructure in the various categories, I think probably is the most compelling reason why we need to go to the market, to get this revenue stream. I think that's what our localities lack right now. If you look at the applications that come in, it's for the moment rather than long term and I think that's institutionalizing and probably allow us to have better spending habits on the part of the Commission and have a better regional rate of return. That's the end of that summary Mr. Chairman.

SENATOR HAWKINS: Let's go around the table real quick. Anyone else have any comments?

DELEGATE JOHNSON: Frank Ferguson, can you think of anything that we have not done that we should have done to protect us when and if something blows up.

MR. FERGUSON: Stephanie probably knows more than I do since it's her area. I don't know of anything off the top of my head.

MS. HAMLETT: I really don't because it's very hard with the market fluctuation and events driving it or plan for what blew up last time. That was totally unforeseen. The exact same thing could occur this time, you could go through all the steps primarily the amount of money to do the deal and still end up, you could go and price bond and it turns out on that particular day, that particular moment the pricing is such that you wouldn't want to sell them because your return would be so small. Then a week later the market may be better. Frankly if you were ready and you had a small period, you could still step back into the market so that interest rate risk may not be quite as bad as the event. If you're getting ready to price and getting ready to close and there's a judgment against Philip Morris for a hundred million dollars or $16 million dollars, we're right back where we were in the beginning. Do you see any of that on the horizon, no, but there's tobacco litigation everywhere.

DELEGATE JOHNSON: Do you feel like we have explored the possibilities and maybe sought expert advice on the bonds that we should have or should we do more?

MS. HAMLETT: The only thing I would suggest as I listen to today's presentation is that if you want to proceed, that you have at least one meeting where you have the whole Commission or the Executive Committee with the bond lawyer present to talk about spending. As I listen to it and as I remember back trying to forget but remembering when I was a bond lawyer, is that what you're going to come down to is that every time you have a project that's remotely iffy and it may even be every project, you're going to end up having to call bond counsel and say can we do this and that's going to be an ongoing expense that you're going to have to pass onto the localities. You're going to have to make the localities pay for bond counsel. You're going to end up, you're going to have to incur it because they're going to be telling you on those proceeds yes you can or yes you can't. I don't think we thought about that the last time but I see it with the Virginia Public School Authority or the Virginia Building Authority. It turns out that whatever issue, whether it's, that every time they want to do something different, it would have to go to bond counsel and can you do it this way.

SENATOR HAWKINS: The advantage we have with securitization, now we have a better understanding of what we're getting into and we're asking the right questions. The last time we were clearly new to this and whatever happened it may have been overall the best thing that happened because we put ourselves in a position now that we can understand better and we didn't know all the implications we were dealing with before.

MS. HAMLETT: I think that's very true.

MR. FERGUSON: Delegate Johnson, we're not there yet with the question you asked but once the underwriters are on board and bond counsel is put in place, I believe we have done everything we should have done up to this point. There's more to do, we're on a tight timeframe to do it but that may require some inconvenience for the Commission to be satisfied that your hearing what you need to hear before making a final decision.

SENATOR HAWKINS: Any other subject to come up?

MR. WALKER: Would it be in order for me to ask a member of the public a question?

SENATOR HAWKINS: Yes.

MR. WALKER: Are you still on the line?

DELEGATE HOGAN: Yes. Carthan, have you covered this?

MR. CURRIN: No, I have not.

DELEGATE HOGAN: Carthan might enlighten you on an issue he's become aware of and I've been talking to him at home and see if maybe we can get a little direction from the Executive Committee on this. Do you want to talk about where we are in general terms on that Carthan?

MR. CURRIN: There has been some recent turmoil to a degree in the economic development arena in Halifax County. Halifax County receives funds from the Tobacco Commission or significant funds and Delegate Hogan and others have brought something to my attention. It's been requested and I'll share some of staff's concerns to the Board of Supervisors at their meeting on March 21st at 7:30 p.m. Delegate Hogan felt the need for me to communicate this to the Executive Committee. I'll be delighted to pass on some of our concerns to the Board. I'm not trying to interject my office or the Commission into the internal politics into this but the fact is we do have significant dollars. There has been some –

DELEGATE HOGAN: Is it appropriate for me to make a comment right now?

SENATOR HAWKINS: Yes, this is a public comment period.

DELEGATE HOGAN: Carthan may have covered it in general terms but certain members of the IDA that hold significant grant monies from the Commission, they're in line to get significantly more including money going into Riverstone that are taking the position that they are a separate political subdivision from the county in which they technically are and that they're not answerable to the county or anyone else in relationship to those projects. I don't want to air the laundry of Halifax in front of the Tobacco Commission and I think it would be remiss or irresponsible for me and other people aware of that not to tell you what that situation is and to the extent that we partner with these different localities. We're partnering with someone who has serious troubles. From a fiduciary responsibility that gives me some heartburn.

SENATOR HAWKINS: Were the grants made to Halifax or the IDA.

DELEGATE HOGAN: Yes. It may be appropriate for the Commission in the personage of Carthan to express these concerns to the Board so that they understand that while they get the money, we're not writing blank checks to people that are doing different things than they said they were going to do.

SENATOR HAWKINS: We've got a baseline that we've always tried to work from that what we obligate our monies for, that's the project is being paid for and it cannot be used for someone else's project.

DELEGATE HOGAN: Who owns the property, that's the issue that is specific in this case? Our assumption is the IDA owns it and they're acting in the best interest of the people of Halifax County. If they're going off on a different tangent from the Board of Supervisors what is that situation? I don't want to get the Commission involved in local politics. I don't want to get involved in it. We have these kinds of problems. If we have these kinds of problems that mess comes back to the Commission and it could affect Riverstone and projects that are going on, VIR and any relationship to Danville and any other things and that concerns me.

MR. CURRIN: I’m not going to try to get into a cat fight into the internal affairs of Halifax County, however, Delegate Hogan has pointed out that if my office were to at least communicate to the Board that we’re aware of some of the situations here, express some concern, we obviously have due diligence to the Commonwealth and the Commission with funds that are allocated to any of the counties or cities within the tobacco region.

SENATOR HAWKINS: The monies that we allocated were based on the applications of the IDA of Halifax County.

DELEGATE HOGAN: I have to look at them technically to know. I know the IDA holds the assets.

SENATOR HAWKINS: If we made a grant to the IDA to invest in various things that’s what they’re doing, if we made them to Halifax it makes a difference.

DELEGATE HOGAN: I’d have to look at the paperwork to know that. I know some of the stuff is to the County but the IDA is doing it and some of the stuff may or may not be directly to the IDA. Without looking at the grant agreement I couldn’t answer that question. I think it’s always been our understanding that when we made these grants to any locality or if we made them to Smyth County and you found out that Smyth County IDA is doing something different from what the Board of Supervisors had in mind, that the assets they were given, that we gave them on behalf of the county creates problems.

SENATOR HAWKINS: I understand your problem Clarke and I’d like to figure out something that we could do to help solve the internal workings of Halifax County. I don’t think they have any appetite to jump in the middle of the swamp without any way out.

DELEGATE HOGAN: I don’t want the Commission to get in a swamp. I think it is appropriate for the Commission to let Halifax County know that there are some issues that are of concern to us and raise questions about what’s going on. We’ve got $20 million dollars in the county.

SENATOR HAWKINS: Give us the documentation on how the monies are allocated and what the conflicts are and what has been the intent so we’ll have some understanding if there’s some sort of breakdown in communication about how the monies have actually been spent and I think that would be very helpful.

MR. WALKER: Mr. Chairman, would it be appropriate for us to direct the staff to review the application and the grant and Carthan could relay that information to them so its clear what we thought we were obligating the funds for and what their spending money on, that's where our responsibility is.

SENATOR HAWKINS: Due diligence of the staff I think that would include looking at those allocations in the normal process. I'm not so sure that would take a motion but I think you all can go ahead and do that anyway under the guidelines of what we're dealing with to make sure that those obligations are in place. Any other problems you want to bring forward.

DELEGATE HOGAN: I've done enough trouble today Mr. Chairman.

SENATOR HAWKINS: Thank you. Any other comments from the public, any comments from Commission members.

MR. ARTHUR: Mr. Chairman, have we made a decision today?

SENATOR HAWKINS: No.

MR. ARTHUR: Do you plan to?

SENATOR HAWKINS: No. I don't know what the decision would be Tom.

MR. ARTHUR: Did I hear a motion from the people here what the general consensus is, to go or no go? If the consensus is go then do we recommend to the Treasurer that it's up to 60 percent? Do we need a motion on that?

SENATOR RUFF: Mr. Chairman, I think we ought to go ahead and have that motion before us.

SENATOR HAWKINS: There's a motion before us that we convey to the Secretary of Finance that we would like to pursue securitization and the maximum amount to be securitized up to 60 percent maximum. That figure of course, is fluid. That ongoing discussion should continue until we are further advised of our position that we will bear the cost. Is there a second, there's a second. It's been moved and seconded, any discussion?

MR. WALKER: Mr. Chairman, we reserve the right to stop if we want to.

SENATOR HAWKINS: Yes. Any discussion, does everyone understand the question? All in favor say aye (ayes). Opposed.

DELEGATE DUDLEY: No.

SENATOR HAWKINS: All right.

DELEGATE BYRON: Tentatively we're going to call for a meeting, long range plan next Wednesday and that the seven day notice of the time, is that enough time?

MR. CURRIN: Three days notice.

DELEGATE HOGAN: I'm gone, thank you.

SENATOR HAWKINS: Stephanie, give us a date so we can make sure that we understand and what timeframe we're dealing with so we can plan an Executive Committee meeting. We got to get some answers to these questions because they're beyond anything we would try to deal with at this time. Is there a motion to adjourn? It's been moved and seconded, we're adjourned.

PROCEEDINGS CONCLUDED

CERTIFICATE OF THE COURT REPORTER

I, Medford W. Howard, Registered Professional Reporter and Notary Public for the State of Virginia at large, do hereby certify that I was the court reporter who took down and transcribed the proceedings of the Executive Committee meeting when held on Wednesday, March 16, 2005 at 11:00 a.m. at the Hotel Roanoke and Conference Center, Pocahontas Room, Roanoke, Virginia.

I further certify this is a true and accurate transcript to the best of my ability to hear and understand the proceedings.

Given under my hand this 24th day of March 2005.

Medford W. Howard
Registered Professional Reporter
Notary Public for the State of Virginia at Large
MY COMMISSION EXPIRES: October 31, 2006