

MINUTES OF MEETING
STATE BOARD OF FINANCE

July 29, 2008

A meeting of the State Board of Finance of the State of Arkansas was held in the Conference Room, Office of the Treasurer of State, Suite 275, Victory Building, Little Rock, Arkansas, at 10:00 a.m., Tuesday, July 29, 2008, pursuant to notice duly given to each member of the Board by the Chairman.

The following members were present:

Richard Weiss, Director, Department of Finance
And Administration
Martha Shoffner, Treasurer of State
Candace Franks, Arkansas State Bank Commissioner
Jim Wood, Auditor of State
James Miller, representing Governor Mike Beebe

Others present were Charlie Frago, reporter for the Arkansas Democrat-Gazette; C. Sam Walls and Jay Wisener, of Arkansas Capital Corporation Group; Jack Williams, of Williams & Anderson, PLC, representing Arkansas Student Loan Authority; Virgil L. Miller, Jr., representing Metropolitan National Bank; Lisa White, of the Auditor's Staff; and Karla Shepard, Wes Goodner, Autumn Sanson, Melissa Corrigan, and Patti Lah of the Treasurer's staff.

Richard Weiss served as acting Chairman in the absence of Governor Beebe and called the meeting to order with recognition of a quorum.

The first item on the agenda was the consideration of \$150,000,000.00 State Board of Finance CD maturing on August 28, 2008, and reinvestment of \$110,000,000.00. Acting Chairman Weiss recognized Bank Commissioner Franks, who recommended the investment rate of 2.20%. She stated that she used her discretion, as discussed at the last Board meeting, mixing

up the banks on the list to maximize the opportunity for better rates and she added that she had included a 7-month CD in the bank averages. A motion was made by State Auditor Jim Wood to accept the recommended rate of 2.20% and James Miller seconded the motion, which was passed unanimously by the Board.

Acting Chairman Weiss recognized Mr. Walls of Arkansas Capital Corporation Group to discuss the second item on the agenda, the consideration of Arkansas Capital Corporation Group's request to: (1) refinance three state notes; (2) change the borrowing formula and rate associated with new state notes; and (3) approve access to an additional \$6,000,000.00 under state line of credit. To provide clarification, Mr. Walls distributed a Memorandum to the Board members, in words and figures as follows:

To: State Board of Finance
From: Sam Walls, CEO
Date: July 24, 2008
RE: Refinance of State Notes

Arkansas Capital Corporation respectfully requests the following:

1. Refinance the following three state notes (Currently priced at the 2-year treasury):

	<u>Current Rate</u>	<u>New Rate</u>
• #157 - \$8,928,000	3.723%	2.25% (Primary Credit)
• #158 - \$6,550,000	5.090%	2.25% (Primary Credit)
• #159 - \$11,400,000	4.765%	2.25% (Primary Credit)

2. Change the borrowing formula and rate associated with new state notes:

- **Current – 10 year note tied to 6 month CD rate, adjusted every six months.**
- **Proposed – 10 year note tied to primary credit rate, adjusted quarterly.**

3. Approve access to additional \$6,000,000 under state line of credit to be drawn as needed to facilitate increasing loan demand.

Historically, the State invested in ACC notes at the federal discount rate fixed for ten years. In 2003, the formula was changed to the 2-year treasury note, adjusted every two years. In 2005, the formula was again changed to the "Average six month CD rate as

determined by the State Bank Commissioner”, adjusted every six months. As a SBA lender, ACC prices its loans in relation to prime with lending rates adjusted quarterly. Due to the unprecedented drop in interest rates, a mismatch in the timing of the repricing of our loans and the state’s invested dollars has occurred. The situation has resulted in ACC incurring an operational loss. As of 5/31/08, ACC’s spread was 3.65% versus the average bank’s spread of 4.35%. ACC estimates our SBA lending cost at 1.2%, if this is taken into account, our spread drops to 2.45%. ACC’s spread calculation is computed using the real time yield of our loan portfolio and the actual annualized cost of funds as of 5/31/08.

A recent examination by the Arkansas State Bank Department resulted in a favorable outcome. The exam concluded that ACC’s earnings performance is hampered by an increasing cost of funds. In addition, it was noted that the mismatching of re-pricing assets (loans) and liabilities (state notes) coupled with SBA lending cost (which lowers risk to the state) has negatively impacted ACC’s earnings and constrained our ability to manage the interest rate risk during the most recent falling rate environment. Our goal is to be equally matched with state borrowings and our clients’ loans both repricing on a quarterly basis, thus minimizing interest rate risk exposure.

Thank you in advance for your consideration.

Chairman Weiss recommended that the requests be examined by the Arkansas Bank Department prior to the State Board of Finance making a decision and the Board would revisit the issue at the next meeting.

As the next order of business, Chairman Weiss recognized Jack Williams. Mr. Williams explained that, due to recently enacted legislation to assure continued access to student loans, the Department of Education now required that every one who was a student loan lender execute a document entitled “Notice of Intent to Participate”. This form was required to be submitted by July 31, 2008. Mr. Williams stated that the form did not commit the Board to do anything, but in the event the Board wanted to sell the loans, the executed document would strengthen the Board’s position. Autumn Sanson, Chief Investment Officer for the State Treasurer, agreed to electronically file the executed document with the Department of Education, and she would then notify Mr. Williams of the electronic receipt.

Minutes of the meeting of May 28, 2008, were approved as distributed.

There being no further business, the Acting Chairman declared the meeting adjourned.

ATTEST:

Secretary of the State Board
of Finance of the State of Arkansas

Acting Chairman of the State Board
of Finance of the State of Arkansas

Secretary's Note: All documents pertaining to the issues considered are filed in the permanent records of the State Board of Finance.