



23rd ANNUAL CALIFORNIA CHARTER SCHOOL CONFERENCE

ROAD TO SUCCESS: Navigating Facilities Financing from Two Perspectives

March 16, 2016

11:00 AM

Beacon Ballroom A



MUSICK PEELER



Introductions: Today's Presenters



Sabrina Ayala
Chief Financial Officer
Green Dot Public Schools National

Leading charter school operator in California and nationwide
One of the top three largest in the U.S.
Serves nearly 11,000 students in grades 6-12 in multiple locations in California
www.greendot.org



Jennifer Cauzza
Executive Director
Julian Charter School

WASC-accredited Independent Study charter school serving Orange, Riverside, and San Diego counties.
Serves over 2,400 students in grades K-12, offering both Home Study and Academy options
www.juliancharterschool.org/

MUSICK PEELER

Neal Millard
Partner
Musick, Peeler & Garrett LLP

Prominent California law firm
Charter school practice focuses on representing charter schools and CMOs in all aspects of operations
www.musickpeeler.com

Brian Colon
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Robert W. Baird & Co.

The leading underwriter of charter school facilities financings
Over 140 financings totaling more than \$2.5 billion for Charter Schools
www.rwbaird.com/charterschools

John Buck
Principal
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Buck Financial Advisors, LLC

Full service financial advisory firm specializing in charter school facility finance
Over 15 years of financial advisory experience with charter schools
www.buckfinancial.net



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Today's Breakout Session Discussion

- **Funding Charter School Facilities**

- Options
- Primary Financing Methods
- Key Factors to Consider
- Characteristics Important to Lenders

- **Charter School Bonds**

An option utilized by Green Dot Public Schools & Julian Charter School

- What Projects can be Financed
- Financing Structure and Primary Participants
- Timing
- Security and Primary Financing Covenants

- **The Financing Process from the School's Perspective**

- Green Dot Public Schools California
- Julian Charter School
- Q&A

- **Current Charter School Bond Market Environment**

Funding Charter School Facilities



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Funding Charter School Facilities – Options

Cash

Nice if you have it but very few schools can afford to finance facilities with outright cash

Philanthropy

Grants or program-related investments (“PRI’s”) provided by a foundation(s) to charter schools, at below market rate or forgivable loans

Short-Term Debt

Construction loans, bank loans, New Markets Tax Credit (“NMTC”) loans (with/without NMTC equity)

Long-Term Debt

Charter School Bonds

Lease Purchase

Developer and/or Investment fund driven
Often provided by contractors, with escalating lease payments and purchase prices.

Funding Charter School Facilities – Primary Financing Methods

Depending on the life-cycle and financial condition of the school, any of the options outlined may be a viable financing option. However, the **Charter School Bond issue option provides the longer financing term and is the only option that removes interest-rate (refinance) risk.**

Types of Financing	Charter School Bonds	Traditional Bank Loans	New Markets Tax Credit (“NMTC”)	Lease Purchase
Generally Appropriate For:	Generally, more seasoned school or organizations with substantial credibility	Newer or seasonal Schools, interim construction possible	New or more seasoned, but project must be in a “qualifying area” defined by census track and poverty levels OR serve targeted population	Newer Schools, Interim Financing until Permanent Takeout Available
Amount Financeable (Loan-to-Value):	+/- 100%	70–80%	+/- 80-90%	Flexible but reflected in cost of lease
Typical Term:	30-35 years	5-10 year, 20-25 year amortization	Usually interest only for the first 7 years	20–30 years
Appraisal Requirement:	Generally, no	Yes	Depends	Depends
Required to Refinance?	No, but school has option	Yes	Yes	No, but option with prepayment penalty
Complexity	Medium	Low	High	Medium
Typical Time Required to Close	+/- 90 days	+/- 30 days	+/- 90-120 days (or longer)	+/- 60 days
Other:	Various covenants required to maintained	Lender may require all deposits and credit lines	20-25% on loan normally “forgiven” at end of year 7	Various covenants required to be maintained

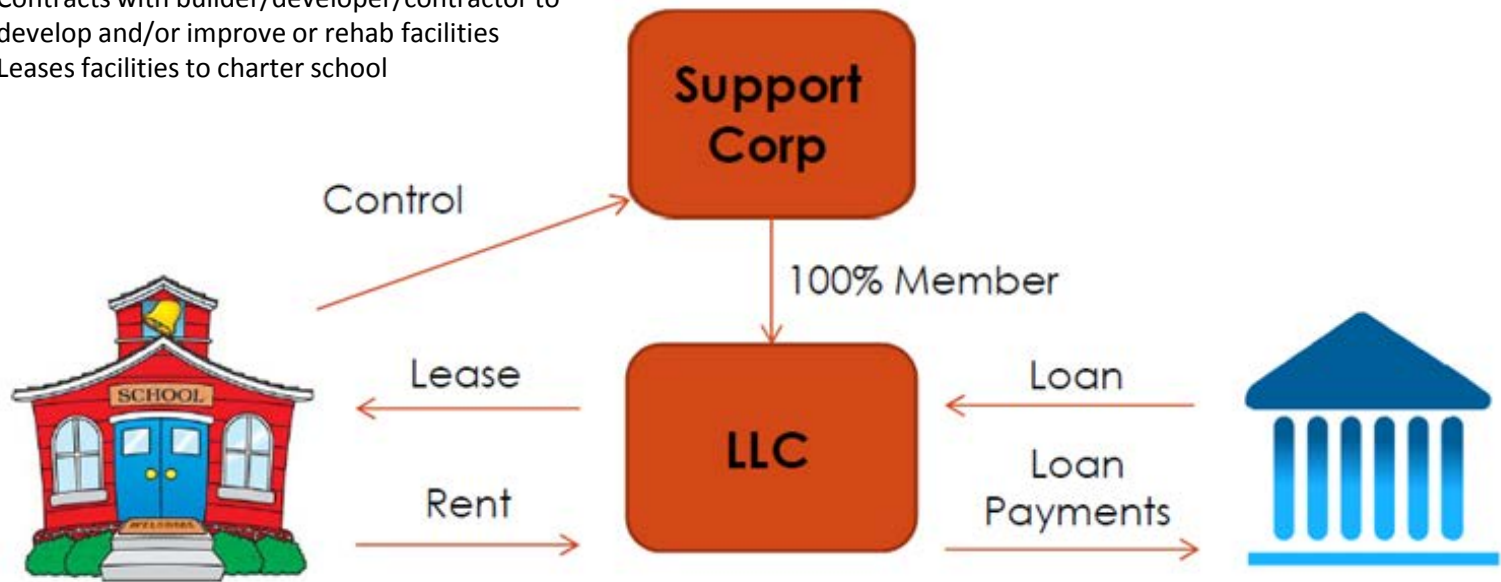
Funding Charter School Facilities – Key Factors to Consider

ABILITY TO FINANCE EXPANSION OF SCHOOL	% OF BUDGET REQUIRED FOR FACILITIES	ABILITY TO PREPAY	REAL ESTATE ISSUES	EXIT STRATEGY
<p>Think long term: Future capital plans</p> <ul style="list-style-type: none"> Facility financing will have “first lien” on revenues Some types of financings will not allow “parity” debt in future <ul style="list-style-type: none"> Parity means having equal claim on revenues and facilities You want as much flexibility as possible to issue parity debt in the future Future capital plans should be considered when evaluating financing options today 	<p>Maximum of 20% of your steady-state budget (not at future full enrollment)</p> <ul style="list-style-type: none"> 15% or less is ideal <p>Example: \$ 10 Million Budget</p> <ul style="list-style-type: none"> Debt Service no more than \$2.0 million annually, \$1.5 million preferable 	<p>Ability to pre-pay will depend upon financing vehicle and negotiated terms</p> <ul style="list-style-type: none"> Tax-exempt bonds can be <u>defeased</u> prior to maturity <u>at the school’s option</u> <ul style="list-style-type: none"> 10-year par call is standard New Markets Tax Credits, other Federal programs involving credits <ul style="list-style-type: none"> Typically cannot be pre-paid prior to the end of the 7-year tax compliance period Equity investors can face penalties if loans are prepaid 	<p>Deal with real estate issues EARLY!</p> <ul style="list-style-type: none"> Deed(s) on all properties – fee simple or leasehold Title insurance Existing surveys (land division? Combination?) Environmental site assessments Geotechnical reports Preliminary plans Conditional use permit (if applicable) Zoning ordinances and building restrictions Property tax information Access, utilities, and other municipal services GET ALL NECESSARY APPROVALS 	<p>Is financing permanent?</p> <ul style="list-style-type: none"> Fully amortized by maturity? Tax-exempt bonds are typically fully amortized Bank loans and NMTCS not fully amortized at maturity <p>Is there refinance risk?</p> <ul style="list-style-type: none"> If not fully amortized, loan will need to be refinanced at maturity Interest rate risk associated with refinancing Do you have the option to refinance?

Funding Charter School Facilities – Key Factors to Consider

Organizational Structure to Access SB740 Facilities Funding

- ✓ **Form a separate property development Limited Liability Company (LLC)**
 - Supporting organization is sole member
- ✓ LLC disregarded for federal tax purposes
- ✓ LLC obtains California tax-exempt status as title holding company
- ✓ **LLC obtains financing**
 - Contracts with builder/developer/contractor to develop and/or improve or rehab facilities
 - Leases facilities to charter school



Funding Charter School Facilities – *Characteristics Important to Lenders*

- ☑ **Enrollment:** Stable and/or increasing?
- ☑ **Debt Factors:** Debt service below 20%?... below 15%?
- ☑ **Financial Condition:**
 - Stable/increasing fund balance?
 - Minimum 5% of operating expenses?
 - Positive net revenues available for debt service?
- ☑ **Fund Raising:** Rely only on pledges in hand?
- ☑ **Governance:**
 - Board buy-in and business acumen?
 - Established policies & procedures?
- ☑ **Academic Program:**
 - Positive test score trends?
 - distinguishing curriculum?
- ☑ **Competition:** Advantages over other education options in the area?
- ☑ **Wait List:** Is a wait list in place?
- ☑ **Charter Term:** One renewal event accomplished?
- ☑ **Student Retention:** At least 90% for each grade from one year to the next?
- ☑ **Teacher Retention:** Low turnover?
- ☑ **Other Capital Plans:** Reasonable?

Charter School Bonds – *An option utilized by Green Dot Public Schools & Julian Charter School*



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Charter School Bonds – *What Projects can be Financed*

- **Capital expenditure projects**

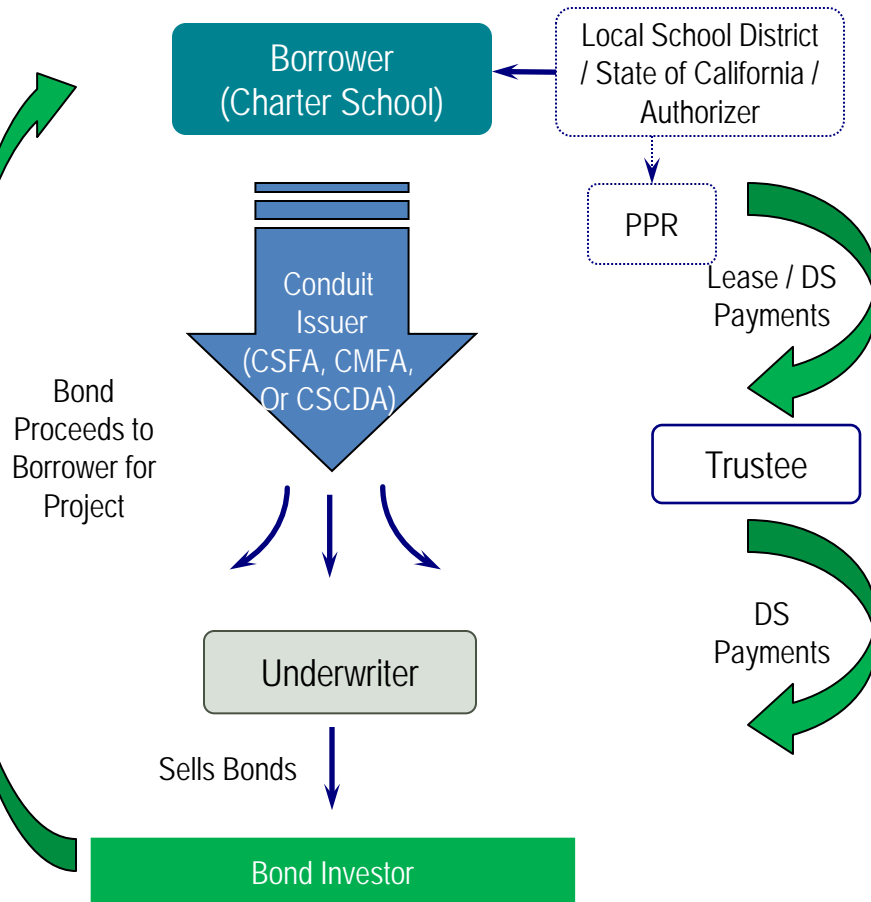
- ✓ Land
- ✓ Facilities – new building or renovate existing facilities
- ✓ Computers/technology equipment
- ✓ Buses/transportation
- ✓ Sports facilities (example: gymnasium)
- ✓ Funds may also be used to reimburse amounts already expended up to 18 months before bonds are issued

- **Refinancing Prior Debt**

- ✓ Refinance outstanding taxable debt acquired in connection with capital projects (construction loans, NMTC, bank loans and mortgages, related party (e.g. board member loans)
- ✓ Refinance existing tax-exempt debt
- ✓ Payoff capital leases

Charter School Bonds – Financing Structure and Primary Participants

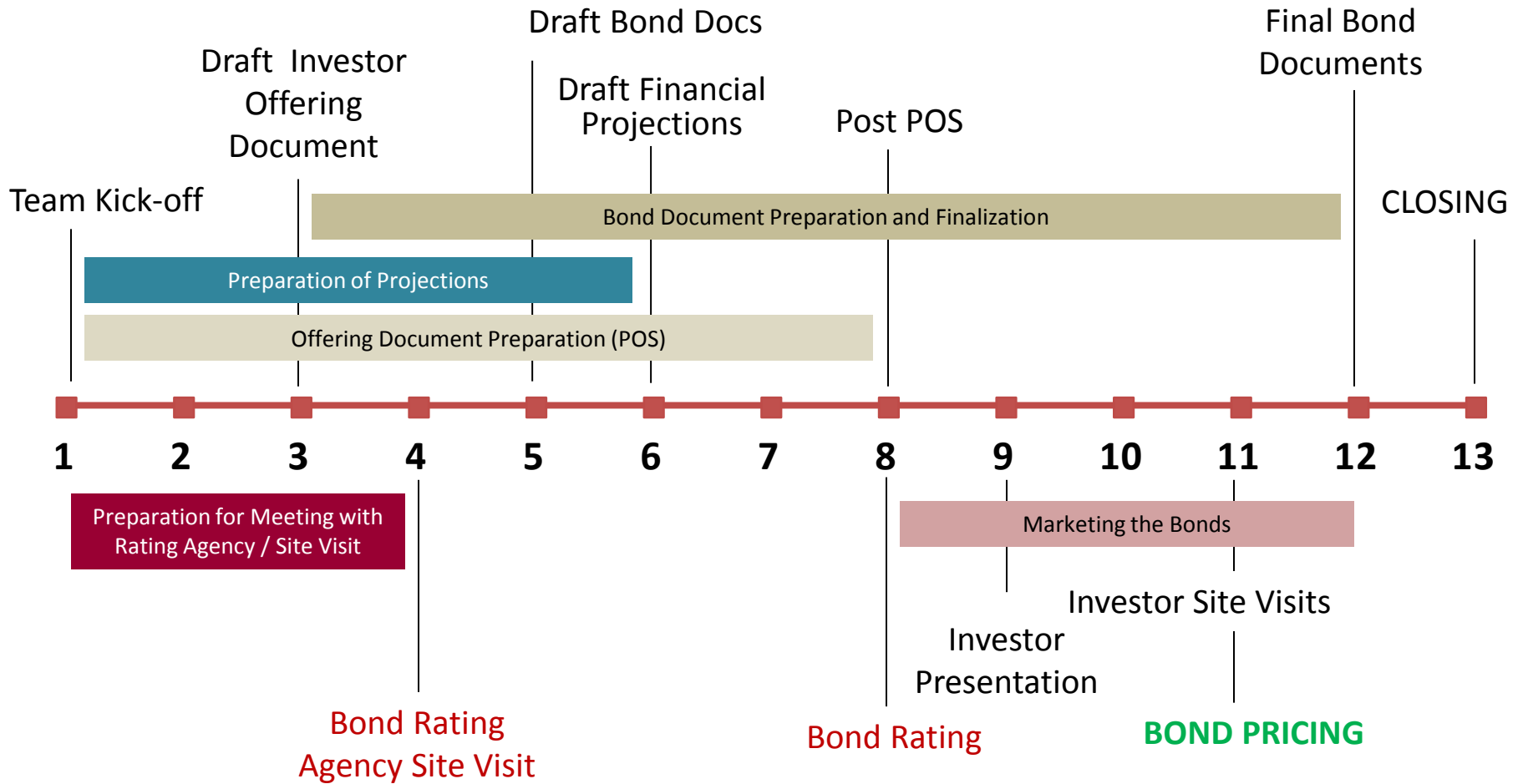
TYPICAL CHARTER SCHOOL BOND STRUCTURE



PRIMARY TRANSACTION PARTICIPANTS

- **Borrower / Obligor** – Charter School Corporation / Charter School (Lessor/Lessee)
- **Borrower’s Counsel** – corporate counsel of the borrower, reviews all legal documentation for accuracy and authority, reviews or prepares real estate documents
- **Bond Counsel** – drafts primary bond documents (trust indenture, lease agreement, and loan agreement) and renders tax opinion
- **Issuer** – conduit issuer through which the bonds are offered such that all tax and legal objectives (opinions) are achieved
- **Issuer’s Counsel** – reviews all documents on behalf of the issuer primarily to ensure that no financial obligation rests with the issuer
- **Underwriter** – structures the bond financing, evaluates credit, negotiates covenants, and markets the bonds to investors
- **Underwriter’s Counsel** – reviews all documents on behalf of the underwriter and constructs the bond purchase agreement and the offering document
- **Financial Advisor** – acts as an independent advisor. Under new SEC rules, has a fiduciary duty to the charter school (duty of loyalty and duty of care)
- **Rating Agency** – third party evaluation of the transaction; not part of team in terms of structuring and credit decisions
- **Trustee** – fiduciary responsibility to hold bond funds (DSRF), makes draws for principal and interest and represents the bondholders
- **Investors** – purchases the Bonds

Charter School Bonds – Timing – by Week (General)



Charter School Bonds – *Security & Primary Financing Covenants*

SECURITY

- **Full Faith and Credit Pledge of Revenues** – *State funds are intercepted by the Trustee (subject to state law) to make payments with remaining revenues released to the school*
- **Mortgage / Leasehold Interest** – *First lien on facilities being financed*

PRIMARY FINANCING COVENANTS

- **Debt Service Coverage** – *Net Income Available for Debt Service/Debt Service*
- **Minimum Net Assets as % of Operating Expenses**
- **Liquidity (Days Cash on Hand)** – *Unrestricted Cash and Investments/Total Operating Expenses x 365*
- **Additional Debt Test:** Generally 1.20x Required; Objective financial test without getting existing bondholder approval
- **Repair and Replacement Fund:** A fixed dollar amount or % of Operating Expenses; Subject to 5 Year Review by a Facilities Consultant
- **Continuing Disclosure:** Requirements to provide periodic (monthly, quarterly, semiannual and/or annual) information on academic, operational and financial results

The Financing Process from the School's Perspective

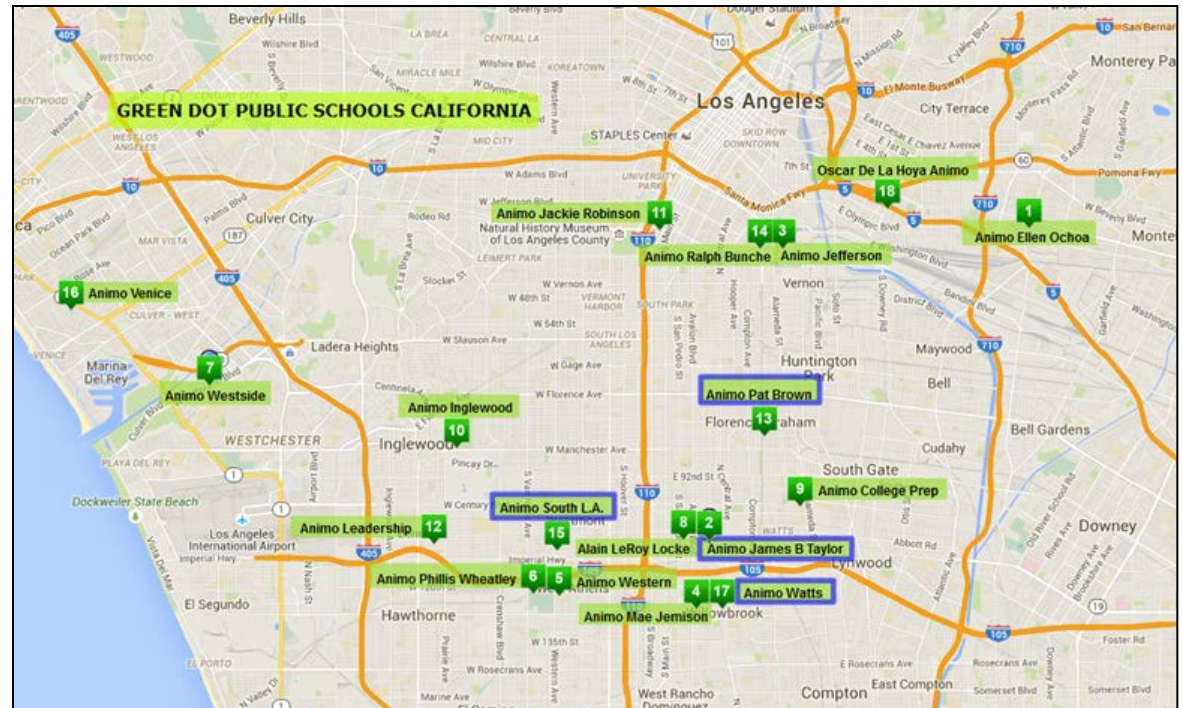
- *Green Dot Public Charter Schools California*

- *Julian Charter School*



Green Dot Public Schools California

- Green Dot Public Schools is a nonprofit charter management organization (“CMO”), founded in 1999, created with the vision of transforming education in California by creating high-performing charter schools to catalyze change in underperforming areas
- Currently operates 11 high schools and 7 middle schools in the highest-need areas of Los Angeles, including 3 turn around schools
- Grown from 140 students in 1999 to over 10,500 students currently
- Unionized since inception



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Green Dot Public Schools California – September 2015

CALIFORNIA SCHOOL FINANCE AUTHORITY

\$26,710,000

School Facility Revenue Bonds
Series 2015A (Tax-Exempt)

\$4,395,000

School Facility Revenue Bonds
Series 2015B (Taxable)



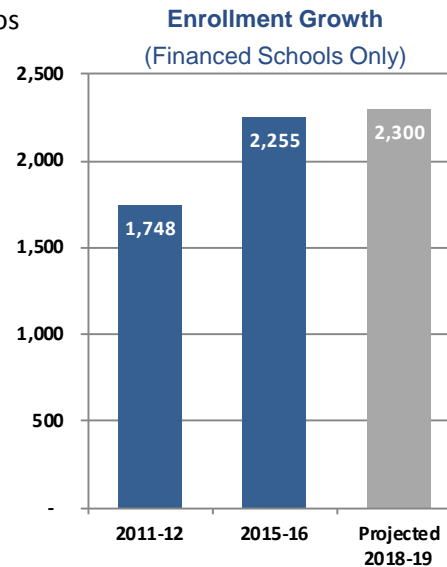
- ⇒ Musick Peeler Served as Borrower’s Counsel
- ⇒ Buck Financial Advisors served as Borrowers Financial Advisor
- ⇒ Baird served as Underwriter

Financing Need:

- **Refinance New Market Tax Credit top tier leverage loans** for facilities located at Animo James B. Taylor, Animo South Los Angeles, Animo Pat Brown and Animo Watts;
- Acquire, construct, expand, renovate, improve furnish and equip educational facilities at the Animo South Los Angeles facility

Financing Results:

- 30-year fixed rate financing
- Rated “BBB-” by S&P
- Secured a True Interest Cost of 4.86%



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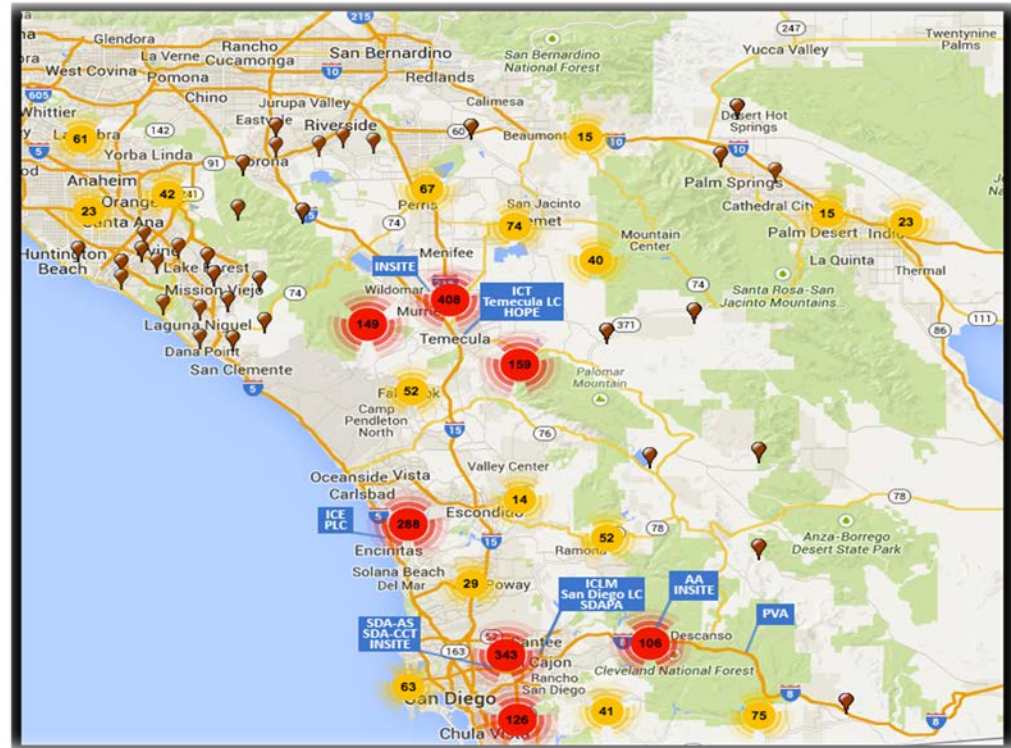
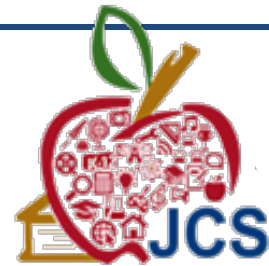
Green Dot Public Schools California – September 2015

- ↪ *Why did you select Bonds as your method of finance?*
- ↪ *What types of internal resources were necessary to dedicate to the financing.*
- ↪ *What challenges had to be overcome to complete the financing?*
- ↪ *What kinds of ongoing responsibilities are there?*
- ↪ *How satisfied are you with the results?*
- ↪ *What changes to the process would you like to see?*



Julian Charter School

- Julian Charter School is a California nonprofit public benefit corporation incorporated in 1999, established to meet the needs of students who are underserved by traditional delivery systems of education and for families who have a strong desire to home school.
- Julian operates as an independent study school and offers various programs that can be tailored to the specific needs and desires of each student.
- Approximately 50% of Julian students participate in the Home Study program and the remaining students participate in the Academy programs
- Julian serves over 2,500 students in grades K-12



Julian Charter School – March 2015

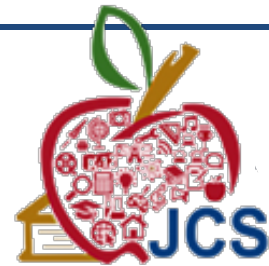
CALIFORNIA MUNICIPAL FINANCE AUTHORITY

\$25,905,000

\$760,000

Charter School Revenue Bonds
Series 2015A (Tax-Exempt)

Charter School Revenue Bonds
Series 2015B (Taxable)



- ⇒ Buck Financial Advisors served as Borrowers Financial Advisor
- ⇒ Baird served as Underwriter

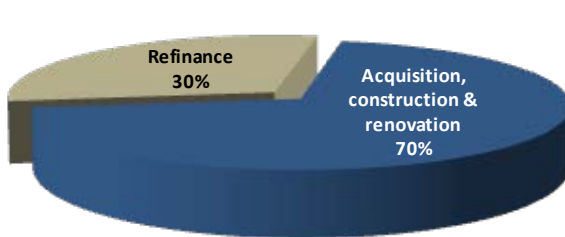
Financing Need:

- Finance and refinance the acquisition, construction, renovation and improvements of educational facilities located in Temecula (2 separate locations), Murrieta, and Encinitas.

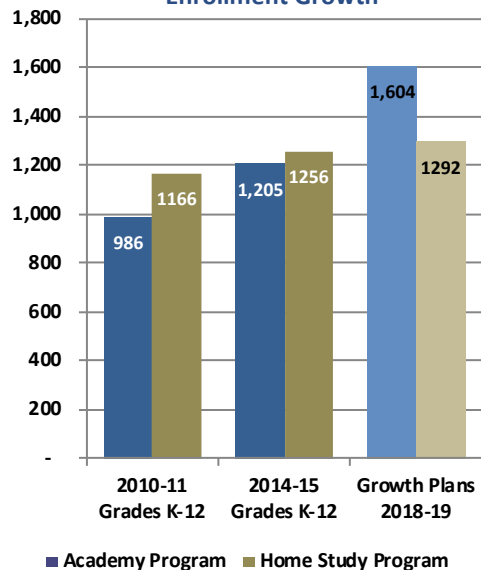
Financing Results:

- Bond Rating of “BB-” by S&P
- 30-year fixed rate financing
- Secured a True Interest Cost of 5.70%

Financing Purpose

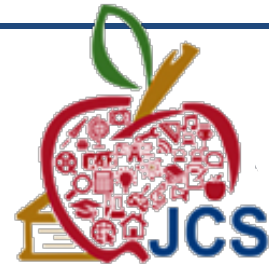


Enrollment Growth



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Julian Charter School – March 2015



- ↪ *Why did you select Bonds as your method of finance?*
- ↪ *What types of internal resources were necessary to dedicate to the financing.*
- ↪ *What challenges had to be overcome to complete the financing?*
- ↪ *What kinds of ongoing responsibilities are there?*
- ↪ *How satisfied are you with the results?*
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Q&A



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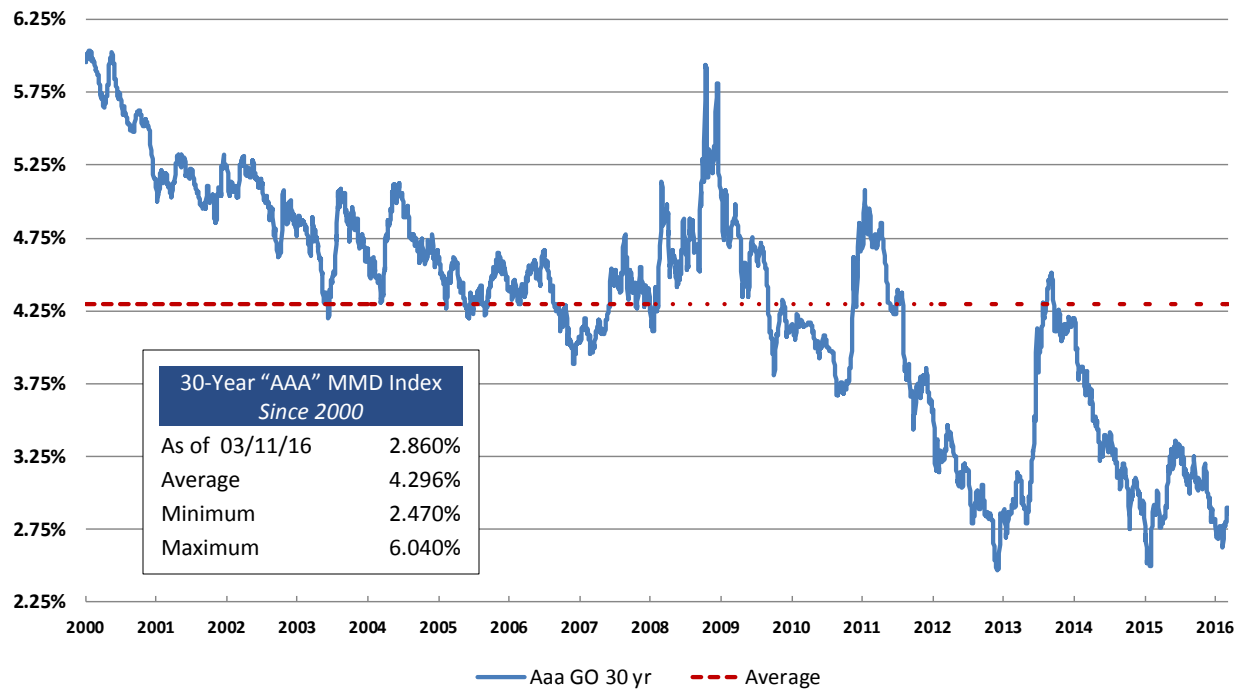
Current Charter School Bond Market Environment



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Current Charter School Bond Market Environment

- **Long-term tax exempt interest rates** are near all-time lows
- Overall, the charter school **bond sector continues to be very well performing** for both Schools/CMO's and investors
- **Larger transactions are in higher demand** relative to smaller issues
- **Investable cash (inflows to both national and high yield funds) has grown to robust levels**; this has fueled demand for a relatively limited supply of investment options
- Investors increasingly focus on **academic outcomes and generally prefer higher performing schools**



SOURCE: Thomson Municipal Market Monitor (TM3) as of March 11, 2016