

**GUIDE TO FACILITIES
AND FINANCING
STRATEGIES**

GUIDE TO FACILITIES AND FINANCING STRATEGIES

ELEMENTS OF SUCCESS FOR RECIPIENTS OF AND APPLICANTS TO IDOE'S KEYS TO QUALITY: CHARTER SCHOOL FACILITIES INCENTIVE GRANT

SUPPORT FOR THIS PROJECT

Support for this Guide to Facilities and Financing Strategies comes from a grant from the United States Department of Education's State Charter School Facilities Incentive Grant Program, to support the Indiana Department of Education's implementation of its Keys to Quality: Charter School Facilities Incentive Grant. More information about this federal grant program can be found at www2.ed.gov/programs/statecharter/.

KEYS TO QUALITY: CHARTER SCHOOL FACILITIES INCENTIVE GRANT

The Indiana Department of Education's Keys to Quality: Charter School Facilities Incentive Grant provides per-pupil facilities aid to Indiana charter schools. The objectives of Indiana's Keys to Quality grant are: (a) to improve consistency of high quality authorizing statewide to reduce the number of poor quality charter schools, (b) increase the number of high quality charter schools statewide via incubation, replication, expansion, or improvement, (c) provide support specific to building the capacity necessary for the Indiana charter school sector to access a variety of facilities funding, and (d) evaluate the impact of increased access to charter school facility funding on Indiana student outcomes. More information about the state program can be found at www.doe.in.gov/grants/csp-keys-quality.

PRIMARY AUTHOR

Oscar Gutierrez
Principal
Bondry Consultants

CONTRIBUTING AUTHORS

Brandon Phillips
Charter School Grant Specialist
Indiana Department of Education



WELCOME ABOUT THIS GUIDE

Hello, and thank you for taking time to review the information and materials provided in this Guide to Facilities and Financing Strategies. I know that as charter school leaders, there are constant and pressing challenges on your time. My hope in this Guide is to provide an accessible introduction to some of the main themes, issues, and strategies that arise in school facilities financing, especially with regard to the unique challenges and needs of charter schools.

Facilities play an immense role in both the financial and academic success of a charter school. Not only do facility costs likely constitute one of your largest expenditures after salaries and benefits, but the facilities themselves are the backdrop and stage to all of the daily activities of your students, teachers, and administrators. The right facilities can enhance and reinforce the behaviors, attitudes, and values that you seek to encourage and build in your students. The right facilities financing can free up valuable resources to reinvest in teachers, programming, and opportunities to further benefit students' growth and development.

As you read this Guide, I hope that you identify new strategies with which to approach your facility needs that then spark follow-up ideas and conversations with your fellow charter leaders, administrators, and board members. This Guide is not meant to be a comprehensive answer to all questions that may arise, nor is it meant to recommend or provide advice as to any specific strategy. All schools' situations are unique, with unique financial needs. Before employing any of the strategies described in this Guide, I encourage you to seek out the advice of a trusted legal, financial, or municipal advisor.

Thank you for your time reviewing this Guide, for your leadership, and for the support you provide for Indiana's young people.



Oscar Gutierrez
Principal, Bondry Management Consultants

AN OVERVIEW OF THE FACILITIES PLANNING PROCESS

For all organizations, facilities planning, and capital planning broadly, is an essential and recurring component of effective management and organizational leadership. It is vital to the financial success of the organization, and consequently, to achieving the organization's underlying mission and goals. Though this planning can at times be stressful or even seem overwhelming, by taking a structured and methodical approach to the process, it can become a routine element of a school's annual planning, budgeting and financial review processes.

All facilities planning begins with a needs assessment, where a school's priority and essential expenditures are identified. The process moves on to an examination of the current facilities structure, followed by an analysis of the current financing structure. Once the school's capital needs, existing facilities, and present financing structure are well understood, leadership can move on to consideration of new and alternative financing options, weighing alternatives and identifying the best options for the school's unique financial circumstances. This stage will include consideration of how the school's underlying mission, academic needs, developmental stage, and long-term goals affect its shortand long-term facilities priorities.



Evaluating the school's capital needs involves identifying capital assets and expenses and performing a needs assessment that results in a capital plan. It begins by answering the question "What are my capital needs versus my capital wants?"

What are my capital needs versus my capital wants?

KEY TERMS:

Capital Assets – buildings, property, or equipment used by the school that have a defined useful life, typically a period of years.

Capital Expenses – any expense that supports capital assets or a capital plan. They often correspond to liabilities on the balance sheet that were created to finance the asset.

Needs Assessment – an examination of a school's current capital situation and circumstances.

Capital Plan – five-year, forward-looking plan for funding needed capital expenses.

An essential component of forming a capital plan is separating capital needs from capital wants. Capital needs are essential expenditures, like the repair of an HVAC system or the purchase of a new school bus to support increased enrollment, without which the school will not be able to operate. Capital wants are purchases that, as the name suggests, are desired but not essential, such as new playground equipment or renovations for a college readiness center. They may greatly enhance the school, but if funds wind up not being available and they are unable to be purchased, the school will still be able to operate.

GUIDE TO FACILITIES AND FINANCING STRATEGIES

Identifying the school's capital needs is the first step in the capital planning process. Funding must be identified for all of the capital needs in the capital plan – each need must be paired with a specific year and specific funding source that will be used to pay for it. The funding source may consist of cash or of financing. If financing is to be used, the plan must include when the loan will be taken out as well as the timing and source of funds for payments on the loan.

Best practice is for your school's board and leadership to review this capital plan annually as part of the regular budget process of your school. Building a routine around capital planning, with engaged leaders and an engaged board, will make a substantial difference in the school's financial health and prevent unexpected capital emergencies that could otherwise wreak havoc on the school's budget and undermine student success.



Along with identifying your school's capital needs and developing a capital plan, the facilities planning process will involve identifying all of your school's current facilities, and the arrangements under which you currently own, occupy, utilize, and pay for them.

This stage of the process involves identifying, for each of your facilities, whether you currently lease, own, co-locate, rent, or otherwise possess interest in the facilities assets you have identified and collecting and organizing all relevant associated documents. These include all financing agreements, payment schedules and histories, loan balances, lease and rental agreements, service agreements, etc.

Collecting thorough and complete documentation at this stage will make the next step of analyzing the school's current financing structure go much more smoothly and efficiently.

In addition to gathering the nuts and bolts of your current facility situation, this is also the stage at which to consider how well your current facility structure meets the school's needs and plans, both with respect to short-term and longterm goals. The question you are answering is "How well do current facilities support the school's needs in the short- and long-term?"

How well do current facilities support the school's needs in the short and long-term?

There are of course basic compliance aspects to facility requirements, but the impact of facilities runs much deeper into the everyday experiences of your school's students, teachers, and administrators. Questions to ask include how well the current types of facilities serve your academic model, how well the current facility locations support your target community, how well the current facilities meet your size and growth plans, and what options and opportunities the facilities provide for any future changes or developments to each of these parameters.

REVIEWING CURRENT FINANCING STRUCTURE

With the documentation compiled in the last step, your school is now ready to review its current financing structure. This entails a deep dive into the current terms of all facilities agreements, from the debt structure of any loans, to purchase options under any lease, to the length and terms of any rental agreements.

There are three basic types of financing structures: renting, leasing, and purchasing. Each has advantages and disadvantages, and identifying the extent and impact of those positives and negatives in your current structure requires looking at particular components of each arrangement.

For renting, key parameters include rental price, CAM (common area maintenance) and utilities included in the rental price, and the agreement term. For leasing, key parameters include lease term, costs for necessary improvements, and end-of-lease purchase options. For ownership, key parameters include loan term, amortization, interest, and debt service coverage.

KEY TERMS:

CAM – Common area maintenance, often grouped with utilities, involves costs associated to your facility that the landlord assumes as part of your rental price.

Purchase Option – the ability to buy a facility that you are leasing, often with priority over other purchasers or at a pre-negotiated price.

Term – the length of time that the agreement covers.

Amortization – the number of years over which debt payments are divided.

Interest – the annual percentage charged on outstanding debt in order to borrow the funds; can be fixed or variable, and is also applied to the amortization.

Debt Service Coverage – how many extra dollars you can afford to spend; the actual cash dollars you have available for facility payments (not your net income after expenses).

The key question to ask as you review the current financing structure and begin to transition to considering your financing options is, “How much can I afford?”

How much can I afford?

The basic rule of thumb is 10-15% of total revenues, though each school’s financial situation is different and the right answer to this question for an individual school will depend upon a thorough analysis of the school’s cash flow. Examining multiple budget scenarios and stress-testing your assumptions is vital to obtaining a realistic, safe, and sustainable measure of your facilities budget.

A brief note on fundraising: While capital campaigns may make up a component of your financing plans, it is important to approach fundraising as a source of facilities funding cautiously. Relying on a single donor is inadvisable, as death, illness, or even a simple change of plans can turn a positive scenario into a crisis. It may be more advisable to target lessessential purchases with fundraising dollars, so that in the event of a change, the school is able to continue essential operations uninterrupted.



CONSIDERING FINANCING OPTIONS

As previously mentioned, the three basic types of financing are renting, leasing, and purchasing. Each comes with general advantages and disadvantages, and the ways in which these interact with the unique circumstances of a school govern which type will work best for that school.

Renting is generally appropriate for short-term, temporary arrangements. Rate fluctuations from market forces and the short-term nature of rental agreements generally make such arrangements unsustainable for most schools in the longterm. However, CAM and maintenance inclusions do help simplify the budgeting process.

Leasing or lease-to-purchase arrangements are generally longer-term arrangements than rentals, and so benefit from the added security of fixed facility costs over that time period. The downside is that your monthly payments don't support investment in the building or your balance sheet, and any lease-hold improvements you make are for the benefit of the owner, not the school.

Purchasing is a longer-term commitment but is a direct investment in the building and in your balance sheet, and costs can sometimes be spread over longer periods of time with longer amortizations

Facilities pose particular challenges for charter schools because charter schools generally can't access property tax revenues to fund capital expenditures as traditional public schools can. While some states provide a facilities subsidy to partially compensate for this difference, such as Indiana's \$750 per pupil grant, this covers only a fraction of the cost.

Charter schools must consequently turn to other forms and source of financing. The development stage and performance of a school at the time of a financing determine which specific financing options are available to it. The question a school first answers is "What is my purpose for financing?"

What is my purpose for financing?

Different options are available for new schools (0-4 years of operation), established schools (over 4 years of operation), and replications and expansions (0-4 years of operation). Within established schools, different options are available based on whether the school has positive or negative enrollment trends. For replications and expansions, different options are available based on whether the new or expanded school has the support of a CMO or network or whether it is to be a standalone school without network support.

For a new school, the available options for facilities financing are as follows:

- Rent temporary space
- Lease to purchase
- CDFI loan
- EB-5 visa loan
- Traditional bank financing

GUIDE TO FACILITIES AND FINANCING STRATEGIES

We have addressed general advantages and disadvantages of renting and leasing already. An important additional factor to consider with renting is that due to the short-term nature of a rental agreement, when the school moves, depending on the distance and change in facilities, it may affect the families whose students attend the school and could have detrimental effects on enrollment. An additional note about lease to purchase arrangements is that the buyout at the end of the lease term is often the market value of the facility plus a premium for the seller. Consequently, none of the payments being made contribute to the school's ultimate ownership of the facility, and so these arrangements are generally only appropriate for short-term facilities solutions.

CDFI (Community Development Financial Institution) loans offer more reasonable terms than many commercial, forprofit companies, typically having 3-5 year terms with amortization of 10-15 years. The loan-to-value ratio for these is typically in the range of 80-90%, meaning the school must cover 10-20% of the facility's value in order to obtain the loan for the remaining amount. Examples of common CDFIs include IFF (Illinois Facilities Fund) and CSDC (Charter School Development Corporation). A challenge of these loans is their relatively limited availability, and their main disadvantage is the relatively short amortizations (10-15 years compared to a typical 25-30 years), resulting in higher payments that can take funds away from the classroom.

The EB-5 visa loan is a unique financing option that involves a foreign investor who is making the investment in order to obtain a visa to live and work in the U.S. There are investment thresholds for these loans as well as restrictions to certain geographic areas. These loans are typically close to market rates but with slightly better terms since the investor is getting the added benefit of the visa.

Traditional bank financings offer longer amortizations (on the range of 25-30 years), and consequently lower monthly payments, but the challenge for charter schools is meeting the loan-to-value requirements. Typically, these loans require an LTV of 60-70%, meaning that the charter school has to be able to cover 30-40% of the facilities cost up front.

Additionally, disparities between appraisal values and facility project costs can exacerbate this LTV problem. First, appraisers typically make conservative value estimates of school facilities due to the unique nature of the buildings and difficulty repurposing for non-school use. Second, rising market values in cities and distressed areas where charter schools are likely to be located result in valuations that are quickly out of date. The result is facility project costs much higher than the appraisal costs on which the bank's 60-70% loan is made – and the charter school is stuck making up the difference.

For an established school with positive enrollment trends, the available options for facilities financing are as follows:

- All options for new schools
- Tax-exempt bonds
- National philanthropic funds

GUIDE TO FACILITIES AND FINANCING STRATEGIES

Tax-exempt bonds are an excellent option for schools that can access them. Typically offering lower interest rates than traditional loans, their repayment terms also allow the facilities cost to be spread over much longer periods of time, often 20-40 years. Because of the long-term nature of these loans, and the comparatively short-term nature of schools' charters (at most 7 years), investors in these bonds seek assurances of ongoing strong academic performance and healthy enrollment. We will discuss the process of obtaining these bonds in greater detail shortly.

National philanthropic funds offer an avenue for obtaining collateral to meet LTV requirements under other options or to enhance credit to receive more preferable loan terms under other options, as we will discuss further below.

For an established school with negative enrollment trends, the available options for facilities financing are as follows:

- All options for new schools
- Tax-exempt private placement bonds

The first thing to note if an established school is seeking financing in the presence of negative enrollment trends is that they are not (or should not be) seeking such financing for the purposes of expansion, but rather to get better terms for current operations.

Tax-exempt private placement bonds function similarly to the tax-exempt bonds described above, but utilize social impact funds from investors willing to take a lower return or greater risk in order to serve social causes.

For replication or expansion supported by a CMO or network, the options are the same as for an established school with positive enrollment trends.

For replication or expansion as a stand-alone school without CMO or network support, the options are the same as for a new school.

Another possibility for getting better loan terms among these various options are credit enhancement agreements. In the simplest terms, these agreements act like a local taxing unit, such as a municipality, school district, or state, cosigning a loan with the charter school. The charter school is responsible for paying the loan back, but if it fails, the cosigning taxing unit is responsible for making the payments. This additional security gives the school access to credit essentially on the same terms as a traditional school that has the power to raise funds itself through taxes. As noted above, an agreement with a CMO or national philanthropic foundation can also serve this co-signing function.

The result is a substantially lower interest rate for the charter school's loan, and consequent savings in their budget that can be redirected to the classroom. The key to obtaining these arrangements is strong relationships or a favorable political climate. Some states have a moral obligation pledge that provides direct access to city and state credit ratings, though at this time Indiana is not among them.

A JOURNEY THROUGH THE LIFE OF A MUNICIPAL BOND OFFERING

Because of the significant value charter schools can often obtain by financing through taxexempt bonds and because we have found the process around them to be less well-known than many other financing options, we expand on the process briefly below:

Step 1: School decides to investigate issuing bonds.

Step 2: School decides whether to hire a municipal advisor.

A municipal advisor guides the school through the bond offering. Because the municipal advisor owes a fiduciary duty to the school, the advisor seeks and is legally obligated to obtain the best terms possible for the school. By having this representation from an experienced advisor throughout all of the complex transactions and negotiations for the bond offering, a school can often achieve significantly better terms than when representing itself.

Step 3: School selects an underwriter.

The underwriter must deal fairly with the school and with investors and offer a fair price.

Step 4: Underwriter provides the offering's Official Statement (describing its terms) to EMMA.

EMMA is the Municipal Securities Rulemaking Board's (MSRB) online portal where investors can find information about the bonds and the school.

Step 5: The underwriter sells the bonds to investors.

Step 6: The school receives and uses the bond proceeds.

Step 7: The school provides continuing disclosures to EMMA to keep investors informed.

The school may hire a Dissemination Agent to help support them in their continuing obligations, posting their disclosures on EMMA for them and helping ensure they remain in compliance with the intricate requirements of the bond offering.

Step 8: Investors use EMMA to understand the bonds and trade them.

Step 9: The school makes payments on the bonds through the maturity date of the bonds.

Step 10: The school owns its facilities outright and can reinvest in new facilities or improvements or redirect funds to the classroom!

GUIDE TO FACILITIES AND FINANCING STRATEGIES

We have addressed general advantages and disadvantages of renting and leasing already. An important additional factor to consider with renting is that due to the short-term nature of a rental agreement, when the school moves, depending on the distance and change in facilities, it may affect the families whose students attend the school and could have detrimental effects on enrollment. An additional note about lease to purchase arrangements is that the buyout at the end of the lease term is often the market value of the facility plus a premium for the seller. Consequently, none of the payments being made contribute to the school's ultimate ownership of the facility, and so these arrangements are generally only appropriate for short-term facilities solutions.

CDFI (Community Development Financial Institution) loans offer more reasonable terms than many commercial, forprofit companies, typically having 3-5 year terms with amortization of 10-15 years. The loan-to-value ratio for these is typically in the range of 80-90%, meaning the school must cover 10-20% of the facility's value in order to obtain the loan for the remaining amount. Examples of common CDFIs include IFF (Illinois Facilities Fund) and CSDC (Charter School Development Corporation). A challenge of these loans is their relatively limited availability, and their main disadvantage is the relatively short amortizations (10-15 years compared to a typical 25-30 years), resulting in higher payments that can take funds away from the classroom.

The EB-5 visa loan is a unique financing option that involves a foreign investor who is making the investment in order to obtain a visa to live and work in the U.S. There are investment thresholds for these loans as well as restrictions to certain geographic areas. These loans are typically close to market rates but with slightly better terms since the investor is getting the added benefit of the visa.

Traditional bank financings offer longer amortizations (on the range of 25-30 years), and consequently lower monthly payments, but the challenge for charter schools is meeting the loan-to-value requirements. Typically, these loans require an LTV of 60-70%, meaning that the charter school has to be able to cover 30-40% of the facilities cost up front.

Additionally, disparities between appraisal values and facility project costs can exacerbate this LTV problem. First, appraisers typically make conservative value estimates of school facilities due to the unique nature of the buildings and difficulty repurposing for non-school use. Second, rising market values in cities and distressed areas where charter schools are likely to be located result in valuations that are quickly out of date. The result is facility project costs much higher than the appraisal costs on which the bank's 60-70% loan is made – and the charter school is stuck making up the difference.

For an established school with positive enrollment trends, the available options for facilities financing are as follows:

- All options for new schools
- Tax-exempt bonds
- National philanthropic funds

GUIDE TO FACILITIES AND FINANCING STRATEGIES

PUTTING THE PIECES TOGETHER

Capital planning and facilities financing are complex processes that require careful analysis of a school's academic model, financial circumstances, short- and long-term size and growth plans, target community, and much more. Both internal and external factors can influence the assumptions and decisionmaking at each step of the process. It is important to account for all of these factors and a full range of possible scenarios, positive and negative, when creating these plans for your school. Facilities and other capital needs are mission-critical elements of your school's operations that require the utmost care and attention from your school board and leadership.

At each stage of the process outlined by this Guide, you are likely to find that help from experienced professionals to define the scope of the inquiry, conduct the analysis, and/or review any resulting recommendations may be a significant benefit to your team or even an absolute necessity. Schools' experiences at different points in this process will vary based on their unique circumstances and the past experiences and knowledge of their internal teams. It is generally a good idea to consult outside experts at minimum to review each stage of your planning, as even experienced internal teams may not be aware of new trends or changes to particular financing options. Keep in mind that though the expenses of outside research, consultants, or advisors may seem large, even a very small change to the terms of a facility financing enabled by such advisors can bring significant savings in the short-term and extremely large savings in the longterm that not only pay for such services but allow substantially more funds to be invested directly in the classroom rather than in background facilities.

Hopefully this Guide has given you a number of ideas to spark follow-up conversations with your fellow charter school leaders, administrators, and board members around facilities financing and strategies. The next page lists several additional resources that you may find helpful as you explore these topics and their application to your school's unique situation further. Please do not hesitate to reach out with any questions that may arise as well. Communication can be directed to inquiries@bondryconsulting.com.

ADDITIONAL RESOURCES



MSRB Education Center

www.msrb.org/EducationCenter

Information on municipal securities markets, from issuance to continuing disclosure.



National Charter School Resource Center

charterschoolcenter.ed.gov/

Comprehensive repository of research and toolkits for supporting and organizing charter school



Charter School Facility Center

<https://facilitycenter.publiccharters.org/>

A project of the National Alliance for Public Charter Schools that researches how charter

Legal Disclaimer: Bondry Management Consultants (Bondry) and the Indiana Department of Education (IDOE) are not herein engaged in rendering legal, accounting, financial or other advisory services, nor does Bondry or IDOE intend that the material included herein be relied upon to the exclusion of outside counsel or a municipal advisor. This publication is intended to provide accurate and authoritative general information and does not constitute advising on any municipal security or municipal financial product. Those seeking to conduct complex financial transactions using the best practices mentioned in this publication are encouraged to seek the advice of a skilled legal, financial and/or registered municipal advisor. Questions concerning this publication should be directed to inquiries@bondryconsulting.com.

ABOUT THE AUTHORS

Bondry Management Consultants provides municipal advising and financial and management consulting to schools, community organizations, and state and local government agencies. With a particular emphasis on meeting the unique needs of charter schools, Bondry provides guidance and support across a full spectrum of financial issues including strategic management, pro forma analysis, policy preparation, capital planning, and continuing disclosure. A Hoosier business certified as both a Minority Business Enterprise and Veteran Business Enterprise, Bondry is committed to making Indiana a place where everyone has the opportunity to succeed. Oscar Gutierrez, Principal

BONDRY CONSULTANTS

600 E. Carmel Dr., Suite 263

Carmel, Indiana 46032

www.bondryconsulting.com

inquiries@bondryconsulting.com

The Indiana Department of Education (IDOE) oversees primary and secondary education in the State of Indiana. IDOE is dedicated to providing the highest quality of innovative support to Indiana's schools, teachers, students, and parents. IDOE is proactively working with educators, policy makers, business leaders, and community-based organizations to achieve its mission of «Working Together for Student Success.»

INDIANA DEPARTMENT OF EDUCATION

Dr. Jennifer McCormick, Superintendent of Public Instruction

115 W. Washington St., Suite 600S

Indianapolis, Indiana 46204

www.doe.in.gov

webmaster@doe.in.gov

BONDRY

CONSULTING

600 E. Carmel Dr., Suite 263
Carmel, Indiana 46032
www.bondryconsulting.com
inquiries@bondryconsulting.com