CALIFORNIA SCHOOL FINANCE AUTHORITY

Meeting of the Board

Wednesday, February 11, 2015
11:00 a.m.

915 Capitol Mall, Room 587
Sacramento, California 95814

Deputy State Treasurer Grant Boyken, serving as Chair, called the meeting to order.

Roll Call

Members Present: Grant Boyken, designee for John Chiang, State Treasurer
Eraina Ortega, designee for Michael Cohen, Director of Finance
Nick Schweizer, designee for Tom Torlakson, Superintendent of Public Instruction

Staff Present: Katrina Johantgen, Executive Director
Laura Martinez, Manager
David Weinberg, Program Analyst (via phone line)
Anne Osborne, Program Analyst
Jodie Jones, Program Analyst
Ian Davis, Program Analyst
Nicolaus Seppi, Office Technician

The Chair declared a quorum present.

Approval of Minutes

The minutes from the January 14, 2015 Authority board meeting were presented to the board for approval. The minutes were approved unanimously by roll call.

Executive Director's Report

Charter School Facility Grant Program:
Ms. Johantgen informed the Board that the Authority has disbursed approximately 90 percent of the advances apportionments for the 14-15 funding round. The Authority is working through the related party issues and matters, which preclude the Authority from reaching 100 percent. Under the Authority's administration of the Program, the following disbursements have been made: 1) $4.3 million was disbursed for 2011-12; 2) $36 million was disbursed for 2012-13; 3) $64 million was disbursed for 2013-14; and 4) $28.7 million was disbursed for the 2014-15 funding round. The Authority anticipated bringing program regulations to the Board at today's meeting, but is holding that item over to the March meeting of the board.

Charter School Revolving Loan Fund Program:
Ms. Johantgen informed the Board that the Authority finalized the transfer request asking to transfer funds from the Security Fund to the Revolving Loan Fund. The request is currently being reviewed by Administration and will be submitted to the Director of Finance. The Authority expects $9 million in available funds and has requested a $2 million transfer from the Security fund which, if approved, would make for approximately $11 million available to award this funding round. The Authority will be sending a reminder notice out next week to remind charter schools of the upcoming February 24, 2015 application deadline for this funding round. The Authority continues to collect on delinquent loans.

Conduit Bond Program:
Ms. Johantgen said that the Authority is bringing the Board a revised fee schedule. There is also a transaction being heard today for Alliance for College-Ready Public Schools Facilities Corporation.

Charter School Facilities Program:
Ms. Johantgen said that the Authority is working with schools seeking preliminary apportionments as well as conversion charters on their final apportionments.

State Charter School Facilities Incentive Grants Program:
Ms. Johantgen reported that the Authority continues to make monthly disbursements under the program. The Authority is making internal preparations needed to commence the eleventh funding round. The Authority anticipates having a larger funding round than the $11 million awarded due to the repurpose of the supplement/supplant funds.

Charter School Facilities Credit Enhancement Grant Program:
The Board was informed that a final award of $132,000 was granted to Rocketship Education at the December board meeting.

Legislative and Administrative Updates:
The Authority has submitted two budget change proposals (BCP) to the Department of Finance. The Authority is tracking a proposal to expand SB 740 by increasing funding and eligibility.

Item 4: Resolution No. 15-04 – Authorizing the Issuance of Bonds in an Amount Not to Exceed $80,000,000 to Finance and Refinance the Acquisition, Construction, Expansion, Remodeling, Renovation, Improvement, Furnishing, and Equipping of Educational Facilities

Ms. Johantgen presented the financing team: Eugene Clark-Herrera from Orrick serving as Bond Counsel; Mike Krutz, Director of Finance for Alliance College-Ready Public Schools; and Bill Wildman from Piper Jaffray & Co. as Underwriter. Ms. Johantgen clarified that because some components are no longer included in this transaction, the costs have been lowered to $60 million.

This bond deal will refinance existing Alliance debt, and provide new money to finance the construction and renovation of facilities. This financing will combine six Alliance schools into a single entity using an Obligated Group Financing (OGF) structure. Standard and Poor's (S&P) rated the transaction BBB-.

The Chairperson called for public comment. Estelle Lemieux of the California Teachers Association (CTA), and David Welker from the National Education Association (NEA) stated their concerns with the financing and its structure. They raised a general concern that more oversight and accountability is required for these Bonds and other programs administered by the Authority.

David Welker suggested that the Authority is not taking into account the implications of Obligated Group Transactions (OCT), which CTA and NEA believe results in private interests using public funds to acquire private property for their own uses and not for the benefit of the community. Mr. Welker believes that this possibility and what he characterized as the rapid escalation in the size and complexity of transactions necessitates further due diligence on the part of the Authority as over $400 million has already been financed through bond transactions. To illustrate his concern, Mr. Welker referred to the recent Rocketship bond discussion that lasted less than five minutes, during which there were no public comments and the Board members asked no questions. In contrast he cited the KIPP LA bond consideration which included an at-length discussion of the financial structure.

The CTA and NEA are specifically concerned with the Alliance transaction because:

- The current plan will lead to a “Legal Fiction Entity”, which combines nine, later corrected to six, Alliance LLC’s into a legally separate entity that will collect lease payments from these schools.
- The growth plan indicates that there will be central control 40 schools with 21,000 students within 5 years and would cap debt at $1100 per student.
- The charter management organization (CMO), its facilities corporations and its LLC’s claim exemptions from the California Public Records Act (PRA) and local control accountability plan requirements.
- Evidence suggests that Alliance officers are signing leases on behalf of charter school boards.
- It is unable to determine whether the individual schools will be paying less in lease payments to the LLC’s, as no accounting is provided.
- The schools are collectively obligated for cumulative payment of the total group amount. CTA and NEA suggest that as a result a new, cash reserve poor school could pay less, at the direction of Alliance, while an established, cash surplus rich school could be directed to pay more; CTA and NEA believe this payment practice could negatively impact spending decisions at individual schools and negatively impact students at those schools.
- An Alliance school board member, who was also an Alliance employee, ran action items at each of the affected schools; CTA and NEA intends to determine what exactly was voted on and believes CSFA should determine whether Board members fully comprehend the obligated group structure documents they were asked to sign.
- The individual campuses maintain their own Board of Directors made up of nine members, five of whom are Alliance board members. CTA and NEA the majority membership of Alliance Board members on each school’s board allows management to have direct control over each school.
- CTA and NEA intend to delve into the question of intercompany lending and smoothing at Alliance Schools; so that students at individual schools are not being shortchanged in any way where moneys intended for the operation of a school are directed by Alliance for any other purpose.
- S&P reports that four schools transactions are rolled into the OGT because Alliance has balloon payments of $40.6 million in 2019.

- Group structures within the bond program raised the same conflict of interests questions examined at length in the Charter School Facility Grant Program. Strong, clear conflict of interest provisions are needed in all CSFA programs.
- CTA and NEA believe the increasing size of bond applications for increasingly complex structures run counter to the intent of local control trends in California. The minimal transparency offered by the PRA is not sufficient to bring public accountability over the Charter Management Organizations or their LLCs. The Authority must act to carry out proper accountability functions.

Mr. Welker asked that the Board table the item until the next board meeting so additional research could be conducted. He stated that the CTA and NEA intent to interact with the Authority more and plan to submit additional PRA requests to the Authority and to the individual charter schools involved.

The Chairperson acknowledges the breadth of the concerns raised, and expressed a desire to come up with a plan to move forward, while being responsive to the concerns presented to the Board. He confirmed that the Authority has been responsive to many PRA requests in the past and proposed continuing the meeting for one week as a matter of professional courtesy. He noted that for CSFA to delay financing that is ready to go is rare and unprecedented, and will be an exception, and not the rule.

Board member Schweizer agreed with a delay, saying he looks forward to hearing answers to the serious implications and questions put forward and wants to make sure they are looking out for the interests of the children at the schools.

Board member Ortega also agreed with a delay as well to investigate the claim of using state funds to buy private property. She asked if there were protections to prevent these actions, and asked if charter school organizations could go elsewhere to obtain financing.

A response was provided and clarified that under the state G.O. bond funded Charter School Facilities Program, the facilities are held in trust for the state public education system, but not under these structures. The finance team replied that there are no built in protections, but that these structures are used to finance nonprofit hospitals and healthcare facilities.

Moira Topp of the California Charter Schools Association (CCSA) came before the Board and said that they wanted to be a partner and help over the next week to provide whatever assistance and information they could with all interested parties.

Mike Krutz from Alliance said that the purposes of their schools are to serve underprivileged students and find affordable facilities where they can support these children.

The motion was made to continue the meeting on February 18th at 3:00 p.m. at 915 Capitol Mall, Room 587, Sacramento, California. The Chair called for public comment, and none was taken. The motion to continue the meeting was subsequently approved unanimously by roll call.

Item 8: Resolution No. 15-06 – Approving the Conduit Financing Fee Schedule

Ms. Johantgen said the Authority is proposing a revision to the conduit financing fee schedule in response to the growing number of transactions that are being brought forward.

The fee structure would only adjust the issuance fee. The Authority proposes fifteen basis points up to $10 million then five basis points on finance deals above $10 million. The Chair called for public comment, and none was taken. Resolution 15-06 was subsequently approved unanimously by roll call.

Reconvenement

The meeting reconvened on Wednesday, February 18, 2015 at 3:00 p.m. at 915 Capitol Mall, Room 587, Sacramento, California.

Deputy State Treasurer Grant Boyken, serving as Chair, called the meeting to order.

Roll Call

Members Present:	Grant Boyken, designee for John Chiang, State Treasurer Eraina Ortega, designee for Michael Cohen, Director of Finance
Staff Present:	Katrina Johantgen, Executive Director Laura Martinez, Manager David Weinberg, Program Analyst (via phone line) Anne Osborne, Program Analyst Kristen Schunk, Program Analyst Steven Theuring, Program Analyst Jodie Jones, Program Analyst Ian Davis, Program Analyst Nicolaus Seppi, Office Technician

The Chair declared a quorum present.

Continuation of Item 4: Resolution No. 15-04 – Authorizing the Issuance of Bonds in an Amount Not to Exceed $80,000,000 to Finance and Refinance the Acquisition, Construction, Expansion, Remodeling, Renovation, Improvement, Furnishing, and Equipping of Educational Facilities

Chairperson Boyken invited the members of the financing committee to speak.

Ms. Johantgen introduced Neal Millard from Musick Peeler to discuss Obligated Group Structures, who will answer questions asked by the NEA at the last meeting with the finance team. Ms. Lemieux represented the CTA.

Ms. Johantgen asked Mr. Wildman from the finance team to address the NEA's concerns and present a summary of their response to the Board.

1. "Bonds are issued to finance property purchases, State funds are used to pay leases that pay part of their debt, publically subsidized or direct public funds result in private charter management organizations obtaining private property for their own use and not for their communities or the public at large."

Because the landlord is a charity, the funds become charitable funds and must be used for charitable purposes by law. Therefore, the money stays within the charity, with SB 740, where the money goes to a private landlord. Mr. Paxson clarified that a related party provision was added to SB 740 specifically to avoid conflicts of interest in these types of structures.

2. “Obligated Group Structure.”

Each Alliance school is a nonprofit. The Alliance Corporation is a sole member of various LLC’s that are the actual property owners. In an OGS, you can combine the credit rating of all the schools, which results in lower borrowing costs. The Alliance attorney took the suggestion to the Boards of the different schools. After explaining the benefits and risks of an OGS, they all voted that it was in their best interest to utilize this structure.

Before continuing, Mr. Paxson declared that Nick Schweizer, designee for Tom Torlakson, was now present; recorded at 11:13.

3. “Alliance projects to centrally administer forty schools with 21,000 students within five years and caps its debt at $1100 per student.”

Alliance consolidates services for the sake of efficiency. Currently, 11,000 students are enrolled in 26 schools on 24 campuses. A five-year projection calls for 7500 additional students, which is in line with the 1100 student growth pattern Alliance used since opening.

4. “The proposed financing will allow as many as nine Alliance schools to lock in low interest rates. We find this statement troubling too because it is the landlord LLC that are locking in low interest rates for their individual debt, not the Alliance schools.”

The lease establishes base rent, the same as debt service for bond payments. The low rates will pass to the lessee schools through the lessee LLC.

5. “What did Alliance tell the independent school board members of this collective obligation in presenting this transition?”

There are four Board Members selected by the school and five selected by the parents. All information is provided in written and verbal form and minutes are adopted regularly. This allows majority control at the school level. Each Board was told the benefits and the downsides to the individual schools. Such organizations exist with public school districts too.

6. “Currently the CMO and its facilities corporation and LLC’s claim exemption from California Public Records Act and exemption from LCCF/LCAP provisions. We have found initial evidence in our research where officers of Alliance are signing long term leases on behalf of the charter schools.”

They do not claim exemption, they are exempt under statute. Alliance has adopted policies and procedures and accounting manuals that offer detailed explanations, and the activities of the schools are described in an annual audit. However, the schools are not considered Brown Act corporations, they are private entities. Additionally, anyone signing leases for the school is an employee of the school or designated as a signee by a Board resolution.

Mr. Paxson clarified that the schools themselves are not exempt from the PRA and must therefore comply with requests.

The finance team said that by law, excess money is held for the benefit of the schools. Each lease has provision that each school agrees to file an intercept notice so money for debt services goes directly to trustee and past the LLC.

The Chair called for public comment. Ms. Lemieux from the CTA said they will discuss their items with Alliance directly and will send the findings to the Authority. They are concerned that applicants coming to the Board are CMO's requesting larger and more complex deals, and suggest the Authority needs more time to assess procedures on what is submitted.

They will pursue PRA requests and submit proposals for better public access and will give suggestions for more complete releases of Bond materials. They have concerns with how Alliance interacts and operates with the Authority and how the management pushes the Authority's boundaries. They think the Authority can play a more active role and look forward to working on PRA requests and conflicts of interest.

Colin Miller from CCSA said CMO's like Alliance are doing good things for low-income students. Mr. Miller cited a Stanford study that shows that low-income children received 100 days more of education in charters, and in California, there are over 90,000 students on waitlists to get into charter schools.

Erik Premack from CSDC said many of the issues are similar to the ones vetted in the past and does not want to see these issues be an impediment in the future. He believes they are more political in nature and would like to see these programs de-politicized.

The Chair clarified that the Treasurer believes the Treasury should be "open for business" and therefore does not want to delay programs already moving.

Board member Schweizer asked if the charter Boards are aware of the OGS and if they were informed of the risks. The financing team answered that if one school cannot make payments, other schools need to fill in. Bonds could possibly not get sold, and there is a risk that they cannot afford the taxes at the end. It can also affect their budget. They were told different options to discuss what is cost effective and what is easiest to accommodate, considering the federal debt to pay at the end of the year.

Board member Ortega clarified the motion with Mr. Paxson and made a motion to approve. It was seconded by Mr. Schwiezer. Public comment was requested, and none was received. Resolution 15-04 was passed unanimously by roll call.

There being no additional public comments or other business to conduct, the meeting was adjourned.

Respectfully submitted,

Katrina Johantgen
Executive Director