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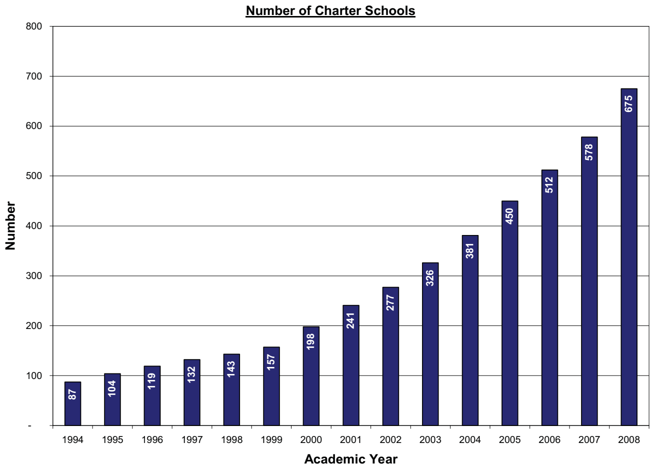
PART 1. PROJECT DESIGN

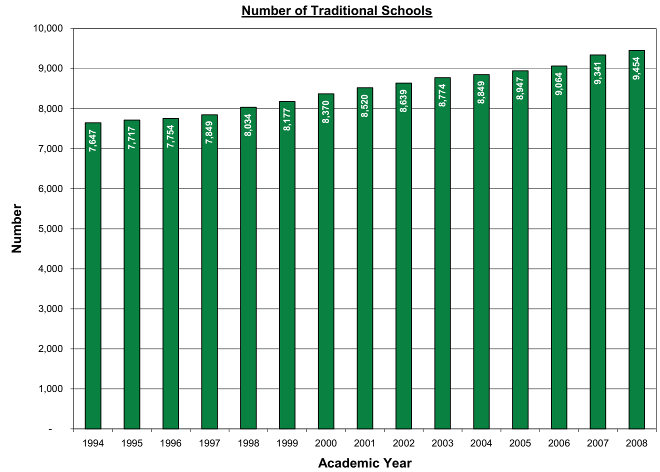
I. General Funding of Charter Schools in California[1]

California adopted its charter school legislation in 1992, becoming the second state in the nation to do so. Since California's charter school law was passed, charter schools have rapidly grown in popularity. At the close of the 2007-08 school year (FY 2008), there were 675 charter schools educating over 248,000 students in California, compared to close to 9,500 traditional schools teaching 6.0 million children. As a percentage of the total student population, charter school enrollment has increased from 0.96 percent in FY 1994 to 3.96 percent in FY 2008, which is equivalent to an annual average growth rate of 12.1 percent over the 14-year period. Enrollment at traditional schools averaged annual growth of 1.0 percent over the same period. In FY 2008, charters averaged 368 students per school relative to an average of 637 students for each per traditional school. The charts on the following page illustrate rapid growth of charter schools versus the static to declining enrollment at traditional schools. It comes as no surprise to California educators that charter schools' access to suitable facilities has been a challenge in light of such rapid expansion.

[1] With much appreciation, much of the content of this section and the next was excerpted from "California Charter School Finance in a Nutshell" http://www.cacharterschools.org/pdf_files/Charter%20Funding%20Basics.pdf as prepared by staff of the Charter Schools Development Center (CSDC). CSDC is a non-profit organization whose goal is to help public education change from a highly regulated, process-based system to one that allows and encourages schools to be more creative, performance-based centers of effective teaching and learning. CSDC aims to achieve this by providing technical assistance to the charter school reform movement in California, nationally, and internationally.



Source: California Department of Education



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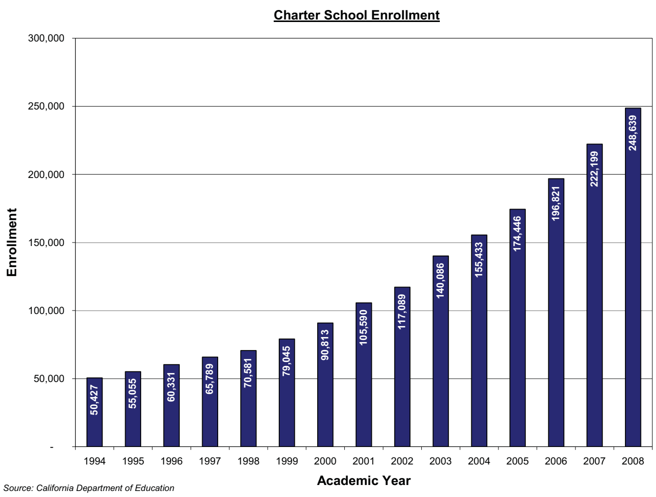

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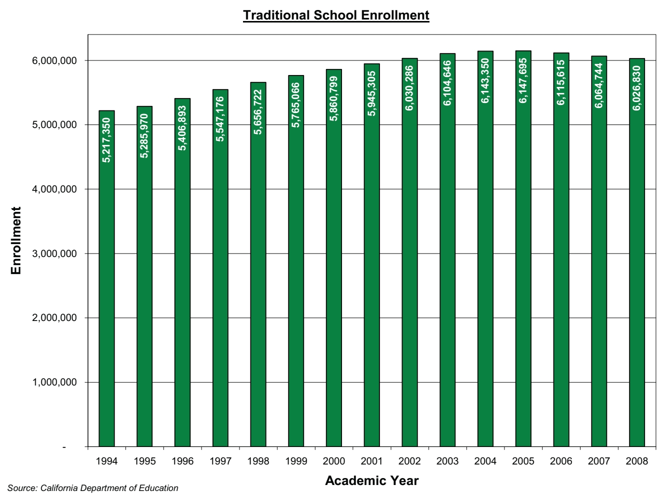

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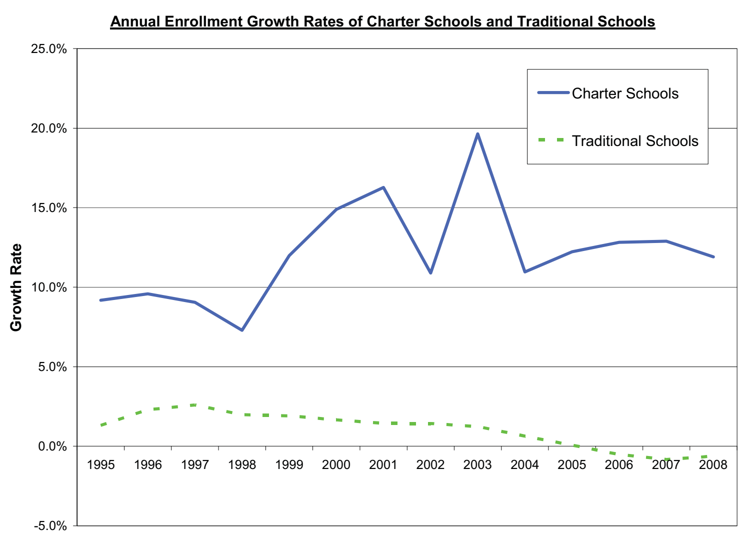

Source: California Department of Education

California has a large and complex system for funding its K-12 schools. School funding is largely state-driven and governed by provisions in California's state constitution that use detailed formulas to establish funding levels. These state laws govern both state and local property tax funding for the K-12 system as well as a growing list of special-purpose state categorical funding programs. The federal government provides a relatively small, but significant and growing, share of funding for California's schools. Federal, state and local sources are supplemented by various special sources such as state lottery dollars.

General-purpose funds are provided to school districts through the "revenue limit" system. The revenue limit is a specific entitlement of funding for each student, measured by average daily attendance (ADA) generated by the district's students. The revenue limit is funded from State and local sources such that local property taxes are subtracted from the school district's total entitlement to revenue limit funding in order to calculate the funding amount provided by the State. In California, local property taxes are capped at one percent of the property's assessed value, which is not necessarily equal to the property's market value. Categorical funding is provided to schools through a long list (over 60) of state-funded programs and over a dozen major federal programs. The larger state-funded categorical programs include funding for special education, incentives to reduce class sizes and home-to-school transportation, etc. School districts must often complete lengthy applications to qualify for categorical funding, and the laws governing the programs often dictate the use of the funds. Since such a high proportion of funds are provided through these often restrictive categorical funding programs, per student funding is dependent on the diligence of staff and thus will vary between school districts.

California's charter schools are funded much like other non-charter California public schools. They receive funding from local property taxes, state education aid programs, the California Lottery, the federal government, fundraising, and other sources. They are prohibited from charging tuition, but may charge fees for certain items to the same extent as non-charter public schools may. As public schools, charters receive state and federal general-purpose and categorical funding for operations based upon a per pupil formula. During the FY 2000 and FY 2005 budget processes, the California Legislature significantly amended the California Charter Schools Act to ensure a high degree of autonomy and flexibility in operational funding. The Legislature created a funding system that is relatively simple and easy to understand, provides similar levels of operational funding for serving similar students, cuts regulatory “red tape” from state funding programs and provides charter schools with the option to receive aid directly from the State, without the local district receiving funds first.

The following table illustrates the primary elements of California’s charter school funding system. First, charter schools receive a per-ADA General Purpose Block Grant that is based on the average level of general-purpose funding the state provides to school districts serving the various grade spans. Second, charter schools receive a per-ADA Categorical Block Grant that provides charter schools with a proportionate share of funding from over 35 different state categorical aid programs. This block grant approach greatly simplifies charter schools financial affairs and provides the schools with a deregulated “no strings attached” share of state aid. The Categorical Block Grant is supplemented with so-called "In-Lieu Economic Impact Aid." These funds are provided to charter schools that serve economically disadvantaged students (students whose family incomes fall below specified federal poverty income caps) and students who are English learners. The funding is provided in lieu of a large categorical funding program for school districts called "Economic Impact Aid." The funding provided varies each year.

Basic Charter School Funding Rates per ADA (estimated for FY 2009)

	K-3	4-6	7-8	9-12
General Purpose Block Grant	$5,351	$5,431	$5,586	$6,478
Categorical Block Grant	500	500	500	500
In-Lieu Economic Impact Aid	318	318	318	318
TOTAL	$6,169	$6,249	$6,404	$7,296

In addition to these basic funding entitlements, charter schools may (1) apply for funding from federal education aid programs, (2) receive a proportionate share of funding from the California Lottery, and (3) may also apply for funding from several special state sources, that are not included in the above-referenced block grants, which could increase revenue per ADA by an additional $500 to $2,000.

California has taken care to ensure that charter schools have a high degree of fiscal autonomy and flexibility. Charter schools may opt to apply for and receive their state and federal funding either in partnership (local/indirect funding) with their local school district or independently (direct funding). California has also designed a special advance apportionment process to ensure that new and growing charter schools receive their funding early in the school year to reduce the need for costly short-term borrowing.

II. Facility Funding of Charter Schools in California[2]

Currently, most of California's charter schools have no readily available source of funding to provide them with facilities. This has proven to be one of the largest obstacles to starting a charter school. Like traditional public schools, if charter schools want to raise capital beyond state and local operational funding levels to meet their facilities needs, they must raise the funds from philanthropic sources or borrow funds at costly rates with financial restrictive terms, if willing lenders can even be found. However, unlike their school district counterparts, charter schools are not permitted to finance facilities by seeking voter approval for the issuance of tax-exempt debt repaid from increased taxes, and must use operational funding to pay for debt service or lease payments on facilities occupied but not owned. Additionally, school districts in California can seek voter approval for non-ad valorem taxes (parcel taxes) to fund operating costs. In most cases, voter approval is not required for school districts to levy so-called “developer fees” on new residential and commercial construction to offset the cost of school facilities for new communities or to issue debt in the form of lease-backed obligations (lease revenue bonds and certificates of participation). These mechanisms are generally not available to charter schools.

Despite staggering state budget crises over the last decade, and a state constitution that severely restricts the ability of state and local agencies to levy additional taxes, the State Legislature and the voters of California have adopted/endorsed a multi-faceted approach to assist charter schools in meeting their facilities needs in the form of grant, loan and bond financing programs. Whereas

[2] Attribution to CSDC’s “Potential for Charter School Facilities Funding” http://www.cacharterschools.org/facilities.html.

California's commitment to funding charter schools is arguably one of the most comprehensive efforts in the nation, most of these programs have traditionally been oversubscribed, and charter schools continue to face significant hurdles to securing facilities. Below we have highlighted the authorizing legislation and programs providing funds for charter school facilities in the State of California.

Proposition 39 Facilities: This proposition, adopted by voters in November 2000, requires school districts to provide charter schools having a projected average daily attendance of at least 80 students with reasonably equivalent facilities to those provided to students in the area where the charter school students reside. This measure took effect on November 8, 2003, generally requiring all California school districts to provide facilities to charter schools that meet the requirements of the regulations. To qualify for Prop 39 facilities a charter school must be "operating in the school district," which is defined as either (1) currently providing education to in-district students or (2) having identified 80 students who are meaningfully interested in enrolling in the charter school for the following year. The school district may charge the charter school a pro-rata share of the district's facilities costs which are paid with unrestricted general fund revenues, based upon the ratio of space the charter school uses divided by the total space of the district.

Charter Facilities Lease Aid Program: This funding program was enacted by Senate Bill 740 (Chapter 892, Statutes of 2001, Education Code Section 47614.5) for the purpose of providing per-pupil facilities funding for charter schools in low-income areas. Eligible charter schools may receive reimbursement for facilities rent and lease costs in an amount of up to $750 per unit of ADA, but no more than 75 percent of their total annual facilities rent and lease costs. This program is targeted toward schools serving exceptionally high proportions of economically-disadvantaged students. Only schools that either serve a student population with a high proportion (70 percent or higher) of free/reduced price meal-eligible students or are physically located in the attendance area of a public elementary school in which 70 percent or more of pupil enrollment is eligible for free or reduced price lunches are eligible for funding from this lease aid program.

Charter School Revolving Loan Fund Program: This funding program was enacted by Senate Bill (SB) 1759 (Charter 586, 2000, Education Code Section 41365 through 41367) to help meet purposes established in a school's charter, such as leasing facilities, making necessary improvements to facilities, purchasing instructional materials and equipment, and program expansion. This program provides start-up loans of up to $250,000 per school. The loans must be repaid within five years, beginning with the first fiscal year after receipt of the loan. Interest on the loan is set at the earning rate of California's Pooled Money Investment Account (PMIA) on the date of loan disbursement. The PMIA rate is the rate earned on various pooled funds in the State Treasury. The rate varies, but is typically from three to five percentage points below the rate that would be available for a loan from a private lender. The loan is available to any charter school that is not a conversion of an existing public school and has not yet been renewed for a second five-year term by its chartering entity. Since this program's inception in 2001, 93 loans totaling over $20 million have been provided to charter schools.

Authority's Charter School Facilities Program (CSFP): The CSFP was enacted in 2002 by Assembly Bill (AB) 14, amended by SB 15 and AB 16, and funded through Proposition 47 ($100 million), Proposition 55 ($300 million) and Proposition 1D ($500 million) for the purposes of constructing, acquiring or renovating facilities for site-based charter school students. Under the CSFP, the State provides funding for charter school facility project costs with 50 percent of the costs awarded as a grant, and with the charter school being responsible for repaying the State for the 50 percent balance. The charter school may elect to repay the State through a funding agreement, or pay its matching share through a lump sum payment. Charter schools receiving preliminary apportionments from the CSFP have up to five years to convert their project to a final apportionment before the reservation of funding is returned to the State. Ownership of facilities funded by the CSFP is retained by the local school district for the benefit of the public education system.

The Authority and the Office of Public School Construction (OPSC) jointly administer this $900 million per-pupil facilities program. The Authority's primary role is to determine the financial soundness of the each participating charter school at the time of preliminary, advance and final apportionments. Twenty-six applications requesting $438 million were received for the Proposition 47 (first) funding round. Preliminary apportionments were awarded to six charter schools for projects totaling approximately $98 million in January 2004. In February 2005, second round funding was awarded to 28 eight schools for projects totaling approximately $286 million. In 2007, 79 applications requesting in excess of $1.51 billion were considered by the Authority and OPSC for the apportionment of $500 million in Proposition 1D monies. Third funding round awards were made in May 2008 to 24 charters schools with a combined apportionment of $463 million. The 2008 per pupil grant amounts were $8,839 for grades K-5, $9,348 for grades 6-8 and $11,893 for grades 9-12.

To ensure that a variety of project types are funded by the CSFP, applications are apportioned based on both preference points and funding category. Preference points are calculated by OPSC based on the following four categories, each with a maximum of 40 points: (1) the percentage of overcrowding for the school district where the project will be located, (2) the percentage of low-income pupils in the school district or in the existing charter school, (3) whether or not the school is a non-profit entity and (4) whether the charter school is rehabilitating facilities owned by the school district. After the preference points have been calculated for each application, the application with the highest number of points is funded in each of the categories: (a) geographical region of the State; (b) urban, rural or suburban area type; (c) size of the charter school; and (d) grade levels served by the project.

State Charter School Facilities Incentive Grants Program: In 2004, the Authority was awarded a $49.25 million federal grant under the United States Department of Education's State Charter School Facilities Incentive Grants Program (Federal Grant Program) to assist charter schools in meeting their facility needs. The Federal Grant Program is designed to fund those charter schools that demonstrate the most need. The Authority designed a 110-point preference point matrix based on the following: (1) the number of students at the school who are eligible for free and/or reduced priced meals; (2) the level of overcrowding the charter school's district is experiencing; (3) whether the charter school is operated by a non-profit entity; and (4) whether the school met its student performance target set by the State. The grant is being allocated over a five-year period, averaging annual awards of $9.85 million through FY 2009. Charter schools may use the grant funds to pay a portion of their rent, lease or debt service payments, or to fund the cost of acquiring, renovating or constructing new facilities. To date, four funding rounds have been conducted and 82 charter schools, serving 25,862 students have received awards totaling $38 million. The fifth and final funding round will be completed by June 30, 2009.

<u>Authority's CA Charter School Conduit Financing Program pursuant to AB 2717:</u> The California School Finance Authority was created in 1985 to provide tax-exempt, low-cost capital and working capital financing to school districts and community college districts for use in the repair and construction of school facilities, as well as for working capital purposes. Since its inception, the Authority has issued a series of bond financings on behalf of school districts under the Smart Bonds School Facility Financing Program. The most recent issuances were in 1999 and 2000 when the Authority issued three pooled financing notes for 14 school districts to provide bridge financing in anticipation of Proposition 1A apportionments. The Authority's act was amended to provide that charter schools are eligible for participation under the act pursuant to AB 2717 (Walters). This bill, which was effective January 1, 2007, authorized the Authority to serve as a conduit bond issuer on behalf of charter schools, as it has done on behalf of school districts and community college districts.

Charter schools participating in this form of the Smart Bonds Program, the California Charter School Conduit Financing Program (Conduit Financing Program), will be required to pledge an intercept of a portion of their per-pupil revenue from the State, but not local sources, to a third party in order to secure the school's share of debt service due on the Authority's conduit debt. The intercept mechanism may be used as either a standby in the case of non-payment by the district, or as an automatic schedule of payments. Because the debt service will be secured by intercepted funds coming directly from the State, investors, lenders and rating agencies are expected to have greater confidence in timely repayment and therefore offer higher credit ratings and more favorable financing terms. Authority staff has been in discussions with the charter school community regarding anticipated demand for the Conduit Financing Program to meet the working capital and facilities needs of charter schools. The Authority's internal legal counsel and bond counsel have prepared draft documents for the Conduit Financing Program, which include the preliminary mechanics of the intercept mechanism.

The Authority hopes to utilize the Federal Enhancement Grant to further strengthen the creditworthiness of the Conduit Financing Program with the dual objectives of providing certain charter schools access to capital at reasonable rates that would otherwise have none and of markedly lowering the cost of capital to charter schools that currently have market access. However, the Authority's application of the Federal Enhancement Grant through the Conduit Financing Program would not be limited to facility funding generated from the public issuance of bonds, as this grant and the intercept mechanism could be made available to private lenders through the structuring of a private bond purchase. While not the highest and best use of the grant because the gearing of federal funds would be diminished, the Authority plans to explore this use of the grant with charter schools that do not participate in the public bond offering, most likely due to a comparatively smaller financial need (less than $1 million).

Issuance of Tax-Exempt Bonds by Conduit Authorities: Due to their corporate structure and low amounts of discretionary operating revenues, charter schools have had difficulty raising funds to finance facilities. Charter schools have generally relied upon a small number of private lenders that understand the inherent credit issues faced by charter schools, such as comparatively smaller enrollment, charter renewal risk and the limited financial flexibility to fund unforeseen costs. While the interest rates charged by these lenders are significantly higher than the interest rates paid by traditional public schools, the capital needs of charter schools in California continues to far exceed the supply of funds made available by the State programs previously described.

Alternatively, some charter schools have had a sponsoring school district borrow funds on their behalf, while an even smaller number of charter schools have raised capital through debt instruments issued on behalf of their educational management organization or through a qualified tax-exempt borrower such as a local governmental entity or special development authority. Charter schools operated by nonprofit public benefit corporations organized as 501(c)(3) nonprofit corporations may legally borrow the proceeds of a tax-exempt financing issued by a governmental entity or special authority.

In California, conduit debt has been issued on behalf of charter schools by non-governmental, special authorities such as the California Statewide Communities Development Authority (CSCDA) and the California Municipal Finance Authority (CMFA). While these authorities provide access to essential capital funds, their up-front fees range from 0.05% - 0.20% of the par amount issued, while the ongoing fees range from 0.00% - 0.03%. For $10 million in bonds issued on behalf on a California charter school, the up-front fees would range from $5,000 - $20,000 while the annual fees would start at $3,000 and decline as principal is repaid. Another drawback to these conduit debt programs is their inability to intercept per-pupil revenue from the State for payment of debt service, which limits the credit ratings of the offering to the non-rated and marginally investment grade rating (Baa3/BBB-) categories and thus increases the funding cost demanded by investors and paid by charter schools.

Our research indicates that six conduit bond issuances for charter schools have been issued through either CSCDA or CMFA since 2001. Of these six bond issues, all were sold without credit enhancement, four were unrated, one was rated BB+ by Fitch Ratings and one was rated BBB- by Standard & Poor's. The two rated bond issues were issued through the CMFA.

III. Adequacy of Charter School Facility Funding in California

The following table provides annual estimates of the facilities needs of new charter school students for the next five fiscal years along with estimated funding sources. While the enrollment growth of charter schools has averaged 12.1% annually since FY 1994, our projections of enrollment beginning with FY 2009 assume an annual rate of 7.5%. For simplification purposes, this analysis assumes the facilities needs of the estimated 267,287 students enrolled during FY 2009 have been met and funded; the facilities needs presented would be significantly higher without this assumption. The $390.9 million cost of providing facilities for new charter school students in FY 2010 is based on the 80 sq. feet per student space demands of approximately 20,000 thousand new students at a per sq. foot cost of $195, plus land costs assumed at 25.0% of facility cost. Annual increases in the up-front cost of new facilities are a function of enrollment growth and 3.0 percent per annum increases in the cost per sq. foot such that the annual need is $587.6 million by FY 2014. The aggregate cost of new facilities over the five years is $2.421 billion.

Based on the demand analysis discussed above, we have provided an annual estimate of the unfunded cost of new charter school facilities in California for the FY 2010 through FY 2014 period in the table on the next page. From the aggregate up-front cost of new facilities we have deducted an estimated 15 percent to be provided by local districts pursuant to Proposition 39 ($363.2 million), an estimated 50 percent to be provided by third-party commercial leases ($1.21 billion) and $500 million in Proposition 1D apportionments through the Charter Schools Facilities Program from FY 2010 through FY 2013 (roughly 21 percent). Approximately 14 percent of the total up-front cost of new charter schools, or $347.4 million, is left unfunded. The Authority would like to assist the charter school community by reducing this projected funding gap through the conduit issuance of long-term bonds for participating charter schools via the California Charter School Conduit Financing Program. Based on the data contained in the table below, the first issuance in FY 2010 would fund new charter school facility costs of roughly $36.8 million. Subsequent new charter school facility costs to be funded by the Authority conduit debt would be $51.5 million (FY 2011), $17.7 million (FY 2012), $35.7 million (FY 2013), and $205.6 million (FY 2014). The FY 2014 figure is a significant increase from the prior years due to the projected exhaustion of Proposition 1D funding.

Projected Costs & Funding Sources for New Charter Schools in California ($000s)

	Project Yr 1 (CA FY 2010)	Project Yr 2 (CA FY 2011)	Project Yr 3 (CA FY 2012)	Project Yr 4 (CA FY 2013)	Project Yr 5 (CA FY 2014)	TOTALS
Demographics						
Charter School Students (1)	287,333	308,883	332,050	356,953	383,725	
Number of Charter Schools (2)	780	839	901	969	1,042	
Up-Front Cost of New Schools (3)						
Unhoused Students	20,047	21,550	23,166	24,904	26,772	
Facility Space per Student (sq. feet)	80.0	80.0	80.0	80.0	80.0	
Facility Cost per Square Foot	$195.00	$200.85	$206.88	$213.08	$219.47	
Facility Cost	$312,726	$346,266	$383,403	$424,522	$470,052	$1,936,969
Land Cost (25.0% of Facility Cost)	$78,181	$86,566	$95,851	$106,131	$117,513	$484,242
Total Up-Front Cost of New Schools	$390,907	$432,832	$479,253	$530,653	$587,566	$2,421,211
Estimated Up-Front Funding Sources						
Facilities Funded/Provided per Prop. 39 (4)	$58,636	$64,925	$71,888	$79,598	$88,135	$363,182
Facilities Funded/ Provided by Leasing (5)	195,454	216,416	239,627	265,327	293,783	1,210,605
Charter School Facility Program (6)	100,000	100,000	150,000	150,000	0	500,000
Total Estimated Up-Front Funding Sources	$354,090	$381,341	$461,515	$494,924	$381,918	$2,073,787
Net Unfunded Up-Front Cost / Funding from CA Conduit Financing Program	$36,817	$51,491	$17,739	$35,729	$205,648	$347,424

Assumptions

(1) Annual enrollment growth from FY 2009 through FY 2014 is projected at 7.5% per year. (From FY 1995 through FY 2008, the average enrollment growth rates was 12.1%.)

(2) 368 students per school based on FY 2008 average.

(3) For simplification purposes, this analysis assumes the facilities needs of the projected 248,639 students in FY 2008 have been met and funded. Facility Cost is the product of unhoused students, space per student and cost per sq. foot. Cost per sq. foot escalates by 3.0% per year.

(4) Estimated based on 15.0% share provided by school districts pursuant to Proposition 39.

(5) Estimated based on 50.0% share provided by third-party commercial leases.

(6) Projected apportionments of $500 million in Proposition 1D funds.

IV. Design of Project Utilizing Funding from the Credit Enhancement Grant

Proposed Use of Credit Enhancement Grant Funds: The California School Finance Authority (Authority) anticipates serving as a conduit bond issuer on behalf of charter schools seeking financing for capital facilities and short-term financing for working capital needs via its the California Charter School Conduit Financing Program (Conduit Financing Program). From FY 2010 through FY 2014, the Authority's staff anticipates utilizing the Conduit Financing Program and a Federal Credit Enhancement Grant of $15.0 million to generate funding for the approximate $347.4 million in new charter school facility costs and $139.0 million for permanent financing and debt refinancing purposes, for a total funding amount of $486.4 million. (For additional detail, please see the Conduit Financing Program cash flow pro forma on Pages 25 and 26.) Specifically, proceeds from these bonds would be applied towards predevelopment expenses, construction costs and permanent (take-out) financing needs. Additionally, the Authority will allow charter schools to borrow to fund leasehold improvements and to refinance existing high cost debt. While the Authority will offer charter schools the options of issuing debt on a stand-alone or pooled basis, by pooling the capital needs of numerous charter schools into one offering, the Conduit Financing Program will create economies of scale by spreading transaction costs across a larger number of borrowers, and garner the attention of more investors.

Charter schools participating in Conduit Financing Program will be required to pledge an intercept of a portion of their per-pupil revenue from the State, but not local sources, to a third party in order to secure the school's share of debt service due on the Authority's conduit debt. The intercept mechanism may be used as either a standby in the case of non-payment by the district, or as an automatic schedule of payments. Because the debt service will be secured by intercepted funds coming directly from the State, investors, lenders and rating agencies are expected to have greater confidence in timely repayment and therefore offer higher credit ratings and more favorable financing terms.

The Authority hopes to utilize a $15.0 million Federal Credit Enhancement Grant to further strengthen the creditworthiness of the Conduit Financing Program with the dual objectives of providing certain charter schools access to capital at reasonable rates that would otherwise have none and of markedly lowering the cost of capital to charter schools that currently have market access. As is shown by the five-year cash flow pro forma, the Conduit Financing Program's projected need for the Federal Credit Enhancement Grant is $30.2 million, but the Authority has requesting the FY 2009 stated maximum amount of $15 million. The Authority is prepared to reduce the amount of conduit bonds issued to reflect the actual amount of the grant awarded. We have calculated the leverage provided by the Federal Credit Enhancement Grant to be 11.5 to 1.

With the added security provided by the Federal Credit Enhancement Grant, we anticipate that the Authority's conduit bonds would be assigned minimum investment grade credit ratings and thereby significantly lower borrowing costs to participating charter schools. However, the Authority's application of the Federal Credit Enhancement Grant through the Conduit Financing Program would not be limited to facility funding generated from the public issuance of bonds, as the grant and the intercept mechanism could be made available to private lenders through the structuring of a private bond purchase. While not the highest and best use of the grant because the gearing of federal funds would be diminished, the Authority plans to explore this use of the grant with charter schools that do not participate in the public bond offering, most likely due to a comparatively smaller financial need ($1 million or less).

At this point, Authority staff estimates the issuance of conduit bonds, possibly in multiple series or tiers, by grouping charter schools with similar average ages and the following financing uses: predevelopment (15%), construction (25%), permanent (30%), leasehold improvements (20%) and refinancing (10%). In structuring the Conduit

Financing Program, CSFA staff anticipates utilizing the Federal Credit Enhancement Grant for the following two specific purposes:

Tier One Borrowers - For the series of bonds issued for the permanent financing and refinancing of facilities owned by charter schools with operating histories of at least three years (Tier One), the Federal Credit Enhancement Grant would not be necessary based on our assumption that these bonds would be assigned investment grade credit ratings based on the creditworthiness of the borrowers, and the additional security provided by the intercept mechanism and a debt service reserve fund to be funded with bond proceeds.

Tier Two Borrowers - For the series of bonds issued to finance the predevelopment and construction needs of charter schools with operating histories of at least one year and to finance the leasehold improvements of any charter school (Tier Two), the Federal Credit Enhancement Grant would be used to fund the primary debt service reserve requirement with the secondary debt service reserve requirement to be funded from bond proceeds. We have calculated that use of the grant would reduce the size of the debt offering by roughly 6.0 percent and create leverage of 11.5 times.

Our pro forma analysis (Pages 25 and 26), which incorporates conduit bond issuance from FY 2010 through FY 2014, assumes that the tax-exempt conduit bonds are priced using fixed interest rates as of February 6, 2009 based on investment grade ratings of Baa/BBB. These bonds are projected to have all-inclusive funding costs of 6.89%, with a 30-year final maturity and level annual debt service payments, to produce an average life of 19.7 years. (This funding cost is very high, reflecting the current, anomalous state of the credit markets. We hope this cost to be lower by the time of first issuance in mid-2009.) It is not possible to estimate what the funding cost to Tier Two Borrowers would be without the Federal Credit Enhancement Grant because we do believe that these charter schools with these projects would have access to the credit markets. To hazard a guess, the funding rate would need to be no less than 8.5% to clear the market, which is based on the current cost of non-rated, tax-exempt debt now being sold in California.

Preliminary Terms of the Conduit Financing Program for Charter School Facilities: With the 2007 legislative changes to the California School Finance Authority Act, Authority staff has been working with its financing team to draft the terms of its Conduit Financing Program. These preliminary terms as provided below are subject to ongoing refinement following discussions with legal counsel, the charter school community, rating agency analysts, lenders, bond underwriters and other stakeholders. Please note that these terms incorporate the use of $15 million in Federal Enhancement Grant funds. The cash flow pro forma that follows on subsequent pages and the tables provided as attachments to our narrative reflect these preliminary terms.

Preliminary Terms of California Charter School Conduit Financing Program Incorporating Federal Enhancement Grant	
Issuing Authority/Program Sponsor	The California School Finance Authority as a conduit issuer on behalf of charter schools.
Governing Statutes	Education Code sections 17170 through 17199.5
Governing Regulations	CCR, Title 4, Division 15, Article 1.5
Agent for Sale	State Treasurer's Office, Public Finance Division
Borrowers	Eligible charter schools domiciled in California whose obligation is to be documented by a Loan Agreement.
Charter School Threshold Eligibility Requirements	▪ Minimum one year of operating history ▪ Possession of current, valid charter ▪ Compliance with the terms of charter and be in good standing with chartering authorizer ▪ Determined to be financially sound ▪ Operation as a non-profit entity ▪ Facilities to be financed will provide classroom-based instruction ▪ Proficient performance by students on State academic

Preliminary Terms of California Charter School Conduit Financing Program Incorporating Federal Enhancement Grant	
	assessments ▪ No risks that could materially threaten ongoing viability
Charter School Selection Criteria	If program capacity is limited, charter schools offering public choice in communities with the greatest need for this choice will be given priority. Preference points will be assigned to applicants based on: ▪ Number of low-income students qualifying for Free & Reduced Price Meals ▪ State (API) and US DOE (AYP) academic assessments of students attending traditional schools in the geographic region of the applicant ▪ Traditional schools identified for improvement, corrective action or restructuring under Title I of ESEA as amended by the NCLB Act of 2001 in the geographic region of the applicant ▪ Student overcrowding in traditional schools in the geographic region of the applicant
Purpose	▪ Financing new charter school facilities in the predevelopment, construction, and permanent (take-out) stages. ▪ Financing leasehold improvements to existing charter school facilities. ▪ Refinancing of existing debt issued to fund charter school facilities.
Borrower Tiers / Bond Series	<u>Tier One</u> – At least three years of operating history; minimum enrollment of 350 students; bond proceeds to be used for permanent financing or refinancing of an owned facility <u>Tier Two</u> – Minimum one year of operating history; bond proceeds to be used for permanent financing or refinancing of an owned facility, to finance predevelopment and construction needs and to finance leasehold improvements
Term of Repayment	Up to 30 years, but not to exceed the useful life of the financed asset.
Source of Repayment	▪ The Loan Agreement with each charter school is expected to be secured by all available revenues of each charter school including, but not limited to, federal, state, local, and extraordinary revenue sources. ▪ All charter schools will be required to pledge an intercept of their annual state allotment of revenue limit funds in order to guarantee their loan (debt service) payments (Section 17199.4 of Education Code).
Security for Bonds	▪ Pledge of Borrower's available revenues with intercept mechanism applied to revenue provided by the State, but not local sources. ▪ Debt service reserve funded by the Federal Enhancement Grant. ▪ Debt service reserve funded from bond proceeds. ▪ Security interest in the financed asset.
Debt Service Reserve Fund	<u>Tier One</u> – One reserve equal to the lesser of 10% of par, maximum annual debt service and 125% average annual debt

Preliminary Terms of California Charter School Conduit Financing Program Incorporating Federal Enhancement Grant	
	service on bonds Tier Two – Primary reserve equal to maximum annual debt service on bonds and to be funded by the Federal Credit Enhancement Grant; secondary reserve equal to the lesser of 10% of par, maximum annual debt service and 125% average annual debt service on bonds, and to be funded from bond proceeds
Interest Rate Mode	Participants will have the option of repaying their obligations using either a fixed or variable interest rate, although fixed rate will be the Authority's recommended mode. ▪ Tax-exempt, fixed interest rates, assuming a 30-year term, are expected to range from 4.50% to 6.00%, not incorporating financing costs. ▪ Tax-exempt, variable interest rates are expected to range from 2.50% to 4.50%, not incorporating financing costs.
Optional Prepayment	Borrowers will be allowed to prepay their loans based on the optional redemption terms of the Authority's bond issue.
Additional Provisions of the Loan Agreements	The Loan Agreements will contain additional standard provisions pertaining to additional debt tests, reporting of debt service coverage, acquisition and disposition of property, maintenance and operation of facilities, insurance, indemnification of the Authority, and events of default and remedies.
Proposed Timeline	Produce First Draft of Regulations .... May 2009 Receive comments.. June 2009 Produce Final Draft of Regulations .... June 2009 CSFA Board Approves Regulations ....July 2009 Regulations Implemented ....August 2009 Application Posted to CSFA Website ....August 2009 Applications Due to CSFA.................................... October2009 Staff recommendations ....February 2010 CSFA Board Decision on Applications................February 2010 Inaugural Bond Issuance .... June 2010
Transaction Costs	Fees paid to the Authority, bond counsel, disclosure counsel, financial advisor, underwriters, private credit enhancers (if any), rating agencies, and other miscellaneous parties, are estimated to aggregate to 0.7% - 1.0% of the charter school's project cost.

Additional Considerations Regarding Charter School Selection Criteria: As the selection criteria for the Conduit Financing Program are further developed, Authority staff will utilize statewide data on charter schools, their student performance and student demographics to ensure that the funds are reaching the student populations set forth in the grant application.

California's charter schools are found throughout the state, and are heavily concentrated in the state's urban areas (76%), with 17% of all charters in rural areas, and only 7% found in suburban areas. These charter school student populations are diverse and tend to reflect the student populations of the school districts in which the charter schools are located.

While preparing the application for a Federal Enhancement Grant was prepared, Authority staff gathered and summarized relevant demographic data from California's charter school student population into the table on the following page. These findings and future updates will be a useful tool in finalizing the selection criteria and targeting potential participants in the program. As the table reflects, 23% of California charter schools have at least 70% of students receiving Free and/or Reduced Price Meals. Additionally, 42.5% of all California charter schools are not meeting their state assessed Academic Performance Index (API) targets. Lastly, 37% of California charter schools are not meeting federal AYP criteria.

All program selection criteria will be vetted by the charter community in the early stages of program development. As it develops program regulations in the coming months, Authority staff plans to conduct a number of informational and technical workshops throughout the state. Please see the "Organizational Capacity" section regarding the Authority's policies and procedures for developing and adopting program regulations.

Selected Statistical Data of Charter Schools in California

		School Receiving Free & Reduced Price Meals			API DATA				AYP DATA	
	NUMBER OF CHARTER SCHOOLS	CHARTER SCHOOLS RECEIVING FRPM	% of CHARTER SCHOOLS RECEIVING FRPM	CHARTER SCHOOLS WITH STUDENTS >70% RECEIVING FRPM	CHARTER SCHOOLS MEETING API	% OF CHARTER SCHOOLS MEETING API	CHARTER SCHOOLS WITH RANK OF 3 OR LOWER	CHARTER SCHOOLS WITH RANK OF 7 OR HIGHER	CHARTER SCHOOLS MEETING AYP	% OF CHARTER SCHOOLS MEETING AYP
ALAMEDA	37	31	83.8%	19	18	48.6%	19	7	19	51.4%
BUTTE	11	9	81.8%	3	5	45.5%	6	3	7	63.6%
CALAVERAS	1	1	100.0%	0	1	100.0%	0	0	0	0.0%
CONTRA COSTA	5	3	60.0%	0	3	60.0%	1	3	2	40.0%
DEL NORTE	2	1	50.0%	1	0	0.0%	1	1	0	0.0%
EL DORADO	10	4	40.0%	1	4	40.0%	2	3	7	70.0%
FRESNO	26	20	76.9%	11	12	46.2%	7	13	13	50.0%
GLENN	1	1	100.0%	0	1	100.0%	0	0	0	0.0%
HUMBOLDT	12	8	66.7%	3	5	41.7%	3	4	6	50.0%
KERN	5	3	60.0%	0	3	60.0%	1	1	3	60.0%
KINGS	9	7	77.8%	0	6	66.7%	2	4	6	66.7%
LAKE	1	1	100.0%	0	0	0.0%	0	0	1	100.0%
LASSEN	3	1	33.3%	0	1	33.3%	2	0	0	0.0%
LOS ANGELES	135	97	71.9%	53	60	44.4%	47	37	68	50.4%
MADERA	5	3	60.0%	1	3	60.0%	1	3	3	60.0%
MARIN	4	2	50.0%	0	4	100.0%	1	2	4	100.0%
MENDOCINO	7	6	85.7%	1	5	71.4%	2	2	6	85.7%
MERCED	2	1	50.0%	0	1	50.0%	0	0	1	50.0%
MODOC	1	1	100.0%	0	0	0.0%	0	0	1	100.0%
MONO	3	1	33.3%	0	1	33.3%	2	1	1	33.3%
MONTEREY	6	3	50.0%	0	4	66.7%	3	2	4	66.7%
NAPA	5	4	80.0%	2	4	80.0%	1	1	4	80.0%
NEVADA	18	15	83.3%	2	11	61.1%	1	10	14	77.8%
ORANGE	11	8	72.7%	2	7	63.6%	4	4	5	45.5%
PLACER	4	3	75.0%	0	2	50.0%	0	3	3	75.0%
PLUMAS	1	1	100.0%	0	0	0.0%	0	0	0	0.0%
RIVERSIDE	12	10	83.3%	1	5	41.7%	3	6	7	58.3%
SACRAMENTO	33	29	87.9%	6	13	39.4%	17	6	18	54.5%
SAN BERNARDINO	17	12	70.6%	3	11	64.7%	7	6	8	47.1%
SAN DIEGO	71	55	77.5%	14	39	54.9%	18	25	45	63.4%
SAN FRANCISCO	10	10	100.0%	1	4	40.0%	3	4	8	80.0%
SAN JOAQUIN	14	11	78.6%	2	8	57.1%	5	5	9	64.3%
SAN LUIS OBISPO	2	1	50.0%	0	2	100.0%	1	1	2	100.0%
SAN MATEO	13	12	92.3%	4	9	69.2%	5	7	11	84.6%
SANTA BARBARA	7	4	57.1%	0	5	71.4%	2	3	3	42.9%
SANTA CLARA	21	15	71.4%	6	14	66.7%	10	8	10	47.6%
SANTA CRUZ	11	8	72.7%	1	7	63.6%	1	7	7	63.6%
SHASTA	11	9	81.8%	0	6	54.5%	1	4	9	81.8%
SISKIYOU	2	1	50.0%	0	1	50.0%	1	0	1	50.0%
SOLANO	4	3	75.0%	0	1	25.0%	2	1	3	75.0%
SONOMA	21	17	81.0%	3	16	76.2%	5	8	16	76.2%
STANISLAUS	18	9	50.0%	1	9	50.0%	5	6	9	50.0%
SUTTER	5	3	60.0%	0	1	20.0%	3	0	1	20.0%
TEHAMA	2	1	50.0%	0	1	50.0%	0	1	1	50.0%
TULARE	8	3	37.5%	1	1	12.5%	4	1	2	25.0%
TUOLUMNE	3	1	33.3%	0	1	33.3%	0	2	1	33.3%
VENTURA	7	2	28.6%	0	3	42.9%	0	2	3	42.9%
YUBA	6	4	66.7%	1	3	50.0%	3	1	4	66.7%
TOTAL/AVERAGE	623	455	81.5%	143	321	57.5%	202	208	356	63.0%

Source: California Dept. of Education (FY 2005-06)

State of California - Cash Flow Pro Forma for Federal Credit Enhancement Grant Application (Page 1 of 2)

	Project Yr 1 (CA FY 2010)	Project Yr 2 (CA FY 2011)	Project Yr 3 (CA FY 2012)	Project Yr 4 (CA FY 2013)	Project Yr 5 (CA FY 2014)	TOTALS
Projected Costs & Funding Sources for New Charter Schools in California						
Demographics						
Charter School Students	287,333	308,883	332,050	356,953	383,725	
Number of Charter Schools	780	839	901	969	1,042	
Up-Front Cost of New Schools						
Unhoused Students	20,047	21,550	23,166	24,904	26,772	
Facility Space per Student (sq. feet)	80.0	80.0	80.0	80.0	80.0	
Facility Cost per Square Foot	$195.00	$200.85	$206.88	$213.08	$219.47	
Facility Cost	$312,725,702	$346,265,534	$383,402,512	$424,522,432	$470,052,463	$1,936,968,643
Land Cost (25.0% of Facility Cost)	$78,181,426	$86,566,383	$95,850,628	$106,130,608	$117,513,116	$484,242,161
Total Up-Front Cost of New Schools	$390,907,128	$432,831,917	$479,253,140	$530,653,040	$587,565,578	$2,421,210,803
Estimated Up-Front Funding Sources						
Facilties Funded/Provided per Prop. 39	$58,636,069	$64,924,788	$71,887,971	$79,597,956	$88,134,837	$363,181,621
Facilities Funded/ Provided by Leasing	195,453,564	216,415,959	239,626,570	265,326,520	293,782,789	1,210,605,402
Charter School Facility Program	100,000,000	100,000,000	150,000,000	150,000,000	0	500,000,000
Total Estimated Up-Front Funding Sources	$354,089,633	$381,340,746	$461,514,541	$494,924,476	$381,917,626	$2,073,787,022
Net Unfunded Up-Front Cost / Funding from CA Conduit Financing Program	$36,817,495	$51,491,171	$17,738,599	$35,728,564	$205,647,952	$347,423,781

State of California - Cash Flow Pro Forma for Federal Credit Enhancement Grant Application (Page 2 of 2)

	Project Yr 1 (CA FY 2010)	Project Yr 2 (CA FY 2011)	Project Yr 3 (CA FY 2012)	Project Yr 4 (CA FY 2013)	Project Yr 5 (CA FY 2014)	TOTALS
Uses and Sources of Funds for California Charter School Conduit Financing Program (Interest Rates as of 2/6/09 assuming Baa/BBB credit ratings)						
Uses of Funds						
Tier One Borrowers (Series A Bonds)						
Permanent Financing (est. @ 30.0% of Total Uses)	$11,045,248	$15,447,351	$5,321,580	$10,718,569	$61,694,386	$104,227,134
Refinancing (est. @ 10.0% of Total Uses)	3,681,749	5,149,117	1,773,860	3,572,856	20,564,795	$34,742,378
TOTAL	$14,726,998	$20,596,468	$7,095,440	$14,291,426	$82,259,181	$138,969,512
Tier Two Borrowers (Series B Bonds)						
Predevelopment Financing (est. @ 15.0% of Total Uses)	$9,204,374	$12,872,793	$4,434,650	$8,932,141	$51,411,988	$86,855,945
Construction Financing (est. @ 25.0% of Total Uses)	15,340,623	21,454,655	7,391,083	14,886,902	85,686,647	$144,759,909
Leasehold Improvements (est. @ 20.0% of Total Uses)	12,272,498	17,163,724	5,912,866	11,909,521	68,549,317	$115,807,927
TOTAL	$36,817,495	$51,491,171	$17,738,599	$35,728,564	$205,647,952	$347,423,781
Total Uses of Funds	$51,544,493	$72,087,639	$24,834,039	$50,019,989	$287,907,133	$486,393,294
Sources of Funds						
Tier One Borrowers (Series A Bonds)						
Reserve Requirement Funded by the Federal Enhancement Grant	***$0***	***$0***	***$0***	***$0***	***$0***	***$0***
Leverage Provided by Federal Enhancement Grant = (A+B)/Grant	***N/A***	***N/A***	***N/A***	***N/A***	***N/A***	
Permanent Financing (A)	$11,045,248	$15,447,351	$5,321,580	$10,718,569	$61,694,386	$104,227,134
Refinancing (B)	3,681,749	5,149,117	1,773,860	3,572,856	20,564,795	$34,742,378
Reserve Requirement Funded from Bond Proceeds	$1,287,550	$1,795,250	$626,250	$1,249,600	$7,131,300	$12,089,950
Transaction Costs						
Net Original Issue Discount /(Original Issue Premium)	435,785	605,726	211,446	421,766	2,411,215	
Bond Counsel ($150,000 for both series)	42,863	42,858	42,861	42,859	42,857	
Disclosure Counsel ($50,000 for both series)	14,288	14,286	14,287	14,286	14,286	
Financial Advisor ($85,000 for both series)	24,289	24,286	24,288	24,287	24,286	
Underwriter's Discount (0.50% of par)	83,225	116,125	40,425	80,775	461,875	
Rating Agencies ($80,000 for both series)	22,860	22,858	22,859	22,858	22,857	
Miscellaneous ($25,000 for both series)	7,144	7,143	7,143	7,143	7,143	
Total Transaction Costs	630,453	833,283	363,309	613,974	2,984,519	
TOTAL PAR AMOUNT	$16,645,000	$23,225,000	$8,085,000	$16,155,000	$92,375,000	$156,485,000
Bond Issuance Statistics						
All Inclusive Cost	6.95%	6.93%	7.02%	6.95%	6.89%	
Average Annual Debt Service	$1,284,663	$1,792,620	$624,010	$1,246,940	$7,129,270	$12,077,503
Average Life (years)	19.73	19.73	19.73	19.73	19.73	
Tier Two Borrowers (Series B Bonds)						
Reserve Requirement Funded by the Federal Enhancement Grant	***$3,213,400***	***$4,483,600***	***$1,562,550***	***$3,119,050***	***$17,825,950***	***$30,204,550***
Leverage Provided by Federal Enhancement Grant = (C+D+E)/Grant	***11.5***	***11.5***	***11.4***	***11.5***	***11.5***	
Predevelopment Financing (C)	$9,204,374	$12,872,793	$4,434,650	$8,932,141	$51,411,988	$86,855,945
Construction Financing (D)	$15,340,623	$21,454,655	$7,391,083	$14,886,902	$85,686,647	$144,759,909
Leasehold Improvements (E)	$12,272,498	$17,163,724	$5,912,866	$11,909,521	$68,549,317	$115,807,927
Reserve Requirement Funded from Bond Proceeds	$3,213,400	$4,483,600	$1,562,550	$3,119,050	$17,825,950	$30,204,550
Transaction Costs						
Net Original Issue Discount /(Original Issue Premium)	1,087,523	1,516,361	529,240	1,056,895	6,027,852	
Bond Counsel ($150,000 for both series)	107,137	107,142	107,139	107,141	107,143	
Disclosure Counsel ($50,000 for both series)	35,712	35,714	35,713	35,714	35,714	
Financial Advisor ($85,000 for both series)	60,711	60,714	60,712	60,713	60,714	
Underwriter's Discount (0.50% of par)	208,025	290,300	101,050	201,925	1,154,675	
Rating Agencies ($80,000 for both series)	57,140	57,142	57,141	57,142	57,143	
Miscellaneous ($25,000 for both series)	17,856	17,857	17,857	17,857	17,857	
Total Transaction Costs	1,574,105	2,085,229	908,852	1,537,387	7,461,098	
TOTAL PAR AMOUNT	$41,605,000	$58,060,000	$20,210,000	$40,385,000	$230,935,000	$391,195,000
Bond Issuance Statistics						
All Inclusive Cost	6.95%	6.93%	7.02%	6.95%	6.89%	
Average Annual Debt Service	$3,210,932	$4,481,263	$1,559,977	$3,116,525	$17,823,333	$30,192,030
Average Life	19.73	19.73	19.73	19.73	19.73	

PART 2. PROJECT SERVICES

I. Meeting the Needs of California Charter Schools

As described in our Project Design section of this proposal, the Authority has outlined a financing program that will help meet the facility needs of California charter schools. The Authority has proven itself to be an extremely capable entity and has played a crucial role in establishing several key programs that support charter schools in their efforts to secure adequate school facilities in California. The charter school programs that the Authority oversees are key enablers in the charter school community's ability to expand educational opportunities in traditionally underserved communities of California. The Authority will utilize the same approach when implementing the Conduit Financing Program that it has when developing its other programs.

II. Support of California Charter School Community

The Authority's success in creating and expanding financing opportunities for California's charter schools is a result of the high level of involvement that the charter school community has had in the Authority's program creation and implementation process. The Authority, charter school stakeholders, and capital market participants work collaboratively as programs are developed and refined, and funds are disbursed. Authority staff will continue this level of engagement as it implements the Conduit Financing Program.

Support for the Authority's administration of the State's $900 million Charter School Facilities Program, the $50 million federally-funded State Charter School Facilities Incentive Grants Program, and the development of the Authority's other programs has been consistently overwhelming. The Authority enjoys broad support because of the early and thorough engagement with the charter community on program criteria and design. The Authority has provided support letters from the following individuals and organizations as Attachment A.

- Honorable Governor of the State of California - Arnold Schwarzenegger
- Honorable Treasurer and Chair of the Authority - Bill Lockyer
- Honorable Superintendent of Public Instruction and Authority Member - Jack O'Connell
- Deputy Director of the Department of Finance - Tom Sheehy
- CEO of the California Charter School Association - Jed Wallace
- Executive Director and Founder of the Charter Schools Development Center - Eric Premack
- President and CEO of EdVoice - Rae Belisle
- Chief Financial Officer of Aspire Public Schools - Mike Barr
- Chief Financial Officer of Green Dot Public Schools - Sabrina Ayala

III. Increasing Access to Financing

By securing this federal grant, the Authority will continue to increase access to financing opportunities to California's charter schools. Without the ability to raise taxes to pay for the cost of facilities like their traditional public school counterparts, charter schools must use operational funds to pay for the cost of their facilities. Most also rely on private funds to supplement their facility budgets. As such, this grant will enable the Authority to broaden its scope of funding for charter schools. While allowing charters to borrow at a lower interest cost, this grant will make long-term facility bond financing an option for more schools.

IV. Assisting Schools with the Greatest Need

Part 1 "Project Design", Section IV., of this proposal describes the criteria which will be used to rank applicants to the Conduit Financing Program. The Authority will work with the charter school community and other stakeholders to develop program regulations that are consistent with the criteria outlined in our proposal. Two of the Authority's current charter school facility programs use similar competitive criteria to award funds to applicants. Such criteria include 1) schools that serve a large population of low-income students eligible for free or reduced priced meals; 2) schools located in districts with overcrowding; 3) schools run by non-profit entities; and 4) schools that are meeting student performance targets set by the state.

PART 3. BUSINESS AND ORGANIZATIONAL CAPACITY

The Authority has the expertise and capacity to implement the project set forth in this application. Below we have highlighted the strengths and abilities of the Authority and its team as demonstration of its ability to execute a successful federal enhancement program for charter schools.

I. Authority Background

The Authority was created in 1985 to provide facility and working capital financing to California school districts and community college districts. The Authority consists of three Board Members: the California State Treasurer Bill Lockyer serving as Chair, and the Superintendent of Public School Instruction Jack O'Connell, and Michael C. Genest, Director of Finance, serving as Members. The Authority maintains offices in Sacramento and Los Angeles, enabling Authority staff to more effectively provide services to constituents throughout the State.

Since its inception, the Authority has implemented several financing programs to address the needs of its stakeholders. In 1999 and 2000, the Authority issued three pooled financing notes for school districts to provide bridge financing for schools that were awaiting Proposition 1A apportionments. Fourteen school districts participated in the program, which provided interim financing to allow districts to commence school construction prior to receiving Proposition 1A funding. This important financing mechanism enabled districts to save valuable time and resources.

Since the passage of California's Charter School Act of 1992, charter schools have become a viable option for parents, students, and educators seeking choice in education. As of the 2008-09 school year, approximately 675 charter schools serve

248,639 California public school students. At the time the Authority was created, charter schools did not exist and therefore were not listed in the definition of entities able to access financing through the Authority.

Recognizing that charter schools should be eligible to access low-cost, tax-exempt facilities and working capital financing – like their traditional public school counterparts – Authority staff spearheaded a legislative amendment to its statute to provide financing opportunities to charter schools. In collaboration with the California Charter Schools Association, the Authority worked with Assembly member Mimi Walters for the successful passage of Assembly Bill 2717, which was signed into law on September 18, 2006. Effective January 1, 2007, the Authority has the ability to issue debt on behalf of charter schools.

Since 2002, one of the Authority's primary functions has been to administer the State's Charter School Facilities Program (Program). The Authority's responsibilities as they relate to the Program include, determining which charter school applicants are creditworthy; conducting ongoing monitoring and due diligence of applicants' financial soundness; and developing and negotiating Program agreements on behalf of the State. The Authority jointly oversees this Program with the Office of Public School Construction (Education Code sections 17078.52 through 17078.66). To date, the program has made preliminary apportionments of $900 million in funding to charter schools throughout the State.

II. Management Experience with Other Federal Programs

In 2004, the Authority applied for and was awarded a $49.25 million federal grant under the United States Department of Education's State Charter School Facilities Incentive Grants Program (Federal Grant Program) to assist charter schools in meeting their facility needs. The Federal Grant Program is designed to fund those charter schools that demonstrate the most need. The Authority designed a 110-point preference point matrix based on the following: (1) the number of low-income students at the school who are eligible for free and/or reduced priced meals; (2) the level of overcrowding the charter school's district is experiencing; (3) whether the charter school is being operated by a non-profit entity; and (4) whether the charter school met student performance standards. The grant is being allocated over a five-year period, averaging annual awards of $9.85 million through fiscal year 2008-09. Charter schools may use the grant funds to pay a portion of their rent, lease or debt service payments, or to fund the cost of acquiring, renovating or constructing new facilities. To date, four funding rounds have been conducted and 82 charter schools, serving 25,862 students have received awards totaling $38 million. The fifth and final funding round will be completed by June 30, 2009.

III. Policies and Procedures

Every department, division, office, bureau, board or commission in the executive branch of California state government must follow the rulemaking procedures in the California Administrative Procedure Act, which sets forth the process for adopting program regulations. The Authority's program design process includes ample public participation and transparency to ensure wide support for its initiatives.

The Authority provides all stakeholders an opportunity to comment on the proposed program criteria prior to finalizing regulations. Once the Authority board has approved regulations, they are distributed to interested parties for a 45-day public comment period. Based on an assessment of all public comments and potential revisions to the proposed regulatory language, the rulemaking file may be re-distributed for an additional 15-day public comment period before the final version of the text is adopted by the Authority members. This process ensures consensus from the charter school community

IV. Underwriting Standards for Participants

In collaboration with the charter school community and capital market participants (i.e., credit rating agencies, bond insurers, lenders, underwriters, and bond counsel) the Authority's team will develop evaluation criteria for charter schools seeking funding through the Conduit Financing Program. The Authority has extensive experience developing underwriting standards for its Charter School Facilities Program (Program). The Authority's standards for determining which schools are financially sound are quite rigorous and take into account numerous quantitative and qualitative factors of the charter schools. The Authority will employ equally thorough underwriting standards for the Conduit Financing Program. Such factors include but are not limited to:

- School's ability to maintain stable financial operations and make program payments;
- Any material risks that would threaten the financial or operational viability of the school;
- Historical, current, and future financial performance of the school or its operator;
- Historical, current and projected enrollment figures as well as student retention rates;
- Reasonableness of projected financial performance and enrollment based on current and historical performance;
- School's reliance on contributions and private funding;
- Qualifications and performance of management and personnel at the school;
- Evidence that the school is in compliance with the terms of its charter and in good standing with its charter authorizer;
- School's contracts, memorandum of understanding, and all agreements;
- Governance structure of the school management and the board; and

- Other factors as deemed necessary.

V. Standards of Conduct

As stewards of state and federal funds, the Authority's standards of conduct are adhered to closely. As a California state agency, the Authority and its management personnel must comply with the State's Political Reform Act, a copy of which has been provided as Attachment B. Briefly, the Act requires that all governmental officials involved in governmental decision-making must disclose all sources of income, investments, and gifts and prohibits such officials from participating in, making, or attempting to influence decisions in which they have a financial interest. The Act also provides for civil and criminal penalties in the case of a violation.

VI. Credit Ratings

The Authority does not have a credit rating, and conduit financings of the Authority have been rated based on the credit quality of the borrower and the security provisions of the individual financings. As discussed in the Project Design section of this application, charter schools participating in the Conduit Financing Program will be required to pledge an intercept of their annual State allotment of revenue limit funds in order to guarantee the debt service on the debt issued on their behalf by the Authority. Because the debt service will be secured by intercepted funds coming directly from the State, investors, lenders and rating agencies are expected to have greater confidence in timely repayment and therefore offer higher credit ratings and more favorable financing terms. The anticipated minimum investment grade credit ratings on the Authority's conduit bonds will offer significantly lower borrowing costs to participating charter schools.

The table below summarizes the State of California's recent long-term General Obligation (GO) bonds rating. This is the credit rating most commonly referenced when speaking on the subject of credit ratings. Revenue Anticipation Notes (RANs), with maturities of approximately one year, are backed by unapplied moneys in the State's General Fund. Copies of the State's most recent long- and short-term credit rating reports have been attached (Attachment C) for your consideration.

Rating Agency	**GO Bonds (long-term)**	**RANs (short-term)**
Fitch Ratings	A+	F2
Moody's Investors Service	A1	MIG 2
Standard & Poor's	A	SP-2

VII. Financial Statements

The Authority does not have its own audited financial statements. As a California state agency, we have included the State of California's Comprehensive Annual Financial Reports from FY 2005, FY 2006 and FY 2007 as attachments to the application for your consideration (refer to Attachment D).

VIII. Enabling Statutes

The Authority's enabling statute, Education Code Sections 17170 through 17199.5, has been provided as Attachment E to the application.

PART 4. PROJECT PERSONNEL

California has assembled a team of professionals that bring a wide range of expertise in the area of finance, with specific and unique charter school facilities financing experience. Team members are drawn from state agencies, top-ranked underwriting, advisory and bond counsel firms, as well as professionals from the Public Finance Division of the State Treasurer's Office. Members of California's charter school community and associations also will provide input as the Authority designs its Conduit Financing Program. Summaries of team member's expertise have been provided below, and résumés are included as Attachment F to the application.

I. California School Finance Authority

The Authority provides tax-exempt, low cost financing to charter schools, school districts, and community college districts for use in the repair and construction of school facilities as well as provide financing for working capital purposes. The Authority's primary focus since 2002 has been providing charter schools with facilities financing.

The Authority's Executive Director, Katrina Johantgen, has over 16 years of municipal finance experience, having served as an investment banker and financial advisor for over eight years, and has been with the Authority for over eight years. As a banker and financial advisor, Ms. Johantgen served numerous school districts, cities, counties and special districts throughout California.

During her tenure with the Authority, Ms. Johantgen has been instrumental in creating and expanding financing opportunities for California charter schools. Most notably, Ms. Johantgen has overseen the development of charter school facility programs that account for $950 million in funding to California charter schools.

The financing and policy expertise of Ms. Johantgen will ensure that the federal enhancement grant is administered in a manner that is consistent with federal guidelines and policy objectives.

Ms. Johantgen will work with Authority staff which is comprised of four full-time professionals and four support staff to implement the conduit financing program. Mark Paxson, General Counsel to the State Treasurer, and Kristin Smith, staff counsel to the State Treasurer will work closely with the Authority to ensure the program's compliance with federal and state law and regulations. Mr. Paxson has provided legal and program financing advice to the Authority since 2000, and will be an integral part of the successful launch of the conduit bond program. Along with the Executive Director, these grant team members have acquired a significant amount of experience and knowledge about the Authority and California's charter school system, and will be actively involved in the administration of the program.

II. State Treasurer's Office – Public Finance Division

The State Treasurer's Office Public Finance Division also will be actively involved in the implementation of the Conduit Financing Program. The Public Finance Division administers programs that carry out the fiduciary responsibilities of the State Treasurer, including but not limited to issuance of State of California general obligation bonds, revenue anticipation notes and certain revenue bonds, and assures compliance with federal tax laws applicable to State debt.

Public Finance Division members assigned to assist in the implementation of the program's bond financing include: Katie Carroll, Director; Jeanne Trujillo, Assistant Director; Deanne Brown, Manager, and Vicki Au-Yeung, Assistant Manager. The Public Finance Division has extensive responsibilities and experience in performing agent for sale functions for conduit and other state bond financings, disseminating financial information to the investment community, providing on-going communication with investors, and researching and responding to inquiries from investors. The Division brought over $23.8 billion in bond transactions to market in calendar year 2008. The Division's unsurpassed experience will be invaluable as the Authority brings its Conduit Financing Program to the bond markets.

The level of experience of staff and consultants working with the Authority is unparalleled. The individuals include experts in finance as well consultants who have been involved in the charter school movement since its inception and who are knowledgeable about all aspects of charter schools, including financing, construction, and operating issues. Many of the staff employed by the Authority and the State Treasurer's office, who will be working on this project have worked with the Authority for several years, and are very familiar with education finance, charter school facilities, and charter school issues in general.

III. Capital Market Participants

The Authority has assembled a team of capital market participants to assist in the implementation of the Conduit Financing Program. The team is comprised of leaders in the underwriting and advisory field as well as from the state's leading bond and tax counsel firm.

First Southwest Company: The Authority has engaged the services of First Southwest Company to assist in the implementation of its Charter School Facilities Program. First Southwest Company has provided financial advisory services to public entities since 1946. The firm has served as financial advisor to more than 1,500 municipal and non-profit entities in their 63 years in the industry. From January 1, 2006 through December 31, 2008, the firm provided financial advisory services to more than 750 public entities, and completed 2,611 bond transactions, totaling $77.08 billion in par amount. For this period, Thomson Financial Securities Data ranks the firm as the number-one financial advisor in the nation in terms of number of tax-exempt transactions completed. In the State of California, First Southwest served as financial advisor on 58 transactions totaling $10.18 billion par amount since January 1, 2004.

Mr. Michael D. Kremer, Vice President, has an extensive amount of education finance experience, including providing investment banking and financial advisory services on nearly 30 debt issues for various educational agencies in California. Mr. Kremer has provided financial advisory services on more than 70 debt issues totaling more than $16.7 billion in par, prepared debt affordability reports and financial feasibility analyses and developed financing plans for large scale, multi-year capital improvement plans. Since 2002, Mr. Kremer has worked closely with the Authority on charter school issues, predominately the evaluation of nearly 100 charter schools' to determine whether the schools could be found financially sound. This financial soundness review balances each school's financial information as well as other operational and educational factors, in order to evaluate the school's likelihood of success.

Ms. Beth Bankhead, Vice President, has provided services, such as debt structuring and cash flow analyses, for several north Texas cities, counties, hospital districts, and economic development corporations. Ms. Bankhead's not-for-profit experience includes healthcare, higher education, secondary education, and charter schools. Specifically, her charter school experience includes assisting Texas charter schools in all aspects of bond transactions, including assistance in applying for credit enhancement from the state. In 2007, Ms. Bankhead served as financial advisor to UPLIFT Education which utilized the Texas Credit Enhancement Program (TECP) for their bond issue. TECP's debt service reserve fund guarantee program fulfilled $1 million of the reserve fund requirement for the bonds at no cost to UPLIFT. In effect, UPLIFT was able to avoid borrowing an extra $1 million to fund the reserve fund and, as a result, negative arbitrage on the reserve fund was avoided and UPLIFT's additional bond capacity was preserved. In 2007 and 2008, Ms. Bankhead assisted CSFA staff with reviewing and summarizing charter school grant applications for preliminary apportionment from the California School Facilities Program (CSFP).

Mr. Phillip Curls, an analyst with First Southwest Company, has the primary responsibility of providing quantitative support to the firm's senior professionals. Mr. Curls provides refunding analysis, debt structuring, cash flow models, credit analysis, and continuing disclosure for charter schools, cities, counties, utilities, higher education, port authorities, and airports. Mr. Curls worked extensively with the Authority staff during the 2008 funding round for the Charter School Facilities Program (CSFP). This included performing financial and credit analysis of approximately 20 charter schools and school districts, involving the calculation of credit ratios utilizing historical and pro-forma financial data.

<u>Orrick, Herington & Sutcliffe</u>: The world-renowned law firm of Orrick, Herrington & Sutcliffe will serve as the Authority's bond and tax counsel as it structures its working capital and long-term facilities programs for California charter schools. John Hartenstein, Esq., will serve as lead bond counsel to the Authority, and Chas Cardell, Esq. will provide his expertise as one of California's top tax attorney.