

MEMORANDUM

DATE: November 6, 2015

TO: David Damschen, Deputy State Treasurer

FROM: Bruce D. Williams
Zions Bank Public Finance

RE: American Leadership Academy Application to the Utah Charter School Finance Authority

The purpose of this report is to document American Leadership Academy’s (“ALA,” or the “School”) adherence to the eligibility standards created for participation in the Utah Charter School Credit Enhancement Program (the “Program”). The analysis contained herein is based on American Leadership Academy’s full application to the State Charter School Finance Authority (the “Authority”), subsequent conversations and a meeting at the School site with the School’s finance team, validation of information contained in the application with data from the Utah State Office of Education, as well as additional information and documents submitted in response to follow up requests by the Authority.

The School has provided all information requested subsequent to the submission of the initial application. This report will examine each category of the Program’s “Standards for Participation,” including Basic Eligibility, Enrollment/Student Demand, Academic Performance, Management, Financial Performance, and Bond Documents. In each of these categories except two, the School met the basic eligibility requirements for participation in the Program, as detailed below. These two areas include an unsatisfactory mark in the State Charter School letter due to not meeting the Charter School Board’s standard for revenue and expenditure forecasting and not meeting the program standard for the Current Ratio. Each of these issues are discussed further within the report.

This report should be examined in direct conjunction with the Letter of Certification for American Leadership Academy from the State Charter School Board (“SCSB Letter”), which provides detailed analysis and historical information on Enrollment/Student Demand, and Academic Performance. Because the Academy has one “Unsatisfactory” mark, related to budgeting and forecasting, the SCSB Letter must be formally approved at the November 12th meeting of the SCSB.

American Leadership Academy—Introduction

American Leadership Academy is a K-12 charter school located in Spanish Fork, Utah. The School opened in 2005 and during the 2006-07 school year had 1,416 students. ALA's enrollment cap is 1,825 students with current enrollment as of 10/1/2015 of 1,799 students. With strong retention and a large waiting list, the School should not have a problem increasing to and maintaining this enrollment into the future.

American Leadership Academy has the following mission statement and vision for students who attend the school and their families.

Mission Statement

The mission of American Leadership Academy (ALA) Charter School is to empower families and support students in grades K-12 to meet and exceed rigorous academic standards, promote life-long learning skills, and to advocate our belief that parental involvement and partnership is critical to student success. ALA is committed to providing all students with a challenging, innovative, and results-oriented education through a quality, unique method of educational reform which emphasizes academic excellence, physical well-being, character development, and accountability and respect for the individual.

Vision Statement

We envision American Leadership Academy (ALA) Charter School as a thriving community of learning that honors and maintains its mission in all that it does. Together this Academy will build a scholarly, creative, and exciting environment that students will want to experience; a place that will attract the most highly skilled and committed educators and community members. Parents will have an active presence during the school day and in all aspects of governance. Accountability and personal responsibility will be embraced by all constituents, particularly the teachers, who will be given maximum freedom and support in helping them fulfill their teaching assignments.

The Project

The School plans to issue approximately \$25,775,000 million in revenue bonds, which will provide \$22.75 million to refinance its existing bonds for economic savings, and \$3.0 million to build a 16,473 square foot addition to the building and make other improvements to the Academy's existing educational facilities.

Basic Eligibility

1. ALA's 2015 bonds will be issued through the Authority.

2. The SCSB Letter indicates that ALA is in good standing with the State Charter School Board, with the exception of forecasting revenues and expenditures. This unsatisfactory mark is a result of underestimating revenues by 8.26% and expenditures by 7.96% during the 2013 fiscal year. This resulted in an increased change in net assets in comparison to budget. The school also underestimated expenditures by 5.92% in fiscal year 2014 but also underestimated revenues by 2.98% which resulted in a reduced change in net assets when compared to the budget. The school's explanation for the variances from budget was that they resulted from conservative budgeting and a desire to increase days of cash on hand.
3. The School has obtained an investment grade rating of "BBB-" from Standard & Poor's ("S&P"). The following is an excerpt from the S&P rating report:

The 'BBB-' rating reflects our assessment of:

- Solid pro forma MADS coverage of 1.65x, based on fiscal year 2015 unaudited operating results;
- Manageable pro forma MADS burden of 13.4%, based on fiscal year 2015 unaudited adjusted operating expenses;
- History of healthy operating surpluses generating solid EBIDA margins, with expectations for a stronger fiscal 2016;
- Recent growth in enrollment and historically stable demand, reflected by a significant waiting list;
- Adequate academic performance, with test scores that are comparable to the local school district; and
- Good working relationship with the charter sponsor, the state, as well as the favorable funding environment for charter schools in the state.

In our opinion, the preceding credit factors are partly mitigated by the school's:

- Adequate cash and investments of just more than \$2.6 million, representing 86 days' cash on hand in fiscal 2015, with unrestricted reserves to pro forma debt of only 10.1%;
 - Lack of ability to grow with the expansion, as numerous portable classrooms already bring the school close to its capacity of 1,825 students;
 - New construction risk associated with the elementary school expansion; and
 - Inherent risks, as with all charter schools, including the possibility that the charter may be revoked (although Utah's charter authorizations are evergreen).
4. ALA recently completed its 10th full year of operations. Financial operating history, as demonstrated by past audited financials, cash position, and increasing unrestricted fund balance, is satisfactory.
 5. The School has a defined and specific mission. Their mission statement reads:

The mission of American Leadership Academy (ALA) Charter School is to empower families and support students in grades K-12 to meet and exceed rigorous academic standards, promote life-long learning skills, and to advocate our belief that parental involvement and partnership is critical to student success.

6. ALA issued bonds in 2006. The 2015 bonds will refinance these bonds for economic savings and fund an addition to the existing facility of 16,473 square feet of additional space. The School is not in default under its existing bonds.

Enrollment/Student Demand

7. The School had 1,720 students enrolled during the 2014-2015 school year with current year growth to 1,799 students for the 2015-16 year. Originally, the school had an enrollment cap of 1,425 students which was increased to 1,525 in 2010 and then again to 1,825 in 2011.
8. Enrollment at ALA has increased each year since operations began in 2005. For the past four years the school has operated above 92% of its enrollment cap. Current enrollment is at 99% of the school's enrollment cap with the school anticipating adding 26 additional students over the next few years. Table 1 from the SCSB Letter includes detailed enrollment history back to the 2006-2007 school year.
9. American Leadership Academy exceeds their enrollment standard established by the SCSB, with the most recent total re-enrollment rate of 82.9%. Over the years, the School has ranged between 76.9% and 88.3% in reenrollment rates. Table 2 from the SCSB Letter details historical enrollment and re-enrollment.
10. The School exceeds the ADM rate requirement. Over the last three years, ALA's Average Daily Membership rate has been 98.2%, 97.8%, and 93.9%.
11. The School has provided wait list statistics by grade, and has provided the detailed waiting list that includes descriptive and personal information on potential students to the Deputy State Treasurer. The waiting list from the application includes 878 potential students applying for admission in the 2015-2016 academic year. The waiting list is relatively strong and includes a satisfactory amount of students for every grade level offered, with a smaller number of less than 40 students on the list in the 6th, 10th, 11th and 12th grades.

Academic Performance

12. The SCSB Letter indicates that the School meets required academic standards. Table 3 from the SCSB Letter provides a breakdown of American Leadership Academy's performance relative to other schools. Over the past three years the School's performance has been lower than the charter medians.

Management

13. The School has adopted reasonable management policies and practices that guide financial, debt, and risk management. The Board has adopted an acceptable Succession Plan as well as a Financial and Risk Management Plan. No formal policy was provided in the application concerning post issuance compliance but in discussion with the School's Business Manager, it was apparent that she is aware of and intends to comply with all post-issuance compliance issues including continuing disclosure.
14. American Leadership Academy has a six-member board. The board members have a diverse set of backgrounds, which include business, banking, engineering, technology and education. The Board serves staggered terms.
15. The School employs Jan Searle as its business manager to provide business management services. Mrs. Searle has been employed in this capacity for more than the five year standard anticipated in the standards.
16. As noted under Table 4 in the SCSB letter, American Leadership Academy's historical budgeted revenues and expenditures did not meet the State Charter School Board recommended standard of the statutory budget to be within 5% of actual revenues and expenditures. The SCSB letter includes a breakdown of adherence to budgeted revenues and expenses over the past three years. The School's budget was lower than actual revenues and expenditures in fiscal year 2013. In fiscal year 2014, the budget was lower than actual expenses.

Financial Performance

The School meets the requirements for the Financial Performance section of the application with the exception of the Current Ratio requirement.

17. Projections used by the School in financial forecasting appear reasonable. ALA seems positioned to continue and improve its healthy financial standing of the past.

In comparing the FY 2016 budget filed by the school with the State Auditor's Office with the estimated revenues included in the application, the revenues in the application were higher by \$962,128. The majority of the difference is explained by the fact that the original budget was based on projections from USOE which included only 1,720 students rather than the 1,799 students actually enrolled in the 2015-16 school year. The remaining difference is due to conservative budgeting practices.

The school has forecasted very conservative revenue growth through 2020 at approximately 1-3 % growth per year. Expenditures are forecasted to grow at a similar rate to expenses. The School appears to be in a healthy financial position.

18. Debt Coverage Ratio

Requirement	Measure	Sufficient?
At least 105%	147%	Yes

Debt coverage ratio is calculated by dividing total revenues available for debt service by the maximum annual debt service payment anticipated for the bonds. Revenues available for debt service is calculated by taking 2015 net income from operations of \$624,651 and adding back depreciation expense of \$622,304 and interest expense of \$1,390,693. This leaves net revenues available for debt service of \$2,637,648. When this number is divided by maximum annual debt service of the existing bonds of \$1,793,327, the coverage is 147%.

	2013	2014	2015
Net Income Available for Debt Service	<u>\$2,047,794</u>	<u>\$2,121,796</u>	<u>\$2,637,648</u>
Maximum Annual Debt Service	<u>1,793,327</u>	<u>1,793,327</u>	<u>1,793,327</u>
Debt Coverage Ratio	114%	118%	147%

Based on projected revenues, expenditures and new debt service after the refunding, debt service coverage is projected to be between 153% and 159% through fiscal year 2018.

	2016	2017	2018
Net Income Available for Debt Service	<u>\$2,734,928</u>	<u>\$2,845,271</u>	<u>\$2,802,597</u>
Maximum Annual Debt Service (New)	<u>1,793,327</u>	<u>1,793,327</u>	<u>1,793,327</u>
Projected Debt Coverage Ratio	153%	159%	156%

19. Debt Burden Ratio

Requirement	Measure	Sufficient?
Less than 25%	14.4%	Yes

The debt burden ratio requirement is based on the level of the School's fund balance, which we calculate at 22% (cash of \$2,632,779 divided by total operating expenses net of depreciation of \$11,836,485). Debt burden ratio is calculated as maximum annual debt service (\$1,793,327) divided by unrestricted operating revenues (\$11,836,485), taken from 2015 financial statements.

	2015	2014	2013
Maximum Annual Debt Service	<u>\$1,793,327</u>	<u>\$1,793,327</u>	<u>\$1,793,327</u>
Unrestricted Operating Revenues	<u>12,461,136</u>	<u>12,124,277</u>	<u>11,533,056</u>
Debt Burden Ratio	14.4%	14.8%	15.5%

20. Operating Margin

Requirement	Measure	Sufficient?
At least 7%	21%	Yes

American Leadership Academy's operating margin requirement of 7% or greater is based on the calculation for days cash on hand (calculated as cash divided by operating expenses multiplied by 365) of 81 days. Operating margin of 21% is calculated by dividing net income available for debt service of \$2,637,648 (see calculation under Debt Coverage Ratio) by total revenues of \$12,461,136.

	2015	2014	2013
Net Income Available for Debt Service	\$2,637,648	\$2,121,796	\$2,047,794
Revenues	12,461,136	12,124,277	11,533,056
Operating Margin	21.2%	17.5%	17.8%

The School has exceeded the operating margin requirement in each of the past three years.

21. Current Ratio

A discussion has been held recently with the School and the School's Financial Advisor concerning whether the amount of debt service payable within one year from outstanding debt should be included in the current ratio calculation as a current liability. In the School's application, long-term debt principal payable within one year was excluded from the current ratio computation. As a result of the discussion, included below are calculations excluding current period long-term debt principal from the equation and also another including current year long-term debt principal in the equation.

	Requirement	Measure	Sufficient?
	At least 150%		
Excluding current year debt payment		186%	Yes
Including current year debt payment		138%	No

The current ratio is defined as current unrestricted assets divided by current liabilities.

Including Current Year Long-term Debt Payment	2015	2014	2013
Current Assets	\$2,816,381	2,306,605	1,865,752
Current Liabilities	2,033,605	1,978,372	1,918,673
Current Ratio	138%	117%	97%

Excluding Current Year Long-term Debt Payment	2015	2014	2013
Current Assets	\$2,816,381	2,306,605	1,865,752
Current Liabilities	1,510,857	1,498,643	1,468,768
Current Ratio	186%	154%	127%

Bond Documents

20-23. ALA's legal bond documents have been reviewed by Chapman and Cutler in their capacity as bond counsel to the Authority, and all requirements have been incorporated. In addition, Ballard Spahr, as bond counsel to American Leadership Academy, has confirmed that each of the required legal provisions is present in the bond documents.