THE BOND BUYER

NABL paper examines bond-financing of charter schools

By

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Published

September 30, 2020, 2:15 p.m. EDT

“I would characterize it as a guide to some big picture items you’d definitely want to keep an eye out for,” said Kareem Spratling, an attorney at Bryant Miller Olive P.A. in Tampa who serves as vice chairman of NABL’s General Law and Practice Committee. ***Courtesy of Bryant Miller Olive P.A.***

The National Association of Bond Lawyers has released a new paper on bond financing laws for charter schools that highlights how the enabling laws vary sometimes significantly by state.

Nationally, there are around 7,500 charter schools in 44 states in addition to the District of Columbia, according to the National Alliance for Public Charter Schools.

“I would characterize it as a guide to some big picture items you’d definitely want to keep an eye out for,” said Kareem Spratling, an attorney at Bryant Miller Olive P.A. in Tampa who serves as vice chairman of NABL’s General Law and Practice Committee.

The NABL paper is more of a guide to high level issues that need to be considered rather than a comprehensive checklist of this growing part of the public finance sector.

“It’s for those who perhaps have done other 501(c)3 deals and not done charter school deals,” Spratling said. “It’s a refresher for those people who can look at it and say, ‘I’d better look at this issue or that issue.’”

Charter schools have issued roughly $25 billion in bonds over the last decade compared to around $1 trillion issued by traditional school districts, according to an estimate by the National Alliance for Public Charter Schools.

Only about 17% of charter schools, or fewer than 1,300, have bond ratings.

“Unlike school districts, most charter schools cannot issue tax-exempt debt on their own behalf, and must use a conduit issuer to issue the tax-exempt bonds benefiting the charter school,’’ the NABL paper said. “Not all conduit issuers have the legislative authority to issue tax-exempt bonds benefiting charter schools, but many states have enacted legislation to establish new entities with the authority to issue tax-exempt bonds to finance charter school facilities or authorize existing entities to issue tax-exempt bonds to finance charter school facilities.”

The vast majority of the rated charter schools -- about 1,200 -- are rated by S&P Global, which has rated around 300 charter operators, some of which have a string of schools they run.

Moody’s Investors Service rates around 58 charter schools and Fitch Ratings only rates eight charter schools.

Leonard Jones, manager of the charter school group at Moody’s, said his agency’s rating methodology was issued in 2016.

S&P Global has been active in the charter school sector much longer.

“There has been a lot of growth in that market, as charter schools have grown as new charter schools have opened,” said Jessica Wood, a senior director at S&P’s U.S. Public Finance Ratings Group and sector leader for the not-for-profit higher education and charter school groups.

“While charter schools are public schools and rely on public state funding, just like traditional school districts, charter schools do not receive funding for capital plans for building,” Wood said.

S&P has issued only around a dozen charter school ratings this year and another dozen last year compared to other recent years when the number was around 40.

“Ratings for traditional school districts are much higher,” said Wood. “And while both traditional school districts and charter schools both depend on per pupil funding, school districts maintain higher reserves, more funding and can levy taxes.”

S&P also rates about 40 independent private schools which are typically rated much higher than charters.

“Those are some of the very high profile well known private high schools around the country,” Wood said. “The big difference is that while the private schools don’t get any state funding at all, they depend on fundraising and the much higher cost of tuition.” They also tend to have much stronger reserves and balance sheets as well as significant endowments.

At S&P, charter ratings can be as high as A+, although none are higher than A-minus. In comparison, colleges and universities, independent private schools, and traditional K-12 public schools can be as high as AAA.

The National Alliance for Public Charter Schools says that charter schools are at a disadvantage in trying to finance their facilities even though they operate as tuition-free public schools.

“They do not receive comparable public funds to pay for their facilities and have to use operating funds to pay for capital improvements,” said Mark Medema, managing director of the Charter School Facility Center at the alliance.

“Charter schools also have to borrow at higher rates than their school districts,” Medema said, urging policymakers “to level the playing field for charter schools and their traditional school district counterparts.”

One positive development is that several investment firms have emerged in recent years that either specialize in purchasing charter school bonds or have high yield bond departments that do. Among them: Tortoise Capital Advisors, Greenwich Investment Management, Hamlin Capital Management, ESJ Capital Partners and Equitable Facilities Fund.

Equitable Facilities Fund published a report in mid-2019 pointing to a $357.1 million offering sold by BB&T in December 2018 on behalf of International Leadership of Texas (ILT), a 33 school charter network with more than 18,000 students, as the largest single charter school debt offering to date.

On the downside, the NABL paper points out that some state charter school laws limit, restrict, or forbid charter schools from pledging their revenue stream to pay bondholders.

“There’s a lot of state law and even local diligence to get a deal done,” Spratling said.

However, a number of states have provided mechanisms for debt financing and the schools have used a number of different ways to raise capital, according to a white paper by the Council of Development Financing Authorities.

At the federal level, the Department of Education operates the Credit Enhancement for Charter School Facilities program. The program provides grants to eligible entities, typically nonprofit intermediary community lending entities like CDFIs to help them enhance the credit of charter schools to help gain access to capital.

Arizona charter schools can apply for tax-exempt bond financing from industrial development authorities. Charter schools in South Carolina have access to tax-exempt financing through the South Carolina Jobs-Economic Development Authority. In Georgia, charter schools can use a local county development authority.

The CDFI report also cited examples of charter schools using financing packages that include Tax Increment Financing (TIF), Property Assessed Clean Energy (PACE), the federal New Markets Tax Credit, the federal Historic Preservation Tax Incentives program and even the EB-5 investment program granting a conditional green card to wealthy immigrant investors.

Around 13 states operate Revolving Loan Fund programs to help finance charter schools. Among them: California, Florida, Illinois, Louisiana, Nevada, South Carolina, Utah, and the District of Columbia.

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