

Unique financing package helps charter school grow

Local academy's use of tax credits, bonds could be model for others.

An innovative financial package that allowed a Milwaukee charter school to expand could serve as a model for charter schools across the country.

In April, the Academy of Learning and Leadership completed \$11 million in New Markets Tax Credit and tax-exempt bond financing for its school at 1530 W. Center St. in Milwaukee.

The money will allow the school to build and equip a second 24,000-square-foot building, refinance the mortgage on the existing 20,000-square-foot building and acquire additional land for future expansion.

Academy of Learning and Leadership, 1530 W. Center St. in the city's impoverished Lindsay Heights neighborhood, began enrolling students in the fall of 2003. Last year's enrollment totaled 270, and the expansion will allow it to enroll a total of 475 students, said Camille Mortimore, ALL's founder.

The school is only one of a handful of entities to combine tax-exempt bonds with New Markets Tax Credits and the first charter school, experts believe.

The financing package not only provides lower than market rate financing for the Academy of Learning and Leadership, it also will provide the school with instant equity after seven years, said Mike Ostermeyer, a partner at Quarles & Brady L.L.P. and head of the real estate practice in the firm's Milwaukee office. Quarles & Brady represented the academy in the deal as well as A.G. Edwards & Sons, the underwriter of the tax-exempt bonds.

"It was a very powerful result for a non-profit borrower who's trying to do something really catalytic in a distressed area," Ostermeyer said.

"It's really put us on a firm footing financially," Mortimore said.

Here's how the financing works:

The Redevelopment Authority of the City of Milwaukee issued \$7.8 million in tax-exempt bonds underwritten by A.G. Edwards. The interest rate on the bonds is between 5.5 and 5.625 percent.

There also are two taxable "tails" totaling \$850,000. They help cover the cost of issuing the bonds and had an interest rate of roughly 7.5 percent.

The remaining \$2.5 million of the project is financed with an equity investment from investor Morgan Stanley, which then received the New Markets Tax Credits.

The tax credits are intended to provide a catalyst for development in qualified low-income areas, Ostermeyer said.

Investors receive a tax credit equal to 39 percent of their investment over seven years.

Federal regulations require the money to pass through an intermediary called a Community Development Entity. A Community Development Entity was created solely for this deal.

Both the equity investment and the bond proceeds were passed through this single-purpose entity, which allowed Morgan Stanley to receive a 39 percent tax credit on the entire \$11 million.

After the tax credit is fully recognized in seven years, Academy of Learning and Leadership can buy Morgan Stanley's interest in the Community Development Entity for an agreed-upon amount of \$80,000.

That means the school will essentially be the collector of its remaining \$1.7 million debt on the equity investment, Ostermeyer said.

That gives the school instant equity in its building, he said.

BENEFITS TO BORROWER

“The economic benefit to the borrower was pretty dramatic,” he said.

It’s challenging for charter schools to find financing, because they usually don’t have enough collateral to get conventional loans, Ostermeyer said.

Many charter schools have used tax-exempt bonds, he said. Charter schools are financed with per pupil payments from the state, so they have the steady income that bond holders like to see, he said. But they don’t have upfront money to pay for their facilities, so most have to start out small.

“The capital markets have shown a real appetite for charter school credit, and that’s been helpful,” he said.

The academy initially looked at tax-exempt bond financing alone, but its revenue stream was not quite sufficient to cover the required debt service ratio, he said.

Combining the tax-exempt bonds with the tax credits reduced the effective rate of borrowing and created the equity, which made the school’s financial picture more attractive to bond investors, he said.

Since the academy’s deal closed, there has been increased interest from others in using the mechanism.

John Buck, principal of Buck Financial Advisors L.L.C. in Englewood, Colo., is talking with several other schools that are interested in it.

Buck worked on the ALL deal and works with charter schools to help them find financing.

“New Markets Tax Credits are sort of another arrow in that quiver where it’s helping projects that would otherwise have a hard time getting financing,” he said. “The bond market, once it understood the project, like the fact that there is other capital in addition to the bond financing that’s going into the project.”

Schools will like not having to fully repay the loan, he said.

“I do see this happening more and more,” he said.

The academy is attached to the LaVarnway Boys and Girls Club and has a 99-year lease with the club for the property on which the building sits. The school is part of a network of 143 Expeditionary Learning schools that use experiential learning.

The school uses the Boys and Girls Club facility throughout the school day and children can go to the club when school ends.

The second building will house a second elementary school. The academy wants to create small units to maintain an intimate environment to help students who need significant support and special care, Mortimore said.

The academy hopes to build a third building for a high school in three to four years, although it will have to alter its charter to add a high school.

The money will allow the academy to acquire additional property in the neighborhood for the third building, develop two outdoor classrooms and expand parking.

The academy’s expansion should also be beneficial to the Lindsay Heights neighborhood, Mortimore said. That was part of her goal when she looked for a place to start the school.

“Our goal continues to be neighborhood revitalization,” she said.