



STATE OF ARIZONA
OFFICE OF THE GOVERNOR

DOUGLAS A. DUCEY
GOVERNOR

EXECUTIVE OFFICE

DATE: April 20, 2017

TO: Credit Enhancement Eligibility Board

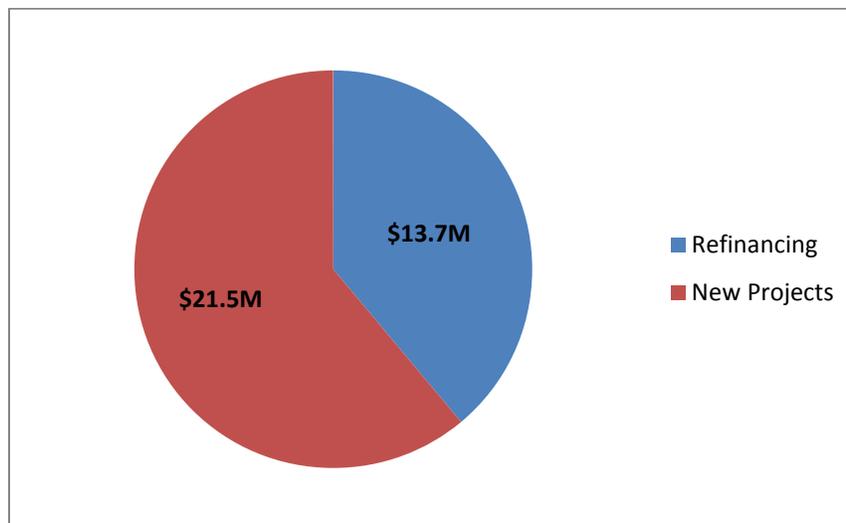
THRU: Dawn Wallace, Director, Governor's Office of Education

FROM: Charlie Martin, Senior Analyst, Governor's Office of Strategic Planning and Budgeting

SUBJECT: Academy of Math and Science – Application for the Public School Credit Enhancement Program

Summary of the Request

The Academy of Math and Science (AMS) has jointly applied as an Achievement District School and for participation in the Public School Credit Enhancement Program with a \$35.2 million proposed financing. In summary, AMS requests \$13.7 million for refunding of existing debt and \$21.5 million for new facilities construction and/or expansion (see Impact of Proposed Funding).



Based on staff review, AMS meets the requirements to qualify as an Achievement District School and for conditional approval for the Public School Credit Enhancement Program. However, the proposed financing is significantly larger than was anticipated for an individual financing and guaranteeing the total amount could negatively impact the enhanced credit rating assigned to all program participants.

Additionally, AMS has disclosed a personal benefit from the proposed financing (see Additional Considerations).

Recommendation

The Board has the following two options regarding AMS's application as an Achievement District School:

1. Approval as an Achievement District School (**Staff recommendation**)
2. Denial of the application to qualify as an Achievement District School

If the Board does not approve the Achievement District application, AMS is not eligible for the Public School Credit Enhancement Program. If the Board approves the application, the following three options are available for the Board to consider:

1. Approval of credit enhancement for the full amount of the proposed financing of \$35.2 million
2. Approval of credit enhancement for an amount that is less than the full amount of the proposed financing (**Staff recommendation**)
 - a. The amount that is proposed to be used for new projects, excluding purchase of existing buildings, is between \$17 million and \$20 million
 - b. The average size of an enhanced financing was assumed to be \$10 million in initial credit rating agency review of the program
3. Denial of credit enhancement for any portion of the proposed financing

Note: Final Board approval of credit enhancement is subject to the AMS' execution of the Terms and Conditions Agreement and Reimbursement Agreement prior to the issuance of a Fund Certificate, which will confirm the guarantee of timely payments of principal and interest on the financing.

Analysis

Applicant Overview

AMS operates three charter schools. Two are located in Tucson, the Academy of Math and Science (AMS Prince) and Math and Science Success Academy (MASSA). One is located in Phoenix, the Academy of Math and Science (AMS Camelback). The three locations currently enroll a total of 1,452 students. AMS has indicated that the schools provide standards-based instruction to exceed Arizona standards, as well as science, technology, math, and engineering (STEM) curriculum and a variety of non-core classes and extracurricular activities. According to the application, the AMS schools have received numerous awards including: 2016 Arizona Charter School of the Year, National Blue Ribbon Award, EPIC Gold Gain Award, and Education Equality Index recognition. In addition, AMS has indicated that their schools outperform peers in the same geographic area and peers that serve a similar percentage of students that are eligible for free or reduced-price lunch.

Application Details:

Date Received: 3/23/2017

Date Complete: 4/13/2017

Deadline to Approve/Deny: 6/12/2017

Applicant Contact: Kim Chayka, Co-CEO
Applicant Contact: Steven Hykes, CFO

Borrower's Counsel: Terry Warren, Warren Charter Law
Bond Counsel: Brigitte Green, Greenberg Traurig
Underwriter Contact: John Snider, RBC Capital Markets
Bond Issuer: Arizona Industrial Development Authority

Achievement District Qualification

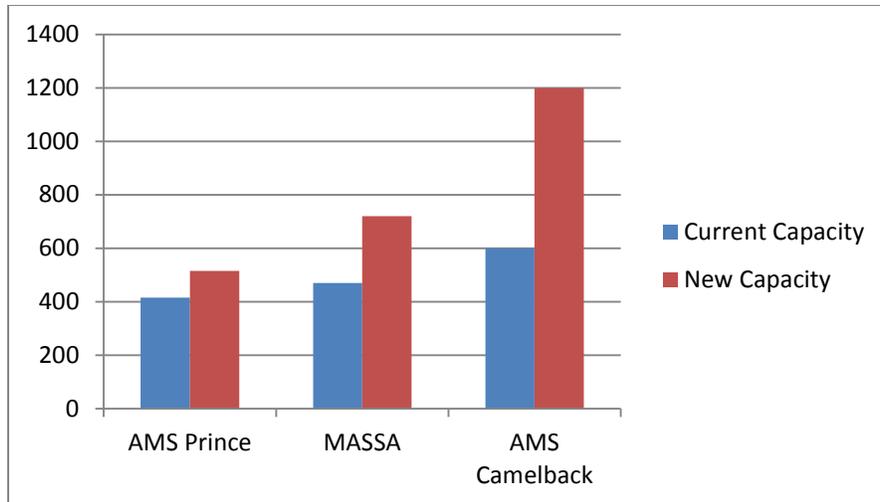
ARS § 15-2141 establishes criteria that an applicant must meet to qualify as an Achievement District School. Based on the review of documents provided by AMS in their application, AMS has met the criteria established in statute.

Requirement	AMS
Assigned a letter grade of A, or an equivalent successor classification	Verified
Proven instructional strategies and curricula that demonstrate high academic outcomes	Materials Provided
Verifiable enrollment demand, including the placement of prospective pupils on a waiting list	Attestation
Sound financial plan that contemplates operational costs and future enrollment growth	Financial Documents
Commitment to provide technical assistance to an underperforming school	Letter Submitted

As of March 23, 2017, AMS reports a wait list of 1,452 potential students that is expected to grow to 2,384 by July 2017. Additionally, AMS has partnered with Phoenix Collegiate Academy, an underperforming charter school in south Phoenix, to provide assistance with finance and school governance. AMS reported that the percentage of students that qualify for free or reduced-price lunch ranges from 71.5% to 95.9% at the applicant's three locations.

Impact of the Proposed Financing

AMS anticipates that the proposed financing will expand student capacity by 950 students. The proposed financing includes refinancing of \$13.2 million of existing debt. New construction and expansion projects funded by new debt include \$5.3 million at the AMS Camelback location to add 17 new classrooms; \$7.6 million at the MASSA campus to build 16 new classrooms and to expand the capacity of existing classrooms by 3 students each; and \$5.3M at the AMS Prince location to build 9 classrooms, expand the capacity of existing classrooms by 3 students each, and to build related facilities (gymnasium, cafeteria, play space, and administrative space). AMS indicated that savings from the refinancing will be used to add instructional staff and to fund start-up costs related to the school's expansion. The financing also includes \$1.1 million to purchase existing buildings that will not be expanded or renovated, \$1.4 million for debt service reserve funds, and \$1.3 million for financing costs.



Eligibility for Credit Enhancement

ARS § 15-2155 requires that applicants provide proof as an Achievement District School, show sustainability of financial operations, provide information about the financing proposed to be guaranteed, and identify any property being pledged as collateral. Charter school applicants are additionally required to demonstrate experience in operating and managing charter schools and acknowledge that the financing will include a debt service reserve fund that is equal to at least the maximum amount permitted by federal law.

AMS' proposed financing meets Board criteria for conditional approval for credit enhancement and compliance with the Terms and Conditions Agreement and Reimbursement Agreement will ensure that all program requirements are met. While AMS does not have an existing credit rating, an underlying credit rating of BB is expected to be assigned to the proposed financing. This is the 12th highest credit rating and is two ratings below what is considered to be an investment grade rating (BBB- or higher). The majority of charter schools that have an underlying credit rating are rated BB, BB+, BBB-, or BBB.

Impact on Credit Enhancement Program

The approval of any individual financing affects the Arizona Public School Credit Enhancement Program's capacity to enhance future financings, compliance with statutory ratios, and potentially the enhanced credit rating assigned to current and future financings.

If the proposed financing is approved as submitted, approximately 10% of the program's total capacity will be used to enhance the financing.

ARS § 15-2155 requires that the Board ensure that the program leverage ratio, which is the ratio of the principal amount of guaranteed financings to the amount on deposit in the Arizona Public School Credit Enhancement Fund, not exceed 3.5 to 1. It also requires that, upon the guarantee of 10 enhanced financings, not more than 25% of the aggregate principal amount of guaranteed financings have an underlying, or unenhanced, credit rating of B+ or lower. If the full amount of the proposed financing is approved for credit enhancement, the program will remain in compliance with the maximum program

leverage ratio. While the Board will have not yet approved 10 financings, the applicant is expected to have a credit rating of BB- or higher and should not negatively affect compliance with the second ratio.

The Board should also consider the impact of approving the proposed financing on the enhanced credit rating assigned to current and future financings. The higher the enhanced credit rating assigned to guaranteed financings, the greater the benefit of the program to participants. The assumptions made by rating agency Standard and Poor's in an initial review of the program included that the program would have approximately 35 participants with an average enhanced financing of \$10 million each. The applicant's proposed financing is significantly larger than the average financing assumed in the rating analysis.

Additional Considerations

The applicant has disclosed that about 1% of the borrowed funds will be used to buy office property that is owned by Tatayana Chayka and Edward Chayka. Tatayana Chayka is the founder and CEO of the Academy of Math and Science. The disclosure relates to \$425,000 that would be used to purchase 3448 N 1st Avenue and an adjacent property. The property at 3448 N 1st Avenue is owned by CAT Investment Properties, LLC, which the applicant's audited financial statements identify as a related party with common members on the board of directors or common management.

Additionally, about \$2 million of the proposed financing will be used to renovate property at the AMS Prince location that is not owned by the school itself. The application identified the property as owned by Seta Properties LLC, which the applicant's audited financial statements identify as a related party with common members on the board of directors or common management.