

**CALIFORNIA EDUCATIONAL FACILITIES AUTHORITY
BOND FINANCING PROGRAM**

EXECUTIVE SUMMARY

<p>Applicant: Pepperdine University (“Pepperdine”) 24255 Pacific Coast Highway Malibu, CA 90263 Los Angeles County</p> <p>Facility Type: Private University</p> <p>New Project Site: Malibu, CA</p> <p>Accreditation: Western Association of Schools and Colleges</p>		<p>Amount Requested: \$50,000,000</p> <p>Date Requested: April 26, 2012</p> <p>Resolution Number: 289</p>														
<p>Use of Proceeds: Bond proceeds will be used to refund all or a portion of the CEFA Series 2003A bonds, as well as to finance capital improvements on the Malibu campus, including but not limited to renovations of the Thornton Administration Center, renovations and construction of student residences, and renovations to parking facilities and other existing structures.</p>																
<p>Type of Issue: Negotiated public offering, fixed rate, \$1,000 minimum denominations.</p> <p>Credit Enhancement: None</p> <p>Expected Credit Rating: Aa3 (Moody’s)</p> <p>Financing Team: <i>Please see Exhibit 1 to identify possible conflicts of interest</i></p>																
<p>Environmental Benefits: Benefits expected from the completion of these university infrastructure projects include the elimination of potentially hazardous materials from multiple student living spaces and increased campus energy efficiency resulting from upgraded lighting and climate conditioning components.</p>																
<p>Financial Overview: Pepperdine’s modest growth in its revenue base, coupled with positive changes in non-operating activities, has generated improved and positive operational and overall results. Pepperdine’s balance sheet reflects stability in assets, good debt service coverage levels, and continued positive liquidity.</p>																
<p><u>Estimated Sources of Funds:</u></p> <table> <tr> <td>Par Amount of Bond</td> <td align="right">\$50,000,000</td> </tr> <tr> <td>Original Issue Premium</td> <td align="right"><u>7,392,560</u></td> </tr> <tr> <td>Total Sources</td> <td align="right"><u>\$57,392,560</u></td> </tr> </table>		Par Amount of Bond	\$50,000,000	Original Issue Premium	<u>7,392,560</u>	Total Sources	<u>\$57,392,560</u>	<p><u>Estimated Uses of Funds:</u></p> <table> <tr> <td>Refunding</td> <td align="right">\$46,115,701</td> </tr> <tr> <td>Project Fund</td> <td align="right">10,649,903</td> </tr> <tr> <td>Financing Cost</td> <td align="right"><u>626,956</u></td> </tr> <tr> <td>Total Uses</td> <td align="right"><u>\$57,392,560</u></td> </tr> </table>	Refunding	\$46,115,701	Project Fund	10,649,903	Financing Cost	<u>626,956</u>	Total Uses	<u>\$57,392,560</u>
Par Amount of Bond	\$50,000,000															
Original Issue Premium	<u>7,392,560</u>															
Total Sources	<u>\$57,392,560</u>															
Refunding	\$46,115,701															
Project Fund	10,649,903															
Financing Cost	<u>626,956</u>															
Total Uses	<u>\$57,392,560</u>															
<p>Legal Review: No information was disclosed to question the financial viability or legal integrity of the Applicant.</p>																
<p>Staff Recommendation: Staff recommends the Authority approve Resolution No. 289 in an amount not to exceed \$50,000,000 for Pepperdine University subject to a bond rating of at least investment grade by a nationally recognized rating agency. Macias Gini & O’Connell, LLP, the Authority’s financial analyst, and Public Financial Management, the Authority’s financial advisor, concur with the Authority’s staff recommendations.</p>																

STAFF SUMMARY AND RECOMMENDATION

Pepperdine University (“Pepperdine”)

April 26, 2012

Resolution Number: 289

I. PURPOSE OF FINANCING: Pepperdine is seeking financing to fund several improvement projects on the main campus in Malibu, CA, and to refund all or a portion of their debt for a net present value savings of approximately \$10.7 million or 23.8%, under existing market conditions.

Refunding \$46,115,701

Pepperdine plans to refund all or a portion of the CEFA Series 2003A bonds. The outstanding balance, which is approximately \$45,000,000, was originally approved for issuance by the CEFA board for that same amount in February of 2003. Those bonds were originally issued to finance the refunding and defeasance of the CEFA Series 1993 A bonds and the CEFA Series 1994 bonds, and the partial refunding of the CEFA 1999 Series B bonds.

Project Fund..... 10,649,903

Pepperdine is addressing the need to renovate, upgrade and equip many of its aging facilities, including student residences, the Thornton Administration Center, the Drescher Graduate Campus, and the Smothers Theatre. These improvements will include but are not limited to the following:

- Grounds and Landscape: landscape mitigation and remediation for mudslide hazard, upgrading of stairs, walkways and handrails, repair of natural gas pipelines, road and parking lot maintenance;
- Facilities: multiple roofing repairs, upgrading of furnishings, exterior repairs, replacing of an emergency power generator; storage area fire code compliance work;
- Residences: refurbishment of multiple residences, roofing repairs, replacement of heaters, replacement of boilers and heat exchangers, enhancement of energy controls and electric vault improvements, installation of pony chiller.

Environmental Benefits:

Pepperdine is committed to advancing the sustainability in design, construction, and operation of campus facilities. The environmental benefits include:

- Elimination of potentially hazardous materials from existing spaces;
- Upgraded lighting and heating/air conditioning components;
- Replacement of chillers / boilers.

Financing Costs	<u>626,956</u>
Cost of Issuance	\$303,682
Underwriter's Discount	<u>324,274</u>
<i>TOTAL USES OF FUNDS</i>	<u>\$57,392,560</u>

II. PROPOSED COVENANTS, SECURITY AND DISCLOSURES:

Executive summary and recommendations include minimum requirements. Additional or more stringent covenants or disclosures may be added following consultation with Authority staff but without further notification to the Authority's Board. These covenants cannot be diluted or removed without subsequent review. If there have been modifications to the covenant proposal following the preparation of this executive summary, staff will report it at the meeting.

After reviewing Pepperdine's credit profile, including its current financial profile, prior bond transactions and considering what the market will support, the financing team has concluded that the covenants listed below align the interests of Pepperdine, the Authority, and the investors and therefore are appropriate to this transaction. The financing team notes that these covenants contain necessary tax and legal covenants that are consistent with those that have applied to Pepperdine's prior bond transactions and Pepperdine's current financial situation does not suggest that additional covenants should be required.

- ✓ **Unconditional Promise to Pay.** *Borrower agrees to pay Trustee all amounts required for principal and interest and other payments and expenses designated in the Loan Agreement. All Revenues¹ and any other amounts held in a designated fund or account under the Bond Indenture are pledged to secure the full payment of the bonds.*
- ✓ **Limited Permitted Encumbrances.** *Borrower is subject to a restrictive set of allowable encumbrances it may incur pursuant to the Loan Agreement.*
- ✓ **Comply with SEC Rule 15c2-12.** *The rule prohibits underwriters from underwriting municipal bond deals unless the issuer or borrower contractually agrees to disclose designated financial and operating information to the marketplace during the life of the bonds and to report designated events such as missed debt service payments, any change in bond ratings, defeasance, redemptions, etc.*

Staff has reviewed the entirety of this financing package and finds it to be acceptable.

¹Capitalized terms are defined in the Indenture.

III. FINANCIAL ANALYSIS:

Pepperdine University
Statement of Activities
 Unrestricted (\$000's)

	Year Ended July 31,		
	<u>2011</u>	<u>2010</u>	<u>2009</u>
Revenues:			
Net tuition and fees	\$ 184,553	\$ 177,451	\$ 175,019
Sales and services of auxiliary enterprises	6,800	6,286	6,760
Government grants and contracts	3,602	3,310	3,500
Private grants, gifts, and bequests	13,622	11,832	10,435
Endowment support	31,377	31,257	30,103
Room and board	31,821	31,483	30,505
Other	3,953	4,657	4,905
Net assets released from restrictions	3,529	1,408	2,329
Total revenues	<u>279,257</u>	<u>267,684</u>	<u>263,556</u>
Expenses:			
Instructional and departmental research	82,314	78,980	81,248
Auxiliary enterprises	19,802	18,037	19,740
Academic support	48,055	44,688	46,762
Student services	46,590	45,203	44,923
Public service	14,895	14,430	14,383
Management and general	48,637	44,008	49,897
Fund-raising activities	7,699	7,550	7,243
Membership development	1,989	1,836	1,833
Total expenses	<u>269,981</u>	<u>254,732</u>	<u>266,029</u>
Increase in net assets from operations	9,276	12,952	(2,473)
Non-operating activities:			
Investment income	15,764	13,292	14,503
Investment expenses	(2,991)	-	-
Other changes	6	(4,165)	(3,884)
Appropriations from endowment	-	-	(26,832)
Net realized and unrealized investment gains	32,367	13,844	(126,809)
Cumulative effect of change in accounting principle	-	-	(33,939)
Change in net assets	54,422	35,923	(179,434)
UNRESTRICTED NET ASSETS, BEGINNING OF YEAR	<u>521,281</u>	<u>485,358</u>	<u>664,792</u>
UNRESTRICTED NET ASSETS, END OF YEAR	<u>\$ 575,703</u>	<u>\$ 521,281</u>	<u>\$ 485,358</u>

Pepperdine University
Statement of Financial Position (000's)

	As of July 31,		
	2011	2010	2009
ASSETS:			
Cash and cash equivalents	\$ 50,172	\$ 54,479	\$ 44,650
Accounts receivables, net	6,660	10,657	9,408
Contributions receivable, net	27,752	37,644	25,853
Inventories, prepaid expenses, and other assets	5,459	5,905	5,717
Student loans receivable, net	24,513	25,960	27,244
Investments	779,682	691,075	658,995
Assets held as trustee or agent	121,656	111,185	104,987
Property, facilities, and equipment, net	346,678	345,898	334,502
Total assets	\$ 1,362,572	\$ 1,282,803	\$ 1,211,356
LIABILITIES AND NET ASSETS:			
Accounts payable and accrued liabilities	\$ 23,801	\$ 28,934	\$ 36,703
Accrued salaries and wages	3,216	3,099	3,067
Deposits, advance payments and deferred revenue	8,613	9,916	9,859
US government-funded student loans	14,685	14,393	14,126
Trust and agency obligations	72,198	70,771	67,794
Long-term obligations	226,978	227,172	226,734
Total liabilities	349,491	354,285	358,283
Net assets:			
Unrestricted	575,703	521,281	485,358
Temporarily restricted	132,378	119,064	104,701
Permanently restricted	305,000	288,173	263,014
TOTAL NET ASSETS	1,013,081	928,518	853,073
TOTAL LIABILITIES AND NET ASSETS	\$ 1,362,572	\$ 1,282,803	\$ 1,211,356

Financial Ratios

	Proforma			
	FYE 7/31/11 (a)	2011	2010	2009
Debt service coverage (x)	2.56	3.50	1.58	0.57
Debt to expendable net assets (x)	0.33	0.32	0.35	0.38
Expendable net assets to operations (x)		2.62	2.51	2.22
Margin		3%	5%	(1%)

(a) Recalculates FY 2011 results to include the impact of this proposed financing

Financial Discussion:

Pepperdine's modest growth in its revenue base, coupled with positive changes in non-operating activities, has generated improved and positive operational and overall results.

Pepperdine has posted improved operating results over the review period. Total revenues have grown from \$263.5 million in FY 2009 to \$279.2 million in FY 2011, a 6.0% increase. This modest increase is the result of growing revenues generated across most of Pepperdine's revenue base. Tuition increases represented the largest dollar value growth, resulting in an approximate 5.4% increase in net tuition and fees, from \$175 million in FY 2009 to \$184.5 in FY 2011. This increase is consistent with inflation rates. In addition, increases in government grants and contracts, private grants, gifts, and bequests, endowment support, and room and board also support the growth in Pepperdine's operational results.

Operating expenses totaled \$269.9 million in FY 2011, increasing by approximately \$3.9 million or 1.5% since FY 2009. A \$2.4 million decrease in net assets from operations in FY 2009, the result of budget priorities, was effectively reversed with decreases in FY 2010 expenses. These expenses remain in line with the growth of revenues, which allowed Pepperdine to post positive operating results of approximately \$9.2 million in FY 2011. According to Pepperdine, much of these increases are generally attributable to increases in overall costs of student services, academic support, and instruction and research.

Total end of the year unrestricted net assets experienced a 18.6% increase from the end of FY 2009 (\$485.3 million) to the end of FY 2011 (\$575.7 million), reversing the negative trends experienced in the wake of the financial crisis in FY 2008 and FY 2009.

Pepperdine's balance sheet reflects stability in assets, good debt service coverage levels, and continued positive liquidity.

Pepperdine's financial strength remains solid. Total assets in FY 2011 have increased 12.5% over the three year review period, up from \$1.2 billion in FY 2009 to \$1.3 billion in FY 2011. While several asset categories experienced fluctuations in value over the three year review period, the bulk of assets in investments, assets held as trustee or agent, and net property, facilities, and equipment experienced steady growth in value. Investments have grown by 18.3% over the review period, from \$658.9 million in FY 2009 to \$779.6 million in FY 2011. The majority of these investments are held in Pepperdine's endowment, which has grown 17.7% from \$528.7 million to \$622.6 million over the review period. Pepperdine cites consistent investment performance for this increase after the financial crisis.

Pepperdine is on path to effectively manage its long-term debt, as their debt service coverage ratio has risen to 3.5x in FY 2011 from 1.58x in FY 2010. In FY 2011, Pepperdine had over \$219 million in long-term debt as compared to over \$1 billion in total net assets. With this proposed financing, Pepperdine's proforma debt service coverage ratio is an acceptable 2.56x.

Pepperdine anticipates they will continue to generate positive financial results due to its continued healthy endowment and investment performance, diversified revenue base, and student demand. According to Pepperdine, they are positioned to continue meeting its additional long-term debt obligations.

IV. BACKGROUND:

General:

Pepperdine University (“Pepperdine”) is an independent private university originally established as Pepperdine College in 1937 by Mr. George Pepperdine, the founder of Western Auto Supply Company. Pepperdine achieved its university status in 1970 with the addition of its graduate and professional schools and became known as Pepperdine University. Pepperdine opened its current Malibu campus in 1972, and currently enrolls approximately 7,500 students in its five colleges and schools. Seaver College, Pepperdine’s undergraduate liberal arts college, the School of Law, and the School of Public Policy are headquartered on 830 acres in the Santa Monica Mountains overlooking the Pacific Ocean in Malibu, California. The Graduate School of Education and Psychology and the George L. Graziadio School of Business and Management are headquartered at Pepperdine’s West Los Angeles, California campus. The Drescher Graduate Campus has provided permanent facilities for the Malibu-based programs of these schools, as well as the School of Public Policy. In addition to the graduate courses taught at the Malibu campus, graduate courses are taught at the West Los Angeles Campus and at four other educational centers in Southern California. Pepperdine also offers educational programs in facilities it owns in Heidelberg, Germany, London, England, Florence, Italy, Buenos Aires, Argentina, Lausanne, Switzerland, and Washington, D.C. Additionally, the University offers educational programs in leased facilities in Shanghai, China.

Administration:

Pepperdine is governed by a maximum 40-member self-perpetuating Board of Regents currently composed of 38 elected, voting members including the President of the University. The Bylaws require that a majority of the Regents in office, a majority of the Executive Committee, the President of the University, and the Chairman of the Board of Regents shall be members of the Churches of Christ. Members of the Board are typically elected for three-year terms. Approximately one-third of the membership is elected annually. The full Board meets four times each year.

Accreditations:

Pepperdine is accredited by the Accrediting Commission for Senior Colleges and Universities of the Western Association of Schools and Colleges (“WASC”), the primary accrediting body for institutions of higher education in the western United States. The last WASC accreditation review was completed in 2000 and resulted in a reaffirmation of Pepperdine’s accreditation. The School of Law is accredited by the American Bar Association and holds membership in the Association of American Law Schools. The Graziadio School of Business and Management is accredited by the Association to Advance Collegiate Schools of Business. The Graduate School of Education and Psychology receives accreditation for both teacher credentialing and doctoral study in psychology. The American Psychological Association accredits the doctoral program in psychology. The California Commission on Teacher Credentialing accredits Pepperdine’s education programs.

Academic Programs:

Pepperdine is comprised of five colleges and schools in Southern California. Seaver College, the School of Law, the Graduate School of Education and Psychology, the Graziadio School of Business and Management, and the School of Public Policy are located on the University’s 830-acre campus overlooking the Pacific Ocean in Malibu. Courses are taught in Malibu, at four graduate campuses in Southern California, permanent program facilities in Washington, D.C., and at international campuses in Germany, England, Italy, Switzerland, Argentina, and China.

- Seaver College is Pepperdine’s college of letters, arts and sciences offering an interdisciplinary curriculum that provides students with a broad and comprehensive

education. With its academic program organized into eight major divisions, Seaver College offers the baccalaureate degree in over 38 fields of study, teaching credential programs in two fields of study, and the master's degree in nine fields of study.

- The School of Law offers a full range of courses dealing with federal, state, and international law, leading to the Juris Doctor or the L.L.M., Dispute Resolution degrees. Additionally, the School of Law offers several Juris Doctor joint degrees.
- The George L. Graziadio School of Business and Management focuses on the development of managers for business, government, and education, and offers graduate and undergraduate degree programs for full-time students and working adults. The school offers several degrees to its students including the Master of Business Administration.
- The Graduate School of Education and Psychology offers masters and doctoral degrees in the education and psychology fields of study, with a total of ten available academic programs.
- The School of Public Policy offers a Master of Public Policy degree along with several joint degree programs in law, business administration, and dispute resolution. It also houses a research and special program division called the Davenport Institute.

V. OUTSTANDING DEBT (\$000's):

<u>Issue:</u>	<u>Original Issue Amount</u>	<u>Amount Outstanding as of 07/31/11</u>	<u>Estimated Amount Outstanding After Proposed Financing</u>
Existing Debt:			
CEFA, 2003A	\$ 45,000	\$ 45,000	\$ -
CEFA, Series 2005A	92,365	92,365	92,365
CEFA, Series 2005B	16,340	16,340	16,340
Pepperdine Taxable Series 2009A	50,000	50,000	50,000
I-Bank Series 2010*	15,345	15,345	15,345
Proposed:			
CEFA, Series 2012		<u>50,000</u>	<u>\$ 50,000</u>
Total		<u>\$ 219,050</u>	<u>\$ 224,050</u>

*"I-Bank" = California Infrastructure and Economic Development Bank

VI. DUE DILIGENCE:

Due diligence has been completed with regard to the following items:

- Religious Due Diligence
- Legal Review
- Compliance with Section 94212(b) of the Education Code – California Environmental Quality Act
- Iran Contracting Act Certificate

VII. STAFF RECOMMENDATION:

Staff recommends the Authority approve Resolution No. 289 in an amount not to exceed \$50,000,000 for Pepperdine University subject to a bond rating of at least investment grade by a nationally recognized rating agency. Macias Gini & O'Connell, LLP, the Authority's financial analyst, and Public Financial Management, the Authority's financial advisor, concur with the Authority's staff recommendations.

EXHIBIT 1

Financing Team Pepperdine University

Borrower:	Pepperdine University
Agent for Sale:	State Treasurer's Office, Public Finance Division
Issuer's Counsel:	Attorney General's Office
Issuer's Financial Advisor:	Public Financial Management, Inc.
Bond Counsel:	Orrick, Herrington & Sutcliffe LLP
Senior Underwriter:	Morgan Stanley
Co-Underwriter:	Bank of America, Merrill Lynch
Underwriter's Counsel:	O'Melveny & Myers LLP
Borrower's Counsel:	Ropes & Gray
Trustee/Escrow Bank:	The Bank of New York Mellon Trust Company, N.A.
Trustee Counsel:	TBD
Rating Agency:	Moody's Investors Service
Auditor to the University:	PricewaterhouseCoopers
OS/Printer:	RR Donelley Financial