

CALIFORNIA EDUCATIONAL FACILITIES AUTHORITY

EXECUTIVE SUMMARY

<p>Applicant: Heald College ("Heald") 670 Howard Street San Francisco, California San Francisco County</p> <p>Facility Type: Private University (Vocational school)</p> <p>Project Locations: Multiple campuses (see Page 2 for details)</p> <p>Accreditation: Accrediting Commission for Community and Junior Colleges of the Western Association of Schools and Colleges</p>	<p>Amount Requested: \$9,800,000</p> <p>Loan Term: 7 Years</p> <p>Date Requested: February 27, 2003</p> <p>Resolution Number: 206</p>																				
<p>Policy issue: Under CEFA bond issuance guidelines the Authority requests a debt service reserve account and a revenue pledge for private placements. Staff recommends waiving this based on the sufficiency of liquidity as well as satisfactory collateral.</p>																					
<p>Use of Bond Proceeds: Bond proceeds will be used to refinance a mortgage loan, with yearly interest savings of approximately \$200,000 and total interest savings of approximately \$675,000, and to purchase and implement a software package for administrative and student use.</p>																					
<p>Type of Issue: Private placement, Fixed rate</p> <p>Credit Enhancement: None</p> <p>Expected Rating: Unrated</p> <p>Underwriter: None; Placement agent will be Wells Fargo Bank NA</p> <p>Bond Counsel: Hawkins, Delafield & Wood</p>																					
<p>Financial Status: Heald's net asset balance is essentially unchanged in our review period, reflecting break-even operations. The college has experienced a short-term reduction in enrollment and is taking steps to ensure that expenses will be reduced. Heald appears to be able to afford the additional debt and will not be significantly leveraged.</p>																					
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<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 a resolution for an amount not to exceed \$9,800,000 for Heald College, subject to the bonds being privately placed with a qualified institutional buyer, a general obligation pledge, a deed of trust on campus property, and minimum bond denominations of \$100,000.</p>																					

STAFF SUMMARY AND RECOMMENDATION

Heald College (“Heald”)

February 27, 2003
Resolution Number: 206

I. PURPOSE OF FINANCING:

Heald plans to refinance a mortgage loan on its Roseville campus, for total interest savings of approximately \$675,000 over seven years. Heald will also use approximately \$6 million for purchase and implementation of a software package, including modules for the college’s accounting, personnel, and admissions functions as well as for student use.

Refinancing of mortgage loan \$4,800,000

Shortly after moving into this facility in July 1999, Heald exercised its option to purchase the property. Heald paid \$7.8 million, using \$2.3 million remaining funds from the 1999 CEFA bond financing, and obtaining a \$5.5 million mortgage loan. This property, along with Heald’s Stockton facility, will be used to secure this private placement.

Recent appraisals value the Roseville property at \$9,650,000 and the Stockton property at \$4,390,000. The total value of \$14,040,000 produces a loan to value of approximately 70%.

Equipment 6,000,000

Heald will be implementing a PeopleSoft higher-education suite of software. This includes a ‘student module’ (including the admissions, financial aid and academics processes), a finance module (including accounts receivable and accounts payable), and a human resources module.

This software is estimated at \$1.5 million, with \$4.1 million to be spent for implementation, testing, and training, and \$400,000 for an additional computer server. Outlying campuses will gain access via a LAN system already in place.

This software is intended to streamline Heald’s activities and provide a more integrated computing environment for its employees and students. Some inadequacies of the existing system are mentioned in the Financial Discussion, below.

Financing Costs 100,000

Bank placement fee.....25,000
Costs of issuance75,000 _____

TOTAL USES OF FUNDS \$10,900,000

Financing Structure:

- Fixed rate (variable, with swap agreement to fixed), 2010 final maturity using a 20 year amortization
- General obligation pledge
- Private placement with a qualified institutional buyer
- Deed of trust on campus property equal to at least 100% of the bond size
- Minimum denominations of \$100,000

II. FINANCIAL ANALYSIS:

HEALD COLLEGE

Statement of Activities

Unrestricted (000's)

	Fiscal Year Ended May 31,		
	<u>2002</u>	<u>2001</u>	<u>2000</u>
Revenues:			
Tuition	\$ 89,682	\$ 85,019 ⁽¹⁾	\$ 72,386 ⁽¹⁾
Bookstore sales	10,002	11,318	10,045
Government grants	2,850	2,441	1,838
Other income	1,672	1,702	1,861
Gain on sale of facilities and equipment, net	59	572	-
Total revenues	<u>104,265</u>	<u>101,052</u>	<u>86,130</u>
Expenses:			
Instruction	29,900	28,524	23,298
Instructional support	11,675	12,690	9,752
Student services	17,269	16,248	12,499
Student recruiting	10,607	8,608	8,383
Operating and maintenance of facilities	11,880	10,423	9,502
Management and general ⁽²⁾	16,663	12,576	11,674
Bookstore cost of sales	7,738	8,579	7,557
Campus closure costs	-	1,126	-
Total expenses	<u>105,732</u>	<u>98,774</u>	<u>82,665</u>
Unrealized loss on interest rate swap	<u>174</u>	<u>340</u>	<u>-</u>
Increase/(Decrease) in unrestricted net assets	(1,641)	1,938	3,465
UNRESTRICTED NET ASSETS, BEGINNING OF YEAR	44,860	42,922	39,457
Prior period adjustment ⁽¹⁾	<u>(4,373)</u>	<u>-</u>	<u>-</u>
UNRESTRICTED NET ASSETS, END OF YEAR	<u>\$ 38,846</u>	<u>\$ 44,860</u>	<u>\$ 42,922</u>

⁽¹⁾ Reflecting a more conservative to recognizing tuition revenue, net assets were reduced by \$4.4 million (\$2.1 million applicable to fiscal 2001, with the remainder applicable to prior years) and the deferred tuition liability was increased.

⁽²⁾ Included in Management General expenses for 2002 is \$1.7 million in prior year corrections, mostly applicable to 2000 and 2001, and a legal settlement and related legal fees in excess of \$1.0 million.

HEALD COLLEGE
Statement of Financial Position (000's)

	As of May 31,		
	2002	2001	2000
ASSETS:			
Current Assets:			
Cash and cash equivalents	\$ 7,793	\$ 4,901	\$ 7,614
Investments	3,027	526	3,971
Student contracts receivable, net ⁽¹⁾	9,007	8,951	8,246
Other current assets	2,028	2,870	1,981
Total Current Assets	21,855	17,248	21,812
Facilities and equipment, net	56,083	56,826	50,052
Student contracts receivable, long-term	2,552	4,219	3,962
Investments, less current portion	-	1,025	489
Cash reserved for long-term debt	1,009	1,009	1,067
Other assets	713	620	364
TOTAL ASSETS	\$ 82,212	\$ 80,947	\$ 77,746
LIABILITIES AND NET ASSETS:			
Liabilities:			
Current Liabilities:			
Accounts payable and accrued expenses	\$ 5,308	\$ 4,358	\$ 3,832
Accrued salaries and benefits	2,412	3,225	4,406
Long-term debt, current	952	487	482
Unearned tuition	12,625	8,164	6,112
Interest rate swap	538	340	-
Deferred rent	123	-	-
Total Current Liabilities	21,958	16,574	14,832
Long-term debt	19,588	19,371	19,858
Deferred rent, long-term	1,684	-	-
TOTAL LIABILITIES	43,230	35,945	34,690
Net assets:			
Unrestricted	38,846	44,860	42,922
Permanently Restricted	136	142	134
TOTAL NET ASSETS	38,982	45,002	43,056
TOTAL LIABILITIES AND NET ASSETS	\$ 82,212	\$ 80,947	\$ 77,746

⁽¹⁾ The college offers installment contracts to students, with financing charges, for payment of tuition.

Financial Ratios:

	Proforma (a)			
	FYE May 31, 2002	2002	2001	2000
Debt service coverage (x)	2.70	4.27	6.43	9.29
Debt to expendable net assets (x)	0.64	0.53	0.44	0.47
Expendable net assets to operations (x)		0.37	0.45	0.52
Margin (%) ^(b)		-1.6%	1.9%	4.0%

^(a) Recalculates 2002 results to include the impact of this proposed financing. Proforma debt service coverage includes this private placement as well as payments under a new capital lease.

^(b) Excluding prior year corrections and non-recurring expenses, the margin in 2002 is approximately 1.0%. As explained in the Financial Discussion below, 2000 and 2001 appear to be essentially breakeven years.

Financial Discussion:

Heald's net asset balance is essentially unchanged in our review period, reflecting break-even operations.

Heald's net asset balance is essentially unchanged since the beginning of fiscal 2000 reflecting that the college has been operating at a breakeven level, using the more conservative approach that Heald has taken to revenue recognition. This approach resulted in a prior period adjustment in 2002 which reduced net assets by \$4.4 million. Factoring in this adjustment, \$1.7 million of prior period corrections, and non-recurring items (including gains on sales of assets and campus closure costs), indicates that Heald has been essentially operating at breakeven since fiscal 2000.

Operationally, revenues have risen significantly with expenses being kept in check in the three years of our review. Since 2000, tuition revenue has increased by approximately 28% (mostly due to annual tuition fee increases that have increased by 61% since 1998) and total revenue has increased by approximately 24%. Expenses in that same period increased by 28%. The largest component was a \$6.6 million increase in instructional expenses (reflecting the addition of a significant number of faculty), which increased at the same rate as tuition revenues.

Heald would have shown a modest profit for fiscal 2002 if not for entries, totaling \$1.7 million, correcting prior year overstatements resulting from computer system errors. Also in fiscal 2002, there were non-recurring legal expenses in excess of \$1 million.

Heald has experienced a short-term reduction in enrollment and is taking steps to ensure that expenses will be reduced.

After a surge of 651 new enrollments between 1998 and 2000, new enrollments have dropped by approximately 1,500 since 2000, leading to a decline in total enrollment. This is partly due to the downturn in the computer industry, since several of Heald's courses are in the computer sciences, including web design and administration, and most Heald's campuses are in Northern California. Also, Heald closed its Martinez campus in 2002, representing approximately 1,000 students, some of whom were absorbed in the nearby Concord campus.

Heald has taken a number of steps related to reduced enrollments. Heald has approximately 10% fewer full-time faculty and approximately 15% fewer part-time faculty (January 2003 compared to January 2002) and management reports that salary expense for the six months ended November 2002 was 9% less compared to the same period in 2001. Heald also envisions 1,000 additional new enrollments in 2003 since it has expanded its Medical Assisting and other healthcare programs to additional campuses.

As a vocational school, Heald lacks certain revenue characteristics of many private institutions, such as alumni support (and therefore lack of endowment contributions), leaving it highly dependent on tuition revenue. Also, despite name recognition resulting from being in existence for 140 years, it must spend considerable sums for advertising and other forms of student recruiting.

However, the College also enjoys certain opportunities. Heald's teachers are not tenured, which, while making them more difficult to retain, also allows Heald to control salaries, cut staff, and to change curriculum as needed to attract students.

Heald may also be aided by the fact that competing community colleges may need to raise their student fees due to budgetary constraints.

Heald appears to be able to afford the additional debt and will not be significantly leveraged.

Heald has become increasingly less liquid, however debt service coverage ratios indicate Heald is capable of handling the additional debt. The refinancing portion will reduce annual debt payments by approximately \$200,000. Overall, even with the new debt, Heald will not be significantly leveraged.

III. STUDENT, COLLEGE COSTS, AND FACULTY STATISTICS:

Applicant Pool

Heald recognizes an application only after the student has passed an entrance exam, met with academic advisors and an admissions counselor regarding academic and career goals, and, if necessary, with a financial aid counselor. Approximately 40% of students who begin this process complete an application.

Fiscal year ended May 31	Number of Applications	Offered Admission	New Enrollments *
1998	8,189	8,189	8,189
1999	8,356	8,356	8,356
2000	8,840	8,840	8,840
2001	8,541	8,541	8,541
2002	7,342	7,342	7,342

* Headcount, not full-time equivalent.

Enrollments and Degrees

ENROLLMENTS / DEGREES (Full-Time Equivalent)

Academic Year*	Enrollments (Headcount)	Enrollments FTE	A.A.S. Degrees Awarded**
1998	8,813	8,727	4,052
1999	9,344	9,110	3,687
2000	9,342	8,968	4,288
2001	10,687	10,366	4,106
2002	9,371	9,183	5,159

* Academic year covers four quarters, beginning in mid to late January.

**A.A.S. stands for Associate of Applied Science, designed to be completed in 6 quarters, or 18 months.

Tuition

The following table sets forth tuition rates for the past five academic years.

<u>Academic Year</u>	<u>Quarterly Tuition</u>
1998	\$1,800
1999	\$2,100
2000	\$2,350
2001	\$2,650
2002	\$2,900

Faculty

The table below summarizes the University's faculty for the last six years. Total faculty has increased by 44% in the five years ended 2002 compared with student growth of 5%. There are no tenured faculty.

<u>Academic Year</u>	<u>Full-time</u>	<u>Part-time *</u>	<u>Total *</u>
1998	263	141	404
1999	286	156	442
2000	300	152	452
2001	345	186	531
2002	378	155	533
2003**	340	115	455

* Part-time faculty is expressed as headcount, not full-time equivalents.

** Faculty, as of January 2003, is included to demonstrate reductions from prior year.

IV. BACKGROUND:

General:

Heald College offers focused, nonresidential programs of post-secondary vocational instruction. Heald offers Associate in Applied Science degrees in seven business programs and three technology programs, as well as a shorter diploma program in most of these programs (see Academic Programs, below).

The College was originally established in San Francisco in 1863 by Edward Payson Heald as Heald's Business College. Heald College has grown to 11 campuses in California, Hawaii and Oregon. California campuses are located at Concord, Fresno, Hayward, Rancho Cordova, Roseville, Salinas, San Francisco, San Jose (Milpitas), and Stockton.

Heald programs are concentrated so that students can complete an associate degree in only six quarters over a period of 18 months. Courses in each program cover topics that are relevant to succeed in the

chosen field. Classroom activities typify real work assignments and emphasize effective interaction. Students are expected to meet industry standards for professional appearance, attitude, and attendance.

The College support system includes workshops, individual tutoring, informal study groups, the Learning Resource Center, open labs, and other academic and personal assistance programs.

Administration:

The college is governed by a self-perpetuating board of directors (the “Board”) consisting of ten elected trustees. The elected trustees are nominated by a Board-appointed nominating committee and are usually elected by the Board to hold office for three years. The terms of one-third of the elected trustees expire annually. The Board appoints the President of the College who together with administrative officers, conducts the activities and affairs of the College and exercises or directs the exercise of all of the College’s corporate powers.

Accreditations:

The Accrediting Commission for Community and Junior Colleges of the Western Association of Schools and Colleges (WASC) originally accredited Heald in 1983. WASC reaffirmed Heald Colleges’ accreditation on June 16, 2000 and scheduled its next site visit for 2005.

Academic Programs:

Heald provides students with an associate in applied science (AAS) degrees (completed in six quarters) or specialist diplomas (completed in four quarters) in business or technology. AAS degrees are offered in Accounting, Business Software Applications, Computer Business Administration, Hospitality and Tourism, Legal Office Administration, Medical Office Administration, Medical Assisting, Computer Technology, Networking Technology, and Electronics Technology.

Competition:

In general, in each of Heald’s 11 geographical markets, Heald’s primary competitors are the local community college and private career oriented schools such as ITT Technical Institute and DeVry Institute of Technology as well as smaller, specialized local schools such as Humphreys.

Heald believes each of its campuses possesses strong competitive advantages with respect to its business and technology programs, job placement assistance, WASC accreditation, and 140 year reputation, versus local community and career colleges.

V. OUTSTANDING DEBT:

<u>Issue Name:</u>	<u>Original Amount</u>	<u>Amount Outstanding As of 5/31/02</u>	<u>Estimated Amount Outstanding after Proposed Financing</u>
Existing			
CEFA, Series 1999	\$15,000,000	\$14,190,000	\$14,190,000
Note payable, Bank of America, December 1999	5,500,000	4,968,343	0
Municipal improvement bonds, July 1999	344,000	279,482	279,482
Capital leases	1,131,719	1,102,306	1,102,306
Proposed			
CEFA Private Placement, 2003			9,800,000
Totals		<u>\$20,540,131</u>	<u>\$25,371,788</u>

V. LEGAL REVIEW:

Staff has reviewed the Applicant's responses to the questions contained in the Legal Status portion of the Application. No information was disclosed to question the financial viability or legal integrity of this applicant.

VII. STAFF RECOMMENDATION:

Staff recommends the Authority approve a resolution for an amount not to exceed \$9,800,000 for Heald College, subject to the bonds being privately placed with a qualified institutional buyer, a general obligation pledge, a deed of trust on campus property, and minimum bond denominations of \$100,000.