STATE UNIVERSITY SYSTEM OF FLORIDA
BOARD OF GOVERNORS
Project Summary
University of North Florida
Refinancing of Existing Housing Debt

Background:

The Debt Management Guidelines of the Board of Governors generally do not require the approval of the Board of Governors for refundings for debt service savings. However, the original financing of the Flats at Kernan ("the Flats"), an apartment complex, was secured by a mortgage, a type of financing which is also exempt from the requirement of Board of Governors' approval, pursuant to s. 1010.62, Florida Statutes. Therefore, the Board of Governors has not previously considered the acquisition of the Flats. Since it is proposed that the Flats will now be financed without a mortgage, and become part of the Housing System, the University is requesting authorization from the Board of Governors for the transaction below. To avoid this situation in the future, the Board is currently considering an amendment to the Debt Management Guidelines which would eliminate the mortgage exemption from Board of Governors approval for student housing or any other facility which competes with a university's existing auxiliary enterprise. Another proposed amendment would limit the exemption for refundings to situations where the original financing was approved by the Board of Governors.

Project Description:

The University of North Florida (the "University") requests approval to issue refunding bonds through the University of North Florida Financing Corporation (the "Corporation") to refinance its entire portfolio of outstanding housing debt. The bonds would refund bonds issued in 2007 by the Corporation to finance the Osprey Fountains housing project and to refund other bonds previously issued to finance the then existing housing system at the University (collectively, the "Housing System"), as well as a separate loan entered into in 2014 with Compass Mortgage Corporation to acquire the Flats. The bonds would be issued in an amount not exceeding $127.1 million.

In 2007, The Board of Governors approved the issuance of fixed-rate, tax-exempt bonds in an amount not exceeding $116 million for the purpose of constructing a student housing facility containing 1,000 beds (the Osprey Fountains) and refunding certain other outstanding housing bonds of the University of North Florida Foundation, which had financed another 2055 beds.

From bond proceeds of $116 million, $74 million financed the construction, installation and equipping of Osprey Fountains. Of the remaining $42 million, $34 million was allocated to refinancing outstanding bonds and $8 million was allocated to capitalized interest. The Housing System, financed or refinanced through the 2007 bond issue, currently includes 3,023 beds.

The University acquired the Flats in 2014 for $30.7 million through a loan secured by a conventional mortgage for $26.2 million, or 85% of the purchase price. This property was purchased from a private owner and contains 480 beds within eight three-story buildings.

The existing financings for the Housing System and the Flats are separate transactions, each paid solely from revenues of the respective housing projects. However, in the loan agreement which financed the Flats, the University agreed that it would not publicly offer additional bonds secured under the lien on the Housing System unless the proceeds were used to refinance the loan used to acquire the Flats. The University further agreed not to incur additional debt secured under the lien on the revenues of the Housing System through a private placement, without the prior written consent of the lender for the Flats loan. Therefore, the University is requesting to consolidate all existing debt on the Housing System and the Flats, in one transaction. The University is estimating present value savings on the proposed refunding of the Housing System bonds of 14.39% or $13.8 million. However, savings on refunding the Flats loan is modest, at an estimated present value savings of 1.34%, or just over $300 thousand. This will result in a combined savings on the refinancing of the Housing System and the Flats of 11.76%, or $14.1 million. The Flats loan is not being refunded solely for debt service savings, but rather to replace the mortgage financing with revenue bonds secured by a lien on revenues of the Housing System. If the interest rate on the proposed bonds were to increase as little as 20 basis points (0.2%), the savings on the Flats refunding would be negative.

Facility Site Location: The Housing System is located on 27 acres situated on the eastern ridge of the University's campus.

The Flats is located directly across from campus on First Coast Technology Parkway on approximately 12.82 acres.

Projected Start and Opening Date: The proposed bond issue is for refinancing only; construction funding is not being requested.

Flats Quantitative Demand Analysis: In summer 2014, after being approached by the property owner with an offer to sell, the University Board of Trustees decided that due to the strategic location and the need for additional housing, they should acquire the Flats property. Prior to the purchase of the Flats, the University had 3,023 student beds that were more than 100% occupied. That fall, 540 students were in triples and there was a sizeable waiting list for upper classmen that could not be accommodated.

Flats Study of Private Sector Alternatives: At the time of the Flats acquisition, the University had demand for additional housing, especially for upper classmen. The Flats property provided a type of housing the University did not have in their inventory to meet the demand from upper class students. Prior to the acquisition, 70% of the residents in the Flats were University of North Florida students. The Flats property is adjacent to campus and the private owner wanted to sell the property.

Flats Project Return/IRR: The Flats property is expected to provide a positive internal rate of return estimated at 4.58%, based upon assumptions provided by the University.

Financing Structure: The University proposes to issue refunding bonds through the Corporation in an amount not exceeding $127.1 million. The maturities on the bonds will not be extended beyond the term of the outstanding debt.

Security/Lien Structure: The bonds will be secured by a lien on the pledged revenues as defined in the Trust Indenture to include lease payments to be made by the University to the Corporation. The lease payments are secured by a pledge of and lien on net operating revenues from the Housing System, including the Flats.

The University has maintained high occupancy rates over the years. Historically, this rate averages 99%. In the future years, the University projects an average of 100% occupancy for the next five years.

Pledged Revenues and Debt Service Coverage:

From fiscal year 2011-12 to 2013-14 pledged revenues from the Housing System alone grew from $9.1 million to $9.5 million. Pledged revenues increased even further in 2014-15 to $11.1 million with the addition of the Flats, and are expected to increase to $12.1 million in 2015-16. During this period debt service coverage ranged from a high of 1.44x in 2012-13 to the current 1.24x expected in 2015-16. The debt service coverage declined primarily due to the ascending nature of the debt service on the 2007 bonds, which financing structure was approved by the Board of Governors in 2007.

The projected pledge revenues, including the Flats, for fiscal year 2016-17 are $12.3 million and are projected to drop 6% to $11.5 million by 2020-21, with the debt service coverage declining from 1.59x to 1.29x. This decline results from the University's current plan of no rate increases over the five year period while O&M is projected to grow 1.6% annually. The projected annual debt service is $8.95 million after the refunding based on a currently estimated interest rate of 2.83%.

(See detailed summary of historical and projected debt service coverage)

Type of Sale:

The University provided a standard competitive versus negotiated sale analysis which analyzed various criteria in making a determination for a negotiated sale. The University believes that two of the criteria, the type of pledged revenues and the security structure, argue for a negotiated sale. With respect to the pledged revenues, it should be noted the Division of Bond Finance has successfully sold university housing transactions secured by revenues of a housing system for many years. Regarding the security structure, the University would like to make a slight reduction to the 1.25x parity test requirement and sell the bonds without a debt service reserve. These changes are not out of the ordinary and should not warrant a negotiated sale by themselves. The stronger argument for a negotiated sale is that the bonds were recently downgraded to "A-." Under the standard analysis, bonds rated below a single "A" are more likely candidates for a negotiated sale. Although the bonds are still in the "A" category, they are at the lower end and, with the recent downgrade from "A", it is not unreasonable to provide additional education to investors about the downgrade that is afforded by a negotiated sale.

Selection of Professionals:

The University has provided information stating that both the financial advisor and the underwriters were selected based upon a Request for Proposal (RFP) process. With respect to the financial advisor, an RFP was mailed and responses were reviewed by a committee of three. Six financial advisory firms responded and four were selected to be interviewed. The four selected for interview were Dunlap & Associates, First Southwest Company, PRAG and The PFM Group. The committee selected The PFM Group.

Selection of the underwriting team followed the same process, except that representatives from The PFM Group were on the review committee. A number of underwriting firms responded, with five firms being selected for interviews. The five selected were Bank of America - Merrill Lynch, JP Morgan, RBC Capital, SunTrust - Robinson Humphrey and Wells Fargo Securities. SunTrust – Robinson Humphrey was selected as senior manager and JP Morgan was chosen as co-senior manager.

The University used the same bond counsel, Bryant, Miller and Olive, that they have used in the past for continuity.

Analysis and Recommendation:

Staff of the Board of Governors and the Division of Bond Finance have reviewed the information provided by University of North Florida with respect to the request for Board of Governors approval for the subject refinancing. Projections provided by the University indicate that sufficient net revenues will be generated from rental income, without the need for a rate increase. It appears that the proposed financing is in compliance with the Florida Statutes governing the issuance of university debt and is in compliance with the Board of Governors' Debt Management Guidelines. Furthermore, the financing will allow the University to bring all of its housing under one system. Accordingly, staff of the Board of Governors recommends adoption of the resolution authorizing the proposed financing.