

Fresno Unified School District Funds New, \$25 Million Central Kitchen By Saving Up Its Federal Lunch Money

By Ruth F. Quinto and David Brodsky

Students in the Fresno Unified School District will be savoring fresh, locally grown ingredients in their school meals beginning in 2007. That's when the district will unveil its state-of-the-art, \$25 million central kitchen. Plans for the new kitchen, which will eliminate the need for preservative-laced packaged foods, had been in the works for several years. However, when the FUSD realized that the money it had accumulated in its National School Lunch Program (NSLP) reserve Fund could not be used for capital expenditures, the district turned to KNN Public Finance for assistance. Working with bond counsel, an investment bank, and other professionals, the financing team developed a complex, but creative and practical solution to address the urgent need of improving nutrition for the district's 77,000 students.

Nutritional Needs in the Nation's "Salad Bowl" Region

Numerous studies show that although they live amidst the nation's most fertile farmlands, children in Fresno County often go hungry and experience food insecurity—not knowing where their next meal will come from. These children often rely on the meals they get at school to stave off hunger. An astounding 80 percent of students in FUSD qualify for free or reduced meals through the NSLP, a program celebrating its 60th anniversary in the United States. FUSD serves approximately 72,000 meals per day to children from pre-school through high school. The district sought to take advantage of its location in the heart of the nation's "salad bowl" region and offer healthy, fresh meals throughout the district.

"By standardizing production in the central kitchen, we can minimize the need for pre-packaged foods that are often high in preservatives and sodium," said Paul Idsvoog, Director of Food Services for FUSD. "We are thrilled to see what a difference the new central kitchen will make for our students' health and academic success next year."

Lunch Money Savings Snag

Upon advice from the State Department of Education, FUSD had been accumulating savings in its school lunch program, planning to pool those resources and upgrade its food service operation. In the summer of 2005, FUSD was informed by the State that its reserves from the NSLP program were

in excess of the program's allowance and must be allocated to eligible uses promptly. To further complicate matters, the district learned that USDA waivers which previously allowed for the use of NSLP funds to buy or build facilities had been eliminated. The silver lining to this budgetary cloud appeared when FUSD determined its' NSLP reserves could be used to pay for an operating lease for a kitchen facility, based on guidelines provided by the Federal Office of Management and Budget (OMB).

The first step toward making the central kitchen a reality was for FUSD to join the Central Valley Support Services Joint Powers Agency (JPA) in February 2006. The JPA was formed in 1999 by neighboring Clovis and Golden Valley Unified School Districts to provide maintenance, operations, food service, transportation, printing and warehouse/delivery services to member districts. As a member, FUSD could partner with its neighboring districts to create a viable financing model. The District leased its own property as the location for the new kitchen to the JPA under a site lease. The JPA would build the facility, then lease it back to the District, thereby creating an "arms length" relationship between the District and the leasing agency, the JPA. The site lease is 40 years long and after it on expires June 1, 2046, the property and facility will revert back to FUSD.

Secondly, the term of the operating lease for the central kitchen was established as 22 years with the JPA, expiring on June 1, 2028. Once built, the kitchen will have a useful life of 40 years, satisfying the OMB requirement that an operating lease not extend beyond 75 % of a facility's useful life. At the end of the first operating lease, the JPA may choose to enter into a new market rate lease for the facility with FUSD, or it may lease the facility to another organization. This ability for the JPA to control the structure for another 18 years after the original operating lease addresses another OMB requirement, that a property cannot be transferred or sold at a "bargain price" to the District at the end of the lease term.

Finally, the District, working with its financing team, put together the financial piece that would pay for the construction of the kitchen facility. The JPA issued two series of bonds. The "Series A" bonds for \$20 million are secured by the District's operating lease payments to the JPA. The NSLP funds are now allocated to an eligible use – operating lease payments. This bond issue raised approximately 85% of the total cost to build the facility and satisfies the OMB guideline that the present value of rental payments for the term of the lease must be less than 90% of the fair market value of the property.

The "Series B" bonds for \$3.6 million, approximately 15% of the total principal for the project, require interest-only payments over the life of the "Series A" bond and are secured by the District's lease payments until 2028. The principal and interest payments for Series B to be made from 2029-

2036 are secured by the central kitchen facility and site through the term of the site lease (2006-2046) and will be paid by whoever leases the facility after the initial 22-year term expires. While the lessee for this second term will presumably be the District, there can be no guarantees under the operating lease rules.

“We took a lot of extra steps in this process to create a sound financing plan that holds up to the scrutiny of local and federal budget offices,” said Ruth Alahydoian, KNN Vice President. “While these transactions are not for the faint of heart, the District understood the risks and parameters involved and moved forward to secure the facility it needed to improve the well being of its students.”

KNN provided the District with support services and counseling for bond presentations to Standard & Poor’s and Moody’s. Because FUSD had made substantial improvement in its fiscal standing by reducing expenditures, replenishing reserves, and settling contract agreements with all unions, Standard & Poor’s gave both bond series an “A” rating. Additionally, Standard & Poor’s removed the “negative” outlook that had been previously assigned to the District’s outstanding bonds. Additional professionals involved in this financing plan included Citigroup as the underwriter; Orrick as bond counsel; McCormick, Barstow LLP as district counsel; Perry Smith LLP as the District’s outside auditor; U.S. Bank, trustee; CB Richard Ellis, independent appraiser; and Winter & Co. Advisors, LLC, investment advisory firm.

Construction of the central kitchen began in July 2006 and it is slated to begin operation in September 2007. FUSD will spend approximately \$5.8 million in accumulated NSLP funds to equip the kitchen upon its completion.

“We were frustrated, but not defeated, in our plans to build the central kitchen,” said FUSD Superintendent Michael Hanson. “Working with our financial advisors, bond counsel and underwriters, we developed a plan that allowed us to meet our goals. Our students will soon benefit from the healthy foods this new facility will provide and we look forward to witnessing the physical and academic improvements that will result.”

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