*** Important Note ***

This information is for Internal CSU purpose only. Do not distribute as the information may be incomplete and subject to change. The CSU and its bond counsel do not make any assurances and consider this information as private.
Agenda

- Introductions
- Key CSU Forms
- Private Business Use
- Case Studies
Key CSU Forms

- Private Use Checklist – Attachment B (CPDC Form)
- Facility Information Sheet – Attachment C (CPDC Form 4-2)
- Allocation of Bond Proceeds Form (F&T)
Who Fills Out the Forms?

- Capital Planning Staff
- CFO Campus Staff
- Program Directors
- Auxiliary Organization Staff
When are forms completed or updated?

- Annual CPDC Tax Compliance, Custodial, Space and Facilities Reporting (in May)
- New Projects
- Changes to Project Use
- Financing Planning
- Closing of Construction project accounts
Why do we have to fill these out?

- CSU has over $3 billion of tax-exempt bonds
- To meet IRS requirements for tax-exempt bonds
- Secure lowest rate of borrowing for CSU
- Maintain strong financial benchmarks and credit ratings
- Meet State Treasurer’s Office requirements for funding State projects
Key Project Information identified on Forms

- Who owns the project?
- Who is leasing or subleasing? Who manages or operates it?
- Public/Private Arrangements
- Who are the users?
  - University users: Students, faculty & staff
  - Nonprofit organizations
  - Federal Government
  - Private Businesses
Focus on these Facilities

Higher incidences of private business use at:
- Student Unions
- Dining
- Bookstores
- Sport Facilities
- Housing (mixed use with retail)
Why so many questions & forms?

- Forms are interconnected to prompt full reporting of relevant facts
- Forms are designed for self-resolution of issues to reduce follow-up inquiries
- The more you fill out, the less follow-up from CPDC, F&T and Bond Counsel
Key CSU Forms
Private Use Checklist – Attachment B

- Checklist is a summary form focusing on project use
- Intended to identify the most basic information before referring to supplemental forms
Private Use Checklist (Cont.)

Basic information about project:
- Ownership and sale of project
- Long and short-term use; lease & sublease
- Manager, operator & franchise
- Output & utilities, water & solar
- Research activity
- Misc use: naming rights, priority rights, joint ventures
CPDC 4-2: Follow-up Form

- Use & Lease Details
- Funding sources for Project
- Tools for self-resolution
- VP/CFO Approval Process Necessary to comply with Allocation Requirement
Allocation Of Bond Proceeds: Follow-up Form

- Use, space and cost information from Form CPDC 4-2 allows for allocation of equity to cover private use
- Preliminary Form before financing and completion
- Final Form when Project Account is closed and project is completed
Auxiliary Study A – Office Space

ALLOCATING EQUITY TO PBU: PROJECT INFORMATION

- Original project cost: $30M, to be funded with $21M bonds (70%) and $9M equity (30%)
- Later: project cost overruns of $5M, all paid with additional equity; no further bonds issued
- Final project cost: $35M, so proportion is $21MM bonds (but 60% now) and $14M equity (40%)
- Conclusion: cost overruns paid with equity means more private use room in project
Auxiliary Study A – Office Space

BENEFITS OF EQUITY

- Equity-financed space not subject to tax restrictions
- The greater the equity contribution, the greater allowance for PBU, and that also dilutes percentage of total project costs financed by tax exempt bonds (which are subject to tax restriction)
Auxiliary Study A – Office Space

FORMAL ALLOCATION

- Revenues & Equity can only address PBU if you document properly
- Get credit for your contribution
- Generally, allocation has to be made within 18 months of project completion
- So make your calculations of final costs & ASF (allocations) in time – F&T Forms
Auxiliary Study B - Bookstore

REDUCING PBU THROUGH BLENDING

- Project financed with 70% bonds & 30% equity
- 30 yr bond term
- Total area 30,000 ASF
- Bookstore is 24,000 ASF (80% of space)
- Question: if 5 years after bond issuance, you discover bookstore has been privately operated and constituted PBU, what can you do?
- Answer: Try a Qualifying Management Contract – Stop the PBU!
Auxiliary Study B - Bookstore

USE OF QUALIFIED MANAGEMENT CONTRACT

- Previous bookstore contract caused PBU. A complying Qualified Management Contract will stop the PBU.
- PBU is measured over term of bonds, so PBU can be blended down (“3-Dimensional Blending”)
- Key Elements of new contract as QMC:
  - Private firm acting merely as operator/service provider, with no management control and equity stake
  - CSU pays fee to private operator for service rendered
  - No part of compensation based on net profit
  - Acceptable percentage of annual compensation is based on periodic fixed fee
  - No hidden early termination or non-renewal penalty
# Auxiliary Study B - Bookstore

## QUALIFIED MANAGEMENT CONTRACT MATRIX

<table>
<thead>
<tr>
<th>KEY TERMS OF CONTRACT</th>
<th>ORIGINAL NON-COMPLYING CONTRACT</th>
<th>FIRST DRAFT OF QMC</th>
<th>FINAL DRAFT OF QMC</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Duration/Term</strong></td>
<td>5 yrs; CSU has no right to terminate by end of Year 3</td>
<td>3 yrs</td>
<td>3 yrs</td>
</tr>
<tr>
<td><strong>Right to review / terminate without cause</strong></td>
<td>For all three contracts’ automatic renew for 1-yr terms by CSU: CSU has 120 days to notify non-renewal.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Stated Compensation</strong></td>
<td>Operator guarantees minimum stated amount to CSU plus percentage of net sales</td>
<td>CSU pays to operator stated fixed fee (FF) and to variable fee (VF) based on percentage of gross sales</td>
<td>CSU pays to operator stated fixed fee (FF) and a variable fee (VF) based on percentage of gross sales</td>
</tr>
<tr>
<td><strong>Compensation parameters</strong></td>
<td>No cap on payment to CSU</td>
<td>VF paid to operator cannot exceed FF: so-called 50% fixed fee model</td>
<td>VF paid to operator cannot exceed FF: so-called 50% fixed fee model</td>
</tr>
<tr>
<td><strong>Compensation deferral</strong></td>
<td>N/A</td>
<td>VF only payable upon bookstore reaching a gross sales target</td>
<td>VF clarified to state that, once earned, it is always payable; can accrue until end of contract, but not forgiven</td>
</tr>
<tr>
<td><strong>Other Cash Compensation</strong></td>
<td>Signing bonus paid to CSU. Unused capital investment also goes to CSU</td>
<td>None</td>
<td>Operator makes cash contribution for scholarships</td>
</tr>
<tr>
<td><strong>Capital Investment and Amortization if early termination by CSU</strong></td>
<td>Operator to amortize investment over 5 yrs. If early termination, CSU pays operator for unamortized portion</td>
<td>8 years, straight line. If early termination, CSU pays operator for remainder unamortized portion</td>
<td>3 years, straight line; amortized remaining portion over 3 yrs.</td>
</tr>
</tbody>
</table>
Auxiliary Study B - Bookstore
How PBU is blended down

- Duration of PBU: Years 1-5, from non-complying contract, but bonds have 30 yr term
- Extent of PBU: 80% - Bookstore is 24,000 ASF / total 30,000
- Sources of funding: Project was funded with 30% equity and 70% bonds
- 1) PBU at Equity-space first, so 30% of PBU in equity-financed space, remaining 50% in bond-financed space (equity space not subject to tax restriction)
- 2) PBU limited in time: if QMC now, then PBU only 5 out of 30 yrs (1/6)
- 3) 50% of PBU in bond space diluted to 8.3% once blended through time (50% times 1/6)
GRAPHIC ILLUSTRATING “3-DIMENSIONAL BLENDING”
Sample – Private Business Use Measured by Use of Space

Total 30,000 Assignable Square Feet

Private Business Use - 24,000 ASF   Government Use - 6,000 ASF
Private Business Use Diluted by Equity

Private Business Use 80%

> 50%

Diluted Private Business Use = 50%

Equity 30%
Private Business Use Blended Down Over Time

50% Private Business Use of Bond-Financed Space

20% Private Business Use of Financing Term

Final Private Business Use = 8%
Variation on bookstore use

What about a new arrangement in bookstore operations after bonds have been issued and the facility has long been placed into service?
Managing PBU

Previous 2 examples illustrate how to manage PBU. So make sure PBU is not exceeded:

- For most CSU activities, limit is 10% of project
- For large size project, also a $15 million PBU limit
- For PBU activities unrelated to normal CSU activities, or disproportionate to CSU activities, 5% limit applies. e.g., leasing office space may be ‘unrelated’
- Watch for increasingly commercial and non-core educational PBU
- Also watch for ‘miscellaneous’ or non-intrusive PBU: e.g., solar, cell tower, photovoltaic
Remediating Excess PBU

What can you do if PBU is exceeded?

- Tax-exempt debt is issued by Trustees
- Only limited actions available if excess PBU cannot be blended down
- Select remedies, to the extent available, may come at a high cost
- F&T & Tax Counsel to work together
- So, plan early & coordinate with F&T to achieve business goals and protect bonds
The End?

What if the excess PBU is discovered too late?

- Consequences of excess PBU can be taxability of bonds
- Bondholders can file claim against Trustees for tax exemption that has been denied by the IRS
- In addition to cost, Trustees credit rating is affected
- So, be diligent in monitoring use and keep good records