



# Building Child Care:

## A New Resource for Financing the Construction, Renovation and/or Acquisition of Child Care Facilities

*Tuesday, June 4, 2002*



# Agenda

1. Facilities Development Process
2. Financing Considerations & Terms
3. Available Financial Resources
4. Case Studies
5. Resources
6. Questions & Answers



# The Facilities Development Process

*The process can be broken into three major phases...*

1. Planning
2. Predevelopment
3. Development



# The Planning Phase

Addresses three key questions:

- 1) Is there market demand for the proposed facility and services?
- 2) Is the proposed facility project financially feasible?
- 3) Is the sponsor organization ready to take on this project?



# Market Demand

- Are there a sufficient number of families demanding the new child care services at the rate to be charged?
- Are the rates sufficient to generate operating revenues to meet staff, program and facilities costs?
- A business plan can be used to answer these questions.

*Refer to: Child Care Financial Planning and Facilities Development Manual  
Chapter 3: Developing a Business Plan: Section 5: Market Feasibility Analysis,  
pg. 11.*



# Financial Feasibility

- What will it cost to build the new facility?
  - Hard costs (acquisition, construction, equipment)
  - Soft costs (design, permits, legal, financing)
  - Hidden costs (staff and board time, attention)
- What are the likely funding sources?
  - Equity
  - Debt (What can be financed?)

*Refer to: Child Care Financial Planning and Facilities Development Manual Chapter 2: Developing Pro Formas and Determining Debt Capacity*



# Organizational Readiness

- Does the agency have the leadership necessary to undertake the project?
- Is the agency financially ready?
- Does the agency have community support?



# Financial Readiness

Is the agency in a financial position to take on a facility project and/or debt?

- **Red** flags – factors that may inhibit provider from obtaining needed funding, meeting commitments, repaying loans.
- **Green** lights – factors that suggest project success



# Red Flags

- Difficulty meeting payroll or taxes
- Borrowing from officers/ directors
- Unable to pay bills promptly
- Large amount of uncollected receivables
- Deficits in recent years
- Agency doesn't know current financial position
- Agency can't explain audit.
- There is no cushion or cash reserve



# Green Lights

- Services are constrained by lack of space
- Agency is financially strong and growing
- Success identifying and obtaining new funding sources each year
- Financial systems are in place, strong
- Agency understands and guides your financial position



If a facility project has green lights for...

- ✓ Market demand
- ✓ Financial feasibility
- ✓ Organizational readiness

*Then its time for the next phase:*

**PREDEVELOPMENT**



# The Predevelopment Phase

- Everything an agency needs to do to begin construction on a new facility
  - Selecting a site
  - Obtaining site control & approval
  - Designing the project
  - Securing a Contractor
  - **Obtaining Financing**

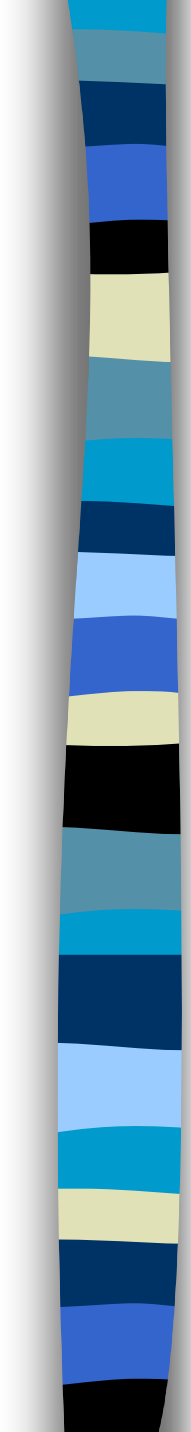
*Refer to: Child Care Financial Planning and Facilities Development Manual Chapter 4: The Facilities Development Process.*



# Obtaining Financing

- Finalize the business plan
- Determine the start up/capital budget for the project
- Identify likely sources (equity and debt)
- Apply for Funding
- Secure Commitments
- Close loans/have cash in hand

*Refer to: How to Start a Child Care Center in San Francisco: Funding the Business, pages 31 to 52.*



Once a site has been selected, secured & approved for child care, the facility has been designed, a contractor has been selected, financing has been secured...

its time to move to the next phase,

## **DEVELOPMENT**



# The Development Phase

- Construction or renovation
- Building sign off
- Equipping the classroom(s)
- Licensing approval (inc. fire clearance)
- Ramp-up
  - Phasing staff & children from day 1 to target enrollment

*Note: Double time estimates for each step.*



# Facilities Development Summary

*The process is comprised of three major phases...*

1. Planning
2. Predevelopment
3. Development



# Basic Finance

## Considerations And Terms

- Each phase of development requires funding
  - Planning and Predevelopment best funded via internal resources or grants or soft loans
  - Development costs (construction and permanent) better suited to loans
- Facility costs can be paid by equity or debt



# Why Consider Financing?

Facility projects are costly.

- Costs vary by several factors including type of project, location, cost of land, labor...



# Why Consider Financing (cont.)?

Financing enables a child care provider to meet high costs and get services to families faster.

- *It takes a long time to raise grants.*
- *Capital campaigns may compete with operating fundraising.*



# Why Consider Financing (cont.)?

It's capital efficient.

- *Allows an agency to leverage savings/grants*
- *Pay for costs over time (the life of the property).*



# Why Consider Financing (cont.)?

Financing may bring *ownership* within reach.

- Long term tenure
- Customize the space for kids and staff
- Build agency financial position



# ABC's of Loans

- **Interest rate**: amount lender will charge.
- **Principal**: original amount of money borrowed.
- **Term**: agreed upon repayment term.
- **Amortization**: period of time on which monthly loan payments are based.



## ABC's of Loans (cont.)

- **Balloon payment**: the final payment of a loan which has a longer amortization than term.
- **Points**: an up front fee a Lender may charge for a loan, expressed as a percentage.
- **Fees**: Charges from a Lender for making a loan.



## ABC's of Loans (cont.)

- **Collateral**: the property pledged to a Lender to secure repayment of a loan.
- **Lien**: a claim a Lender will place on property in return for making a loan.
- **Guaranty**: A promise to repay a loan, usually from a third party.



## ABC's of Loans (cont.)

- **Loan to Value Ratio**: The relationship of a loan to the appraised value of the collateral  
(loan amount/appraised value)=LTV
- **Debt Service Coverage**: A calculation a Lender uses to determine the ability to repay  
(net income/ loan payment) = DSC.



# What Lenders Consider (5 C's)

1. Cash flow/Capacity to Repay
  - Will an agency be able to meet its monthly payment?
  - Typically determined by debt service coverage ratio
  - First step out of the box for most lenders



# What Lenders Consider (5 C's)

2. Character/Capacity to Execute Project
  - Is there a sound vision and business plan?
  - Is there leadership and technical capacity to execute that plan?
  - Lenders will typically analyze agency leadership (staff and board) and experience of development team (consultants, architect, contractor).



# What Lenders Consider (5 C's)

3. Capital/Equity Investment in Project
  - What agency dollars are invested?
  - What other equity sources are invested?
  - Lender's typically look for a significant investment by the agency.



# What Lenders Consider (5 C's)

## 4. Collateral

- What is the value of the property being pledged for repayment of the loan?
- Lenders typically commission appraisals of property or other assets.
- Most Lenders have policies regarding loan to value ratios e.g. will lend only 80% of value.



# What Lenders Consider (5 C's)

## 5. Credit History

- What is the credit history of the agency, owners, and guarantors, if any?
- Credit reports are available on nonprofit and for profit agencies and will be reviewed
- Lenders will look at past performance carefully

*Refer to: Child Care Financial Planning and Facilities Development Manual Chapter 2: Developing Pro Formas and Determining Debt Capacity, pg. 15.*



# Case Studies: Facilities Financing

## **Points to remember:**

- There is no “standard” way to finance a project
- Financing structures vary widely from project to project depending upon the circumstances



# Case Studies: Facilities Financing

## **Kids First, Inc.**

- Located in Anytown, CA
- New site: leasing a modular unit and construction of a new building for more classrooms and administrative space
- Cost: \$1,045,700
- Financing provided by:
  - City of Anytown Economic Development Department
  - Prop 10 Commission
  - A regional community development corporation



# Case Studies: Facilities Financing

## Child's Play

- Located in Bigtown, CA
- Purchasing and rehabilitating a single family home for use as a child care center
- Cost: \$464,000
- Financing provided by:
  - A statewide loan fund
  - A local commercial lender
  - The owner's equity

SAMPLE PROGRAM--- PURCHASE PORTABLE ON PUBLIC LAND

<b><u>SOURCES</u></b>		<b><u>Amt.</u></b>	<b><u>USES</u></b>		<b><u>Amt.</u></b>
Agency Savings		12,350	Deposit for leased land		1,000
Community Development Block Gran		77,000	Architecture/Engineering		10,000
Prop 10 Grant		60,000	Permits/Fees		5,000
Revolving Loan Fund Loan		120,000	Grading/Site Prep		30,000
Total		269,350	Portable		120,000
			Security System		6,000
			Fire Alarm		8,000
			Fence		12,000
			Playground		55,000
			Contingency (5%)		12,350
			Equipment		10,000
			Total		269,350
Cost per square foot (2400)		\$112	<b><u>Monthly Facility Costs</u></b>		
Cost per space (48)		\$5,611	Loan Payment (10 yr., 0 int)		\$1,004.52
			Lease Payment for Land		<u>\$250.00</u>
			Total		\$1,254.52



# Financial Resources for Facilities Development

- There's a broad "landscape" of facilities financing resources
  - Different institutions, different products
- One size does not fit all
  - Each facility development project will have its own unique financing needs



# The Financial Institution Landscape

- Conventional Institutions
- Alternative Lenders
- Government-Certified Small Business Lenders
- Government Resources
  - Local
  - State
  - Federal



# Sample Federal Resources

- U.S. Department of Housing and Urban Development (HUD)
- Small Business Administration Programs



# Sample State Resources

- Low Income Housing Fund
- Department of Education: Child Care Facilities Revolving Fund Program



# Sample Regional Resources

- Northern California Community Loan Fund
- Santa Cruz Community Credit Union



# Where to turn for further information?

- Child Care Facilities Development Financial Resources and Technical Assistance in California (matrix form)
- A Resource Guide: Financing Child Care Facilities Development in California
  - Expanded version of matrix



# Building Child Care Collaborative

- **Purpose**: To begin to build a statewide technical assistance infrastructure for facilities development finance.
- **The Members**: National Economic Development and Law Center, California Child Care Resource and Referral Network, Child Development Policy Institute Education Fund, Child Care Facilities Fund of the Low Income Housing Fund.