California Department of Education

Executive Office

SBE-002 (REV. 11/2017)

memo-ssb-csd-aug18item01

# **MEMORANDUM**

**DATE:** August 1, 2018

**TO:** MEMBERS, State Board of Education

**FROM:** TOM TORLAKSON, State Superintendent of Public Instruction

**SUBJECT:** Financial Condition of State Board of Education-Authorized Charter Schools–Fiscal Year 2017–18

## Summary of Key Issues

This Information Memorandum provides a summary and analysis of the financial condition of the State Board of Education (SBE)-authorized charter schools for fiscal year (FY) 2016–17 and through the second interim projections for FY 2017–18. As the charter authorizer, the SBE must provide oversight monitoring of the schools it authorized. The SBE has delegated this responsibility to the California Department of Education (CDE), and under the terms of the Memorandum of Understanding (MOU) between the SBE and each of the SBE-authorized charter schools, the CDE reviews all revenue and expenditure reports submitted by the charter pursuant to California *Education Code* (*EC*) Section 47604.33. In the course of oversight monitoring, if the CDE finds that a charter school failed to meet generally accepted accounting principles or engaged in fiscal mismanagement, it must provide recommendations to the SBE to take appropriate action, as deemed necessary, including issuing a notice of violation or revocation.

The 27 SBE-authorized charter school sites in operation for 2017–18 were required to submit financial reports and budgetary updates to the SBE. The FY financial reporting cycle begins with a budget submitted to the SBE by July 1. Budgetary reports, known as interim reports, are due to the CDE on December 15 and March 15 of the current FY to update the charter school’s budget. After the end of the FY, each charter school must report an unaudited annual financial report on or before September 15 with the submittal of the final independent audit report by December 15, which completes the FY reporting cycle. All of the SBE-authorized charter schools that were operational in FY 2016–17 submitted their annual audit report for FY 2016–17. Each SBE-authorized charter school received an unqualified audit opinion with no significant audit findings noted. An unqualified opinion means that the auditor has opined that the charter school’s financial statements are fairly presented, are free of material misstatements, and have been prepared in accordance with generally accepted accounting principles. The CDE reviews the audit report in assessing trends, ratios, and significance of any footnote disclosures.

With the exception of one charter school, as noted in Attachment 2, all of the SBE-authorized charter schools filed the required FY 2017–18 interim financial reports to date. The CDE also requests balance sheets and accounts payable aging reports to be submitted with each interim report in order to see the financial position and the unpaid invoices by date ranges.

The CDE uses FY 2017–18 financial reports, budgetary updates, and pertinent budget assumptions provided by each SBE-authorized charter school in its overall assessment of a charter school’s current and projected financial condition, fiscal sustainability, and appropriateness of fiscal management practices. Specifically, the CDE reviewed each charter school’s budgets to identify, manage, and focus on signs of fiscal decline and possible fiscal mismanagement. As a guide, the CDE uses the general themes of the state’s budget reporting and monitoring system used for school districts; that process requires school districts to self-certify their financial condition as positive, qualified, or negative related to current and projected financial conditions. In the review of SBE-authorized charter schools, CDE considered these and other factors that included, but were not limited to: measuring the adequacy of managing cash; evaluating debt levels; reviewing sustainability of budget operations; reviewing trends in enrollment and attendance; determining the reasonableness of revenue and expenditure projections; and assessing the multi-year projected financial position of the charter school. For a definition of fiscal terms used in the review, refer to Attachment 1, p. 2.

The CDE analysis included a review of the independent audit reports and audit notes for FY 2016–17, the budgetary updates for FY 2017–18 as reported in the first and second interim reports, supplementary reports, and budget information provided by the charter school.

The CDE also determined for compliance the fiscal conditions specified in the MOU that included, but were not limited to, compliance with reserve levels as stated in the MOU as follows:

The MOU requires each SBE-authorized charter school to maintain reserves at a level at least equivalent to a school district of similar size, as identified in *California Code of Regulations,* Title 5 Section 15450.

For table below:

\*Percentage applied to total expenditures and other financing uses.
\*\*The dollar amounts are to be adjusted annually by the prior year statutory cost-of-living adjustment pursuant to *EC* Section 42238, rounded to the nearest thousand.

| School Average Daily Attendance | Expected Reserves |
| --- | --- |
| 0–300 | Greater of 5%\* or $66,000\*\* |
| 301–1,000 | Greater of 4%\* or $66,000\*\* |
| 1,001–30,000 | 3% |

## Financial Condition of State Board of Education-Authorized Charter Schools

For purposes of preparing this summary report, the SBE-authorized charter schools were each grouped into one of three categories, based on CDE’s analysis of the financial condition of each charter school. These categories serve as the basis for the level of monitoring and subsequent action taken by the CDE. A charter school’s financial condition is categorized as good, fair, or poor. The definitions for each category are described below. For FY 2017–18, the CDE finds that there were twenty charter schools in good financial condition, two charter schools in fair financial condition, and five charter schools in poor financial condition. For the five newly operational charter schools, three charter schools were found to be in good financial condition, one charter school was found to be in fair financial condition, and one charter school was found to be in poor financial condition, based on FY 2017–18 information. The financial highlights for all SBE-authorized charter schools that were in operation for FY 2017–18 are summarized in Attachment 2.

### Good Financial Condition

Twenty SBE-authorized charter schools were found to be in good financial condition. A charter school in good financial condition has demonstrated an ability to operate with a balanced budget, maintain stable enrollment and attendance ratios, manage cash liquidity, maintain a low debt level, maintain a positive fund balance, and has met the recommended reserve level specified in the MOU. The following SBE-authorized charter schools found to be in good financial condition are:

* Audeo Charter lI
* Barack Obama Charter
* Baypoint Preparatory Academy
* Grossmont Secondary School (newly operational)
* High Tech (operates six sites: High Tech Elementary Chula Vista, High Tech Elementary North County, High Tech Middle Chula Vista, High Tech High Chula Vista, High Tech High North County, and High Tech Middle North County)
* Magnolia Science Academy Santa Ana
* New West Charter
* Olive Grove Charter
* OnePurpose
* Ridgecrest Charter
* Ross Valley Charter (newly operational)
* School of Arts and Enterprise
* Sweetwater Secondary School (newly operational)
* The New School of San Francisco
* Thrive Public

### Fair Financial Condition

Two SBE-authorized charter schools are considered to be in fair financial condition. Charter schools in fair financial condition are showing some signs of fiscal distress and need to take appropriate action to address the decline in financial condition. Specifically, charter schools in fair financial condition may have an out-of-balance (deficit spending) budget; declining enrollment or attendance ratio; cash liquidity that is not adequate; debt levels that are high; declining or low fund balances; or reserve levels that are below the levels required in the MOU. The SBE-authorized charter schools in fair financial condition are:

* Anahuacalmecac International University Preparatory of North America
* Celerity Himalia Charter School (newly operational)

CDE staff has informed these charter schools about the concerns the CDE has regarding their fiscal condition and has discussed the objectives of maintaining fiscal sustainability and building reserves up to the recommended amounts by a certain period. The CDE has issued a Letter of Concern to the charter school Board identifying the specific items of concern with a request for a Board-approved fiscal corrective action plan (FCAP). If the CDE determines that the charter Board’s actions are not sufficient, the CDE may recommend that the SBE consider further action which may include issuing a Notice of Violation to the charter Board. Additional financial data and information for these SBE-authorized charter schools are outlined in Attachments 1 and 2.

### Poor Financial Condition

Five SBE-authorized charter schools are considered to be in poor financial condition. Charter schools in poor financial condition are in danger of jeopardizing their fiscal operations going forward. Timely and appropriate action by the charter school’s Board is critical in addressing and mitigating the serious decline in financial condition. Specifically, charter schools in poor financial condition have a negative fund balance and no reserve. These schools do not have an adequate cash level and have a high debt level. The SBE-authorized charter schools in poor financial condition are:

* Academia Avance Charter
* Celerity Rolas Charter School (newly operational)
* Paramount Collegiate Academy (voluntary closure February 7, 2018)
* Prepa Tec Los Angeles High
* Rocketship Futuro Academy

The CDE has informed these charter schools about the concerns the CDE has regarding their fiscal condition and has discussed the objectives of maintaining fiscal sustainability and building reserves up to the recommended amounts by a certain period. The CDE has issued a Letter of Concern to each charter school’s Board identifying specific financial items of concern with a request for a Board-approved FCAP. If the CDE determines that the Board’s actions are not sufficient, the CDE may recommend that the SBE consider further action which may include issuing a Notice of Violation. Additional financial data and information for each charter school are outlined in Attachments 1 and 2.

## Attachment(s)

* **Attachment 1:** State Board of Education-Authorized Charter Schools in Fair or Poor Financial Condition (18 Pages)
* **Attachment 2:** State Board of Education-Authorized Charter Schools Financial Highlights (6 Pages)