



## Charter Schools

Some School Districts Improperly Authorized and Inadequately Monitored Out-of-District Charter Schools

Report 2016-141

COMMITMENT  
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October 17, 2017

2016-141

The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
State Capitol  
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the California State Auditor presents this audit report concerning the oversight and monitoring of charter schools operating outside the geographic boundaries of their authorizing school districts (district).

This report concludes that some districts are using exceptions in state law to authorize charter schools that operate outside of their respective boundaries. These authorizations have allowed districts to increase their enrollments and revenue without being democratically accountable to the communities that are hosting the charter schools that they authorize. In addition, the districts we visited could not demonstrate that they limited the fees they charged to their actual costs of providing oversight, as state law requires, and two of the districts charged additional service fees without justifying the costs of providing related services.

Further, the districts do not generally have robust processes to ensure that their respective charter schools are financially stable and academically successful. State law requires districts to monitor the fiscal condition of the charter schools they authorize but does not identify specific procedures that authorizers should perform to fulfill this responsibility. Accordingly, the districts we visited provided varying levels of oversight regardless of whether the charter schools operated inside or outside their boundaries. The districts could strengthen their financial oversight of charter schools by incorporating best practices into their processes, such as by obtaining charter school lease agreements and evaluating the reasonableness of the charter schools' financial projections.

None of the districts we visited could demonstrate that they consistently monitored the academic performance of their respective charter schools. However, state law identifies academic performance as the most important factor to consider when deciding to renew or revoke a school's charter. As a result, districts that fail to document regular academic assessments of their charter schools may not have sufficient evidence to revoke an underperforming school's charter.

Respectfully submitted,



ELAINE M. HOWLE, CPA  
State Auditor

## Selected Abbreviations Used in This Report

ASAM	Alternative School Accountability Model
CMO	charter management organization
FCMAT	Fiscal Crisis Management and Assistance Team
LCFF	Local Control Funding Formula
MOU	memorandum of understanding

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# Summary

## Results in Brief

The Charter Schools Act of 1992 (Charter Schools Act) allows teachers, parents, students, and community members to initiate the establishment of charter schools that operate independently of existing school district (district) structures. To grant charter schools autonomy and allow them to try innovative teaching methods, state law generally exempts charter schools from most requirements governing districts. However, charter schools must comply with select statutes and meet certain conditions for funding. Further, state law holds each charter school accountable to the authorizing entity (authorizer)—which could be a district, a county office of education, or the State Board of Education (State Education Board)—that approves its charter petition (petition). A petition must include a comprehensive description of the proposed charter school’s educational program, measurable student outcomes, governance structure, and manner of conducting annual financial audits, among other things. To demonstrate community support, a petition must also include a minimum number of parent or teacher signatures. Once approved, a petition becomes an agreement—or charter—between the authorizer and the charter school. Later, if the authorizer’s oversight activities indicate that the established charter school has not fulfilled the charter’s agreements, the authorizer then has the authority to revoke or deny the renewal of the school’s charter.

Although state law sets some requirements related to districts’ authorizations of charter schools outside their geographical boundaries, many of these requirements are vague and ineffective. As a result, two of the three districts we visited—Acton-Agua Dulce Unified School District (Acton-Agua Dulce Unified) and New Jerusalem Elementary School District (New Jerusalem)—used exceptions within state law to authorize out-of-district charter schools that, in effect, expanded the districts’ reach into neighboring communities. However, our review found that Acton-Agua Dulce Unified and New Jerusalem could not demonstrate that they complied with state law when they authorized Assurance Learning Academy (Assurance Academy) and Acacia Elementary Charter School (Acacia Elementary), respectively. Specifically, state law requires charter schools to be located within the geographical boundaries of the districts that authorize them unless the schools are unable to locate sites or facilities in the area in which the school chooses to locate or unless the site is for temporary use during construction. Nonetheless, neither Acton-Agua Dulce Unified nor New Jerusalem could demonstrate that they or the out-of-district charter schools they authorized had attempted to locate suitable facilities within the districts’ boundaries at the time of authorization.

## Audit Highlights . . .

*Our audit concerning the oversight that authorizing districts provided three out-of-district charter schools highlighted the following:*

- » *Requirements related to districts’ authorizations of charter schools outside their geographical boundaries are vague and ineffective.*
  - *Districts we visited authorized charter schools outside of their districts that, in effect, expanded the districts’ reach into neighboring communities.*
  - *Districts that authorize out-of-district charter schools are not accountable to the communities in which the schools are located (host districts) because residents in host districts cannot vote for an authorizing district’s school board.*
  - *Authorizing districts can significantly increase their enrollments and revenue by authorizing out-of-district schools.*
- » *The State is unable to determine how many out-of-district charter school locations exist. We found that over 10 percent of the State’s charter schools have at least one school outside of the authorizing district’s boundaries.*
- » *We identified oversight issues at the three districts we visited.*
  - *None had formal procedures for evaluating their charter schools’ financial information so as to respond to indicators of financial distress.*
  - *The level of financial and academic oversight conducted by each district varied significantly due to vague state laws.*
  - *The three districts could not demonstrate that they consistently monitored the academic performance of their charter schools, even though they performed below the average of comparable schools.*

Furthermore, state law allows districts to expand their reach while limiting their accountability. Specifically, because the residents near the location of an out-of-district school cannot vote for an authorizing district's board members, a district that authorizes an out-of-district school is not accountable to the community in which the school is located. In addition, the districts in which the out-of-district schools are located (host districts) do not have a means of challenging the schools' authorizations. In fact, we identified one instance in which Acton-Agua Dulce Unified authorized an out-of-district charter school within a host district even though the host district had previously rejected the same school's petition. In its lawsuit against Action-Agua Dulce Unified, the host district noted that it denied the petition because the school failed to identify how it would attract a diverse population, serve English language learners, and address serious financial concerns.

Through the authorization of out-of-district schools, both Acton-Agua Dulce Unified and New Jerusalem were able to increase their enrollments and revenue significantly. Charter schools receive state funds based on the average daily attendance of their enrolled students, but the way they receive these funds depends upon whether the schools are directly funded or locally funded. A charter school's organizational structure and degree of autonomy from its authorizer typically determines its funding method, which affects the way its authorizing district receives revenue. For example, Acton-Agua Dulce Unified historically has charged all its directly funded charter schools—schools that receive their funding directly from county offices of education, which act as pass-through agencies for distributing state funding to the charter schools—a 2.5 percent administrative services fee and a 1 percent oversight fee, effectively collecting a total of 3.5 percent of each school's revenue. The district received \$1.9 million total in fees from charter schools in fiscal year 2015–16. Nonetheless, some of Acton-Agua Dulce Unified's charter schools appear to have made only sporadic use of the services for which the district charged them. In contrast, New Jerusalem has authorized locally funded out-of-district charter schools, which are charter schools that usually have the same governing board as their authorizing districts and that depend heavily on those districts for services, such as those for special education and data reporting. These schools typically receive their funding through their authorizers, so New Jerusalem has been able to manage the charter schools' funding. In fiscal year 2015–16, New Jerusalem's four locally funded out-of-district charter schools generated more than \$5 million in revenue, which the district managed. Because the parents of students in an out-of-district school cannot vote for the authorizing district's board members, New Jerusalem was able to expand its reach and increase its revenue without being accountable to the residents of the communities in which the charter schools reside.

Moreover, we found that the State is unable to determine how many out-of-district charter school locations exist. Because state law does not require charter schools to report all their school locations—including school sites, resource centers, and administrative offices—some charter schools that operate multiple sites report only their in-district addresses to the California Department of Education (Education). When we analyzed data from multiple sources, we found that 165 of the State’s 1,246 charter schools operated at least one of their school locations outside their respective authorizing districts’ geographic boundaries in fiscal year 2016–17. These 165 charter schools operated in a total of 495 out-of-district locations statewide. However, complete data are not available, and additional out-of-district charter school locations may exist.

Acton-Agua Dulce Unified’s and New Jerusalem’s decisions to authorize the out-of-district charter schools we reviewed may have resulted partly from weaknesses in the districts’ authorization processes. Specifically, neither of the two districts has an adequate process for ensuring that petitions comply with state law. For example, Acton-Agua Dulce Unified approved a petition that did not have any parent or teacher signatures attached, and the district’s records for evaluating this petition indicate that it did not review this critical element. Petition signatures indicate that individuals are interested meaningfully in either teaching at or having their children attend the proposed school. A lack of signatures may indicate a lack of community support, which could limit the charter school’s ability to obtain adequate funding or to employ qualified teachers. Similarly, New Jerusalem approved a petition that did not have the required number of signatures attached, and it also authorized two petitions that did not contain information about parental involvement, even though state law requires a petition to describe how parents will be involved in the governance of the school. New Jerusalem’s superintendent stated that parents can participate by attending public board meetings; however, we believe this approach may not be adequate to provide parents with the opportunity for active and effective representation.

Further, the three districts we visited—Acton-Agua Dulce Unified, Antelope Valley Union High School District (Antelope Valley Union), and New Jerusalem—did not have written procedures for reviewing their charter schools’ financial information. As a result, Antelope Valley Union and New Jerusalem could not show that they responded promptly to early indicators of financial problems at Los Angeles County Online High School (LA Online) and Acacia Elementary, respectively, which eventually led these two charter schools to close. State law requires districts to monitor the financial conditions of the charter schools they authorize, but it does little to address what effective oversight should entail beyond requiring the districts to perform school site visits and to obtain financial reports.

Consequently, neither Antelope Valley Union nor New Jerusalem could demonstrate that they consistently reviewed and responded promptly to available information about their charter schools' financial conditions, which showed signs of financial distress. Instead, the districts moved to revoke the two schools' charters only after the schools reported significant deficits.

Regardless of whether charter schools operated inside or outside their authorizing districts' jurisdictions, the level of financial oversight conducted by the districts we visited varied significantly. These inconsistencies likely occurred because state law is vague; thus, authorizers may have interpreted their responsibilities differently. Although state law directs authorizers to monitor the financial conditions of charter schools under their authority, it does not specify what procedures authorizers should perform to fulfill this oversight responsibility. We believe that school districts could improve their financial oversight by combining best practices, such as those that California's Fiscal Crisis Management and Assistance Team (FCMAT) recommends, with their current processes. FCMAT's best practices include obtaining charter school lease agreements and ensuring that charter schools' financial projections and assumptions are reasonable. If Antelope Valley Union and New Jerusalem had adopted these best practices, they might have noticed sooner that their charter schools' financial conditions were deteriorating. In addition, if Acton-Agua Dulce Unified and Antelope Valley Union had used their authority under state law to place representatives on their charter schools' governing boards, they would have been better positioned to question their charter schools' other problematic decisions, including a potentially illegal agreement that LA Online had with a sectarian school as well as Assurance Academy's plan to contribute reserves to a nonprofit corporation.

The authorizing districts we visited also provided inconsistent levels of academic oversight to charter schools because state law does not identify specific oversight activities that districts must perform. Although state law requires authorizers to conduct annual site visits at their charter schools, it does not clearly define the minimum level of oversight that authorizer's must provide with any specificity. In addition, state law only requires authorizers to assess a charter school's academic performance once every five years, when the school seeks to renew its charter. Although each of the districts we visited established requirements for academic oversight that exceed those in state law, the districts did not always perform the academic monitoring identified in their agreements with their charter schools. As a result, none of the districts held their charter schools accountable for measurable student outcomes outside the process of revoking a school's charter. For example, the three districts we visited could not demonstrate that they consistently monitored the academic performance of the charter schools we reviewed, even though their respective charter

schools performed below the average of comparable schools. State law requires districts to consider increases in academic achievement for all groups of students as the most important factor in deciding whether to revoke a charter, so districts that fail to document their ongoing assessments of academic performance may not have sufficient evidence to revoke failing schools' charters.

Finally, a series of changes in state law has diminished academic accountability for certain charter schools. Specifically, because of recent legislative changes, the only remaining academic performance criterion for renewing a school's charter is a comparison to other public schools that the charter school's students would attend if they were not enrolled in the charter school. However, charter schools are exempt from such comparisons if they qualify for an exception within state law. For example, one charter school we reviewed—Assurance Academy—qualified for that exception during our audit period because it serves high-risk students, such as those who are habitually truant, who are recovered dropouts, or who are parents. As a result, Assurance Academy was allowed to obtain a charter renewal without the district's assessing the school's academic performance. The State Education Board recently approved the development of a new program to hold such schools accountable. However, this new program will not be implemented until fall 2018, so gaps within the State's accountability system will likely exist until that time.

## Select Recommendations

### *Legislature*

To ensure that districts obtain community support for charter schools that they authorize, the Legislature should amend state law to do the following:

- Further clarify the conditions prospective charter schools must meet to qualify for the geographic exception. For example, the Legislature could clarify whether prospective charter schools qualify for the exception when their petitions indicate that they will serve primarily students residing outside the authorizing district's jurisdiction.
- Require any district that is considering authorizing an out-of-district charter school to notify the school's host district 30 days in advance of the board meeting at which the potential authorizing district is scheduled to make its authorization decision. The Legislature should also require the potential authorizing district to hold the public hearing within the host district's boundaries, notwithstanding restrictions in the State's Ralph M. Brown Act that would otherwise require the hearing to be held in the authorizing district.

To ensure charter school accountability, the Legislature should amend state law to require charter schools to annually report all their school locations—including school sites, resource centers, and administrative offices—to their authorizers and Education.

To remove the financial incentive for districts to authorize out-of-district charter schools, the Legislature should amend state law to prohibit districts from charging fees for additional services above the actual cost of services provided.

To ensure that authorizers have adequate tools and guidance for providing effective financial oversight, the Legislature should require the State Education Board and Education to work with representatives from county offices of education, representatives from districts, and subject-matter experts, such as FCMAT, to either establish a committee or work with an existing committee to report to the Legislature recommendations on the following:

- Defining criteria that would allow authorizers to revoke or deny renewal of schools' charters for financial mismanagement despite increases in academic achievement.
- Developing a template that authorizers can use to provide their charter schools with annual feedback on their financial performance.

To ensure that districts are aware of significant issues that may impact the out-of-district charter schools they authorize, the Legislature should amend state law to require each district to place a district representative as a nonvoting member on each out-of-district charter school's governing board and allow such a representative to attend all meetings of the charter school's governing board.

To ensure that charter schools improve the educational outcomes of their students, the Legislature should amend state law to require authorizers to assess annually whether their charter schools are meeting the academic goals established in their charters.

### ***Districts***

To make certain that they authorize only qualified petitions, Acton-Agua Dulce Unified and New Jerusalem should revise their charter school authorization policies to require the documentation of their evaluations of charter school petitions. The districts should present this documentation to their governing boards for their consideration.

To better ensure effective oversight of their charter schools' finances, the districts we visited should do the following:

- Develop written procedures for reviewing charter schools' financial information and conducting annual oversight visits. These procedures should include relevant requirements from the districts' agreements with the charter schools as well as best practices.
- Develop written procedures for addressing financial concerns.
- Place a district representative as a nonvoting member on each charter school's governing board.

To better ensure effective oversight of their charter schools' finances, Antelope Valley Union and New Jerusalem should provide charter schools with written feedback and recommendations for improving their financial operations after completing their financial review and annual oversight visits.

To ensure that charter schools work toward the academic goals established in their charters, the authorizing districts we visited should do the following:

- Adopt a policy requiring them to provide their charter schools with timely feedback and recommendations regarding academic performance.
- Adopt an academic oversight policy that includes steps for working with charter schools with poor performance results.
- Provide their charter schools with annual oversight reports on their academic performance.

**Agency Comments**

Acton-Agua Dulce Unified and Antelope Valley Unified generally agreed with our findings and conclusions, and indicated they will take actions to implement our recommendations. Although New Jerusalem disagreed with our findings and conclusions, it stated that it plans to implement some of our recommendations.

# Introduction

## Background

In 1992 the California Legislature enacted the Charter Schools Act of 1992 (Charter Schools Act), which allows teachers, parents, students, and community members to initiate the establishment of charter schools that operate independently of existing school district (district) structures. According to state law, the legislative intent of the Charter Schools Act is for charter schools to improve student learning; to increase learning opportunities for all students, with special emphasis on expanded learning experiences for academically low-achieving students; to meet measurable student outcomes; to operate under performance-based accountability systems; and to stimulate continual improvements in all public schools. It also encourages charter schools to develop innovative teaching methods, to create new professional opportunities for teachers, to provide parents and pupils with expanded choices in the types of educational opportunities that are available, and to create vigorous competition in order to improve the State's public school system. Like districts, charter schools are publicly funded, nondiscriminatory, and tuition-free.

Charter schools are generally exempt from most laws governing districts, but they are required to comply with select statutes, such as those establishing a minimum age for public school attendance. State law also requires charter schools to meet certain conditions for funding, such as participation in the statewide testing of students. In addition to providing classroom-based instruction at school sites, charter schools can also open resource centers that must be used exclusively for the educational support of students enrolled in nonclassroom-based study programs, including independent study, home study, work-study, and distance and computer-based education.

## Charter School Authorization Process

Charter schools can be authorized by three different types of entities: the governing board of a district, a county board of education, or the State Board of Education (State Education Board). These authorizing entities (authorizers) are responsible for overseeing the charter schools they authorize, as are the charter schools' own governing boards if nonprofit public-benefit corporations operate the schools. In fiscal year 2016–17, California had more than 300 charter authorizers and about 1,250 active charter schools that served more than 600,000 students. About 87 percent—or 1,080—of these charter schools obtained their authorizations from districts.

### Elements That State Law Requires in Charter School Petitions:

- Description of the school's educational program.
- Measurable student outcomes the school plans to use.
- Method for measuring student progress in achieving those outcomes.
- School governance structure, including the process the school will use to ensure parental involvement.
- Qualifications that individuals the school employs must meet.
- Procedures to ensure the health and safety of students and staff.
- Description of how the school will achieve a student racial and ethnic balance reflective of the general population residing in the district.
- Admission requirements, if applicable.
- Description of how annual financial audits will be conducted and how audit exceptions and deficiencies uncovered by the audits will be resolved.
- Procedures for suspending or expelling students.
- Provisions to cover employees under the California State Teachers' Retirement System, the California Public Employees' Retirement System, or the federal Social Security program.
- Public school alternatives for students residing within the district who choose not to attend charter schools.
- Description of the rights of any school district employee who leaves the employ of the school district to work in a charter school and of any rights of an employee to return to the school district after employment at a charter school.
- Procedures to resolve disputes between the authorizer and the charter school relating to conditions of the charter.
- The procedures to be used if the charter school closes.

Source: Education Code section 47605(b)(5).

The authorization process begins when a group of parents, teachers, or community members submits a charter petition (petition) to an authorizer for a prospective charter school. State law requires each petition to contain certain components, including either parent or teacher signatures, proposed budgets and financial projections, and a reasonably comprehensive description of required elements, which we list in the text box. In addition, the petition must affirm that the school will not charge tuition and will not discriminate against any student based on ethnicity, national origin, religion, gender, disability, or other protected characteristics.

Upon receiving a petition, an authorizer has 30 days to hold a public hearing on the provisions of the charter, at which time the authorizer must consider the level of support for the petition by members of the community, such as parents and teachers. The authorizer reviews the petition and makes a recommendation to the relevant board (the school district board, the county board, or the State Education Board). Within 60 days of receiving the petition, the relevant board must approve or deny the petition. In the case of a petition submitted directly to the county board of education, these deadlines are extended by 30 days. The relevant board cannot deny a petition unless it makes written factual findings that the petition does one of the following:

- Presents an unsound educational program.
- Indicates that the school is demonstrably unlikely to successfully implement the educational program set forth in the petition.
- Does not contain the required number of signatures—either half the parents of the number of students the school expects to enroll in the first year or half the teachers it expects to employ in the first year.
- Does not contain a declaration that the school will remain nonsectarian, not charge tuition, and not discriminate.
- Does not contain a reasonably comprehensive description of all statutorily required elements.

- Does not contain a declaration of whether the charter school will be the exclusive public school employer of the charter school employees.

Once approved, the petition becomes an agreement—or charter—between the authorizer and the charter school. The authorizer and charter school may also expand upon this agreement by entering memorandums of understanding that further define each party’s legal responsibilities. For example, the authorizer may agree to provide additional services to the charter school for a fee.

State law limits the effective term of a charter school to five years, after which an authorizer may renew the charter. The charter-renewal process is similar to the initial authorization process, but a charter school seeking a renewal must also satisfy academic performance requirements. State law requires an authorizer to consider increases in academic achievement as the most important factor in determining whether to grant a charter renewal.

### Responsibilities of Charter School Authorizers

State law requires that an authorizer perform certain duties, as the text box shows. For example, an authorizer must provide timely notification to the California Department of Education (Education) if it revokes a school’s charter. State law allows an authorizer to take steps to revoke a school’s charter if the authorizer finds that the school has committed a material violation of its charter, failed to achieve or pursue any of its student outcomes, engaged in fiscal mismanagement, or violated any provisions of law. However, as in the charter-renewal process, state law intends that an authorizer consider increases in student academic achievement for all groups of students as the most important factor in determining whether to revoke a charter.

If an authorizer believes that it has substantial evidence showing sufficient grounds for revoking a charter, it must adhere to the revocation timeline established in state law. Specifically, state law requires the authorizer to first notify the school of its violations and give it a reasonable amount of time to correct each violation unless a violation constitutes a severe and imminent threat to student health and safety. If the school does not take corrective action, the authorizer can then proceed

#### Authorizers’ Key Statutory Responsibilities

State law requires an authorizer to do the following for each charter school under its authority.

- Visit each charter school at least annually.
- Ensure that each charter school prepares and submits annually the following reports by the following dates:
  - Preliminary budget by July 1.
  - Local control and accountability plan by July 1.
  - First interim financial report by December 15.
  - Second interim financial report by March 15.
  - Final unaudited financial report by September 15.
  - Annual independent financial audit report for the preceding year by December 15.
- Monitor the fiscal condition of each charter school.
- Provide timely notification to Education if the authorizer revokes a school’s charter or grants or denies the renewal of a school’s charter. It must also inform Education if a charter school will cease operations.

Source: Education Code sections 47604.32, 47604.33(a), and 47605(m).

to revoke the charter by providing the school with a written notice of intent to revoke and a notice of facts in support of revocation. Within 30 days of the authorizer's sending the revocation notice, the authorizer's board must hold a public hearing to decide whether enough evidence exists to revoke the school's charter. The board then has another 30 days to issue its decision on charter revocation.

As part of these legal requirements, the Education Code requires an authorizer to fund the cost of performing these duties with supervisory oversight fees. State law allows an authorizer to charge for the actual costs of supervisory oversight not to exceed 1 percent of a charter school's revenue, or 3 percent of its revenue if the authorizer provides substantially rent-free facilities. Oversight fees are separate from fees associated with any additional services that a charter school may purchase from its authorizer.

### **Charter School Funding**

Like traditional public schools, California charter schools receive funding based on the State's local funding plan, which generally considers the grade levels a school serves and the average daily attendance of a school's enrolled students. Under this plan, charter schools receive funding primarily from three sources: state aid, the Education Protection Account, and local revenue. Proposition 30 created the Education Protection Account, which sets aside additional state aid for public schools. Local revenue, on the other hand, refers to the funding that charter schools receive in lieu of property taxes. In the years since the implementation of the local funding plan, state aid has consistently been the biggest source of revenue for charter schools statewide, followed by local revenue and the Education Protection Account. However, the proportions of the funding that charter schools receive from each of these three sources vary.

Charter schools' organizational structures and degrees of autonomy from their authorizers typically determine how they elect to receive funding. Locally funded charter schools usually have the same governing board as their authorizing districts, and they are highly dependent on those districts for services, such as those for special education and data reporting. These schools typically receive their funding through their authorizers. In contrast, directly funded schools are operated typically by nonprofit public-benefit corporations. These schools receive their funding from county offices of education, which act as pass-through agencies for distributing state funding to the charter schools. When nonprofit public-benefit corporations operate or manage multiple charter schools, the corporations are commonly referred to as *charter management organizations* (CMOs). CMOs share resources

and centralize certain functions among schools—such as hiring, professional development, and advocacy—and they may be involved in submitting petitions for charter schools they propose to operate. In exchange for these services, CMOs typically charge their charter schools management fees or allocate centralized expenses to the schools.

### **The Charter Schools Named in the Audit Request**

In 2002 the Legislature amended state law to provide additional requirements specific to the locations of charter schools, among other things. An analysis by the Senate Committee on Education quoted the bill's author to state that amendments were needed to address concerns related to a charter school that accumulated a \$1.3 million debt in one year. The amount of this debt raised questions about how the school used state and federal funding. For example, the bill analysis stated that one of the school's sites may have provided sectarian studies and charged tuition, activities that state law prohibits. According to the bill analysis, the district cited the difficulties of keeping track of remote operations as a reason it did not discover the various anomalies sooner. The site in question was located outside its authorizing district's geographical boundaries and an Assembly Committee on Education hearing for the same bill cited the Legislative Counsel's conclusion that charter schools do not have authority to establish locations outside the boundaries of their authorizing school districts.

Similarly, the audit request for this report resulted from concerns about management and oversight of out-of-district charter schools. Specifically, the request identified as subjects for review Acacia Elementary Charter School (Acacia Elementary), Assurance Learning Academy (Assurance Academy), and Los Angeles County Online High School (LA Online). Each of these three charter schools either operated or currently operates outside its authorizing district's geographical boundaries. Table 1 on the following page provides background information about these out-of-district charter schools.

Acacia Elementary was a directly funded charter school authorized by New Jerusalem Elementary School District (New Jerusalem) and managed by Tri-Valley Learning Corporation (Tri-Valley). Although New Jerusalem is located in Tracy, Acacia Elementary operated within the boundaries of Stockton Unified School District (Stockton Unified). Tri-Valley filed for bankruptcy during fiscal year 2016–17, forcing Acacia Elementary to cease operations at the end of fiscal year 2016–17. Chapter 2 discusses the events leading to Acacia Elementary's closure.

Assurance Academy is a directly funded charter school authorized by Acton-Agua Dulce Unified School District (Acton-Agua Dulce Unified) and managed by the Lifelong Learning Administration Corporation. Although Acton-Agua Dulce Unified is located in Acton, Assurance Academy operates primarily within the boundaries of Los Angeles Unified School District (Los Angeles Unified).

LA Online was a directly funded charter school authorized by Antelope Valley Union High School District (Antelope Valley Union). Portable Practical Educational Preparation, Inc.,-California (PPEP) operated LA Online through the end of fiscal year 2013–14, at which time PPEP changed its name to Olin Virtual Academy. For the purposes of this report, we refer to both entities collectively as LA Online. LA Online’s board of directors resolved to file for bankruptcy during fiscal year 2015–16, and LA Online ceased operations in February 2017. Although Antelope Valley Union is located in Lancaster, LA Online’s administrative office operated within the boundaries of Glendale Unified School District (Glendale Unified). We discuss the events leading to LA Online’s bankruptcy in Chapter 2.

**Table 1**  
**Profiles of the Three Out-of-District Charter Schools Identified in the Audit Request**

SCHOOL PROFILE	ACACIA ELEMENTARY	ASSURANCE ACADEMY	LA ONLINE
Authorizing district	New Jerusalem	Acton-Agua Dulce Unified	Antelope Valley Union
District office city	Tracy	Acton	Lancaster
Type of school	Classroom-based	Nonclassroom-based	Nonclassroom-based
Status as virtual or nonvirtual school	Not virtual	Not virtual	Fully virtual
Charter school city	Stockton	Los Angeles	La Crescenta
Charter school county	San Joaquin County	Los Angeles County	Los Angeles County
Annual average daily attendance for fiscal year 2015–16	382	763	255
Grades served	K–5	9–12	9–12
Fiscal years of operation	2013–14 through 2016–17	2012–13 to present	2007–08 through 2016–17
State funding allocation for fiscal year 2015–16	\$3.5 million	\$8.5 million	\$2.4 million

Sources: California State Auditor’s analysis of data from Education and from fiscal year 2015–16 audited financial statements for Assurance Academy and LA Online.

In addition to reviewing the charter schools and authorizing districts named in the audit request, we also examined the policies and procedures of the districts in which the three charter schools

operated (host districts). Table 2 provides background information on the authorizing districts and host districts of the charter schools identified in the audit request.

**Table 2**  
**Profiles of the Authorizing School Districts and Host School Districts for the Three Out-of-District Charter Schools That We Reviewed**

SCHOOL DISTRICT PROFILE	ACACIA ELEMENTARY		ASSURANCE ACADEMY		LA ONLINE	
	AUTHORIZING SCHOOL DISTRICT	HOST SCHOOL DISTRICT	AUTHORIZING SCHOOL DISTRICT	HOST SCHOOL DISTRICT	AUTHORIZING SCHOOL DISTRICT	HOST SCHOOL DISTRICT
	NEW JERUSALEM	STOCKTON UNIFIED	ACTON-AGUA DULCE UNIFIED	LOS ANGELES UNIFIED	ANTELOPE VALLEY UNION	GLENDALE UNIFIED
School district's county	San Joaquin	San Joaquin	Los Angeles	Los Angeles	Los Angeles	Los Angeles
<b>Fiscal Year 2015–16</b>						
Number of students enrolled in district	5,015	40,324	7,475	639,337	24,127	26,117
Percentage of socioeconomically disadvantaged students	54%	81%	36%	81%	71%	48%
Number of noncharter schools	1	50	3	732	13	33
Number of charter schools	13	13	14	274	3	0
Number of out-of-district charter schools*	10	0	11	0	2	0

Sources: California State Auditor's analysis of multiple documents, interviews, and data obtained from Education, and the Accrediting Commission for Schools—Western Association of Schools and Colleges' directory of schools.

\* A single charter school may have a number of different locations. We did not include these locations when calculating the number of out-of-district charter schools.

### Scope and Methodology

The Joint Legislative Audit Committee (Audit Committee) directed the California State Auditor to determine the adequacy of the financial and academic oversight that authorizing districts provided to three out-of-district charter schools: Acacia Elementary, Assurance Academy, and LA Online. We list the objectives that the Audit Committee approved and the methods used to address them in Table 3 beginning on the following page.

**Table 3**  
**Audit Objectives and the Methods Used to Address Them**

AUDIT OBJECTIVE	METHOD
1 Review and evaluate the laws, rules, and regulations significant to the audit objectives.	Reviewed relevant laws, rules, regulations, and other background materials.
2 Determine whether the districts that are authorizing multiple charters are adhering to the limitations for authorizing charter schools outside their geographical boundaries.	<p>For Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem, we did the following:</p> <ul style="list-style-type: none"> <li>• Interviewed district staff and obtained the districts' policies and procedures for authorizing charter schools.</li> <li>• Reviewed the districts' policies and procedures to determine whether they reflect the state law's limitations for authorizing charter schools that are located outside of an authorizing district's geographical boundaries.</li> <li>• Obtained and reviewed evidence to determine whether Acacia Elementary, Assurance Academy, and LA Online—the three out-of-district charter schools named in Objective 6—attempted to locate facilities within the boundaries of their authorizing districts and whether their authorizing districts attempted to locate sites within their geographic boundaries before authorizing the out-of-district locations.</li> <li>• Determined the districts' total number of out-of-district charter school locations. We also reviewed petitions for Acacia Elementary, Assurance Academy, LA Online and one additional directly funded out-of-district charter school per district to determine whether the petitions complied with state law. Further, we reviewed New Jerusalem's locally funded out-of-district charter school to determine whether the district followed its authorization process.</li> <li>• In addition, we obtained lists of charter school locations from Education and used them to determine the number of out-of-district charter schools statewide. To make the lists more complete, we included addresses from the directory of schools used by the Accrediting Commission for Schools, Western Association of Schools and Colleges.</li> </ul>
3 Determine whether the districts' authorizing processes for charter schools located outside their geographic boundaries meet legal requirements and are rigorous enough to ensure the likely success of the charter schools they authorize. Compare those processes to the authorizing processes of other districts with charter schools located within the district and determine the reasons for any significant differences.	<p>For Acton-Agua Dulce Unified, Antelope Valley Union, Glendale Unified, Los Angeles Unified, New Jerusalem, and Stockton Unified, we did the following:</p> <ul style="list-style-type: none"> <li>• Interviewed district management and staff to identify the process the districts use when authorizing charter schools and to identify any differences in the processes depending on the charter schools' geographic locations.</li> <li>• Obtained and reviewed administrative procedures from each school district related to reviewing petitions and identified gaps that may exist between the districts' processes and state law.</li> <li>• Determined whether the district's policies for authorizing petitions aligned with the criteria that the State Board of Education uses to evaluate petitions.</li> <li>• Compared processes within and among districts.</li> </ul> <p>For Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem, we determined whether each district followed its own authorization process for one locally funded in-district charter school, one directly funded in-district charter school, and the out-of-district charter school named in Objective 6.</p>
4 Assess the districts' oversight and monitoring of the financial information for charter schools they authorize that are located outside their respective district's geographic boundaries and compare those processes to the oversight and monitoring performed by the districts when the charter schools are located within the authorizing district.	<p>For Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem, we did the following:</p> <ul style="list-style-type: none"> <li>• Interviewed district staff and obtained the district's policies and procedures for performing financial oversight. We determined that the financial oversight policies and procedures the districts provide to charter schools do not differ based on the schools' geographic locations.</li> <li>• Reviewed the districts' policies and procedures to determine whether they include state law's requirements for the oversight and monitoring of charter schools. Because state law does not establish a minimum level of oversight that districts must perform, we used best practices from the Fiscal Crisis and Management Assistance Team (FCMAT) and the National Association of Charter School Authorizers to assess the districts' oversight and monitoring processes.</li> <li>• Obtained and reviewed the financial reports for the last three years for Acacia Elementary, Assurance Academy, and LA Online and determined whether the districts followed their monitoring processes for reviewing the schools' finances. We also compared each district's monitoring processes to its process for monitoring directly funded in-district charter schools.</li> <li>• If a district had revoked one of its charter schools, obtained and reviewed documents that supported the district's decision and determined whether the conditions justifying the revocation exist in any of the other selected charter schools.</li> </ul>

AUDIT OBJECTIVE	METHOD
<p>5 Assess the adequacy of the academic oversight performed by the authorizing districts for the charter schools located outside of their geographic boundaries and, to the extent possible, compare the academic oversight performed with that of charter schools operating within the boundaries of the authorizing districts.</p>	<p>For Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem, we did the following:</p> <ul style="list-style-type: none"> <li>• Interviewed district staff and obtained the districts’ policies and procedures for performing academic oversight. We determined that the academic oversight that the districts provide to charter schools does not differ based on schools’ geographic locations.</li> <li>• Obtained and reviewed the last three fiscal years’ academic reports that Acacia Elementary, Assurance Academy, LA Online and a directly funded in-district charter school in each district sent to their authorizing districts, as required under their memorandums of understanding with the districts, and determined whether the districts followed their monitoring processes for reviewing the charter schools’ academic performance.</li> </ul>
<p>6 For Acacia Elementary, Assurance Academy, and LA Online, perform the following:</p>	
<p>a. Determine whether the selected charter schools are financially stable and are meeting accepted financial norms and state requirements.</p>	<ul style="list-style-type: none"> <li>• Interviewed school staff and obtained policies and procedures about the schools’ accounting and budgeting processes.</li> <li>• Determined whether the schools’ financial reporting complied with requirements in state law.</li> <li>• Determined whether the schools’ reserves met the minimum levels required by the agreements with their authorizing districts.</li> <li>• Reviewed charter schools’ audited financial statements for transactions among charter schools and their related parties during our audit period. We noted that LA Online did not report any related-party transactions, while Assurance’s related-party transactions generally pertained to the shared costs of operating expenses and educational services. We further describe Acacia’s related-party transactions in Chapter 2.</li> </ul>
<p>b. Assess whether the selected charter schools’ three-year financial projections meet the requirements of their respective county offices of education.</p>	<p>We did not find any applicable requirements.</p>
<p>c. Determine the academic results of the selected charter schools and compare them to county averages and similar noncharter public schools.</p>	<ul style="list-style-type: none"> <li>• Selected similar noncharter public schools for comparison based on school type, grade levels served, number of students, percentage of socioeconomically disadvantaged students, and percentage of English learners. We selected traditional schools in Stockton Unified for comparison to Acacia Elementary, Alternative School Accountability Model schools in Los Angeles Unified for comparison to Assurance Academy, and primarily or exclusively virtual schools statewide for comparison to LA Online because no comparable schools exist in Los Angeles County.</li> <li>• Obtained the California Assessment of Student Performance and Progress (CAASPP) results for fiscal years 2014–15 through 2015–16 and compared each charter school’s results to results of the schools we selected for comparison. For fiscal year 2013–14, we obtained the Academic Performance Index because the State did not implement CAASPP until fiscal year 2014–15.</li> <li>• Compared the graduation rates and expulsion rates of each charter school and the schools that we selected for comparison. We found that the three charter schools we visited had lower expulsion rates than did similar schools.</li> </ul>
<p>7 Determine whether the financial oversight fees of the chartering districts exceed the limits set by state law for charter schools located outside the authorizing districts’ geographic boundaries.</p>	<p>For Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem, we did the following:</p> <ul style="list-style-type: none"> <li>• Obtained the past three years of invoices the districts sent to Acacia Elementary, Assurance Academy, and LA Online, as well as evidence of payment.</li> <li>• Determined whether the districts charged the charter schools based on the actual costs of providing oversight and services and whether they charged more than the legal maximum.</li> <li>• Identified any additional service fees that the districts imposed and determined whether the charter schools benefited from those services.</li> </ul>
<p>8 Review and assess any other issues that are significant to the audit.</p>	<p>We reviewed the FCMAT audit report of Tri-Valley Learning Corporation. In this report, we identified findings related to Acacia Elementary, and we obtained supporting documentation for such findings, when possible.</p>

Sources: California State Auditor’s analysis of Joint Legislative Audit Committee audit request 2016-141 and information obtained from the school districts of Acton-Agua Dulce Unified, Antelope Valley Union, Glendale Unified, Los Angeles Unified, New Jerusalem, and Stockton Unified; Acacia Elementary, Assurance Academy; LA Online, Education; and FCMAT.

### Assessment of Data Reliability

In performing this audit, we obtained electronic data files extracted from the data sources listed in Table 4. The U.S. Government Accountability Office, whose standards we are statutorily required to follow, requires us to assess the sufficiency and appropriateness of computer-processed information that we use to support findings, conclusions, or recommendations. Table 4 describes the analyses we conducted using data from these sources, our methods for testing, and the results of our assessments. Although these determinations may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.

**Table 4**  
**Methods Used to Assess Data Reliability**

DATA SOURCE	PURPOSE	METHOD AND RESULT	CONCLUSION
Education's DataQuest	To determine the enrollment; percentages of English learners and socioeconomically disadvantaged students; school climate; and cohort outcomes for schools and school districts.	We did not perform accuracy and completeness testing on these data because it is a paperless system with any records stored at local educational agencies throughout the state, making testing cost-prohibitive. Alternatively, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews.	<b>Undetermined reliability for these audit purposes.</b>  Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.
Education's Local Control Funding Formula—Funding Snapshot	To determine annual funding summaries for individual school districts and charter schools.	We did not perform accuracy and completeness testing on these data because the system is a paperless system and local educational agencies submit data electronically, making testing cost-prohibitive. Alternatively, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews. To gain some assurance of the data's reliability, we reviewed existing information and found that local educational agencies report data that Education uses to calculate funding exhibits and updates throughout the year. According to Education's website, county offices of education serve as one mechanism for checking the accuracy of data used in the LCFF Funding Snapshot. Additionally, according to a fiscal consultant with Education, her unit conducts reviews and testing of the data prior to releasing the data on Education's website.	<b>Undetermined reliability for these audit purposes.</b>  Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.

DATA SOURCE	PURPOSE	METHOD AND RESULT	CONCLUSION
Education's California School Directory	To determine all locations of charter schools as of May 2017, to select schools comparable to the charter schools named in the scope and objectives, and to provide background information.	<p>We used this system for a purpose for which it was not originally intended; however, this system was the best source of information for our purpose. We performed data-set verification procedures and electronic testing of key data elements and did not identify significant issues. We did not perform comprehensive accuracy and completeness testing because the source documents are stored throughout the State, making testing cost prohibitive. To gain some assurance of the data's reliability, we reviewed existing information and determined that according to Education's website, local educational agencies are responsible for updating and maintaining information for charter schools and the charter schools' personnel can review their schools' data. The school directory data contains only two charter school addresses at most—a street address for the charter school's main location and a mailing address for the charter school. Since some charter schools have more than two locations, these data are incomplete for the purpose of determining all charter school locations.</p> <p>To improve the completeness of the location data we included addresses from Education's Charter School Division survey database. We performed data-set verification procedures and electronic testing of key data elements and did not identify any significant issues. To test the completeness of the data we compared it to the Accrediting Commission for Schools–Western Association of Schools and Colleges' public directory. We found that 12 of the 29 records we tested were not in the survey data.</p> <p>To further improve the completeness of the data we included addresses for charter schools that have multiple campuses from the Accrediting Commission for Schools—Western Association of Schools and Colleges' public directory. We did not assess the reliability of these data because not all charter schools have to pursue accreditation through the Accrediting Commission for Schools, Western Association of Schools and Colleges and we only obtained a list of charter schools with multiple campuses which lead to inherent limitations in the completeness of these data for our audit purpose.</p>	<p><b>Not sufficiently reliable for purposes of determining all locations of charter schools, and undetermined reliability for the other audit purposes.</b></p> <p>Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.</p>
Education's California Assessment of Student Performance and Progress System's Smarter Balanced Summative Assessments	To determine academic performance of charter schools and comparable entities.	We did not perform accuracy and completeness testing on these data because the system is a primarily paperless system, making testing cost-prohibitive. Alternatively, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews.	<p><b>Undetermined reliability for these audit purposes.</b></p> <p>Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.</p>

Sources: California State Auditor's analysis of multiple documents, interviews, and data from the entities listed in the Table.

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## Chapter 1

### **SOME DISTRICTS HAVE EXPANDED THEIR REACH AND INCREASED THEIR REVENUE BY AUTHORIZING OUT-OF-DISTRICT CHARTER SCHOOLS**

Two of the three districts we reviewed—Acton-Agua Dulce Unified and New Jerusalem—expanded their reach by using exceptions in state law to authorize out-of-district charter schools. However, neither district was able to demonstrate that the schools they authorized actually qualified for these exceptions. Further, state law does not provide host districts with a process for challenging the authorization of out-of-district charter schools, even if the host districts have previously rejected the schools' petitions. As a result, Acton-Agua Dulce Unified and New Jerusalem were able to authorize charter schools with little evidence of community support in the host districts. Acton-Agua Dulce Unified's and New Jerusalem's authorizations of out-of-district charter schools led to significant increases in the districts' enrollment numbers and provided a method for the districts to substantially increase their revenue. Further, both Acton-Agua Dulce Unified and New Jerusalem authorized charter schools despite their petitions missing basic components, such as the minimum number of parent or teacher signatures. Finally, all three districts we visited had outdated charter school policies and did not ensure that their staff thoroughly reviewed petitions for compliance with all legal requirements.

#### **By Authorizing Charter Schools Outside Their Jurisdictions, Two of the Districts We Reviewed Impaired Local Control of Education**

Acton-Agua Dulce Unified and New Jerusalem have used exceptions within the state law on charter school authorization to expand their reach through the establishment of out-of-district charter schools. According to Education's guidance, the State's educational system relies on local control for the management of districts on the theory that the people closest to the problems and needs of each individual district are best able to make appropriate decisions on its behalf. In addition, state law requires charter schools to operate within the geographic boundaries of their authorizers, with limited exceptions. Specifically, state law allows a charter school to establish one out-of-district site within the district's county if no available site or facility exists to house the entire school program in the area in which the school chooses to locate or if the site is for temporary use during construction. However, neither Acton-Agua Dulce Unified nor New Jerusalem could provide evidence that their out-of-district charter schools had, in fact, qualified for these exceptions during the authorization process.

***Some of the charter schools' petitions we reviewed indicated their intent to locate outside the district's jurisdiction by identifying their target student populations as those in another district—a circumstance that appears to conflict with the 2002 amendments to the Charter Schools Act.***

Further, some of the charter schools' petitions we reviewed indicated their intent to locate outside the district's jurisdiction by identifying their target student populations as those in another district—a circumstance that appears to conflict with the 2002 amendments to the Charter Schools Act that specify charter schools should be located within their authorizing districts. For example, Acacia Elementary's petition stated that the school's intention was to serve students within San Joaquin County, with particular attention to underserved students in Stockton, even though the authorizing district was in Tracy. Likewise, Assurance Academy's petition proposed to serve students throughout Los Angeles County and adjacent counties.

According to New Jerusalem's superintendent, his district's charter schools meet the legal exception for situations in which no available facilities exist within the district. However, given the statutory limitations that require a charter school to be located in the geographic boundaries of the chartering district, New Jerusalem's reliance on this exception is misplaced because to be consistent with the law, the schools that New Jerusalem has authorized should have petitioned the districts where the students the charter schools chose to target were located. By using this exception in state law, New Jerusalem increased its enrollment with students who would otherwise attend schools in neighboring districts. According to 2010 U.S. Census data, the total population of school-age residents within New Jerusalem's geographical boundaries was only about 330 people. However, New Jerusalem increased its enrollment from 686 students in fiscal year 2010–11 to 5,015 students in fiscal year 2015–16 by increasing the number of its out-of-district charter schools from zero to 10, as Table 5 shows. For example, in the case of Acacia Elementary, none of its 421 students in fiscal year 2015–16 lived within New Jerusalem's geographical boundaries. Thus, the decision of New Jerusalem's board to authorize out-of-district charter schools has resulted in the diversion of a significant number of students from other districts to New Jerusalem's charter schools. According to New Jerusalem's superintendent, the district is meeting the intent of the Charter Schools Act by providing students and parents in districts within San Joaquin County and contiguous counties with expanded learning opportunities and by providing vigorous competition within the public school system. However, New Jerusalem's actions do not appear to meet the Legislature's intent for local districts to authorize the charter schools operating in their districts.

Similarly, Acton-Agua Dulce Unified has increased its enrollment by authorizing out-of-district charter schools. At a time when the number of its students had significantly decreased, Acton-Agua Dulce Unified's former superintendent presented a plan to his district's board to reverse its declining enrollment.

In December 2013, the board approved the former superintendent’s plan to take advantage of state law to earn revenue as a charter authorizer. Specifically, the proposal estimated that the district could increase enrollment to more than 30,000 students by the summer of 2016 through the authorization of approximately 24 charter schools. Although these projections were overly optimistic, Acton-Agua Dulce Unified increased its enrollment from 2,383 students in fiscal year 2013–14 to 7,475 students in fiscal year 2015–16, despite having an in-district school-age population of only about 2,500 according to the latest census data. As of May 2017, Acton-Agua Dulce Unified had authorized 12 charter schools that operated a total of 33 out-of-district locations, some of which were more than 50 miles away from the district. According to the district’s director of charter schools, she was unaware of the district’s plan, and no one has referred to it since she took her position in February 2016.

**Table 5**  
**By Authorizing Out-of-District Charter Schools, Two of the Three Districts We Reviewed Substantially Increased Their Numbers of Schools and Students**

SCHOOL DISTRICT	FISCAL YEAR											
	2010–11		2011–12		2012–13		2013–14		2014–15		2015–16	
	NUMBER OF SCHOOLS*	NUMBER OF STUDENTS										
<b>Acton-Agua Dulce Unified</b>												
Noncharter	4	1,696	4	1,506	4	1,377	4	1,301	3	1,083	3	1,098
In-district charter	0	0	0	0	0	0	0	0	3	266	3	362
Out-of-district charter <sup>†</sup>	0	0	0	0	1	165	2	1,082	9	2,694	11	6,015
<b>District total</b>	<b>4</b>	<b>1,696</b>	<b>4</b>	<b>1,506</b>	<b>5</b>	<b>1,542</b>	<b>6</b>	<b>2,383</b>	<b>15</b>	<b>4,043</b>	<b>17</b>	<b>7,475</b>
<b>Antelope Valley Union</b>												
Noncharter	13	23,183	13	23,350	13	22,933	13	22,220	13	22,071	13	21,616
In-district charter	0	0	0	0	1	257	1	237	1	254	1	331
Out-of-district charter <sup>†</sup>	2	2,901	2	2,187	2	1,626	2	2,011	2	2,294	2	2,180
<b>District total</b>	<b>15</b>	<b>26,084</b>	<b>15</b>	<b>25,537</b>	<b>16</b>	<b>24,816</b>	<b>16</b>	<b>24,468</b>	<b>16</b>	<b>24,619</b>	<b>16</b>	<b>24,127</b>
<b>New Jerusalem</b>												
Noncharter	1	27	1	28	1	16	1	23	1	25	1	28
In-district charter	2	659	2	767	2	873	2	970	2	734	3	845
Out-of-district charter <sup>†</sup>	0	0	1	435	3	2,228	5	2,599	10	3,777	10	4,142
<b>District total</b>	<b>3</b>	<b>686</b>	<b>4</b>	<b>1,230</b>	<b>6</b>	<b>3,117</b>	<b>8</b>	<b>3,592</b>	<b>13</b>	<b>4,536</b>	<b>14</b>	<b>5,015</b>

Sources: California State Auditor’s analysis of Education’s school directory, charter school survey, and DataQuest; and the Accrediting Commission for Schools—Western Association of Schools and Colleges’ directory of schools.

\* The number of schools includes both in-district and out-of-district charter schools. It does not include the number of resource centers or other facilities that a school may operate.

† If the majority of a charter school’s locations were outside their authorizing district’s boundaries, we classified the school as an out-of-district charter school.

State law sets some requirements for the authorization of out-of-district charter schools, but the requirements that apply to an authorizing district are vague and ineffective. For example, if a charter school is unable to locate within the boundaries of an authorizing district, state law requires that the potential host district receive notice before the petition's authorization. However, state law does not specify how far in advance the host district needs to receive notice or which party—the authorizing district or proposed charter school—is responsible for providing the notification. As a result, New Jerusalem adhered to the law even though it did not notify Stockton Unified until a few hours before it authorized Acacia Elementary to operate within Stockton Unified's jurisdiction. In contrast, if an applicant submits a petition to a county office of education, state law requires that any district in which the applicant proposes to operate a charter school location receive at least 30 days' notice. According to Stockton Unified's principal auditor, Acacia Elementary provided an incomplete petition to Stockton Unified in December 2012 but then discontinued the process and instead sought authorization through New Jerusalem. Without sufficient notice of the potential authorization, the host district does not have time to respond to the possibility of a new school opening in its community. Further, the authorizing district may not identify issues that previously led the potential host district to reject the petition.

Moreover, even if a host district is aware of the petition, nothing in law establishes an administrative process for the host district to challenge the authorization of the charter school within its jurisdiction. For example, Acton-Agua Dulce Unified authorized charter schools to operate within the jurisdiction of potential host districts that had previously denied those charter schools' petitions. A board member from one potential host district attended an Acton-Agua Dulce Unified board meeting and raised concerns that his district had turned down the proposed charter school several times, but Acton-Agua Dulce Unified still chose to authorize the charter school. Because state law has not established a procedure for a host district to challenge the authorization of an out-of-district charter school within its jurisdiction, litigation is the host district's only recourse, potentially resulting in costly legal fees for both districts. According to a lawsuit that another host district filed against Acton-Agua Dulce Unified, the host district had denied a petition because the petition failed to identify how the charter school would attract a diverse population, serve English language learners, and address serious financial concerns.

***Because state law has not established a procedure for a host district to challenge the authorization of an out-of-district charter school within its jurisdiction, litigation is the host district's only recourse.***

State law allows a charter applicant to appeal a district's denial by submitting the petition first to the pertinent county office of education and then to the State Education Board if the county office of education also denies the petition. However, because state law does not prohibit a charter applicant from submitting a denied

petition to a neighboring school district, a charter applicant could potentially circumvent this process. If the out-of-district charter school then closes, its students are displaced, and this displacement may significantly impact the host district that will need to reenroll the students.

These gaps in state law also allow a district to authorize a charter school without the support of the local community where the charter school plans to operate. Specifically, nothing in state law requires the authorizing district to hold public hearings within the potential host district. For example, when New Jerusalem planned to authorize and operate an out-of-district charter within the boundaries of Stockton Unified, it held its public hearing in Tracy, 26 miles from where the district established the charter school. New Jerusalem's board thus authorized a locally funded charter school to operate in the jurisdiction of another district with minimal opportunity for the local community to provide public feedback. Moreover, because the parents of students in an out-of-district school cannot vote for the authorizing district's board members, the authorizing district is not accountable democratically to the charter school's community. In this way, state law allows authorizing districts to expand their reach, but it does not hold these districts accountable to the residents of the communities in which the districts' charter schools operate.

Further, two of the authorizing districts we visited made little effort to prevent charter schools from establishing additional out-of-district locations. For example, charter schools in Acton-Agua Dulce Unified and Antelope Valley Union opened out-of-district locations without the prior approval of their authorizing districts. When a charter school proposes to establish operations at one or more additional locations, state law requires it to submit a material revision of its charter to its authorizing district for approval. However, when Assurance Academy opened a resource center in fiscal year 2014–15, it did not notify or seek Acton-Agua Dulce Unified's approval. Similarly, LA Online entered into lease agreements for five resource centers in fiscal year 2015–16 without notifying Antelope Valley Union. Moreover, neither district required its charter schools to submit material revisions to their charters even after each district became aware of the location changes. According to Antelope Valley Union's assistant superintendent of educational services, it was a pervasive practice throughout the State for virtual and independent-study charter schools to open additional resource centers until a November 2016 appellate court decision in the *Anderson Union High School District v. Shasta Secondary Home School* case. The decision limited the ability of charter schools to establish out-of-district locations because the appellate court held that state law does not distinguish between classroom-based and nonclassroom-based charter schools and that geographic

***Two of the authorizing districts we visited made little effort to prevent charter schools from establishing additional out-of-district locations.***

restrictions apply to all charter schools. These restrictions state that a charter school may operate a nonclassroom-based location, such as a resource center, in an adjacent county as long as more than half of the school's students are residents of the authorizing district's county. However, with limited exceptions, it does not allow a charter school to operate a nonclassroom-based location outside the district's boundaries but within the same county. Districts throughout the State authorized charter schools to operate multiple nonclassroom-based locations outside the authorizing districts' boundaries, sometimes in the same county and sometimes in nonadjacent counties.

Although the appellate court decision provided additional guidance on geographic restrictions, it did little to clarify how those restrictions apply to charter schools that move locations or operate virtually. For example, Antelope Valley Union did not authorize any out-of-district charter schools directly, but it allowed one of its charter schools—LA Online—to relocate outside the district's boundaries without submitting a material revision to the school's charter. Antelope Valley Union's former director of categorical and special programs explained that the district did not believe geographical restrictions applied to LA Online because it was a virtual school that only moved its administrative office. State charter school law does not distinguish between virtual and nonvirtual schools, nor does it specifically include guidance about whether changing the location of a facility is a material revision of the charter that would require the charter school to apply to the authorizer for a material revision. Accordingly, Assurance Academy did not obtain a material revision from Acton-Agua Dulce Unified when it moved a resource center in fiscal year 2015–16. In addition, we noted that Acton-Agua Dulce Unified authorized a virtual charter school that has its administrative office in San Marcos—roughly 100 miles away from the district's boundaries. Although the district's director of charter schools explained that the school closed all its resource centers to comply with the appellate court decision, the remoteness of this site may make it difficult for the district to provide effective oversight.

***State law provides exceptions that have allowed some charter schools to continue operating nonclassroom-based locations outside their authorizing districts' boundaries.***

Moreover, state law provides exceptions that have allowed some charter schools to continue operating nonclassroom-based locations outside their authorizing districts' boundaries. The State Education Board can approve waivers to allow noncompliant charter schools to continue to operate during fiscal year 2017–18. These waivers thus give charter schools a grace period to comply with the appellate court ruling, avoiding disruption to educational programs. In May 2017, the State Education Board approved geographic waivers for about 30 charter schools from about 20 districts. Although the State Education Board required the authorizing districts to visit any resource centers that they had not previously visited that are

subject to the waiver, it did not prescribe specific procedures for the authorizing districts to follow during those site visits. Alternatively, charter schools that have exclusive partnerships with state or federal workforce programs, such as the California Conservation Corps or the federal Workforce Innovation and Opportunity Act, may avoid the geographic restrictions altogether.

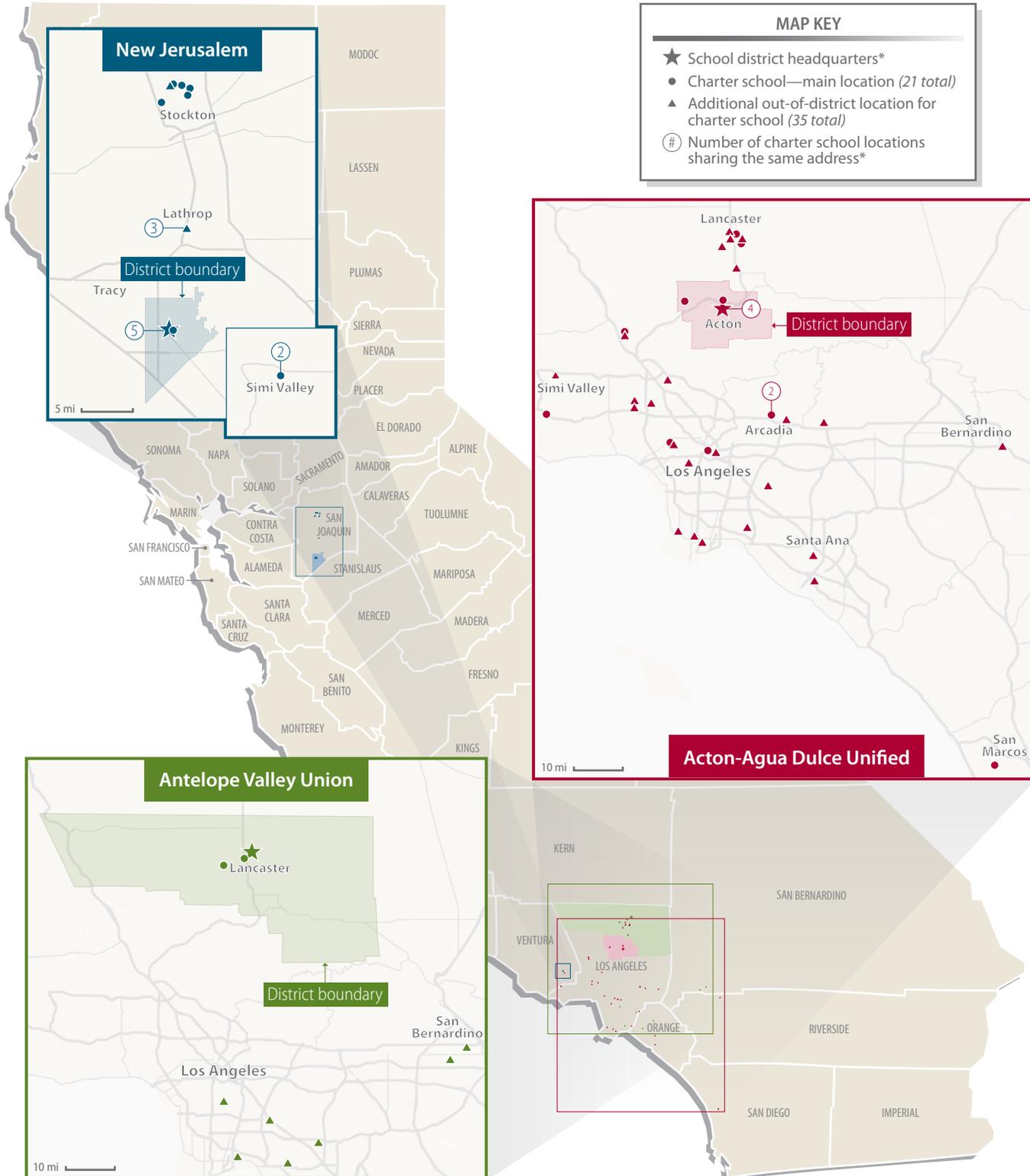
Finally, Education is unable to determine how many charter schools operate remotely because state law does not require charter schools to report all their locations—including school sites, resource centers, and administrative offices. Education conducts an annual survey to update its charter school data, including the locations of all additional sites. However, according to a manager in Education’s technology services division, about 300 charter schools did not submit charter surveys in the 2016–17 year. When we analyzed data from multiple sources, we found that of the State’s 1,246 charter schools in May 2017, 165 district-authorized charter schools operated at least one of their school locations outside their authorizing districts’ geographic boundaries in fiscal year 2016–17. These 165 charter schools operated in a total of 495 out-of-district locations statewide. Further, we determined 52 nonvirtual or primarily classroom-based schools had at least one location more than 20 miles from their authorizing districts’ boundaries. However, since complete data are not available, there may be more out-of-district charter school locations than we identified. For example, as of May 2017, Education’s online directory of charter schools lists only 30 charter school locations for the three districts we visited, but we identified 35 additional out-of-district charter school locations, as Figure 1 on the following page shows.

*As of May 2017, Education’s online directory of charter schools lists only 30 charter school locations for the three districts we visited, but we identified 35 additional out-of-district charter school locations.*

### **Districts Have a Financial Incentive to Authorize Charter Schools Outside Their Jurisdictions and to Charge Extra Fees**

Two of the school districts we visited were able to increase their revenue significantly by authorizing out-of-district charter schools. As the Introduction discusses, state funding for school districts and charter schools is linked to the average daily attendance of their enrolled students. New Jerusalem was able to increase its revenue by bolstering its enrollment through the authorization of locally funded charter schools located outside its boundaries. Acton-Agua Dulce Unified, on the other hand, increased its revenue by authorizing directly funded out-of-district charter schools that it then charged a flat administrative fee for services. Further, it did not justify the appropriateness of that fee. Finally, although state law limits administrative fees to a district’s actual costs, none of the three school districts we visited tracked their actual costs of providing oversight. This failure to track actual oversight costs could result in the undue diversion of funds from charter schools’ educational programs.

**Figure 1**  
Selected Districts and Charter School Locations



Sources: California State Auditor’s analysis of Education’s school directory, Education’s charter school survey, and the Accrediting Commission for Schools—Western Association of Schools and Colleges’ directory of schools as of May 2017; U.S. Census data; interviews with district administrators; and charter school websites.

\* Nine charter schools list their authorizing district’s headquarters as their main address.

**Two Districts We Visited Have Increased Their Revenue by Authorizing Out-of-District Charter Schools**

New Jerusalem and Acton-Agua Dulce Unified have significantly increased their enrollments and revenue by authorizing out-of-district charter schools. Districts we visited were able to generate revenue from the charter schools they authorized either by operating them as locally funded schools, which resulted in the districts’ receiving and managing the schools’ state funding, or by offering services to their charter schools in exchange for fees. New Jerusalem took the former approach, authorizing mostly locally funded charter schools. Acton-Agua Dulce Unified, on the other hand, authorized only directly funded charter schools but charged those schools for administrative services. Through these authorizations, New Jerusalem and Acton-Agua Dulce Unified have received a significant amount of revenue annually, as the text box shows.

**Two Districts’ Fees and Funding Plan Revenue From Out-of-District Charter Schools for Fiscal Year 2015–16**

NEW JERUSALEM	
Oversight fees	\$633,515
Local funding plan	\$5,496,798
<b>Total</b>	<b>\$6,130,313</b>
ACTON-AGUA DULCE UNIFIED	
Oversight fees	\$543,153
Administrative service fees	\$1,357,882
<b>Total</b>	<b>\$1,901,035</b>

Sources: California State Auditor’s analysis of financial statements, district invoices, interviews with district administrators, and Education’s Local Control Funding Formula Funding Snapshots.

New Jerusalem authorized four locally funded out-of-district charter schools, allowing it to manage those charter schools’ funding. Because state law does not prevent locally funded charter schools from operating outside their authorizing district’s jurisdiction, New Jerusalem was able to significantly expand its reach and increase its enrollment. New Jerusalem’s superintendent asserts that the district is meeting the intent of the Charter Schools Act; however, we disagree. New Jerusalem’s actions have enabled the district to expand its average daily attendance from outside its boundaries and do not appear to meet the Legislature’s strong preference to limit charter schools to the jurisdiction of their authorizing districts.

In contrast, before this audit, Acton-Agua Dulce Unified charged all its directly funded charter schools a 2.5 percent administrative services fee and a 1 percent oversight fee, effectively collecting a total of 3.5 percent of each charter school’s revenue. However, some of Acton-Agua Dulce Unified’s charter schools may have only made sporadic use of the services for which they paid. For example, the district’s memorandum of understanding (MOU) with Assurance Academy describes the administrative services as including the use of a library, reference materials, and equipment, as well as opportunities for training. Assurance Academy’s chief academic officer does not, however, believe the school has received all the services described by the MOU in every fiscal year. In addition, Assurance Academy has a separate agreement for administrative and educational services with its CMO, Lifelong Learning Administration Corporation, for which it pays 14 percent

*Assurance Academy has tripled the number of resource centers it plans to operate in fiscal year 2017–18. This could thus result in the school spending even more state funding on administrative fees for services that it does not consistently use instead of on the school's educational program.*

of its revenue. As a result, Assurance Academy paid more than \$1.5 million in fees for fiscal year 2015–16. The district's board voted to reduce the 2.5 percent fee to 2 percent in a May 2017 board meeting. Nevertheless, Assurance Academy has tripled the number of resource centers it plans to operate in fiscal year 2017–18. This change could thus result in the school spending even more state funding on administrative fees for services that it does not consistently use instead of on the school's educational program.

### ***Two Districts We Visited Charged Oversight Fees That Exceeded the Limits in State Law***

In violation of state law, both New Jerusalem and Antelope Valley Union charged their charter schools for oversight fees that exceeded 1 percent of the schools' revenue. State law allows an authorizer to charge for its actual costs of oversight of a charter school up to 1 percent of the charter school's local funding plan revenue or up to 3 percent if the authorizer provides facilities that are substantially rent-free—circumstances that do not apply to either New Jerusalem or Antelope Valley Union. Although Antelope Valley charged LA County Online more than 1 percent in fiscal year 2014–15, it charged less than 1 percent in the other two years we reviewed, reducing its average fee to 0.6 percent across the three years. In contrast, during the three years we tested, New Jerusalem overcharged Acacia Elementary by a total of about \$100,000—more than double the legally permitted amount. New Jerusalem's superintendent asserted that he had a verbal agreement with Tri-Valley's former chief executive officer for a higher fee level. He explained that the district's legal counsel advised the district that it could charge its charter schools an oversight fee greater than 1 percent, and Tri-Valley agreed to pay a higher oversight fee for Acacia Elementary in return for the district's advice and other types of administrative services. Although Tri-Valley's board meeting minutes from May 2015 showed the board's approval of New Jerusalem's proposal for a fee increase to 3 percent, the minutes also indicated that the proposal did not include a breakdown describing what the school would receive in exchange. Similarly, we found that the district's invoices for these fees were unclear because they did not identify what portion of the invoiced amount was attributable to non-oversight services. Moreover, the district did not identify these additional services in its MOU with the charter school. In February 2016, New Jerusalem revised its charter school policy to specify that whenever the district agrees to provide administrative or support services, the district and charter school shall develop an MOU that clarifies the financial and operational agreements.

However, New Jerusalem never developed a new MOU to identify these additional services and, in August 2016, the district sent Tri-Valley an invoice for oversight fees totaling 3 percent of Acacia Elementary's local funding plan revenue. By overcharging its charter schools, New Jerusalem has directed funds away from the schools' educational programs without clear justification.

In addition, each of the three districts we visited had agreements with their charter schools that called for no more than a 1 percent oversight fee; however, none of the districts tracked the actual costs of their oversight activities despite the legal limitation that they can only charge their actual costs. Administrators at the three districts offered different justifications for not tracking their actual oversight costs. Acton-Agua Dulce Unified's chief financial officer stated that it would be an undue burden on the district to track the costs of its various accounting streams. According to New Jerusalem's superintendent, district staff have other roles in addition to monitoring charter schools, and the district does not have a written policy or procedure for tracking oversight costs. However, we believe these districts could implement time-reporting tools that would allow staff to differentiate between their activities. The districts' failures to track their time and expenses related to oversight are examples of general weaknesses in their documentation of charter school-related activities, as we describe in later chapters.

### **The Districts We Visited Authorized Charter School Petitions That Did Not Comply With State and District Requirements**

To determine whether the districts we visited complied with state and district requirements when authorizing charter schools, we reviewed the petitions of both in-district and out-of-district schools. We found that the districts we visited did not fully comply with state law when they authorized a number of the charter schools we selected for review. For example, both Acton-Agua Dulce Unified and New Jerusalem accepted and authorized petitions that were missing standard requirements, such as the minimum number of parent or teacher signatures state law requires. Absent such signatures, the districts had little evidence of community support for the schools. Finally, during our audit period, two of the three districts had not updated their charter school policies to reflect changes in state law.

*None of the districts tracked the actual costs of their oversight activities despite the legal limitation that they can only charge their actual costs.*

*Attending monthly board meetings at the district may not be adequate to ensure that the governance structure of the charter school provides parents with the opportunity for active and effective representation.*

### ***Two Districts Authorized Charter Schools Without Ensuring the Schools Had Adequate Community Support***

Two of the three districts we visited authorized charter schools without ensuring adequate community support, as state law requires. For example, New Jerusalem authorized Acacia Elementary despite its petition having signatures from fewer than half the number of teachers that the school expected to employ in its first year of operation. As we discuss in the Introduction, state law requires charter school applicants to obtain signatures of either half the parents of the number of students the school expects to enroll in the first year or half the teachers it expects to employ in the first year. A lack of signatures may indicate inadequate community support, which could limit the charter school's ability to enroll students or employ qualified teachers. State law further reinforces the importance of community support by requiring prospective charters to describe in their petitions how they will ensure parental involvement. However, we also noted that New Jerusalem approved two petitions that did not meet this requirement. According to New Jerusalem's superintendent, parents can participate by attending monthly board meetings at the district. Nevertheless, this approach may not be adequate to ensure that the governance structure of the charter school provides parents with the opportunity for active and effective representation.

Similarly, Acton-Agua Dulce Unified approved the petition for a charter school—Albert Einstein Academy for Letters, Arts and Sciences—Agua Dulce Partnership Academy (Albert Einstein Academy)—even though the petition did not include any parent or teacher signatures. The authorization matrix the district used to evaluate the petition indicates that the district did not review this critical element. Although Acton-Agua Dulce Unified's director of charter schools provided a list of signatures that she believed might have related to the petition, the list was from the file of a different charter school. In addition, the signatures from that list were dated a month after the district received the Albert Einstein Academy's petition, even though state law requires prospective charter schools to attach signature pages to their charter petitions. Without the appropriate number of signatures, Acton-Agua Dulce Unified should not have accepted the petition for consideration.

Further, Acton-Agua Dulce Unified did not adequately consider Albert Einstein Academy's failure to obtain community support—an indicator of potential enrollment—when evaluating the charter petition's proposed financial plan. Specifically, the district's chief financial officer expressed his concern with the accuracy of the estimated enrollment numbers and projected revenue contained in the petition. However, the former superintendent of Acton-Agua Dulce Unified recommended the petition for approval.

According to the chief financial officer, the former superintendent recommended approving the petition because none of the financial concerns was severe enough to warrant denying the petition. However, we believe the chief financial officer identified valid concerns with the financial plan, such as overstated revenue and understated expenses. Further, before authorizing Albert Einstein Academy, the district operated its own noncharter school at the same location, which it ultimately closed because of low enrollment. Since charter school funding is largely based on enrollment, this experience should have heightened the district's scrutiny of the number of parent and teacher signatures to ensure that the school had the community support necessary to succeed.

We also identified other potential areas of concern related to Albert Einstein Academy's financial planning. For example, the school submitted a revised budget for its first year of operation that projected it would end the year with a \$30,000 reserve—an amount significantly less than the \$600,000 reserve it projected in its petition. Further, the school has consistently failed to meet the district's minimum reserve requirement, which we identified as an early indicator that preceded the closure of other charter schools we reviewed. Although Albert Einstein Academy is still operating, low enrollment could lead to the school's bankruptcy and eventual closure, as we discuss in the next chapter.

***The Three Districts We Reviewed Lacked Updated Charter School Policies, and Some Had Not Established Criteria for Assessing Petitions***

The three districts may have failed to comply with state law when authorizing and renewing petitions because they did not update their charter school policies to reflect changes in state law. For example, New Jerusalem did not update its charter school policy between September 2008 and February 2016, so its authorization process did not address requirements related to educational programs and measurable student outcomes that became effective in 2013. Similarly, Antelope Valley Union last updated its charter school policy in February 2009 and its regulations in May 2007, and thus its policies did not include the 2013 requirements either. Finally, although Acton-Agua Dulce Unified adopted its charter school policy in December 2013, it also failed to include the requirements that had recently gone into effect.

Because of these outdated policies, New Jerusalem did not assess whether petitions included sufficiently detailed annual goals or measurable student outcomes. Specifically, the petitions we reviewed did not delineate the goals and outcomes meant for all students schoolwide and those meant for each significant subgroup of students the charter schools would serve, as state

***The three districts may have failed to comply with state law when authorizing and renewing petitions because they did not update their charter school policies to reflect changes in state law.***

***Some of the districts we visited did not establish criteria for assessing whether petitions contained reasonably comprehensive descriptions of the elements state law requires.***

law requires. By not requiring charter schools to provide this level of detail in their petitions, New Jerusalem may find it more challenging to consider increases in student academic achievement for all subgroups of students when contemplating revocations in the future.

Further, some of the districts we visited did not establish criteria for assessing whether petitions contained reasonably comprehensive descriptions of the elements state law requires, as the Introduction describes. State law allows authorizers to deny petitions if they do not contain reasonably comprehensive descriptions of these elements. Because the Legislature recognized that the term *reasonably comprehensive* is somewhat subjective, it required the State Education Board to establish criteria for evaluating petitions. The State Education Board issued these criteria as regulations; however, only the State Education Board is required to use those criteria when evaluating charter school petitions. As a result, when we compared the charter school policies of Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem to those of neighboring host districts—Glendale Unified, Los Angeles Unified, and Stockton Unified—we found that the level of detail the districts require in petitions varies significantly.

Specifically, Antelope Valley Union, Glendale Unified, New Jerusalem, and Stockton Unified use the California School Board Association's guidance, which closely mirrors state law, for establishing a baseline for their authorization processes; however, Antelope Valley Union and Glendale Unified require prospective charter schools to submit some additional information. For example, Antelope Valley Union and Glendale Unified both require petitions to include information about the proposed charter schools' bylaws, articles of incorporation, and other management documents, as applicable. In addition, they both require descriptions of the education, experience, credentials, degrees, and certifications of the directors, administrators, and managers of proposed charter schools. In contrast, New Jerusalem and Stockton Unified have made minimal changes to the California School Board Association's sample policy and thus do not require prospective charter schools to provide additional information with their petitions. However, none of these four districts' charter school policies incorporates the State Education Board's criteria or defines what a reasonably comprehensive petition should include. Although New Jerusalem's policy does not describe its use of the criteria, New Jerusalem's superintendent asserted that it uses a rubric containing the State Education Board's criteria for evaluating petitions. Nevertheless, he was able to provide only a copy of the rubric for the petition we reviewed that was two-thirds completed.

Unlike the districts that rely solely upon the California School Board Association's guidance, Acton-Agua Dulce Unified and Los Angeles Unified established their own charter school policies that define criteria for assessing whether a petition is reasonably comprehensive. Los Angeles Unified's policy, which describes the requirements and timeline for its authorization process, states that it uses the State Education Board's criteria as a guideline for evaluating petitions. Acton-Agua Dulce Unified's policy does not state that it uses the criteria but rather defines its own criteria for a reasonably comprehensive description for each petition requirement.

Although Acton-Agua Dulce Unified's policy is expansive and detailed, we found that the district often did not follow the authorization process described in its policy. For example, Acton-Agua Dulce Unified authorized Assurance Academy's petition even though it did not present reasonably comprehensive descriptions of proposed measurable student outcomes. Instead, Assurance Academy defined a target for only one measurable student outcome—85 percent attendance. The district's policy states that a reasonably comprehensive description of measurable student outcomes should include detailed exit outcomes that encompass both academic and non-academic skills. Similarly, the State Education Board's criteria require measurable student outcomes, at a minimum, to specify skills, knowledge, and attitudes that reflect schools' educational objectives and can be frequently assessed by verifiable means to determine whether students are making satisfactory progress. Further, it requires charter schools to describe how they will hold themselves accountable for these outcomes. However, Assurance's petition did not include the level of detail described in either the district's policy or the State Education Board's criteria. When districts authorize petitions that fail to provide comprehensive descriptions of measurable student outcomes, the districts may find it difficult to hold charter schools accountable for poor academic performance and may be unable to revoke the charters of poorly performing schools, as we discuss in Chapter 3.

## Recommendations

### *Legislature*

To ensure that districts obtain community support for charter schools that they authorize, the Legislature should amend state law to do the following:

- Further clarify the conditions prospective charter schools must meet to qualify for the geographic exception. For example, the Legislature could clarify whether prospective charter schools qualify for the exception when their petitions indicate that they will serve primarily students residing outside the authorizing district's jurisdiction.
- Require any district that is considering authorizing an out-of-district charter school to notify the school's host district 30 days in advance of the board meeting at which the potential authorizing district is scheduled to make its authorization decision. The Legislature should also require the potential authorizing district to hold the public hearing within the host district's boundaries, notwithstanding restrictions in the State's Ralph M. Brown Act that would otherwise require the hearing to occur in the authorizing district.

To reduce the need for litigation between authorizing districts and host districts, the Legislature should establish an appeals process through which districts can resolve disputes related to establishing out-of-district charter schools.

To ensure charter school accountability, the Legislature should amend state law to do the following:

- Require districts to strengthen their authorization processes by using the State Education Board's criteria for evaluating charter school petitions.
- Require charter schools to report annually all of their school locations—including school sites, resource centers, and administrative offices—to their authorizers and Education.

To remove the financial incentive for districts to authorize out-of-district charter schools, the Legislature should amend state law to prohibit districts from charging fees for additional services above the actual cost of services provided.

### ***Districts***

To make certain that they authorize only qualified petitions, Acton-Agua Dulce Unified and New Jerusalem should revise their charter school authorization policies to require the documentation of their evaluations of charter school petitions. The districts should present this documentation to their governing boards for their consideration.

To ensure that they have a method to hold charter schools accountable for their educational programs, Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem should, as a best practice, strengthen their authorization processes by using the State Education Board's criteria for evaluating petitions.

To ensure compliance with state law, Acton-Agua Dulce Unified, Antelope Valley Union, and New Jerusalem should immediately do the following:

- Establish a procedure to periodically review and update their charter school policies to include all of the requirements in state law.
- Review petitions to ensure they include all of the requirements in state law at the time of their approval.
- Require their charter schools to submit material revisions when they add new locations.
- Track their actual costs for providing oversight and verify that their oversight fees do not exceed legal limits.

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## Chapter 2

### THE SCHOOL DISTRICTS WE REVIEWED NEED TO PROVIDE STRONGER FINANCIAL OVERSIGHT TO THEIR CHARTER SCHOOLS

The three districts that we visited—Antelope Valley Union, New Jerusalem, and Acton-Agua Dulce Unified—could strengthen their financial oversight processes for charter schools they authorize. Although state law requires authorizers to monitor the financial conditions of their authorized charter schools, it does not prescribe specific procedures that authorizers must follow to fulfill this responsibility. However, the three districts we visited did not develop their own written procedures detailing the steps that they expected their staffs to perform to ensure effective financial monitoring of the districts' charter schools. If Antelope Valley Union and New Jerusalem had established such procedures, they might have responded sooner to initial indicators of financial difficulties at LA Online and Acacia Elementary, respectively. Both of these charter schools filed for bankruptcy and ceased operations in 2017.<sup>1</sup>

In addition, the three districts did not always incorporate best practices into their financial oversight processes. Specifically, we found that the districts inconsistently applied select best practices we identified, such as providing charter schools with annual written reports summarizing the schools' performances and identifying areas needing improvement. Similarly, Antelope Valley Union and Acton-Agua Dulce Unified did not use their authority under state law to place representatives on their charter schools' governing boards, which contributed to the two districts being unaware of some of LA Online's and Assurance Academy's significant financial decisions. By incorporating best practices into their financial oversight processes and by fully using their authority under state law, authorizers could better ensure that they provide effective financial oversight to the charter schools they authorize.

#### **Antelope Valley Union and New Jerusalem Did Not Respond Promptly to Indicators of Financial Difficulties at Their Charter Schools**

Two of the three charter schools we visited—LA Online and Acacia Elementary—filed for bankruptcy in 2016 and subsequently closed in 2017, forcing a total of roughly 500 students to change schools. LA Online's bankruptcy stemmed from a significant decline in enrollment that it experienced in fiscal year 2014–15 and its inability

<sup>1</sup> Tri-Valley's bankruptcy petition stated that it did business as Acacia Elementary; thus we note in this report that *Acacia Elementary* filed for bankruptcy.

***We found that none of the three districts we reviewed had written procedures for reviewing their charter schools' financial conditions.***

to align its expenses with lower revenue. In Acacia Elementary's case, the nonprofit corporation that managed it—Tri-Valley—filed for bankruptcy due to a high level of debt and possible fiscal mismanagement by its management team. Although these schools' respective authorizing districts—Antelope Valley Union and New Jerusalem—eventually revoked the schools' charters, as described in the next section, they could not demonstrate that they responded promptly to initial indicators of the schools' financial distress. This may have happened because they lacked robust financial oversight processes.

In fact, we found that none of the three districts we reviewed had written procedures for reviewing their charter schools' financial conditions. In addition, the three districts did not always incorporate best practices into their financial oversight processes, such as using comprehensive checklists for periodic or annual reviews. As a result, the three districts were unable to ensure that they consistently provided effective financial oversight to the charter schools they authorized and that they responded promptly and appropriately to indicators of charter schools' financial difficulties.

#### ***LA Online and Acacia Elementary Filed for Bankruptcy After Extended Periods of Financial Distress***

LA Online filed for bankruptcy in April 2016 with the intent of reorganizing its finances and continuing operations. However, after the school was unable to recover from its financial problems, its governing board decided to cease operations in 2017. According to the declaration LA Online's president presented to the bankruptcy court, a significant drop in LA Online's enrollment, which in turn affected its average daily attendance and revenue, caused its financial problems. As Table 6 shows, LA Online's average daily attendance fell from 691 students in fiscal year 2013–14 to 255 students in fiscal year 2015–16. Because average daily attendance is a key factor that determines a charter school's state funding, this significant drop in average daily attendance was a primary factor causing LA Online's revenue to decrease from \$5.4 million in fiscal year 2013–14 to \$2.7 million in fiscal year 2015–16.

LA Online alleged that its drop in enrollment at the beginning of fiscal year 2014–15 was the result of deliberate efforts by its previous provider of educational and administrative services—K12 Inc.—to recruit LA Online's students into another K12 Inc. school after LA Online terminated its agreement with K12 Inc. in June 2014. According to LA Online's notice of intent not to renew its agreement with K12 Inc., LA Online stopped using K12 Inc.'s services after LA Online's board undertook a review in response to ongoing concerns related to low student retention and graduation rates.

In December 2014, after LA Online failed to pay K12 Inc. \$2.9 million for services that K12 invoiced for fiscal year 2013–14, K12 Inc. filed a lawsuit against LA Online seeking damages plus interest. In response, LA Online filed a cross-complaint against K12 Inc., seeking damages for K12 Inc.’s alleged misconduct and breach of contract.

**Table 6**  
**Two of the Three Out-of-District Charter Schools That We Reviewed Experienced Significant Financial Challenges From Fiscal Years 2013–14 Through 2015–16**

OUT-OF-DISTRICT CHARTER SCHOOL	FISCAL YEAR		
	2013–14	2014–15	2015–16*
<b>Acacia Elementary</b>			
<i>Annual average daily attendance</i>	129	269	382
Total revenue	\$1,614,853	\$3,641,932	\$5,137,722
Total expenses	(1,672,934)	(4,005,507)	(5,560,515)
Excess (deficiency) of revenue over expenses	(58,081)	(363,575)	(422,793)
<b>Ending net assets (deficit)†</b>	<b>(\$58,081)</b>	<b>(\$421,656)</b>	<b>(\$844,449)</b>
<b>Assurance Academy</b>			
<i>Annual average daily attendance</i>	622	629	763
Total revenue	\$5,595,577	\$6,288,882	\$9,618,877
Total expenses	(5,489,240)	(6,243,602)	(9,477,473)
Excess (deficiency) of revenue over expenses	106,337	45,280	141,404
<b>Ending net assets (deficit)†</b>	<b>\$362,549</b>	<b>\$407,829</b>	<b>\$549,233</b>
<b>LA Online</b>			
<i>Annual average daily attendance</i>	691	181	255
Total revenue	\$5,448,571	\$2,147,778	\$2,673,812
Total expenses	(5,892,973)	(4,247,910)	(3,379,031)
Excess (deficiency) of revenue over expenses	(444,402)	(2,100,132)	(705,219)
<b>Ending net assets (deficit)†</b>	<b>\$551,486</b>	<b>(\$1,548,646)‡</b>	<b>(\$2,442,704)</b>

Sources: Audited financial statements of LA Online and Assurance Academy for fiscal years 2013–14 through 2015–16 and of Acacia Elementary for fiscal years 2013–14 and 2014–15; Education’s Local Control Funding Formula Funding Snapshot database and unaudited financial report of Acacia Elementary for fiscal year 2015–16.

\* Acacia Elementary never published audited financial statements for fiscal year 2015–16. Acacia Elementary’s financial information for fiscal year 2015–16 presented above is from its unaudited financial report dated September 2016. The financial report that Acacia Elementary submitted to New Jerusalem in March 2017, which presented fiscal year 2016–17 activity, indicated that the school’s ending deficit for fiscal year 2015–16 was (\$1,089,776), not (\$844,449).

† We refer to a charter school’s deficiency of assets over liabilities as a *deficit*.

‡ In its financial statements for fiscal year 2015–16, LA Online restated its ending deficit for fiscal year 2014–15 from (\$1,548,646), as the table shows, to (\$1,737,485).

Although LA Online stated in its initial bankruptcy filing that it intended to reorganize its finances and continue operations, its board of directors eventually decided to close the charter school after it received another large claim while struggling to restore its student enrollment. Specifically, in August 2016, LA Online and K12 Inc. reached a settlement agreement to avoid complex and costly litigation. However, shortly before the court hearing to consider this settlement agreement, the State Board of Equalization (Equalization) submitted a claim against LA Online for roughly \$478,000 in delinquent sales and use taxes associated with student packages that K12 Inc. had shipped to LA Online students from another state. Because of Equalization's claim, LA Online could no longer adhere to the payment schedule in its proposed settlement agreement with K12 Inc., and LA Online voluntarily dismissed its request for approval of the settlement

agreement. In light of the unresolved litigation with K12 Inc., its continuing low enrollment, and Antelope Valley Union's charter revocation proceedings that we discuss further in the next section, LA Online's board decided to voluntarily close the school in February 2017, forcing roughly 200 students to change schools.

Our review of Acacia Elementary showed that its CMO, Tri-Valley, filed for bankruptcy because of its inability to make payments on a bank note and line of credit, possibly due to fiscal mismanagement by some members of its management team. According to the bankruptcy declaration of Tri-Valley's CEO in November 2016, Tri-Valley had past due debt of roughly \$3.3 million, consisting of trade debt, loans, and a line of credit. Shortly after Tri-Valley's initial bankruptcy filing in November 2016, the Alameda County Office of Education requested that California's Fiscal Crisis and Management Assistance Team (FCMAT) audit Tri-Valley's Livermore-based charter schools because of allegations of fiscal irregularities. In June 2017, FCMAT published its audit report. As the text box shows, FCMAT concluded that fraud, misappropriation of assets, or other illegal activities may have occurred at Tri-Valley.

Although the focus of FCMAT's audit was Tri-Valley's charter schools in Livermore, some of the issues that FCMAT included in its report also affected Acacia Elementary. For example, Tri-Valley engaged Acacia Elementary in a number of highly questionable transactions

### Select Conclusions and Recommendations From FCMAT's Audit of Tri-Valley

FCMAT's analysis concluded that Tri-Valley's management may have done the following:

- Filed incomplete Fair Political Practices Commission Form 700s.
- Failed to fully disclose affiliated or related parties to the district and Tri-Valley's auditor.
- Concealed the true nature of related-party transactions.
- Misled independent auditors.
- Converted the use of tax-exempt public bonds totaling more than \$67 million to purchase land and buildings under the pretext that the acquisition was for a public charter school.
- Diverted more than \$2.7 million in public funds for off-book transactions.
- Diverted its charter schools' funds and commingled them with those of potentially related entities.
- Contributed to an environment of significantly deficient internal controls.

FCMAT recommended that the county superintendent notify the governing board of Alameda County Office of Education, the governing board of Tri-Valley, the governing board of Livermore Valley Joint Unified School District, the State Controller, the Superintendent of Public Instruction, and the local district attorney that fraud, misappropriation of assets, or other illegal activities may have occurred.

Source: FCMAT's June 8, 2017, audit of Tri-Valley.

with other charter schools it operated and with other entities. Specifically, FCMAT reported that Tri-Valley pledged its revenue, including that of Acacia Elementary, in a lease agreement for a Tri-Valley school in Livermore, the proceeds of which covered interest and principal payments related to a 2015 bond issuance for purchasing a facility for one of Tri-Valley's Livermore-based charter schools. Although Tri-Valley was not able to provide evidence that it actually used Acacia Elementary's revenue to make payments under this agreement, FCMAT noted that in fiscal year 2015–16, Acacia Elementary transferred \$145,000 to a non-profit corporation that was involved in the 2015 bond issuance. FCMAT also noted that at the end of fiscal year 2015–16, Acacia Elementary owed other Tri-Valley entities \$2.7 million, while other Tri-Valley entities owed Acacia Elementary \$1.6 million. Although these balances suggest that Acacia Elementary needed to transfer \$1.1 million to other Tri-Valley entities, Tri-Valley could not provide any supporting documentation justifying the nature of these transactions. Similarly, Tri-Valley was unable to provide documentation or evidence of board approval for an undisclosed loan that New Jerusalem discovered after reviewing Acacia Elementary's bank statements and that FCMAT described in its report. Specifically, in 2014 Tri-Valley obtained a loan for \$600,000; however, Tri-Valley never disclosed this loan in its audited financial statements. FCMAT reported that over 18 months Acacia Elementary and other entities paid interest totaling roughly \$132,000, or 15 percent per year—a significantly higher interest rate than the rates on Tri-Valley's other credit lines, which ranged from 4.75 to 5 percent per year.

Although Tri-Valley planned to reorganize its finances and continue operations at the time it filed for bankruptcy, it subsequently decided to close its schools. The initial bankruptcy declaration of Tri-Valley's CEO states that the primary purpose of the bankruptcy filing was to gain the short-term financial stability needed to preserve its charter schools, including Acacia Elementary. However, Tri-Valley subsequently decided to cease operations, stating that it had insufficient funds to pay administrative expenses and no ability or intent to reorganize its operations. As a result, Tri-Valley closed all four of its charter schools at the end of fiscal year 2016–17, leaving over 1,500 students to find new schools, including about 300 attending Acacia Elementary at that time.

According to our review of financial information, the third charter school that we visited, Assurance Academy, appears to be financially stable. For example, we noted that during fiscal years 2013–14 through 2015–16, Assurance Academy did not experience deficits and had reserves that consistently exceeded the minimum level in its MOU with its authorizing district.

***Tri-Valley closed all four of its charter schools at the end of fiscal year 2016–17, leaving over 1,500 students to find new schools, including about 300 attending Acacia Elementary.***

***State law requires authorizing districts to monitor the financial conditions of charter schools under their authority, but does not establish a minimum level of financial oversight that districts must perform.***

***Antelope Valley Union and New Jerusalem Could Not Always Demonstrate Their Use of Financial Reports to Monitor the Financial Conditions of Their Charter Schools***

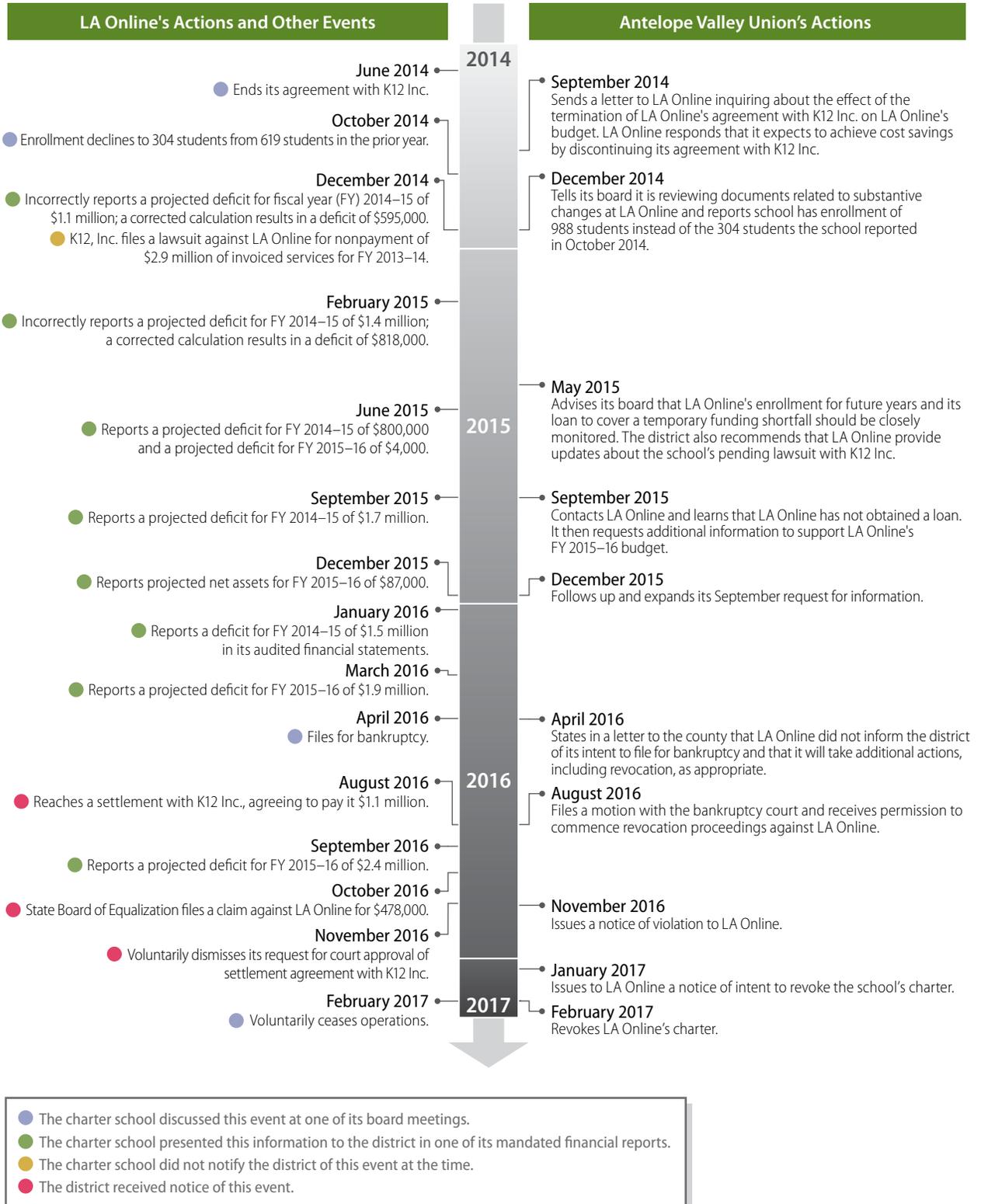
Although state law requires authorizing districts to monitor the financial conditions of charter schools under their authority using any financial information obtained from the schools, it does not establish a minimum level of financial oversight that districts must perform. The law also requires charter schools to submit regular financial reports to their authorizers, but it does not describe how authorizing districts should use these reports to ensure effective and timely oversight. Accordingly, we noted that Antelope Valley Union and New Jerusalem could not show that they responded to early indicators of their charter schools' financial distress. These indicators preceded the schools' eventual failures.

In fiscal years 2014–15 and 2015–16, LA Online submitted to Antelope Valley Union financial reports containing indications of the charter school's financial distress. To show Antelope Valley Union's responses to LA Online's financial condition as well as the timing and extent of LA Online's financial difficulties, Figure 2 juxtaposes information from LA Online's financial reports, board meeting minutes, and court documents with information from documents Antelope Valley Union provided to us to demonstrate its oversight efforts.

Although Antelope Valley Union asserts that it monitored LA Online's financial condition, it could not demonstrate that it took prompt and concerted action when LA Online's financial reports showed that LA Online had not met Antelope Valley Union's minimum reserve requirement and was experiencing significant financial distress. Antelope Valley Union's MOU with LA Online required LA Online to maintain a reserve equal to the greater of either 4 percent of LA Online's expenses for the year or \$50,000. As Figure 2 shows, LA Online did not meet this reserve requirement for the first time in December 2014, when it submitted its first interim report for fiscal year 2014–15, as state law required. This report showed that LA Online projected that its revenue would be roughly 40 percent lower than it originally budgeted and that it would end the year with a deficit of more than \$1.1 million.<sup>2</sup> The two subsequent financial reports that LA Online submitted to Antelope Valley Union in February and June 2015 continued to show that LA Online projected it would end fiscal year 2014–15 with a significant deficit. According to Antelope Valley Union's assistant superintendent of educational services, Antelope Valley Union's staff had conversations with LA Online about these reports, during which LA Online asserted that it had secured a loan to cover the funding shortfall. However, Antelope Valley Union did not take significant action when LA Online failed to prove that it had, in fact, obtained this loan. As a result, the district did not learn that LA Online had not obtained the loan until September 2015—almost nine months after LA Online submitted its first financial report showing indicators of significant financial difficulties.

<sup>2</sup> We refer to a charter school's deficiency of assets over liabilities as a *deficit*.

**Figure 2**  
**Events Leading to LA Online’s Bankruptcy and Antelope Valley Union’s Responses to Those Events**



Sources: California State Auditor's analysis of LA Online's financial reports, court documents, board meeting minutes and resolutions; Antelope Valley Union's board meeting minutes and correspondence; and data from Education.

***Antelope Valley Union did not perform its oversight efforts promptly enough to aid LA Online in aligning its expenses with its significantly reduced revenue.***

Although Antelope Valley Union took additional action starting in September 2015 to monitor LA Online's financial condition, its oversight efforts were again delayed. In September 2015, three months after LA Online submitted estimated results for fiscal year 2014–15 and a budget for fiscal year 2015–16, Antelope Valley Union asked LA Online to provide information on its enrollment, average daily attendance, and reductions in expenses so that the district could assess the reasonableness of LA Online's budget. In addition, Antelope Valley Union strongly recommended that LA Online obtain a line of credit to avoid near-term cash flow shortages. However, Antelope Valley Union waited another three months, until December 2015, before making its first formal request for additional information about the school's financial situation, at which point it asked for a strategic financial plan to ensure that the school had the ability to cover its operating expenses adequately for fiscal year 2015–16.

Although this request demonstrates that Antelope Valley Union took action to assess LA Online's financial condition, the district did not perform its oversight efforts promptly enough to aid LA Online in aligning its expenses with its significantly reduced revenue. For example, we noted that LA Online had higher total salary and benefits expenses in fiscal years 2014–15 and 2015–16 than in fiscal year 2013–14, despite losing more than half of its students. According to LA Online's last board president, the school did not reduce its staffing expenses because it believed it could increase its enrollment and average daily attendance rates and recover from deficit spending. He also said that, notwithstanding the lawsuit with K12 Inc., the board felt it needed to protect its students from severe educational disruption. Nevertheless, this decision not to perform a timely alignment of its staffing expenses with its significantly reduced enrollment may have contributed to LA Online's bankruptcy. Although Antelope Valley Union could not demonstrate that it promptly raised this particular issue as a concern, it eventually issued a notice of violation to LA Online in November 2016 and a notice of intent to revoke the school's charter in January 2017. In its notice of intent to revoke, the district scheduled a public hearing in February 2017 to discuss the issue of whether evidence existed to revoke LA Online's charter. Although LA Online initially stated that it planned to close the school at the end of fiscal year 2016–17, shortly after receiving Antelope Valley Union's notice of intent to revoke, LA Online filed an emergency motion with the bankruptcy court seeking permission to close the school sooner. In its court documents, LA Online stated that it decided to cease operations earlier to allow students and staff a seamless transition to a new school prior to the start of the new semester. After receiving permission from the bankruptcy court, LA Online's board decided to voluntarily close the school on February 1, 2017. Antelope Valley Union revoked LA Online's charter two weeks after the school ceased operations.

Antelope Valley Union may not have responded promptly and effectively to indicators of LA Online’s financial difficulties because the district did not have a robust process to review charter schools’ financial reports effectively and to respond appropriately to indicators of financial distress. State law requires authorizers to monitor the financial conditions of charter schools under their authority, but it does not prescribe specific procedures that authorizers should perform or state how quickly authorizers should review and respond to charter schools’ financial reports. However, Antelope Valley Union did not develop its own formal procedures detailing the steps that it expects its staff to perform when reviewing charter schools’ financial information. As a result, Antelope Valley Union’s responses to indicators of LA Online’s financial distress were delayed.

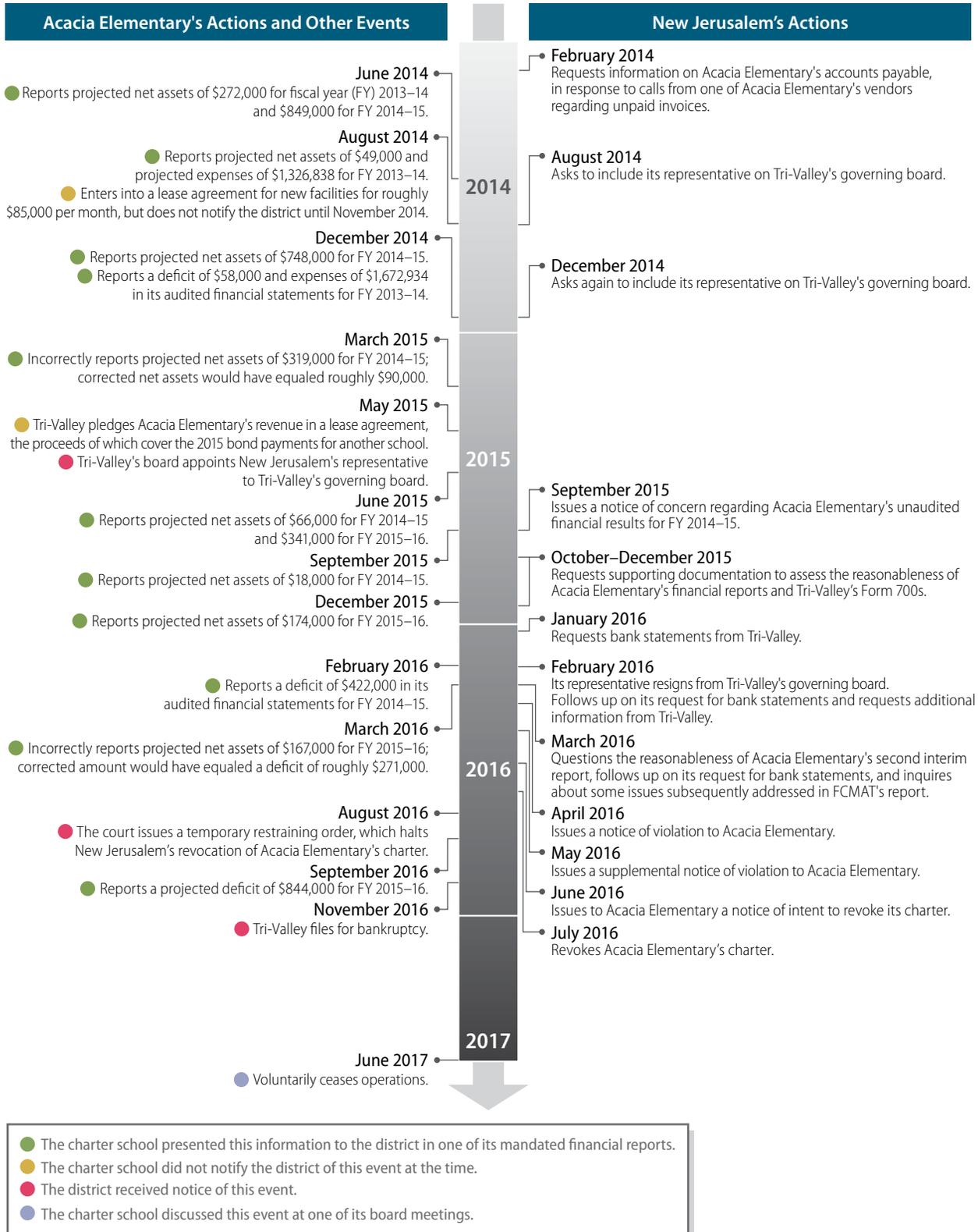
Like Antelope Valley Union, New Jerusalem did not have a formal process for reviewing and responding to financial reports. If it had established such a process, it might have responded to Acacia Elementary’s financial condition more quickly than it did. Acacia Elementary started exhibiting signs of financial problems as early as August 2014, when it submitted its unaudited financial report for fiscal year 2013–14, estimating that it ended the year with only about \$49,000 in net assets.<sup>3</sup> This estimate represented a radical departure from Acacia Elementary’s estimates in previous financial reports, in which it projected that it would end its first year of operations with significantly higher net assets, as we show in Figure 3 on the following page. In addition, New Jerusalem’s MOU with Acacia Elementary required the school to have unexpended funds to pay its creditors in its first year of operations and to maintain a reserve equal to 3 percent of the school’s annual revenue during all subsequent years. As Figure 3 demonstrates, Acacia Elementary failed to meet this requirement for the first time in December 2014, when its audited financial statements showed that Acacia Elementary ended its first year of operations with a deficit of \$58,000.

According to New Jerusalem’s superintendent, the district did not see the need to take further action in response to Acacia Elementary’s financial condition at the time. He stated that charter schools rarely end their first year of operation with a significant excess of revenue over expenses because of start-up costs and that the magnitude of Acacia Elementary’s ending deficit for fiscal year 2013–14 was not indicative of severe financial issues. However, in aggregate with other indicators present in Acacia Elementary’s financial reports for fiscal year 2013–14, as shown in Figure 3, this deficit should have led New Jerusalem to start taking further action regarding Acacia Elementary’s financial condition.

***In aggregate with other indicators present in its financial reports for fiscal year 2013–14, Acacia Elementary’s deficit should have led New Jerusalem to start taking further action regarding Acacia Elementary’s financial condition.***

<sup>3</sup> For a nonprofit entity, *net assets* are the excess of assets over liabilities.

**Figure 3**  
**Events Leading to Acacia Elementary’s Bankruptcy and New Jerusalem’s Responses to Those Events**



Sources: Acacia Elementary's and Tri-Valley's financial reports, board meeting minutes and resolutions, court documents, and lease agreements, as well as New Jerusalem's correspondence.

However, unlike Antelope Valley Union, New Jerusalem revoked Acacia Elementary's charter before Acacia Elementary filed for bankruptcy. Acacia Elementary fell below the minimum reserve requirement in June 2015, when its estimated results for fiscal year 2014–15 showed that it was ending the year with \$66,494 in net assets, a reserve of only about 2 percent of its revenue. In September 2015, after Acacia Elementary's unaudited financial report for fiscal year 2014–15 showed a further reduction in its ending net assets to \$17,656, New Jerusalem issued a formal notice of concern to Tri-Valley stating that Acacia Elementary did not meet the minimum reserve requirement and requesting additional information about the school's financial condition. After working with Tri-Valley to determine whether Acacia Elementary's unaudited financial report for fiscal year 2014–15 and budget for fiscal year 2015–16 were reasonable and after reviewing Tri-Valley's Form 700s, Statements of Economic Interests, New Jerusalem requested Tri-Valley's bank statements in January 2016. By reviewing Tri-Valley's bank statements and other financial information, New Jerusalem identified some of the issues that FCMAT subsequently investigated in more detail during the audit that we discuss on page 42. In response, New Jerusalem promptly commenced revocation proceedings against Acacia Elementary and eventually revoked its charter in July 2016. However, the San Joaquin Superior Court then halted New Jerusalem's charter revocation based on the district's insufficient consideration of the school's increases in academic achievement. We discuss this issue further in Chapter 3. As a result, Acacia Elementary did not cease operations until Tri-Valley's board of directors voted to close it voluntarily at the end of fiscal year 2016–17.

The third district that we visited—Acton-Agua Dulce Unified—demonstrated that it generally reviewed Assurance Academy's financial reports and assessed Assurance Academy's financial condition. However, because Assurance Academy's financial reports did not show problems during our audit period, we could not evaluate the timeliness or the quality of its responses to indicators of financial distress. Nevertheless, like Antelope Valley Union and New Jerusalem, Acton-Agua Dulce Unified does not have written procedures for reviewing charter schools' financial reports. Without robust oversight processes, districts cannot ensure the consistent quality of their reviews of charter schools' financial reports. In addition, without written procedures, district staff may not always take appropriate or prompt action if charter schools' financial reports start exhibiting indicators of financial distress.

*Without written procedures, district staff may not always take appropriate or prompt action if charter schools' financial reports start exhibiting indicators of financial distress.*

***We noted that the three districts' processes for providing financial oversight to charter schools missed opportunities to incorporate best practices for monitoring charter schools' financial conditions.***

### ***Districts Could Strengthen Their Financial Oversight of Charter Schools by Incorporating Best Practices Into Their Processes***

Due to the vagueness of state law, authorizers may interpret their responsibilities differently and provide varying levels of financial oversight to charter schools. Although state law requires authorizers to monitor the financial conditions of charter schools under their authority, it does not identify specific procedures that authorizers should perform to fulfill this oversight responsibility. Therefore, it is incumbent on authorizers to identify and establish appropriate monitoring processes. We noted, however, that the three districts' processes for providing financial oversight to charter schools missed opportunities to incorporate best practices for monitoring charter schools' financial conditions. Further, we observed that the three districts' charter school policies did not vary based on the location of the charter school; thus the districts provided a similar level of oversight to the in-district and out-of-district charter schools we reviewed.

We identified two sources that suggest procedures or best practices that we believe authorizers should follow to ensure their financial oversight of charter schools is effective. Specifically, FCMAT publishes a detailed *Charter School Annual Oversight Checklist* (oversight checklist) that authorizers could use as a guide to conducting annual visits and providing ongoing financial oversight. FCMAT developed the oversight checklist to aid authorizers in addressing their annual oversight responsibilities. Similarly, the National Association of Charter School Authorizers (NACSA) publishes *12 Essential Practices*, which contains recommendations for conducting effective financial oversight. Nonetheless, we found that the three districts we reviewed did not always incorporate the best practices from these two sources into their financial oversight processes, as Table 7 shows.

For example, NACSA recommends that districts review charter schools' performance and provide annual written reports to charter schools that summarize the schools' performance and identify areas needing improvement. However, Antelope Valley Union and New Jerusalem did not always provide such reports to LA Online and Acacia Elementary, respectively. For instance, although Antelope Valley Union prepared annual reports on LA Online for fiscal years 2014–15 and 2015–16, these reports did not always contain meaningful recommendations related to improving LA Online's financial operations and did not point out the need for LA Online to align expenses with its significantly reduced revenue in fiscal years 2014–15 and 2015–16, when the school was experiencing financial difficulties. Similarly, after completing site visits of Acacia Elementary and reviewing its financial reports, New Jerusalem did not provide annual reports to Acacia Elementary

identifying areas needing improvement. If districts do not provide feedback to the charter schools they oversee, the schools may not remedy weaknesses in a timely manner, which could eventually lead to the deterioration of the schools' financial conditions.

**Table 7**  
**The Three Districts We Reviewed Missed Opportunities to Incorporate Many Best Practices Into Their Financial Oversight Processes During Fiscal Years 2013–14 Through 2015–16**

BEST PRACTICE	AUTHORIZING SCHOOL DISTRICT		
	ACTON-AGUA DULCE UNIFIED	ANTELOPE VALLEY UNION	NEW JERUSALEM
<b>NACSA</b>			
Require and review annual, independent financial audits and regular financial reports of its charter schools.	✓	◇	◇
Provide an annual written report to each charter school on its performance.	✓	◇	✗
<b>FCMAT</b>			
Use a comprehensive checklist for periodic or annual reviews.	✗	✗	◇
Obtain lease agreements when charter schools plan to operate in new facilities.	✗	◇	◇
Ensure that charter schools' financial projections and assumptions are reasonable.	◇	◇	◇
Have a current memorandum of understanding with each charter school.	✓	◇	✓
Ensure that each charter school maintains a prudent level of reserves for economic uncertainties.	✓	◇	◇

Sources: California State Auditor's analysis of NACSA's *12 Essential Practices*, FCMAT's *Charter School Annual Oversight Checklist*, interviews with the districts' key staff, the districts' policies and procedures, and other documentation related to the districts' financial oversight processes.

- ✓ = The district applied this practice consistently during fiscal years 2013–14 through 2015–16.
- ◇ = The district could not demonstrate that it applied this practice consistently during fiscal years 2013–14 through 2015–16.
- ✗ = The district could not demonstrate that it applied this practice at all during fiscal years 2013–14 through 2015–16.

Neither Acton-Agua Dulce Unified nor Antelope Valley Union could demonstrate that they used an oversight checklist when conducting their legally required annual site visits or as part of their ongoing financial oversight of Assurance Academy and LA Online, respectively. Further, although New Jerusalem developed an oversight matrix based on FCMAT's oversight checklist, New Jerusalem could not show that it used the matrix effectively. According to New Jerusalem's superintendent, before its site visits in fiscal years 2014–15 and 2015–16, New Jerusalem asked Acacia Elementary's management to complete the oversight matrix and submit it, along with key supporting documents, to the district for review. Although New Jerusalem kept copies of Acacia Elementary's completed oversight matrices, it could not demonstrate that it consistently reviewed these matrices and provided feedback to Acacia Elementary on its findings. Specifically, New Jerusalem left

***Although FCMAT recommends authorizers obtain lease agreements when charter schools plan to operate in new facilities, the three districts did not always obtain lease agreements from the charter schools we reviewed.***

blank the portions of the fiscal year 2014–15 matrix designated for a reviewer’s signature and did not include recommendations to Acacia Elementary on improving its fiscal operations in this matrix. As a result, although New Jerusalem developed a tool to aid its staff in conducting site visits and ongoing oversight of charter schools, it could not show that it used this tool in a meaningful way or that it provided feedback to Acacia Elementary.

In the oversight checklist, FCMAT also recommends authorizers obtain lease agreements when charter schools plan to operate in new facilities. However, the three districts did not always obtain lease agreements from the charter schools we reviewed. For example, although New Jerusalem was aware that Acacia Elementary relocated to a new facility in September 2014, New Jerusalem could not provide evidence that it had reviewed promptly the lease agreement for this facility. In August 2014, Acacia Elementary entered into a lease agreement to rent facilities in Stockton at rates that were significantly higher than those for its previous location. Specifically, for its previous location Acacia Elementary paid roughly \$9,000 per month during fiscal year 2013–14, whereas for its new location it agreed to pay more than \$85,000 per month during fiscal year 2014–15, with rates increasing even further in subsequent years. Although Acacia Elementary did not make payments for the full amounts due under this lease agreement, its actual rent payments were substantial, exceeding \$700,000 in fiscal year 2015–16 alone. New Jerusalem’s superintendent asserted that he first started questioning this lease agreement in October 2015; however, he could not demonstrate that the district acted in response to the high rates until April 2016, when the district issued its notice of violation to Acacia Elementary.

We also found that the three districts did not always incorporate into their processes FCMAT’s suggestions pertaining to authorizers’ reviews of charter schools’ budgets. In the oversight checklist, FCMAT directs authorizers to ensure that charter schools’ financial projections and their underlying assumptions are reasonable. However, the three districts did not always obtain supporting documentation for the key assumptions that the three charter schools used to develop their budgets. For example, none of the three districts required charter schools to submit waiting lists or other forms indicating parents’ intent to enroll their students—evidence supporting the schools’ enrollments and revenue projections. As a result, we noted that for at least one of the years in our audit period, the three charter schools’ actual revenue was more than 10 percent below their projected revenue. When they do not require that charter schools have robust support for their budgets, the districts miss an opportunity to better ensure the schools’ financial stability.

Finally, FCMAT suggests that authorizers ensure that charter schools' governing boards function effectively and appropriately. FCMAT does not explicitly recommend authorizers to attend charter schools' board meetings or direct authorizers to assign their representatives to charter schools' governing boards, as state law allows. Nevertheless, as we discuss in the following section, we believe that this practice could improve authorizing districts' financial oversight.

### **Two Districts Did Not Use Their Authority Under State Law to Place a Representative on Their Respective Charter School's Governing Board**

Although state law allows authorizers to place their representatives on charter schools' boards of directors, two of the three districts that we visited have chosen not to do so. Specifically, Acton-Agua Dulce Unified and Antelope Valley Union did not appoint representatives to Assurance Academy's and LA Online's boards of directors, even though doing so could have increased their awareness of their charter schools' financial conditions and decisions. For example, although LA Online's governing board consistently discussed LA Online's large decline in enrollment starting in July 2014, Antelope Valley Union appears to have been unaware of this decline until December 2014. In a report that Antelope Valley Union presented to its board of trustees in December 2014, it stated that LA Online's enrollment was 988 students, when in fact it was only about 300 students at that time. Had Antelope Valley Union attended LA Online's board meetings or even just reviewed the meeting minutes, it would have been aware of this development sooner and could have promptly advised LA Online on revising its budget to account for its decreased enrollment.

In addition, because it did not attend LA Online's governing board meetings, Antelope Valley Union was unaware of LA Online's potentially illegal arrangement to include students who were enrolled concurrently in a sectarian school in its average daily attendance and consequently in its state funding claims. Specifically, after experiencing a significant decline in enrollment, LA Online and a sectarian school entered into an MOU in which the sectarian school agreed to provide LA Online with 25 students during the spring 2015 semester. The MOU required both parties to provide financial, material, and labor resources in order to create blended learning opportunities for the students of the sectarian school. However, state law prohibits the appropriation of state funding for the support of any sectarian school and specifically requires that a charter school be nonsectarian in its programs, admissions policies, employment practices, and other operations.

*State law prohibits the appropriation of state funding for the support of any sectarian school and specifically requires that a charter school be nonsectarian in its programs, admissions policies, employment practices, and other operations.*

When we asked Antelope Valley Union about this agreement, its assistant superintendent of educational services stated that the district had been unaware of it. However, an LA Online governing board meeting discussed LA Online's decision to enter into the agreement. According to LA Online's board meeting minutes, the partnership would increase average daily attendance, expand LA Online's name, and lead to partnerships with other private schools. In addition, the minutes state that students would be enrolled full-time with LA Online while continuing their full-time enrollment at the sectarian school. Had Antelope Valley Union regularly attended LA Online's governing board meetings or assigned a representative to the school's governing board, it would have been better able to provide oversight and ensure that LA Online's practices were legal.

According to Antelope Valley Union's superintendent, his district has chosen not to place district representatives on its charter schools' governing boards because it could potentially create conflicts of interest between the schools and the district. He explained that a district representative on a charter school's governing board might have to make a decision that would negatively impact either the school or the district, and that this lack of separation could cause the district to accept liability for the charter school's actions. He also noted that such an arrangement might prevent charter schools from pursuing innovative educational processes. Nevertheless, authorizers could maintain a presence on charter schools' governing boards without exposure to perceived conflicts of interest by designating their representatives as nonvoting members. This would ensure that authorizers are aware of significant issues that might impact their charter schools.

***Designating their representatives as nonvoting members would ensure that authorizers are aware of significant issues that might impact their charter schools.***

Similarly, Acton-Agua Dulce Unified was unaware of certain financial decisions Assurance Academy's governing board made. For example, Acton-Agua Dulce Unified was unaware that in June 2014 Assurance Academy's governing board approved a resolution for annually transferring up to 45 percent of its reserves to Choices in Learning National Foundation, a nonprofit corporation located in the same office park. According to Assurance Academy's board meeting minutes, the purpose of this resolution was to support and promote charitable work consistent with the mission and purpose of Assurance Academy. Although Assurance Academy's executive vice president of finance stated that Assurance Academy did not make any transfers under this plan, the approval of such a process appears questionable. As a charter school, Assurance Academy receives state school funds that are exclusively available for the purpose of educating enrolled students, not for supporting another organization. In September 2017, after we discussed this issue with Assurance Academy, its board rescinded the resolution.

When asked about the appropriateness of Assurance Academy's board resolution, Acton-Agua Dulce Unified's chief financial officer stated that he was not aware of Assurance Academy's decision to transfer 45 percent of its reserves annually to another organization and that he could not comment upon the appropriateness of the resolution without having all the facts. He also explained that he was not aware of any district employees attending the board meeting at which Assurance Academy's board passed that resolution. Because the district did not attend Assurance Academy's board meeting or review the minutes, this board resolution has been in effect and unmonitored by the district for more than three years. The chief financial officer stated that the district has considered putting a representative on its charter schools' board of directors, but he opined that the district has not needed to do so because Assurance Academy's financial reports have not indicated financial difficulties. Nevertheless, we believe that attending charter school board meetings is a critical component of administering effective financial oversight.

## **Recommendations**

### ***Legislature***

To ensure that authorizers have adequate tools and guidance for providing effective financial oversight, the Legislature should require the State Education Board and Education to work with representatives from county offices of education, representatives from districts, and subject-matter experts such as FCMAT, to either establish a committee or work with an existing committee to report to the Legislature recommendations on the following:

- Establishing a minimum reserve requirement for charter schools.
- Defining criteria that would allow authorizers to revoke or deny renewal of schools' charters for financial mismanagement despite increases in academic achievement.
- Developing a template that authorizers can use to provide their charter schools with annual feedback on their financial condition.

To ensure that districts are aware of significant issues that may impact the out-of-district charter schools they authorize, the Legislature should amend state law to require each district to place a district representative as a nonvoting member on each out-of-district charter school's governing board and allow such a representative to attend all meetings of the charter school's governing board.

***Districts***

To better ensure effective oversight of their charter schools' finances, the districts we visited should do the following:

- Develop written procedures for reviewing charter schools' financial information and conducting annual oversight visits. These procedures should include relevant requirements from memorandums of understanding with the charter schools and best practices.
- Develop written procedures for addressing financial concerns, such as a charter school's failure to meet the minimum reserve requirement established in the district's memorandum of understanding with the charter school.
- Place a district representative as a nonvoting member on each charter school's governing board.

To better ensure effective oversight of their charter schools' finances, Antelope Valley Union and New Jerusalem should provide charter schools with written feedback and recommendations for improving their financial operations after completing their financial reviews and annual oversight visits.

## Chapter 3

### **STATE LAW REQUIRES DISTRICTS TO PROVIDE ONLY A MINIMAL LEVEL OF ACADEMIC OVERSIGHT TO THE CHARTER SCHOOLS THEY AUTHORIZE**

State law requires authorizing districts to conduct annual site visits at their charter schools, but it does not identify specific oversight activities that the districts must provide. For example, although state law requires charter schools to establish measurable student outcomes within their petitions, it does not require authorizing districts to assess annually whether charter schools are meeting those outcomes. Rather, it requires only that authorizers monitor the academic performance of their charter schools once every five years, when the schools seek to renew their charters. Thus, we were not surprised to find that the districts we visited provide varying levels of academic oversight. In general, these districts lack procedures for providing charter schools with timely feedback on specific areas in which a charter school is either succeeding or failing academically. Further, none of the districts regularly raised concerns about academic performance, even though the charter schools we reviewed consistently scored lower on statewide tests than comparable schools on average. According to the districts we visited, changes in state law—such as the elimination of the academic performance index—have also made it more difficult for them to conduct effective academic oversight and to hold charter schools accountable for poor academic performance. In addition, one of the districts we visited noted that one of its charter schools qualifies for an exception within state law, which limits the criteria against which the district could hold the school accountable for academic performance.

#### **The Districts We Reviewed Had Different Processes for Holding Their Charter Schools Accountable for Academic Performance**

While state law generally describes certain duties that an authorizer must undertake with respect to its charter school, the law does not clearly define the minimum level of oversight that authorizers must provide with any specificity. Consequently, the districts we visited provide varying levels of academic oversight of their charter schools. For example, according to state law, an authorizing district must visit its charter schools' sites annually; however, state law does not describe the specific oversight activities that the district must perform. Nevertheless, without periodically monitoring their schools for compliance with academic goals, authorizers cannot ensure that schools are making progress in improving student learning, nor are they in a position to identify the need for corrective actions or possibly the revocation of the schools'

charters. For example, New Jerusalem provided evidence that it had visited Acacia Elementary annually throughout our audit period; however, for one of the years, it was unable to demonstrate that it had conducted any substantive assessment of the school's academic performance. Nevertheless, state law does not require districts to do more than visit school sites annually. Moreover, Acton-Agua Dulce Unified and Antelope Valley Union could not demonstrate that they had performed these site visits for all the years in our audit period.

Similarly, although state law requires charter schools to establish measurable student outcomes within their petitions, it does not require authorizing districts to assess annually whether charter schools are meeting those outcomes. Accordingly, the districts we visited could not demonstrate that they had evaluated whether their charter schools had met their measurable student outcomes each year. For example, New Jerusalem's superintendent stated that the district has required its charter schools to report certain financial and educational information since fiscal year 2014–15, and he further asserted that the district has reviewed this information during annual site visits. However, New Jerusalem was unable to provide evidence that it verified the accuracy of any of Acacia Elementary's self-reported information. New Jerusalem's superintendent explained that he does not have any documentation related to Acacia Elementary's academic performance because he periodically reviewed the school's test scores online and would have only documented his review if he identified an issue. However, we do not believe this process would have allowed the district to obtain enough information to assess whether Acacia Elementary was meeting the measurable student outcomes in its charter.

***The districts we reviewed did not consistently perform the academic monitoring included in their agreements with their charter schools.***

In fact, we found that the districts we reviewed did not consistently perform the academic monitoring included in their agreements with their charter schools. Although state law requires authorizers to monitor the academic performance of their charter schools only when the schools seek to renew their charters every five years, authorizers may choose to implement more stringent requirements as part of their MOUs or policies. All the authorizing districts we reviewed have established requirements for academic oversight that exceed those in state law. For example, New Jerusalem established an MOU with Acacia Elementary requiring the school to self-report whether it was meeting the goals and outcomes in its charter. However, New Jerusalem's superintendent stated that the district never received these reports or followed up with Acacia Elementary about them before beginning the revocation process. Similarly, Acton-Agua Dulce Unified's policy requires its charter schools to hire an outside auditor to conduct periodic audits of their academic and financial performances; however, the district has not enforced this requirement. The district's director of charters, who started her role in 2016, believes district staff already perform

these duties annually, as part of the district's annual oversight process. Nevertheless, Acton-Agua Dulce Unified was not able to demonstrate that it regularly assessed whether its charter schools were achieving the measurable student outcomes identified in their charters and thus were on track for renewal.

Antelope Valley Union also failed to provide effective monitoring of LA Online's academic performance, even when the school provided it with information that would have allowed it to identify that the school was struggling. Although Antelope Valley Union's assistant superintendent of educational services stated that the district did not have an active agreement requiring LA Online to self-report measurable student outcomes as part of a programmatic audit, LA Online still provided these programmatic reports to the district for two of the three years we audited. LA Online's reports for fiscal years 2013–14 and 2014–15 revealed that it had not met many of its academic goals, such as those related to English language arts and math. Further, LA Online failed to meet those measurable student outcomes throughout our audit period. Nonetheless, Antelope Valley Union could not demonstrate that it identified the severity of LA Online's academic performance problems until it filed a notice of violation in November 2016. In fact, although Antelope Valley Union's annual review report for fiscal year 2015–16 included a section on Assessment and Accountability, the district did not describe within it LA Online's history of failing to meet measurable student outcomes. Antelope Valley Union's assistant superintendent asserted that the district assessed LA Online's academic performance by reviewing test results online, but it did not retain evidence of these assessments.

Similarly, New Jerusalem did not report any issues with Acacia Elementary's academic performance until it began the process to revoke the school's charter. Specifically, we determined that Acacia Elementary did not meet some of its measurable student outcomes in fiscal years 2014–15 and 2015–16, such as having its students meet or exceed the average achievement of schools located in Stockton. New Jerusalem's superintendent explained that academic performance data for fiscal year 2014–15 was not available until fall 2015, around the same time it became aware of Tri-Valley's potential financial mismanagement. He also explained that the district neither compared Acacia Elementary's academic performance to similar schools in its host district nor evaluated whether the school achieved its charter's goals because the district was concerned that the school's financial issues would have immediate consequences. Although the district asserted that it would have reported any academic performance issues, it did not formally report concerns about Acacia Elementary's academic performance until it filed a notice of intent to revoke in June 2016. As we discuss in Chapter 2, the San Joaquin Superior

***All three districts lack procedures for providing charter schools with timely feedback on specific academic areas in which the schools are either succeeding or failing.***

Court reviewed New Jerusalem's support for revoking Acacia Elementary's charter and determined that New Jerusalem had not adequately considered increases in academic achievement as part of its revocation decision. Because state law requires authorizers to consider increases in student academic achievement for all groups of students as the most important factor in revocations, districts that do not document their ongoing assessments of academic performance may not have sufficient evidence to revoke the charters of failing charter schools.

In general, all three districts lack procedures for providing charter schools with timely feedback on specific academic areas in which the schools are either succeeding or failing. For example, during our audit period, Antelope Valley Union reviewed its charter schools' curriculum, professional development, and education technology, among other things; however, it did not determine whether the schools complied with academic requirements established in the district's policies, MOUs between the district and the charter schools, and charters. New Jerusalem's superintendent stated the district relied on its charter schools' self-assessments of their educational programs; however, it was unable to demonstrate that it verified the schools' responses or evaluated whether they had met measurable student outcomes.

Moreover, we noted that Antelope Valley Union provided less academic oversight to LA Online than it did to the in-district charter school we reviewed—Desert Sands Charter High School (Desert Sands). Although the district asserted that it uses the same academic oversight process regardless of a charter school's location, the district did not visit LA Online in fiscal year 2013–14, while it visited Desert Sands every year of our audit period. In addition, the district did not prepare an annual review report for LA Online for fiscal year 2013–14, even though it prepared Desert Sands' annual review reports for all three years of our audit period. Antelope Valley Union's assistant superintendent stated it did not visit LA Online during fiscal year 2013–14 because during that fiscal year it met with representatives from LA Online at the district's offices. Nevertheless, state law requires authorizing districts to conduct site visits. Moreover, because the district did not retain evidence that it had performed any reviews during fiscal year 2013–14, Antelope Valley Union cannot demonstrate that it held all its charter schools equally accountable.

Finally, Acton-Agua Dulce Unified could not demonstrate that it assessed Assurance Academy's academic performance for one of the years in our audit period because Assurance Academy was an Alternative School Accountability Model (ASAM) school. The California Public Schools Accountability Act of 1999 established ASAM to provide school-level accountability for alternative schools

servicing high-risk students, such as those who are habitually truant, who are recovered dropouts, or who are parenting. ASAM was an alternative accountability system in effect during our audit period, which we discuss further in a following section.

### **The Academic Performance of the Out-of-District Charter Schools We Visited Was Below the Average Performance of Comparable Schools**

According to analyses we conducted, the standardized test scores for English language arts and math at the three charter schools we visited were below the combined average scores of comparable schools for fiscal years 2014–15 and 2015–16. State law requires both charter and noncharter schools to participate in standardized statewide testing. Education publishes each school’s test results on its website, and these results can aid authorizers in gauging the academic achievement of their charter schools. For example, test scores help authorizers determine whether their charter schools are meeting the academic goals in their charters and if their schools’ performances are above or below the average of comparable schools.

State law includes five academic criteria for charter renewal and requires that charter schools need only meet one of the five criteria to have their charters renewed. However, three of the five criteria are no longer applicable because they refer to an accountability system that the State suspended in fiscal year 2013–14 and subsequently replaced in March 2017. The two remaining criteria are that a charter school’s academic performance must be equal to or better than that of the noncharter schools its students would have otherwise attended or that the charter school qualifies for an alternative accountability system.

Because the authorizers we visited could not demonstrate or provide documentation that they consistently monitored the academic performance of their charter schools, we conducted our own evaluation. Specifically, we used the State’s new accountability system to compare the fiscal year 2014–15 and 2015–16 English language arts and math scores for the three out-of-district schools we visited to the scores of comparable noncharter schools. Because Education was field testing the new accountability system during fiscal year 2013–14, no data was available until the system was fully implemented in fiscal year 2014–15. We identified comparable schools based on school type, location, size, percentage of socioeconomically disadvantaged students, and percentage of English learners. Because Acacia Elementary operated in Stockton Unified’s jurisdiction, we selected schools from Stockton Unified serving kindergarten through grade 5 that had similar enrollment sizes and percentages of socioeconomically disadvantaged students and English learners.

*The authorizers we visited could not demonstrate or provide documentation that they consistently monitored the academic performance of their charter schools.*

***All our selected charter schools' math scores were below the combined averages of comparable schools for both years.***

We chose LA Online's comparable schools based on whether the schools were primarily or exclusively virtual, had similar enrollment sizes, and served similar percentages of socioeconomically disadvantaged students and English learners in grades 9 to 12. Because there are so few noncharter virtual schools, we broadened our search to the entire State.

As we mention previously, during our audit period, Assurance Academy was an ASAM school that served students in grades 9 to 12 who mostly lived in LA Unified's jurisdiction. Because ASAM schools use varying methods to serve unique populations, the effectiveness of comparing academic performance among ASAM schools may be limited. Accordingly, state law makes certain exceptions for ASAM schools, as we describe below. We therefore compared Assurance Academy to other ASAM schools in LA Unified, such as continuation schools with similar enrollment sizes and percentages of socioeconomically disadvantaged students and English learners. According to its ASAM application, 95 percent of Assurance Academy's students qualified as high-risk students.

As Tables 8 and 9 on pages 63 and 64 show, all our selected charter schools' math scores were below the combined averages of comparable schools for both years. Similarly, the schools' English language arts scores were below the combined average of comparable schools for both years, except in one instance, when the scores were the same. As shown in Table 8, Acacia Elementary English language arts results significantly improved from fiscal year 2014–15 to fiscal year 2015–16. However, with one exception, its scores were still below the combined average of comparable schools. In addition, Acacia Elementary's improvement might have been overstated because it did not report scores for its fourth graders for fiscal year 2014–15 as they were deemed invalid. Tri-Valley's chief executive officer could not provide an explanation why Acacia Elementary did not report the test scores. According to one of Education's administrators, invalid test scores may be the result of cheating, testing of students at the wrong grade level, students' failing to complete enough questions, or parents requesting exemptions from testing.

All the authorizing districts we visited stated that they were aware of their charter schools' academic performance because they reviewed the testing data online; however, they asserted that they did not follow up with the charter schools to create corrective action plans either because the schools qualified for an alternative accountability system or because the State had implemented changes to its accountability system. For example, the assistant superintendent of Antelope Valley Union indicated that the district monitors whether its charter school students are meeting measurable outcomes; thus, his district should have been

aware of LA Online’s poor test scores. However, the assistant superintendent stated that the district did not follow up with the school in fiscal year 2014–15 because LA Online had just adopted a new curriculum. He explained that properly evaluating a new curriculum takes time; however, LA Online also had poor academic results in fiscal year 2013–14 under its old curriculum, and the district could not demonstrate that it had followed up then either. Antelope Valley Union’s assistant superintendent also pointed to the State’s transition to a new accountability system as a hindrance to the district’s ability to provide consistent academic oversight. He stated that the district relied heavily on the old accountability system to determine a school’s academic achievement and that the discontinuance of academic performance reports the State issued under the previous system limited the district’s ability to assess academic performance.

**Table 8**  
**Acacia Elementary’s Academic Performance Fell Below the Averages for Comparable Elementary Schools During Fiscal Years 2014–15 and 2015–16**

SCHOOL	CALIFORNIA ASSESSMENT OF STUDENT PERFORMANCE AND PROGRESS (CAASPP)— PERCENTAGE OF STUDENTS MEETING OR EXCEEDING STATE STANDARDS						OTHER STUDENT OUTCOMES*	
	ENGLISH LANGUAGE ARTS			MATHEMATICS			PERCENTAGE OF STUDENTS SUSPENDED	PERCENTAGE OF STUDENTS EXPULSED
	GRADE 3	GRADE 4	GRADE 5	GRADE 3	GRADE 4	GRADE 5		
<b>Fiscal Year 2014–15</b>								
Acacia Elementary	0%	0% <sup>†</sup>	12%	0%	9%	3%	0%	0%
<i>Averages for Comparable Schools</i>	21	22	27	26	25	16	10	0
El Dorado Elementary	17	18	19	11	11	10	12	0
Kennedy Elementary	14	21	27	30	33	18	11	0
Rio Calaveras Elementary	33	33	49	36	41	34	8	0
George W. Bush Elementary	21	18	20	27	25	11	7	0
Victory Elementary	21	22	19	25	16	7	10	0
<i>San Joaquin County</i>	27	30	34	31	26	21	8	0
<b>Fiscal Year 2015–16</b>								
Acacia Elementary	17%	14%	29%	11%	7%	12%		
<i>Averages for Comparable Schools</i>	29	23	29	36	30	21		
El Dorado Elementary	23	21	24	25	20	8		
Kennedy Elementary	30	17	34	39	31	23		
Rio Calaveras Elementary	47	43	48	58	46	49		
George W. Bush Elementary	20	19	26	27	28	19		
Victory Elementary	25	14	15	29	27	5		
<i>San Joaquin County</i>	32	32	38	36	29	24		

Sources: California State Auditor’s analysis of fiscal years 2014–15 and 2015–16 CAASPP data and fiscal year 2014–15 suspension and expulsion data from Education.

\* Suspension and expulsion data from Education are not yet available for fiscal year 2015–16.

† None of Acacia Elementary’s fourth graders had valid test scores for English language arts in fiscal year 2014–15.

**Table 9**  
Assurance Academy's and LA Online's Academic Performance Fell Below the Averages for Comparable High Schools During Fiscal Years 2014–15 and 2015–16

SCHOOL	CAASPP—PERCENTAGE OF STUDENTS MEETING OR EXCEEDING STATE STANDARDS		OTHER STUDENT OUTCOMES*		
	ENGLISH LANGUAGE ARTS	MATHEMATICS	PERCENTAGE OF STUDENTS GRADUATED	PERCENTAGE OF STUDENTS SUSPENDED	PERCENTAGE OF STUDENTS EXPELLED
	GRADE 11	GRADE 11	GRADE 12	SCHOOLWIDE	SCHOOLWIDE
<b>Fiscal Year 2014–15</b>					
Assurance Academy	17%	1%	5%	0.0%	0.0%
<i>Averages for Comparable Schools</i>	23	2	9	0.0	0.0
Cal Burke High	32	6	13	0.0	0.0
Central High	24	0	4	0.7	0.0
Metropolitan Continuation High	30	0	1	0.0	0.0
Will Rogers Continuation High	8	0	14	0.0	0.0
Frida Kahlo High	23	2	10	0.0	0.0
<i>Los Angeles County</i>	54	28	79	2.2	0.0
LA Online	50%	10%	27%	0.0%	0.0%
<i>Averages for Comparable Schools</i>	61	16	91	0.0	0.0
Redlands eAcademy	†	†	100	0.0	0.0
Rivercrest Preparatory	35	13	100	0.0	0.0
Riverside Virtual	87	18	73	0.0	0.0
<i>Los Angeles County</i>	54	28	79	2.2	0.0
<b>Fiscal Year 2015–16</b>					
Assurance Academy	19%	1%	6%		
<i>Averages for Comparable Schools</i>	22	3	17		
Cal Burke High	30	0	34		
Central High	10	5	11		
Metropolitan Continuation High	37	3	3		
Will Rogers Continuation High	10	0	21		
Frida Kahlo High	24	6	18		
<i>Los Angeles County</i>	58	30	81		
LA Online	47%	7%	18%		
<i>Averages for Comparable Schools</i>	68	27	82		
Redlands eAcademy	†	†	83		
Rivercrest Preparatory	51	6	87		
Riverside Virtual	84	48	75		
<i>Los Angeles County</i>	58	30	81		

Sources: California State Auditor's analysis of fiscal years 2014–15 and 2015–16 CAASPP data from Education, fiscal year 2014–15 suspension and expulsion data from Education, and fiscal years 2014–15 and 2015–16 graduation data from Education.

\* Suspension and expulsion data from Education are not yet available for fiscal year 2015–16.

† Education does not publish the data if fewer than ten students were tested.

State law describes that the intent of the Legislature is to hold charter schools accountable for meeting measurable student outcomes. Further, state law establishes that districts must consider increases in student academic achievement as the most important factor in determining whether to renew or revoke schools' charters. If authorizers do not consistently monitor the academic performance of charter schools and hold the schools accountable, they cannot ensure that charter school students are academically prepared to advance or graduate.

### Changes in State Law Have Diminished Certain Charter Schools' Academic Accountability

Although state law requires authorizers to assess the academic performance of schools petitioning for charter renewal, schools that qualify for an alternative accountability system, such as ASAM, do not need to demonstrate academic achievement as a condition for their charter renewal. Accordingly, Acton-Agua Dulce Unified recently renewed Assurance Academy's charter without assessing Assurance Academy's academic performance. According to Acton-Agua Dulce's director of charter schools, the board did not evaluate the charter school's academic performance as a criterion for renewal because of Assurance Academy's ASAM status. She stated that due to the lack of criteria for holding ASAM schools accountable the district instead considered other factors, such as enrollment, retention and graduation rates, and the number of students reclassified as fluent in English.

Before fiscal year 2009–10, state law held ASAM schools accountable based on their choice of readiness indicators, contextual indicators, and academic completion indicators, as the text box shows. However, due to budget constraints, ASAM schools became accountable under the State's general accountability model beginning in fiscal year 2009–10. This model measured schools' academic growth based on their academic performance index and adequate yearly progress. However, the academic performance index was suspended at the end of fiscal year 2013–14 and adequate yearly progress was discontinued the following year. In September 2016, the State Education Board approved key elements of a new accountability system, the California School Dashboard (Dashboard), but it did not determine how the Dashboard's indicators should be measured

#### ASAM's 15 Indicators of Academic Performance

From fiscal years 2001–02 through 2009–10, ASAM schools were required to choose three of the following 15 indicators to measure their academic performance.

##### Readiness indicators:

- Improved student behavior
- Suspensions
- Student punctuality
- Sustained daily attendance
- Student persistence

##### Contextual indicators:

- Attendance
- California English Language Development Test

##### Academic and completion indicators:

- Writing achievement
- Reading achievement
- Math achievement
- Promotion to next grade
- Course completion or average course completion
- Credit completion or average credit completion
- High school graduation
- General Educational Development (GED) completion, California High School Proficiency Examination, or GED section completion

Source: Education's website.

for alternative accountability model schools. As a result, state law does not establish academic metrics against which it will hold those alternative schools accountable.

On July 12, 2017, the State Education Board approved the development of the Dashboard Alternative School Status program to replace ASAM. According to Education's director of the Analysis, Measurement & Accountability Reporting Division, the new program will hold alternative schools accountable to the same indicators as traditional schools, but it may measure those indicators differently. For example, the program may track indicators related to graduation rates by one-year graduation rates for alternative schools instead of the four-year cohort graduation rates applicable to traditional schools. According to its website, the State Education Board expects to incorporate this new program into the Dashboard in fall 2018. However, the director stated that, pursuant to state law, the Dashboard may still be used to identify schools, including charter schools, in need of technical assistance or charter schools subject to revocation. Nevertheless, while this gap exists in the State's accountability system, authorizers must continue renewing the charters of schools that qualify for alternative accountability systems without the schools having to demonstrate that they are expanding learning experiences effectively for high-risk students, as the Legislature requires.

## **Recommendations**

### ***Legislature***

To ensure that charter schools improve the educational outcomes of their students, the Legislature should amend state law to require authorizers to annually assess whether their charter schools are meeting the academic goals established in their charters.

### ***Districts***

To ensure that charter schools work toward the academic goals established in their charters, the authorizing districts we visited should do the following:

- Adopt a policy requiring them to provide their charter schools with timely feedback and recommendations regarding academic performance.
- Adopt an academic oversight policy that includes steps for working with charter schools with poor performance results.

- Provide their charter schools with annual oversight reports on their academic performance.

Authorizing districts should maintain active memorandums of understanding with their charter schools that describe the district's oversight responsibilities and ensure the schools meet the measurable student outcomes to which they have agreed.

We conducted this audit under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives specified in the Scope and Methodology section of the report. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Respectfully submitted,



ELAINE M. HOWLE, CPA  
State Auditor

Date: October 17, 2017

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For questions regarding the contents of this report, please contact Margarita Fernández, Chief of Public Affairs, at 916.445.0255.

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September 22, 2017

California State Auditor<sup>s</sup>  
621 Capitol Mall Suite 1200  
Sacramento, CA 95814

Subject: *Charter Schools: Some School Districts Improperly Authorized and Provided Inadequate Oversight to Out-of-District Charter Schools, Audit Number 2016-141, dated October 2017.*

The Acton-Agua Dulce Unified School District ("District") appreciates the opportunity to respond to the recommendations made to the District in the draft Audit Report No. 2016-141 regarding charter school authorization and oversight. The District's Administration has reviewed the draft Audit Report and its recommendations, and provides the following responses.

Geographic Restrictions on Charter Schools and Assurance Learning Academy

Acton-Agua Dulce authorized Assurance Learning Academy ("ALA") in May 2012 to operate a nonclassroom-based independent study program. The District and ALA believed that the Charter Schools Act permitted such a program to operate resource centers to support independent study students outside of its authorizer's boundaries. The District and ALA were not alone in this belief, and like other school districts and charter schools relied on previous guidance from the State Superintendent and the California Department of Education. In October 2016, an appellate court concluded that nonclassroom-based independent study programs were subject to the same geographic restrictions as classroom-based programs (the *Anderson v. Shasta* decision). The District promptly notified ALA of the decision and required ALA to prepare a plan for complying with the court decision if the ruling became final. ALA did this, and in January 2017, ALA sought and obtained a material revision to its petition to provide student instruction exclusively in partnership with Workforce Innovation Act boards and programs.

Prior to the *Anderson v. Shasta* decision, the District required charter school petitioners proposing classroom-based programs to comply with Education Code sections 47605(a)(5) and 47605.1(c). These schools had to operate within the

\* California State Auditor's comments appear on page 75.

District's boundaries or, prior to approval, demonstrate that they were permitted to operate a single out-of-District site under Sections 47605(a)(5) and 47605.1(c). The District's Administration and Board would assess whether the petitioners had presented credible evidence that they had recently conducted a diligent search for a single suitable site within the District's boundaries.

Since the *Anderson v. Shasta* decision became final in January 2017, the District applies the Education Code's geographic restrictions in Sections 47605(a)(5) and 47605.1(c) equally to authorized or prospective charter schools, regardless of whether they are classroom or nonclassroom-based programs.

#### Draft Audit Report Recommendations

The District appreciates the Auditors' recommendations. The Administration will work to implement any new practices or procedures suggested in the Audit Report and, where necessary or appropriate, present the recommendations to the District's Board for further consideration. The District responds to specific recommendations below:

①

#### Recommendations at pages 11 and 12 of the Draft Report:

To make certain that they authorize only qualified petitions, Acton-Agua Dulce Unified [redacted] should revise their charter school authorization policies to require the documentation of their evaluations of charter school petitions. The districts should present this documentation to their governing boards for their consideration.

To better ensure effective oversight of their charter schools' finances, the districts we visited should do the following:

- Develop formal written procedures for reviewing charter schools' financial information and conducting annual oversight visits. These procedures should include relevant requirements from the districts' agreements with the charter schools, and best practices.
- Develop formal written procedures for addressing financial concerns.
- After completing their financial reviews and annual oversight visits, provide charter schools with written feedback and recommendations for improving their financial operations.
- Place a district representative as a nonvoting member on each charter school's governing board.

To ensure charter schools work toward the academic goals established in their charters the authorizing districts we visited should do the following:

- Adopt a policy requiring them to provide their charter schools with, timely feedback and recommendations regarding academic performance.



- Adopt an academic oversight policy that includes steps for working with charter schools with poor performance results.
- Provide their charter schools with annual oversight reports on their academic performance.

Response:

District Staff review charter petitions submitted for approval, renewal, or material revision with the aid of a “Matrix” which covers the elements of Education Code 47605 and incorporates the State Board of Education’s standards for assessing charter petitions contained at Title 5 of the California Code of Regulations, Section 11967.5.1. The Staff’s recommendation and the completed Matrix are submitted to the Board for its consideration before the Board takes action.

The District is proud of the depth of its oversight work, but the District will begin to formalize in writing the District’s practices and procedures for reviewing charter schools’ financial information, presenting petitioners with any financial concerns, and conducting annual oversight visits.

The District’s CFO provides District-authorized charter schools with written feedback after completing their financial reviews, noting any areas of concern and requesting financial plans that address any projected shortfalls. The District will seriously consider the Auditors’ recommendation to provide charter schools with more detailed recommendations to address any identified financial concerns, but the District’s Staff believes that it is first and foremost an independently operated charter school’s responsibility to develop and present a sound financial plan for addressing any of the District’s financial concerns.

The District’s Administration will present the District’s Board with the Auditor’s recommendation that the District place a non-voting member on each authorized charter school’s governing board. However, the District’s authorized charter schools operate as, or are operated by, non-profit public benefit corporations. The District believes that California Corporations Code section 5047 prohibits non-voting directors on boards of non-profit public benefit corporations. The District will consider alternatives to non-voting directors.

②

The District's existing policy and practice is to provide charter schools with timely feedback and recommendations regarding academic performance. The District's annual charter school oversight report addresses academic performance. The District will incorporate steps for working with charter schools with poor performance results into the District's written policies.

① Recommendations at Page 43 of the Draft Report:

To ensure that they have a method to hold charter schools accountable for their educational programs, Acton-Agua Dulce Unified, [redacted] should strengthen their authorization processes by using the State Education Board's criteria for evaluating petitions.

To comply with state law, Acton-Agua Dulce Unified, [redacted] should immediately do the following:

- Update their charter school policies to include all of the requirements in state law, and periodically review and update as necessary such policies thereafter.
- Review petitions to ensure they include all of the requirements in state law at the time of their approval.
- Require their charter schools to submit material revisions when they add new locations.
- Track their actual costs for providing oversight and verify that their oversight fees do not exceed legal limits.

Response:

③ The District uses the State Board of Education criteria as addressed above.

④ The District will update its charter school policy to reflect recent changes and clarifications of state law, and going forward will annually review its policy to make any necessary updates. The District does review all charter petitions (approvals, renewals, and material revisions) for compliance with the law, including the geographic restrictions on charter school sites, and through MOU's the District requires charter schools to obtain pre-approval of a material revision to their petitions before adding new locations. The District will develop and implement a process for tracking actual costs of oversight.

① Recommendations at Page 64 of the Draft Report:

To better ensure effective oversight of their charter schools' finances, the districts we visited should do the following:

- Develop formal written procedures for reviewing charter schools' financial information and conducting annual oversight visits. These procedures should include relevant requirements from MOUs with the charter schools and best practices.



- Develop formal written procedures for addressing financial concerns such as a charter school's failure to meet the minimum reserve requirements established in the district's MOU with the charter school.
- After completing their financial reviews and annual oversight visits, provide charter schools with written feedback and recommendations for improving their financial operations.
- Place a district representative as a non-voting member on each charter school's governing board.

Response:

While the District is proud of the extensive fiscal oversight it provides to authorized charter schools, the District will update and expand its formal written policies and procedures related to the review of charter schools' finances to reflect the District's practices.

The District's existing policy and practice is to provide charter schools with timely feedback and recommendations regarding their operations and financial condition. The District will seriously consider the Auditors' recommendation to provide charter schools with more detailed recommendations to address any identified financial concerns, but the District's Staff believes that it is first and foremost an independently operated charter school's responsibility to develop and present a sound financial plan for addressing any of the District's financial concerns.

The recommendation to place a non-voting member on charter schools' governing boards was addressed previously.

Recommendations at Page 76 of the Draft Report

①

To ensure charter schools work toward the academic goals established in their charters, the authorizing districts we visited should do the following:

- Adopt a policy requiring them to provide their charter schools with timely feedback and recommendations regarding academic performance.
- Adopt an academic oversight policy that includes steps for working with charter schools with poor performance results.
- Provide their charter schools with annual oversight reports on their academic performance.

Authorizing districts should maintain active MOUs with their charter schools that describe the district's oversight responsibilities and ensure the schools meet the measurable student outcomes to which they have agreed.

Response:

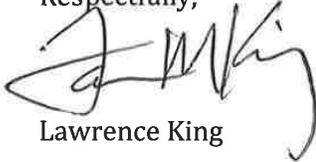
Most of these recommendations have been addressed above in earlier responses.

The District follows Education Code section 47607 when reviewing renewal petitions from authorized charter schools. To obtain a renewal of its petition, a charter school must demonstrate that it has satisfied one or more of the academic performance criteria in Section 47607(b). However, as the draft Audit Report notes, this has been very difficult to assess in recent years since the Academic Performance Index ("API") was suspended in the 2013-2014 school year. With the implementation of the new CAASPP system and the California School Dashboard Report, the District will develop procedures for monitoring charter schools' academic performance throughout the terms of their charter petitions.

Conclusion

The Acton-Agua Dulce Unified School District is firmly committed to thorough charter petition review, approving and denying charter petitions in compliance with law, and rigorous charter school oversight. As part of the District's continuing efforts to strengthen and improve its policies and processes, the District will take appropriate actions to address issues presented in this Audit Report and implement its various recommendations.

Respectfully,



Lawrence King

Superintendent

## Comments

### CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM ACTON-AGUA DULCE UNIFIED SCHOOL DISTRICT

To provide clarity and perspective, we are commenting on Acton-Agua Dulce Unified School District's (Acton-Agua Dulce Unified) response to our audit. The numbers below correspond with the numbers we have placed in the margin of Acton-Agua Dulce Unified's response.

While preparing our draft report for publication, some page numbers shifted. Therefore, the page numbers Acton-Agua Dulce Unified cites in its response do not correspond to the page numbers in our final report.

Our report recommends that the Legislature amend state law to grant clear authority for a nonvoting member to be on an out-of-district charter school's governing board and allow such a representative to attend all meetings of the charter school's governing board. We did not disclose this legislative recommendation in the draft report we sent to the district because the recommendation was not directed to the district.

Although the district states that it uses the State Board of Education's (State Education Board) criteria as a guideline for evaluating petitions, we noted that the district's criteria and its authorization matrix do not include all of the State Education Board's criteria.

Although the district asserts that it reviews all charter petitions for compliance with the law, including the geographic restrictions on charter school sites, we note on page 21 that the district could not demonstrate that its out-of-district charter school had, in fact, qualified for the exception in state law during the authorization process.

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**ANTELOPE VALLEY UNION HIGH SCHOOL DISTRICT**

44811 SIERRA HIGHWAY, LANCASTER, CALIFORNIA 93534-3226  
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STUDENT SERVICES  
  
BRIAN HAWKINS  
ASSISTANT SUPERINTENDENT  
BUSINESS SERVICES

September 22, 2017

Elaine M. Howle, CPA\*  
Jim Sandberg-Larsen  
California State Auditor  
621 Capitol Mall, Suite 1200  
Sacramento, CA 95814

Re: Charter School Audit Report 2016-141

Dear Ms. Howle and Mr. Larsen:

Please find attached the Antelope Valley Union High School District's response to the Charter Schools Audit Report 2016-141. We appreciate the open and consistent dialogue with the audit team and the multiple opportunities to provide input through the draft and revision process. It is our sincere hope that the ultimate outcome of this report is improved policies, practices and procedures that work to continually improve the educational experience and progress for all of our students.

Please feel free to contact me with any questions or comments.

Sincerely,

A handwritten signature in black ink, appearing to read "David J. Vierra".

David J. Vierra, Ph.D.  
Superintendent

Enclosures:

\* California State Auditor's comments begin on page 87.

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**ANTELOPE VALLEY UNION HIGH SCHOOL DISTRICT'S  
RESPONSE TO  
CALIFORNIA STATE AUDITOR'S REPORT  
(2016-141)**

**DATED SEPTEMBER 22, 2017**

### Introduction

The Antelope Valley Union High School District (“District”) appreciates the opportunity to provide the following response to the California State Auditor’s Report entitled *Charter Schools: Some School Districts Improperly Authorized and Provided Inadequate Oversight to Out-of-District Charter Schools* (“Report”).

At the outset, the District wishes to underscore the importance it places on providing a quality education to all public school students so that they have every opportunity to succeed in their post-secondary endeavors. The District is also committed to ensuring that the charter schools under its authorization are held accountable for improving student academic achievement and performance and implementing sound operational and fiscal practices. The District recognizes there is always room for improvement and continually strives to review, develop, and modify its practices, procedures, and operations to better serve the interests of students, staff, families, and the community.

### Practical Considerations

Prior to addressing details of the Report, it is important to highlight several legislative, philosophical, and practical considerations that play a critical part in understanding the evolution of the charter school movement in California and the manner in which school districts, as charter authorizers and oversight agencies, fit within that context. These considerations include the following:

- ❖ **The Laws Governing California Charter Schools Encourage Operational Autonomy.** When the Legislature enacted the Charter Schools Act of 1992 (Education Code sections 47600 *et seq.*; “CSA”), the Legislature sought to provide opportunities for teachers, parents, students, and the community to establish charter schools that would operate independently from the existing school district structure. The Legislature specifically intended for charter schools to be free from most state laws applicable to school districts in an effort to improve student learning, increase learning opportunities, create new professional opportunities for teachers, and provide expanded educational choices to parents and students. (Educ. Code § 47601.) In effect, while charter schools are subject to certain restraints, the Legislature bestowed upon charter schools a significant degree of operational autonomy and flexibility to develop and implement their own educational programs.
- ❖ **Laws Governing Charter School Oversight are Both Limited and Vague.** As the audit team repeatedly notes in the Report, the laws governing charter school oversight are both limited and vague. Consequently, the range of oversight activities performed by charter authorizers throughout the state (e.g., school districts) vary widely in degree and function.

In 2003, the Legislature amended the CSA to add Education Code sections 47604.32 and 47604.33, which provide a general list of the oversight duties of a charter authorizer and

reporting requirements of a charter school, respectively. At the time the Legislature enacted these provisions, it certainly had the opportunity to detail an exhaustive list of oversight activities and obligations of charter authorizers, but it chose not to do so. Rather, the Legislature included a general, non-exhaustive summary of oversight duties that provide little direction or guidance for charter authorizers. For example, charter authorizers are charged with the responsibility of visiting a charter school annually, but there is no authoritative mandate of what should occur at the site visit, the scope of the authorizer's review/audit of the charter school's program and operations, or the preparation of any documentation reflecting that visit (e.g., an annual report, recommendations for improvement, etc.). Consequently, because the laws lack important detail, charter authorizers are left to their own discretion to determine the breadth and scope of their oversight activities. In turn, this has resulted in a lack of uniformity and inconsistency in application of oversight by charter authorizers across the state. In fact, charter authorizers who choose to implement more extensive oversight functions can sometimes receive pushback from charter schools that may feel they are being overregulated or excessively monitored.

Various agencies and organizations have developed recommended guidelines and best practices for charter school oversight, some of which are identified in the Report. However, none of these are mandated by statute. Therefore, whether a charter authorizer chooses to adopt such guidelines and/or practices, develop its own policies and procedures, and/or simply follow the minimum statutory requirements in the CSA is a matter of that agency's discretion.

- ❖ **The Charter School Landscape Has Significantly Changed Since the Enactment of the Charter Schools Act of 1992.** California was one of the first states in the country to authorize the establishment of charter schools. Since that time, there have been a series of legislative changes to the CSA. However, those changes in the law still have not caught up to the practical realities facing school districts who have authorized charter schools.

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For example, as noted in the Report, there was a pervasive practice among virtual and nonclassroom-based charter schools to open "resource centers" outside of the authorizing school district's boundaries without the district's knowledge or prior approval. This spurred a series of lawsuits throughout the state over the legality of this practice, which many charter school proponents argued to be a "gray area" in the law. Ultimately, in October 2017, the California Court of Appeal ruled in the case of *Anderson Union High School District v. Shasta Secondary Home School* ("Anderson") that, regardless of whether a charter school operates a classroom-based or nonclassroom-based program, it may not operate resource centers or other sites outside of its authorizing district's boundaries unless a very narrow exception applies. As a result, charter schools are now being forced to take proactive measures to come into compliance with the geographical limitations under the Education Code.

The *Anderson* case illustrates the evolving nature of the charter school movement and the considerable adjustments that charter authorizers and charter schools must make in their

operations and practices to comply with the law. Therefore, when considering the scope of the audit, which included the 2013-2014, 2014-2015, and 2015-2016 school years, it is important that the Report be viewed critically and in a proper context that considers how the law was being interpreted and the commonly accepted practices of charter schools and their authorizers throughout the state during that time period.

- ❖ **The Legal Means Provided by the Legislature to Hold a Charter School Accountable for its Actions is Through Revocation or Non-Renewal of its Charter.** The District recognizes that, in enacting the CSA (and through subsequent amendments to the law), the Legislature afforded charter authorizers with a certain degree of authority to oversee and hold charter schools accountable for their actions and improving student outcomes. However, the extent of this authority is limited. Specifically, while the law gives school districts the authority to compel a charter school to respond to reasonable inquiries and the right to inspect the charter school's records and observe the charter school at any time, there is no guaranteed method or means to hold the charter school accountable, unless the district initiates lengthy and detailed revocation proceedings or takes action to non-renew the charter school's charter when the charter is due to expire (e.g., after a five-year term). Therefore, while the District is certainly supportive of implementing increased oversight practices of its authorized charter schools, practically speaking, short of revocation or non-renewal, the District is constrained in its ability to hold those charter schools strictly accountable for their actions during the term of their charter due to the limitations in the law.

### **District Response to Key Subject Areas of Audit Report**

The Report focuses on several areas related to charter school oversight, including charter school policies and criteria for evaluating charter petitions, and financial and academic oversight. The District does not address, point by point, each of the findings detailed in the Report. Rather, where applicable, the District provides further clarification or explanation for those areas where it believes it is needed to give appropriate context to the particular findings in the Report.

#### **Charter School Policies and Criteria for Evaluating Charter Petitions**

The Report indicates that the District *may* have failed to comply with state law when authorizing and renewing charter petitions because it did not update its charter school policies to reflect changes in state law. Specifically, the Report states that the District last updated its charter school policy in February 2009 and its corresponding administrative regulation in May 2007; thus its policies did not include the "2013 requirements" (i.e., amendments to the CSA that were enacted into law in 2013).

Although the District's charter school policy and regulation may not have been updated to include the 2013 requirements, it cannot be inferred that the District failed to comply with the law when it authorized or renewed charter petitions. While the District agrees that periodically updating and modifying school district policies and regulations to ensure consistency with applicable law is a sound practice, the lack of such updates does not mean that the District failed to carefully evaluate and consider the legal sufficiency of the charter petitions it approved. The

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District thoroughly reviews all charter petitions according to the law before it makes a staff recommendation to the District's Board of Trustees regarding its findings.

Further, the Report references the regulations promulgated by the State Board of Education ("SBE"), which set forth specific criteria for considering charter petitions. Notably, the Report explains that the Legislature required the SBE to establish this criteria because it recognized that the evaluation of whether petitions contain "reasonably comprehensive" descriptions of the elements required by state law is subjective. The Report then suggests that the District use the SBE's criteria for evaluating charter petitions.

- ③ The District recognizes that the SBE's criteria provides helpful guidelines for reviewing charter petitions, but the adoption of this specific criteria was intended for charter petitions that are filed with the SBE and not individual school districts. Therefore, these guidelines are not legally required for school districts. If the Legislature intended to hold school districts to the same standard as the SBE, it would have amended the law or developed regulations to apply this (or similar) criteria to school districts. Evaluating whether a charter petition includes reasonably comprehensive descriptions of the required elements is a subjective analysis and school districts possess the discretion to determine, either through articulated standards in board policies/administrative regulations *or otherwise*, whether that standard has been met in the petition. In all cases, the District reviews charter petitions in accordance with the law.

#### Financial Oversight

- ④ The Report discusses the financial issues that Los Angeles County Online High School ("LA Online"), a charter school previously authorized by the District, had encountered. When the District became aware of those problems, it engaged in a series of written and verbal correspondence with LA Online representatives to express concerns regarding its fiscal condition and to ask for corrective action. LA Online continuously provided the District with assurances that it was taking steps to bring it into a positive cash balance and adequately cover its operating expenses, such as potentially securing a loan or line of credit, increasing its student average daily attendance ("ADA"), trimming operating expenses, etc. The District had hoped that its concerns and inquiries would precipitate meaningful action on the part of LA Online, but it did not. Despite the District's correspondence, requests for information, and request for a strategic plan to correct these fiscal issues, LA Online could not pull itself out of fiscal insolvency. Given the circumstances, the District finds it highly doubtful that further inquiry, requests for information, or recommendations by the District could have reversed or significantly improved LA Online's financial situation or prevented LA Online's fiscal insolvency and decision to later file for bankruptcy.

- ⑤ The Report correctly notes that state law requires charter authorizers to monitor the fiscal condition of their authorized charter schools, but it does not prescribe any specific procedures for authorizers to follow to fulfill this obligation. Again, the District points out that the only legal mechanism or remedy to address a charter school's fiscal mismanagement or failure to meet generally accepted accounting principles is to initiate revocation proceedings against the charter school, which is precisely what the District did. As the District was preparing its documentation and evidence to initiate this process, LA Online filed for bankruptcy. This complicated and

delayed the District's efforts because the District had to obtain permission from the bankruptcy court before it could continue the revocation process. Once the District secured that approval, it proceeded with the revocation process required by the Education Code.

As the audit team is likely aware, the revocation process is both lengthy and detailed. It was not until after the District had issued a notice of intent to revoke LA Online's charter based on its determination that significant violations continued to exist, and notified LA Online that it would be holding a public hearing on the matter on February 1, 2017, that LA Online filed an emergency motion with the bankruptcy court requesting permission to cease operations and instructional services to its students. LA Online "voluntarily closed" two weeks prior to the District Board of Trustees taking action to revoke its charter. The District believes that LA Online's decision to close was precipitated by the District moving forward with the final steps of the revocation process.

The District also wishes to address statements in the Report that it "could not demonstrate" that it responded to initial indicators of financial difficulties at LA Online and did not always incorporate best practices into its financial oversight processes. It is important to note that a lack of specific documentation reflecting the District's fiscal oversight of LA Online during certain time periods does not mean that the District did not engage in communications or additional follow up with the charter school to address these matters. Moreover, the failure to implement certain best practices (e.g., use of the Fiscal Crisis and Management Team ("FCMAT") checklist) does not equate to a lack of fiscal oversight by the District. As with the SBE charter petition review criteria, these types of best practices are certainly worthwhile and helpful, but the law contains no requirement to implement these guidelines.

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The District has engaged in several recommended practices and will continue to consider using these types of tools when reviewing the fiscal condition of its authorized charter schools. Nevertheless, while the District is not attempting to diminish in any way its oversight obligation to monitor the fiscal condition of these charter schools, there is a certain level of responsibility and ownership charter schools must assume in managing their budgets.

#### Academic Oversight

The District wholeheartedly believes that the purpose of a charter school is to provide its students with a sound and quality education that will afford them the opportunity to succeed. Unfortunately, LA Online did not demonstrate adequate student academic achievement and progress. This lack of academic progress was a critical factor in the District's decision to issue a notice of violation and proceed with the revocation of its charter. Again, the District points out that, short of revocation or non-renewal of a charter, there is no authority for a school district to demand academic achievement other than monitoring progress and providing feedback for improvement.

In addition, while consistent academic monitoring and reporting can be suggested by the charter authorizer or included in a memorandum of understanding between the parties, a charter authorizer cannot be the guarantor of academic success for all of the charter school's students. A charter school must be accountable to the parents/guardians of its students and its governing

board. Further, while the District finds the suggestion of working with its charter schools to improve academic achievement and performance to be noteworthy, charter authorizers must still be mindful that heightened involvement in the educational programming of a charter school could be viewed by members of the charter community as undermining the independent nature of the charter school structure.

### **State Auditor Recommendations**

The Report includes several recommendations developed by the audit team that provide for an increased level of oversight of charter schools. Generally, the District is supportive of those recommendations and believes that the development and implementation of additional internal policies, procedures, checklists, and other tools are beneficial for consistency in performing charter school oversight for all charter authorizers, including the District.

However, there are a few recommendations in the Report that the District believes may not align with the spirit or intent of the law or could result in unintended consequences. These are addressed below.

#### **Oversight Costs**

The Report recognizes that during the combined fiscal years that are within the scope of the audit, the District charged less than the maximum one percent (1%) oversight fee allowable by law. The Report includes a recommendation to clearly track actual oversight costs incurred by the District, noting that a failure to track such costs could result in the undue diversion of funds from charter schools' educational programs. This issue highlights the delicate balance between a school district performing its oversight duties while being fiscally responsible to its own constituency.

- ⑧ The District is supportive of tracking the actual costs of its charter school oversight to ensure compliance with the law. However, if the District were to perform the heightened level of oversight monitoring suggested in the Report for all aspects of charter school operations (e.g., academic, fiscal, governance, etc.), the amount of staff time and resources the District would be required to dedicate would likely result in costs that exceed the maximum 1% allowed by the law. The District also notes that there is no mechanism for reimbursement of these additional costs by the state. Consequently, the District would be required to absorb those additional costs, which could potentially result in the diversion of funds from the *District's* educational programs. For this reason, while the District certainly will not limit its oversight where it believes a heightened degree of monitoring or involvement may be warranted, it must also be mindful of how it dedicates its resources to ensure it is done prudently and in a manner that serves the best interests of its students and the educational community.

#### **District Representative on Charter School Governing Board**

The CSA authorizes a school district to place a single representative on the board of the non-profit public benefit corporation that operates the charter school (where applicable). (Educ.

Code § 47604(b).) The Report recommends that the District elect to place a representative as a non-voting member on each charter school’s governing board.

As part of its findings, the audit team recognized the District had already chosen not to place district representatives on its charter schools’ governing boards due to potential conflicts of interest. It appears that the audit team believes that these concerns would be alleviated if the District were to designate a *non-voting member* to these boards. However, the District disagrees with this assessment. Even if the District placed a non-voting member on a charter school’s governing board, there is still the potential for conflicts of interest to arise. Charter school governing boards are typically subject to the Ralph M. Brown Act (Government Code sections 54950 *et seq.*). To illustrate a real conflict of interest issue, if the non-voting member participated in a closed session discussion of the charter school’s board and learned confidential information, the representative would be prohibited under the Brown Act from disclosing that information to the District. (Gov. Code § 54963.) This could be problematic for the District if the information implicated the District in some way or could serve as a potential ground for revocation or non-renewal of the charter school’s charter. Whether the representative voted or did not vote on the matter would not necessarily alleviate this potential conflict.

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The District recognizes the value of careful observance of a charter school’s governance practices and operations to verify that it is complying with the law. However, it does not believe that including a non-voting member is critical to this oversight function, especially considering that the law makes the appointment of a school district representative optional. As the audit team appears to suggest, there are other effective means to monitor the governance and operations of a charter school, including attending the charter school’s board meetings; reviewing agendas, meeting materials, and board minutes for compliance with the charter and applicable law; and issuing requests for information to clarify or obtain more information on governance issues.

### **Proactive Steps for Effective Charter Oversight**

The District has thoughtfully considered the proposed recommendations in the Report and has already begun to proactively take measures to improve the consistency and effectiveness of its charter oversight activities. These include the following:

- ❖ The District has developed updated written procedures that address the charter petition submission and renewal processes.
- ❖ The District has developed an inter-office memorandum and timeline for the submission of charter school academic and financial reports with their corresponding deadlines.
- ❖ Members of District administration have participated in professional development and trainings on charter school topics.

The District is also in the process of reviewing and preparing suggested changes to its board policies and regulations concerning charter schools, and developing written tools and checklists for academic, fiscal, governance, and operational oversight of its charter schools, among other things.

### **Conclusion**

The District takes its charter oversight responsibilities seriously and is supportive of refining and expanding upon its policies, practices, and procedures for holding charter schools under its authorization accountable for their actions, student outcomes, and the law. However, there is an appropriate balance the District must strike between carrying out its oversight obligations while still affording charter schools under its authorization the ability to operate independently from the traditional school district structure, as contemplated by the law.

It is the District's hope that the Report and the District's corresponding response will serve to highlight the myriad of issues and complexities charter authorizers face in overseeing charter schools due to the vagueness and lack of specificity in the law. To that end, the District welcomes future legislative amendments to the CSA that will provide much-needed clarity and direction for charter authorizers in carrying out these important duties.

## Comments

### CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM ANTELOPE VALLEY UNION HIGH SCHOOL DISTRICT

To provide clarity and perspective, we are commenting on Antelope Valley Union High School District's (Antelope Valley Union) response to our audit. The numbers below correspond with the numbers we have placed in the margin of Antelope Valley Union's response.

For clarification, the statement that it was a pervasive practice throughout the State for virtual and independent-study charter schools to open additional resource centers was presented as an assertion from Antelope Valley Union's assistant superintendent of educational services, as we note on page 25.

Our conclusion that Antelope Valley Union may have failed to comply with state law is based on the fact that it did not ensure that Desert Sands Charter High School's 2014 renewal petition identified goals and outcomes meant for each significant subgroup of students that the charter school would serve. Desert Sands Charter High School's 2014 renewal petition only identifies measurable student outcomes for students schoolwide, similar to the way it identified goals and outcomes in the school's 2010 renewal petition, before state law changed.

As we state on page 34, we agree that only the State Education Board is required to use its regulations as criteria for evaluating charter petitions. However, nothing precludes Antelope Valley Union from using the criteria as helpful guidance. Furthermore, because the Legislature recognized that the term *reasonably comprehensive* is somewhat subjective, we stand by our recommendation that districts should strengthen their authorization processes by using the State Education Board's criteria for evaluating petitions to ensure that they have a method to hold charter schools accountable for their educational programs.

Although our report does not suggest that the District could have prevented LA Online's fiscal insolvency, we note on pages 44 and 46 that the district could not demonstrate that it took prompt and concerted action when LA Online's financial reports showed that LA Online had not met Antelope Valley Union's minimum reserve requirement and was experiencing significant financial distress.

We acknowledge Antelope Valley Union's actions in response to LA Online's deteriorating financial condition on pages 44 through 46; however, we also note on page 44 that Antelope Valley Union

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did not take significant action when LA Online failed to prove that it had obtained a loan to cover its funding shortfall. As a result, the district did not learn that LA Online had not obtained this loan until September 2015—almost nine months after LA Online submitted its first financial report showing indicators of financial difficulties.

- ⑥ Although state law may not require the district to implement best practices regarding financial oversight, we believe that a robust oversight process would result in documentation that would corroborate the district's assertions regarding its actions.
- ⑦ Our report does not suggest that failure to implement certain best practices equates to a lack of financial oversight. Instead on pages 50 and 51, we state that the districts' processes for providing financial oversight to charter schools missed opportunities to incorporate best practices for monitoring charter schools' financial conditions. Similarly, we do not indicate that state law requires districts to implement the best practices for financial oversight that we discuss in the audit report.
- ⑧ As we note on page 31, none of the districts tracked the actual costs of their oversight activities as required by law. The district stated in its response that performing a heightened level of oversight monitoring may result in costs that exceed the legal maximum while not having any mechanism for reimbursement of these additional costs. However, if the districts had tracked their time and expenses related to oversight, we could have assessed whether a maximum of one percent is reasonable.
- ⑨ As we state on page 53, state law allows an authorizing district to place its representative on a charter school's governing board. Our recommendation does not suggest that district representatives attend all charter school's governing board meetings. However, by placing a representative on a charter school's governing board, the authorizing district would secure access to such meetings. Moreover, we recommended that the Legislature amend state law to grant clear authority for a nonvoting member to be on an out-of-district charter school's governing board and allow such a representative to attend all meetings of the charter school's governing board.

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DAVID THOMING  
Superintendent

DONALD PATZER  
Principal

September 22, 2017

Elaine M. Howle, State Auditor\*  
California State Auditor  
621 Capitol Mall, Suite 1200  
Sacramento, CA 95814

Re: State Auditor's Report on Charter School Oversight, 2016-141

Dear Ms. Howle:

Thank you for the opportunity to review and respond to the State Auditor's report, no. 2016-141, titled *Charter Schools: Some School Districts Improperly Authorized and Provided Inadequate Oversight to Out-of-District Charter Schools ("Oversight Report")*.

New Jerusalem Elementary School District ("District") values charter schools as an alternative educational framework to provide innovative learning opportunities for a student population with a diverse set of needs, based on the unique focus of each charter school. The District has a present and continuing interest in providing effective oversight of its charter schools to ensure high quality academic environments for students, long-term viability of the schools, and compliance with laws and regulations.

In responding to the concerns raised by the Oversight Report, the District respectfully provides additional context about the District, its infrastructure, and the charter schools it authorizes. Such information is incomplete in the Oversight Report and critical to a full understanding of the District's oversight practices. Further, significant aspects of the circumstances leading to the bankruptcy of Tri-Valley Learning Corporation ("TVLC") and closure of its four charter schools, including Acacia Elementary Charter School ("Acacia Elementary"), are not addressed. Instead, the Oversight Report evaluates the Acacia Elementary closure in a vacuum – without analysis of Acacia Middle Charter School ("Acacia Middle," collectively with Acacia Elementary, the "Acacia Schools") or Livermore Valley Charter Prep High School and Livermore Valley Charter School (both authorized by Livermore Valley Joint Unified School District ("LVJUSD"), and collectively, the "Livermore Charter Schools"). The root causes of TVLC's bankruptcy stemmed from aspects of operation of the Livermore Charter Schools. Without the ability to evaluate all aspects of TVLC and its charter schools, the State Auditor has been unfortunately limited in considering and advising on best practices and legislative amendments related to authorization and oversight of charter schools. Such recommendations are needed to ensure accountability in the operations of charter schools for their students and California taxpayers and to provide guidance to all charter authorizers, regardless of agency type or size.

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\* California State Auditor's comments begin on page 103.

- ① ② For these reasons, the District respectfully requests that complete information about the District’s infrastructure and oversight practices, as well as a full analysis of TVLC’s operations (including the Livermore Charter Schools and the oversight practices employed by LVJUSD) be included in the final Oversight Report.

The District welcomes the best practice recommendations in the Oversight Report and encourages the Legislature to consider amending the Charter Schools Act (the “Act”) to clarify the legal oversight responsibilities of chartering authorities. Such amendments are necessary so that chartering authorities will have certainty regarding oversight obligations, which are only briefly outlined in the Act without detail to guide implementation. Incorporating the recommendations into law will also provide charter authorizers necessary authority to conduct oversight activities. In the District’s experience, provision of oversight beyond the statutory minimums is often challenged by “independent charter schools” operated as a non-profit corporation or by a non-profit charter management organization (“CMO”) (corporations established for the purpose of operating multiple charter schools, but are separate entities from the charter schools themselves). Changes to the law more clearly defining the authorizer’s role will benefit students and taxpayers by providing a tool for authorizers and charter schools to work together to ensure accountability.

### Overview of California Charter School Structure

- ④ The Act permits a variety of organizational and funding structures for charter schools. These structures are only partially described in the Oversight Report. A clear understanding of these structural options will facilitate the discussion about charter school operations and the District’s oversight practices.
1. Independent versus Dependent Charter Schools
- ④ Charter schools may be structured as independent or dependent charter schools. These are terms used in practice to describe particular organizational structures, though the terms are not found in law. Dependent charter schools are charter schools established and operated by the chartering school district. The governing board of the chartering school district also governs the charter school. Charter schools can alternatively elect to be operated as, or by (as with a CMO structure), nonprofit public benefit corporations pursuant to Education Code section 47604(a). The nonprofit structure and such charter schools are commonly referred to as independent charter schools. Independent charter schools are operated as nonprofit corporations with their own governing board, or by a CMO and its governing board. Independent charter schools must still be authorized by a school district, a county board of education, or the State Board of Education.
2. Directly Funded versus Locally Funded Charter Schools
- ④ The Oversight Report addresses locally funded versus direct funded charter schools, but seems to conflate these funding options with dependent or independent charter school status. The District requests clarity in the Oversight Report around the funding descriptions. Charter schools elect to receive the state aid portion of the charter school’s total local control funding formula allocation either *directly* to the charter school’s account with the county treasury, or *locally*, from the county

superintendent to the charter authorizer to the charter school. (Ed. Code, § 47651(a)(2).) The funding election is not governed by the charter school’s organizational structure, and does not affect the amount of funding received. Charter schools are not authorized as locally funded or directly funded, because each charter school elects to receive its funding either locally or directly, and may make this election every year by June 1. (Ed. Code, § 47651(b).) In practice, however, independent charter schools typically elect to receive direct funding and dependent charter schools typically elect to receive local funding. Direct funding of independent charter schools, and local funding of dependent charter schools, is generally a matter of convenience.

The Oversight Report references locally funded versus directly funded charter schools, with an overview of charter school funding on page 18. References locally funded charter schools authorized by the District are found on pages 28, 31, 32, and 34. With respect to the District, the Oversight Report implies the District increased its own revenue by authorizing locally funded charter schools. (Oversight Report, pp. 31 – 32.) This is not accurate.

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Locally funded monies that pass through the charter authorizer are not owned by the authorizer, nor is the authorizer entitled to keep funds from the charter school for the authorizer’s own purposes aside from fees or costs that may be charged to the charter school pursuant to other provisions such as Education Code section 47613. It is inaccurate to state the District received “revenue” from the charter school local funding, apart from the fees and costs charged for oversight and services. (Oversight Report, 31 – 32.) The District only receives a portion of a locally funded charter school’s revenue when it is in consideration for oversight fees or charges for services.

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Though the District receives and manages the funds of its dependent charter schools (the District would manage the funds even if it is elected direct funding through a county treasury account), it maintains the balances for each school and the school’s reserves. It also budgets for the longer term needs of its dependent charter schools, such as building reserve monies to fund additional facilities for charter school programs. The \$5,497,855 amount identified on page 32 as District revenue from local funding plan is not District revenue, but appears to be the total local control funding formula allocation for those charter schools, which is received and managed by the District on behalf of those charter schools.

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### 3. Liability for Independent versus Dependent Charter Schools

The structure of the charter school dictates an authorizer’s liability for debts and claims against the charter school. A school district operating a dependent charter school is liable for the debts and actions of the charter school, just as it is for the traditional public schools it operates. As its own legal entity, a nonprofit charter school and CMO are liable for operations of an independent charter school. An authorizer is statutorily immune for the operations of independent charter schools: “An authority that grants a charter to a charter school to be operated by, or as, a nonprofit public benefit corporation is not liable for the debts or obligations of the charter school, or for claims arising from the performance of acts, errors, or omissions by the charter school, *if the authority has complied with all oversight responsibilities required by law, including, but not limited to, those required by Section 47604.32 and subdivision (m) of Section 47605.*” (Ed. Code, § 47604(c), emphasis added.) Thus, the statutory scope of oversight is critically important to an authorizer. To the extent the Oversight Report’s recommendations stray beyond the plain language of the statute, the District requests clarity in the

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- ⑦ Oversight Report on the scope of opinion and recommended best practices versus application of existing law to the subjects of the audit.

### Charter Authorizer Statutory Oversight Obligations

#### 1. Charter School Oversight

- ⑤ ⑧ Oversight duties for charter authorizers are specified in Education Code section 47604.32, and listed as “key” duties on page 17 of the Oversight Report. To clarify, the duties listed on page 19 are not just the “key” duties, they are the only statutory prescribed oversight duties specified in the Act, found in Section 47604.32, as follows:

1. Identify at least one staff member as a contact person for the charter school.
2. Visit each charter school at least annually.
3. Ensure that each charter school under its authority complies with all reports required of charter schools by law, including the local control and accountability plan and annual update to the local control and accountability plan required pursuant to Section 47606.5.
4. Monitor the fiscal condition of each charter school under its authority.

Section 47604.32 was added in 2003 as part of AB 1137, legislation following the 2002 State Auditor’s report regarding charter school oversight, which found that oversight of charter schools at all levels could be stronger to ensure charter school accountability. (California State Auditor, *California’s Charter Schools: Oversight at All Levels Could Be Stronger to Ensure Charter Schools’ Accountability* (November 2002), p. 1.) The intent of AB 1137, and Section 47604.32, was to specify oversight duties of each chartering authority with respect to the charter schools under their authority. (AB 1137, Legislative Counsel’s Digest.) As made clear in the Oversight Report, the specified oversight duties may fall short of the providing the desired clarity, particularly if the State wants authorizers to use the specific best practices recommended by the Oversight Report to comply with the statutory oversight responsibilities. *Nothing in current law states how these tasks should be accomplished or what record should be kept of actions.* As such, the law is open to wide interpretation of the level of involvement by an authorizer that is required or *permitted*.

- ⑨ Greater specificity in the law is also necessary if the Oversight Report’s recommended best practices will become the standard for determining whether a chartering authority has fulfilled its oversight responsibilities. As noted above, the question of liability for an authorizer for the actions of a charter school is directly linked to its oversight. Charter schools, like TVLC, have made it clear to their authorizers they do not have the right to participate in the day-to day control over charter school operations. For example, and relevant to the Oversight Report, TVLC refuted the District’s authority to review for sufficiency the 2016-2019 Local Control and Accountability Plan and Annual Update (“LCAP”), an annual update required by state law. (TVLC November 4, 2016 Response to October 5, 2016 Notice of Violation Regarding Acacia Middle, p. 6.) According to TVLC, the LCAP’s purpose is to “provide the District an opportunity to annually monitor the outcomes of [TVLC’s] internal assessments.” (*Id.*) “The District has no jurisdiction to determine if our LCAP is deficient or legally compliant.” (*Id.*) Despite TVLC’s protestations, the District did have authority to review the LCAP

for compliance with state law, pursuant to its section 47604.32(a)(3) duty to “ensure that each charter school under its authority complies with all reports required of charter schools by law, including the annual update required pursuant to Section 47606.5” [the annual update to the LCAP].

Similarly, there are different interpretations of the duty to monitor the fiscal condition of each charter school. As identified in Chapter 2 of the Oversight Report, section 47604.32(a)(4) does not establish a minimum level of financial oversight that districts must perform. In practice, there are even different interpretations of the meaning to “monitor” the fiscal condition of the charter school, and the extent of a charter authorizer’s ability to exercise authority over proposed charter school transactions and financial decisions.

Though opinions regarding best practices for authorizers oversight duties vary, the District complied with its statutory duties in providing oversight to Acacia Elementary, including: 1) identifying a contact for Acacia Elementary, 2) visiting the school at least once each year, 3) ensuring compliance with reports, and 4) monitoring Acacia Elementary’s fiscal condition. The District respectfully requests the Oversight Report clarify the District fulfilled its statutory obligations even if its practices could be improved. ⑩

## 2. CMO Operations

Though the Act anticipates the operation of charter schools by CMOs, the Act’s oversight obligations relate to charter schools and not CMOs. This limited scope means authorizers may not always have access to all information or ability to fully evaluate CMO operations. This includes lack of access to reports, records, and facilities that provide a comprehensive picture of the CMO, its management, and financial viability. The complexity of CMOs can also be used to obfuscate potential issues.

With respect to TVLC, this limitation meant that the District’s oversight did not extend to the Livermore Charter Schools chartered by LVJUSD. The District thus did not receive records of the Livermore Charter Schools and did not evaluate transactions related to the Livermore Charter Schools that may have raised red flags at an earlier point. Similarly, LVJUSD likely did not have access to information about the Acacia Schools. The District had no involvement in the transactions related to the Livermore Charter Schools described in the AB 139 Extraordinary Audit prepared by the Fiscal Crisis Management Assistance Team (“FCMAT”) regarding the Tri-Valley Learning Corporation, dated June 8, 2017 (“FCMAT Extraordinary Audit”), and the Oversight Report, including school bonds (totaling more than \$67 million) which financed the Livermore Charter Schools’ facilities, the related lease that pledged Acacia Elementary revenues for the lease payments that were assigned to the bond trustee, and undisclosed transactions of self-dealing. (FCMAT Extraordinary Audit, p. 10, 63; Oversight Report, p. 48.) Much of the financial pressure that led to TVLC’s bankruptcy was due to financial issues created by the Livermore Charter Schools transactions, including various loans, and loss of enrollment of the Livermore Charter Schools attributable to upheaval around the bonds and the private school involved in the facilities transactions. (FCMAT Extraordinary Audit, p. 59.)

As a result, TVLC was able to obfuscate its financial problems as a CMO. Funds were moved between its four charter schools as needed, and without proper documentation. (FCMAT Extraordinary Audit, p. 56 – 58; Oversight Report, p. 48 – 49.) TVLC funds were moved to private entities, and commingled. (FCMAT Extraordinary Audit, p. 40 – 46.) A loan to Acacia Elementary was

- undocumented and not disclosed in the annual audit report or TVLC’s accounting records. (FCMAT Extraordinary Audit, p. 57 – 58.) The Act does not require specificity in its required financial records, and the Acacia Elementary financial records did not provide the detail regarding TVLC’s finances that would have raised additional red flags, other than the negative ending balance and lack of reserves.

When the District began investigating the status of TVLC’s finances in Fall 2015, it had limited records related to the Acacia Schools. This led to a series of requests by the District for TVLC records, as the District tried to understand the limited information in financial records and audit reports, and then bank statements. Ultimately, the District had to rely on publicly available records such as the bond statements and records that TVLC only disclosed in response to the Acacia Schools revocation proceedings. The District learned additional information, which had been withheld from it, only when the FCMAT report was released.

- Based on this experience, the District believes it would be valuable for the State Auditor’s report to include additional analysis of TVLC’s status as a CMO and its relationship to TVLC’s financial dealings and liabilities.

### The District and Its Charter Schools

#### 1. District Schools

During the 2016-17 school year, the District authorized 13 charter schools (seven dependent charter schools and six independent charter schools) that varied by location and program type:

#### Dependent Charter Schools

- New Jerusalem Elementary School, at District campus
- Delta Charter, at District campus
- Delta Bridges Charter, Stockton
- Delta Charter Online, independent study (virtual)
- Delta Home Charter, independent study (virtual)
- Delta Keys Charter, independent study (virtual)
- Delta Launch Charter, independent study (virtual)

#### Independent Charter Schools

- Acacia Elementary, Stockton
- Acacia Middle, Stockton
- California Virtual Academy – San Joaquin, independent study (virtual)
- Humphreys College Academy of Business, Law, and Education
- Insight @ San Joaquin, independent study (virtual)
- Valley View Charter Prep, independent study (virtual)

Of the six independent charter schools, two were operated as nonprofit corporations, and four were operated by a CMO (including the two Acacia Schools operated by TVLC).  
Of the six site-based charter schools, two of the schools are located within the District's boundaries.

Seven of these charter schools provided virtual independent study programming, accounting for approximately 56% of the charter school students that attended District-authorized charter schools. These independent study charter schools either located within the District's boundaries, outside the District's boundaries pursuant to a relevant exception under Education Code section 47605.1, or do not have educational programming facilities.

## 2. Charter School Compliance and Oversight Infrastructure

Unlike many small school districts, the District infrastructure is built to provide proper oversight of, and ensure charter school's compliance with, the Act. From its staffing to authorizing procedures, the District has prudently managed its resources to ensure the successful operation of its dependent charter schools and proper oversight of all its charter schools.

Under the umbrella of the District and its Superintendent, the District's charter team is led by a Deputy Superintendent of Educational Services who manages the charter school oversight and compliance activities, and is supported by other District administrators with expertise in budget/finance and special education. The Deputy Superintendent serves as the contact to each charter school, and supervises the teams conducting annual visits. District staff members working with charter school matters routinely attend charter school conferences and other professional development opportunities to stay current with charter school development. The District also works with legal counsel experienced with the oversight of charter schools.

The District has developed policies regarding charter school authorization, oversight, renewal, revocation, and facilities. As noted on page 39 of the Oversight Report, these policies are based on guidance from the California School Board Association ("CSBA"), which closely mirrors state law. The CSBA model policies are the industry standard in California adopted by the majority of school districts throughout the State. The policies are current and the District is committed to updating them to stay on pace with changes in the law and best practices.

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Further, the District routinely requires charter petitioners to submit documentation necessary to supplement or clarify aspects of each charter petition to ensure compliance with the Act. The District's new charter petition application guide requires the following information be submitted with each petition: a letter of intent, teacher resumes and credentials, information regarding the governing board, a three-year budget, enrollment forms, due diligence questionnaire, and administrator and governing board member questionnaires. Legislative or regulatory changes mandating that petitioners submit such information as part of a petition would assist authorizers in addressing resistance from petitioners to submitting documentation in support of each petition outside of the elements of the Act.

The District created a rubric to analyze petitions that will be submitted to the District's Board this year for review. The rubric relies in part on the State Board of Education ("SBE") criteria for charter school approval. This effort is consistent with the recommendations set forth in the Oversight Report, but are not required by law. The District also utilizes the support of legal counsel, as appropriate,

during the petition review process. Altogether, the District's detail in petition review has generally resulted in authorization of well qualified charter schools. Not all charter petitions meet the legal requirements of the Act and, in those instances, such petitions have not been approved (including three petitions in the past two years). With respect to Acacia Elementary, when TVLC submitted its petition to the District, it was regionally recognized as a successful CMO with two charter schools authorized first by the SBE, and renewed by LVJUSD. At the time, closer scrutiny of the petition is unlikely to have revealed the egregious financial mismanagement that followed.

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Other infrastructure assists the District's oversight following charter petition approval. The District created a semi-annual oversight matrix for the charter schools to complete. The matrix asks for evidence of support for indicators in the areas of student attendance, cash receipts, disbursements, records retention, payroll, budget/accounting/financial reporting, audit, financial condition, equipment condition, educational program, services to special populations, curricular materials, professional development and teacher qualifications, ongoing assessment, facilities, organizational management, capacity/composition, structure, clarity, meetings, parent and staff involvement, employees, admissions, discipline, health and safety, and parent notifications.

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The District also has a rubric to evaluate the statutorily required annual LCAP. District staff use the rubric to evaluate the annual LCAP update prepared by the charter schools. Notably, TVLC challenged the District's ability to evaluate the sufficiency of the LCAP report, stating that the law only provided the District the authority to ensure that the report was submitted. (TVLC November 4, 2016 Response to October 5, 2016 Notice of Violation Regarding Acacia Middle, p. 6.)

By pressing TVLC on this and other issues through the District's robust oversight process the District flagged discrepancies in TVLC's mismanagement of the Acacia Schools. In fact, the District was the first agency to identify and attempt to correct these issues with TVLC – steps not taken by LVJUSD until over a year later after FCMAT, at the request of the Alameda County Office of Education, confirmed the factual findings that were the basis for District's revocation of the Acacia Schools charters.

### **Other Issues Raised in Oversight Report**

#### 1. Location

The Oversight Report raises questions about the location of Acacia Elementary and whether it qualified for an exception to locate outside of the District's boundaries pursuant to Education Code section 47605.1. (Oversight Report, pp. 23 – 28.) The District followed the plain language of the law, which states:

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[A] charter school that is unable to locate within the geographic boundaries of the chartering school district may establish one site outside the boundaries of the school district, but within the county within which that school district is located, if the school district in which the charter school proposes to operate is notified in advance of the charter petition approval, the county superintendent of schools is notified of the location of the charter school before it commences operations, and either of the following circumstances exist:

- 1) The charter school has attempted to locate a single site or facility to house the entire program, but such a facility or site is unavailable in the area in which the charter school chooses to locate.
- 2) The site is needed for temporary use during a construction or expansion project.

(Education Code section 47605.1(d).)

Acacia Elementary qualified for this exception as it was unable to locate within the District. When the petition was presented to the District, its staff and Board knew with certainty that no facilities were available within the District adequate to house Acacia Elementary. The District is a rural school district outside of the City of Tracy. The only community within its boundaries is the unincorporated community of New Jerusalem, consisting of the District's school facilities, a fire station, residential buildings, and a small airport. The rest of the District is agricultural land, with agricultural and residential buildings. With the exception of the District's buildings, the facilities within the District are unsuitable for school facilities, and the District was aware that its own buildings could not house a classroom-based elementary school program with over 200 students.

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In reviewing the petition, the Board considered Petitioner's intent to serve students in San Joaquin County, which includes the District and its constituents. As a school of choice, the charter school may enroll students throughout the county regardless of location. Since Acacia Elementary was unable to locate within the District's boundaries, the Board approved the Stockton location consistent with Section 47605.1(d). Proper notice was provided to Stockton Unified School District without objection.

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## 2. Review of Charter School Petitions

Petitions to establish charter schools must contain signatures by parents or teachers, with the number of signatures meeting certain requirements. (Ed. Code, § 47605(a)(1).) The Oversight Report identifies an irregularity with the Acacia Elementary charter petition, that the petition did not have the required number of signatures. (Oversight Report, pp. 23 & 36.) The Acacia Elementary charter petition was one signature short, and that one signature was crossed out. The District's count of the total number of signatures was off by one. This error was an oversight, and not indicative of the District's practices.

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## 3. Review of Acacia Elementary Finances

The Oversight Report makes several comments to the effect the District was not timely in identifying Acacia Elementary's financial problems. (Oversight Report, pp. 45, 50, 53.) The District strongly disagrees with this assessment and respectfully requests that these statements be corrected in the final Oversight Report. Each item is addressed below:

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  - Page 54 (\$58,000 ending fund balance identified in December 2014 audit): Given the size of the charter school, its budget and being the first year of operation, the ending fund was not indicative of financial mismanagement. A small, but positive, ending fund balance is typical for a new charter school. The District was also aware that Acacia Elementary School's first year enrollment was short of projections because of a facilities delay that resulted in a temporary enrollment limitation for the first year; second year enrollment increased significantly, so financial projects at the time were reasonable. The District also relied on the reputation of TVLC as a successful CMO with charter schools that had been approved by the SBE.
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  - Page 58, Figure 3 (lease for new facility for \$85,000 per month): In August 2014, Acacia Elementary entered into a lease for a new facility at a rate of roughly \$85,000 a month, more than nine times greater than the rent for its initial facility. When the District was notified of the move in September 2014, the lease had already been approved. (*Id.*) Independent charter schools are operated by the nonprofit governing board, and the charter authorizer does not have authority to approve the nonprofit corporation's financial decisions and transactions. While the lease rate, when realized, was a red flag for the District – and, indeed, raised by the District prior to and during the revocation process, review of the lease prior to TVLC entering into the lease would have placed the District in the position of making day-to-day operational decisions for Acacia Charter School, which is beyond the scope or authority of its oversight duties described by law.
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  - Page 58, Figure 3 (unaudited actuals): By the end of the second year of operation and receipt of Acacia Elementary's 2014-2015 unaudited actuals financial report in September 2015, the District was concerned about Acacia Elementary's financial status because of the failure to meet the three percent reserve for the second year, and requested additional records and financial documentation. Between September 2015 and April 2016, the District corresponded and met with TVLC officials, requesting additional records and notifying TVLC of the District's concerns. When the District learned more about TVLC's finances, and TVLC did not cooperate in providing the information and records requested by the District, the District issued the April and May 2016 notices of violation that eventually led to revocation of the Acacia Elementary charter.
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Financial issues that later surfaced could not have been known by the District at the time they occurred. As discussed in this response, the District did not authorize and was not responsible for providing oversight to the Livermore Charter Schools. TVLC did not disclose to the District that it pledged Acacia Elementary's revenues to make lease payments for Livermore Charter School facilities that were assigned to the trustee for the bonds. In addition, TVLC hid its financial problems, moving monies between its charter schools, entering into an undocumented loan, and failing to disclose that loan in the annual audit. (FCMAT Extraordinary Audit, pp. 56 – 58; Oversight Report, pp. 48 - 49.)
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The lack of detail required of charter school financial reports and the annual audit also made it difficult for the District to ascertain financial status and the nature of some of the transactions.

The timeline in Figure 3 also identifies the District’s requests to include its representative on the TVLC Board, as is its legal right pursuant to Education Code section 47604(b). These requests were made at the beginning of Acacia Elementary’s second year of operation, and then several months later. By the time TVLC added the District representative to its board, TVLC had already entered into many of the transactions that contributed to its financial problems, including the Acacia Elementary lease (August 2014), the undisclosed \$600,000 loan (2014), and the lease that pledged the Acacia Elementary revenues as security (May 2015). (Oversight Report, Figure 3, p. 49.) Since TVLC’s bylaws restricted charter authorizer representatives participation to voting on open session matters related to the charter school it authorized, District representative on the TVLC Board still did not have access to information related to the rest of TVLC’s finances and operations.

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Thus, through its oversight practices, the District did identify the early indicators that were available to the District related to Acacia Elementary’s financial distress. The District responded responsibly and quickly after reviewing the unaudited actuals financial report detailing Acacia Elementary’s finances in its second year of operation.

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The questions asked by the District following receipt of the unaudited actuals report, and its own research, led to the discovery of information about TVLC’s financial transactions, including the Livermore Charter Schools’ bonds and TVLC’s debts, that eventually led to revocation of the Acacia Elementary charter on the bases of failure to comply with material terms of the charter (particularly terms related to Acacia Elementary’s finances) and fiscal mismanagement. The issues identified by the District during the revocation process led to increased scrutiny of the Livermore Charter Schools by LVJUSD, and eventually Alameda County Office of Education, which requested the FCMAT extraordinary audit. FCMAT was given access to TVLC documents and information to which the District did not have access, and FCMAT’s extraordinary audit confirmed many of the District’s allegations.

#### 4. Academic Performance

As described in the Oversight Report, there are limited statutory requirements related to the authorizer’s role in reviewing a charter school’s academic performance. Authorizers are only required to assess academic performance when a charter petition is renewed (Ed. Code, § 47607(a) & (b)) and when a charter is revoked. (Ed. Code, § 47607(c)(2).) (Oversight Report, p. 65.) On the other hand, *charter schools* are required to assess stated measurable student outcomes each year. (Oversight Report, pp. 65 - 66.) There is no clear authority for the District to intervene in the assessment or review process outside the renewal or revocation processes. State law does not require, direct, or arguably even permit, academic performance to be evaluated at the annual site visits. (Oversight Report, p. 65.) With this context in mind, the District respectfully requests the State Auditor to reconsider aspects of the Oversight Report related to the District’s evaluation of Acacia Elementary’s academic performance, and to make certain factual corrections to the Oversight Report related to this issue.

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- ②⑨ Acacia Elementary’s charter petition indicated that student performance would be evaluated based upon statewide testing. (Acacia Elementary Charter, Element C.) In 2013-14, its first year of operation, no data was available for the District to review because Acacia Elementary did not utilize the California Assessment of Student Performance and Progress (“CAASPP”) because statewide testing was transitioning to this new tool for scoring academic performance. Acacia Elementary’s 2014-2015 CAASPP scores were available in Fall 2015. The charter was revoked in July 2016. The 2015-2016 scores were released in the Fall of 2016, *after* revocation (a very limited snapshot of 2015-2016 data was provided by TVLC to the District prior to revocation, but did not contain the detail necessary for a complete evaluation). Since the District did not have two years of data to compare prior to revocation, the District could not determine, much less put the charter school on notice regarding academic progress concerns, prior to initiating and approving revocation. In light of the egregious financial mismanagement triggering the revocation process, which was subsequently confirmed by the FCMAT Audit some 10 months following revocation, the District felt compelled to proceed with revocation notwithstanding the limited data available related to student achievement.
- ③⑩ Related, the District requests the State Auditor to correct the statement in the Oversight Report that the San Joaquin Superior Court determined the District had not adequately considered increases in academic achievement as part of its revocation decision. (Oversight Report, pg. 69.) The Superior Court’s determination was made for the limited purpose of a preliminary injunction and the issue has not been finally adjudicated. (*TVLC v. NJESD*, et al. (Super. Ct. San Joaquin County, 2016, NO, STK-CV-UWM-2016-0007774.)
- ③⑪ Finally, the Oversight Report’s Table 8 comparing Acacia Elementary’s 2014-2015 and 2015-2016 CAASPP scores is also misleading because it compares the Acacia Elementary scores to the scores of other local schools similar to Acacia Elementary. This comparison would be made after four years of operation when the charter school is requesting renewal of its petition not in the revocation context. (Ed. Code, § 47607(b)(4).) A measurement over four years provides a more accurate picture of whether a charter school’s teaching methods are resulting in improved pupil performance.

## 5. Oversight Fees

- ⑤ The Oversight Report raises concerns regarding the oversight fees charged by the District to charter schools. (Oversight Report, pp. 31, 34 – 36.) The supervisory oversight fee specifically funds the oversight activities listed in sections 47604.32 and 47607.3. (Ed. Code, §§ 47604.32(b), 47613(g).) Charter schools may also separately purchase administrative or other services from the charter authority. (Ed. Code, § 47613(d).)
- ③② The District and Acacia Elementary verbally agreed to a 3 percent oversight fee even though Acacia Elementary did not receive rent-free facilities. TVLC Board minutes reflected the TVLC Board’s approval of the higher rate. (Oversight Report, p. 34.) This verbal agreement should have been in writing so that the terms were memorialized.
- ⑤ The District and Acacia Elementary verbally agreed to a 3 percent oversight fee even though Acacia Elementary did not receive rent-free facilities. TVLC Board minutes reflected the TVLC Board’s approval of the higher rate. (Oversight Report, p. 34.) This verbal agreement should have been in writing so that the terms were memorialized.
- ③② Despite the statutory cap, oversight fees in excess of the statutory cap are analogous to developer fees or other circumstances where parties willingly contract at rates that exceed the statutory rate.

It is common practice for authorizers and charter schools to agree on a flat rate percentage to the extent that tracking District staff time and costs related to supervisory oversight can be burdensome since it is part of the day to day work conducted by District employees. Given the significant staff time and costs related to supervisory oversight the statutory oversight fee is not likely to cover the direct costs. Thus, the conclusions in the Oversight Report that collection of the fee results in funds being improperly directed away from charter schools' educational programs is not accurate. In fact, in a matter unrelated to TVLC, the District legally challenged the practice of another CMO that retained in excess of \$1 million in reserves for two charter schools whose operation was moved from the CMO to the District.<sup>1</sup> This demonstrates the District's strong commitment to keeping dollars meant for education with students.

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Finally, the District wishes to clarify it did not develop a new agreement with TVLC and Acacia Elementary following its amended policy specifying the District's agreement to provide administrative or support services should be memorialized in a memorandum of understanding. (Oversight Report, p. 34 – 35.) At the time the policy was updated in February 2016, the District was preparing to file a Notice of Violation with TVLC regarding Acacia Elementary and TVLC. The priority at that time was addressing the various deficiencies in TVLC's operations, which ultimately resulted in revocation and closure.

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#### 6. Board Membership

The Oversight Report recommends that charter authorizers place a district representative as a nonvoting member on each charter school's governing board. (Oversight Report, p. 12.) The Charter Schools Act expressly allows this, as "[the] governing board of a school district that grants a charter for the establishment of a charter school formed and organized pursuant to this section shall be entitled to a single representative on the board of directors of the nonprofit public benefit corporation." (Ed. Code, § 47604(b).) As used in the Corporations Code, however, directors of nonprofit corporations have voting rights; a person who does not have the authority to vote as a member of the governing body of the corporation is not a director. (Corp. Code, § 5047.) The District requests clarity on this recommendation.

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In practice, charter authorizers in California typically do not appoint a member to the charter school's governing board. There are concerns regarding the potential for conflicts given the issues that may arise between the charter authorizer and the charter school.

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<sup>1</sup> The District initiated litigation against a CMO that retained the unspent funds of two charter schools following transfer of management of the charter schools to the District. The District took the position that state funds allocated to the charter schools were for the benefit of the charter schools, and did not belong to the CMO. (*NJESD vs. Academy of Arts and Sciences Charter School*, et al., (Super. Ct. San Joaquin County, 2016, No. STK-CV-UWM-2016-0007774.)

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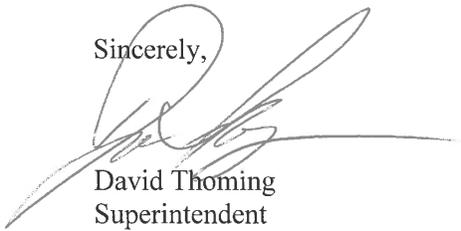
### Conclusion

Consistent with the foregoing, the District respectfully requests the final Oversight Report be revised as follows:

- ④ 1. Clarify the types of charter school structures;
- ⑫ ⑬ ⑭ 2. Include relevant information regarding the District and its current infrastructure related to charter school authorization and oversight;
- ① ② 3. Include and evaluate relevant information related to TVLC and the Livermore Schools;
- ①-35 4. Correct factual errors in the Oversight Report as identified in this response;
- ⑦ 5. Clarify current law related to oversight practices and distinguish those requirements from best practice recommendations as applied to the subjects of the audit; and
- ③ ③5 6. Make recommendations regarding Legislation to address authorization and oversight of charter schools operated by CMOs, operation of such charter schools by CMO, including required transparency by CMO to authorizers regarding CMO operation.

Thank you for the opportunity to respond to the Oversight Report. If you have any questions regarding these responses, please contact Superintendent, David Thoming at (209) 830-6363.

Sincerely,



David Thoming  
Superintendent

## Comments

### CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM NEW JERUSALEM ELEMENTARY SCHOOL DISTRICT

To provide clarity and perspective, we are commenting on New Jerusalem Elementary School District's (New Jerusalem) response to our audit. The numbers below correspond to the numbers we have placed in the margin of New Jerusalem's response.

We disagree that information on the district is incomplete. We present detail on the district as necessary throughout our report. In addition, we provide background information about the district in Table 2 on page 15 and changes to the district's number of charter schools and enrollment in Table 5 on page 23. Contrary to New Jerusalem's assertion, our report includes significant information regarding the circumstances leading to the bankruptcy of Tri-Valley Learning Corporation (Tri-Valley) and the closure of Acacia Elementary.

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As we state on page 15, our audit focused on charter schools specifically identified in the audit request and on these charter schools' authorizing school districts. Because the audit request named Acacia Elementary Charter School (Acacia Elementary) but did not name other Tri-Valley charter schools, we provided information on other Tri-Valley schools to the extent that such information was relevant to Acacia Elementary. In addition, California's Fiscal Crisis and Management Assistance Team (FCMAT) performed an audit of Tri-Valley's Livermore schools and published the results of its audit in June 2017. We summarize FCMAT's key findings and recommendations in the text box on page 42.

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We disagree. The scope of our audit as approved by the Joint Legislative Audit Committee has resulted in our report citing relevant best practices and making numerous legislative recommendations related to the authorization and oversight of charter schools.

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As we note on page 12, our report makes clear that we are discussing the common practice of locally funded and directly funded charter schools. We do not use the terms dependent and independent, which are sometimes used within the education community to describe a charter school's structure, because they are not found in state law. On page 12, we note that locally funded charter schools usually have the same governing board as their authorizing districts while directly funded charter schools are typically operated by nonprofit public-benefit corporations. The district's response acknowledges that this practice is typical of how charter schools elect to receive their funding. Thus, we believe we have sufficiently covered the structures of charter schools for the purposes of our audit report.

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- ⑤ While preparing our draft report for publication, some page numbers shifted. Therefore, the page numbers New Jerusalem cites in its response do not correspond to the page numbers in our final report.
- ⑥ We disagree with the district's statement that it did not increase its revenue as a result of authorizing locally funded charter schools outside the district's geographic boundaries. As shown in the text box on page 29, the district's out-of-district locally funded charter schools generated nearly \$5.5 million in local control funding formula revenue, which we refer to as the local funding plan, described on page 12. Although we do not discuss this in the report, the revenue of locally funded charter schools that New Jerusalem authorized is included in the district's audited financial statements. Moreover, the charter petitions of New Jerusalem's locally funded charter schools state that the district provides all support services to these charter schools, including personnel, financial, legal, purchasing, and facility services. The petitions further state that New Jerusalem's superintendent determines the charter schools' costs for these services, subject to the district's governing board ratification. Given that the district receives its locally funded charter schools' funding and makes spending decisions in relation to this funding, we stand by our conclusion that New Jerusalem increased its revenue by authorizing locally funded charter schools outside its geographic boundaries.
- ⑦ We disagree that our recommendations are not clear. The report clearly distinguishes between the law and best practices in its discussion of the authorization and monitoring of charter schools. Our recommendation specific to ensuring compliance with state law on page 37 clearly states this focus.
- ⑧ In the text box on page 11, we describe key statutory responsibilities of charter authorizers. An example of a responsibility that we did not include in the text box is state law's requirement that charter authorizers consider increases in student academic achievement for all groups of students served by a charter school as the most important factor in determining whether to grant a charter renewal or revoke a charter. Thus, we stand by our description of the items as key statutory responsibilities.
- ⑨ The example that New Jerusalem provides in its response is not relevant to Acacia Elementary, as New Jerusalem refers to a document that pertains to Acacia Middle Charter School (Acacia Middle)—another Tri-Valley charter school. As we describe in Comment 2, the audit request named Acacia Elementary but did not name other Tri-Valley charter schools as being within this audit's scope.
- ⑩ As we state on page 15, the Joint Legislative Audit Committee directed us to determine the adequacy of the financial oversight provided by the authorizing districts for the charter schools located

outside of their geographic boundaries. State law does not prescribe specific procedures that authorizers must follow to fulfill their oversight responsibilities, which we acknowledge several times throughout the report—including on pages 4, 39, 44, and 50—so we relied upon best practices to assess their financial oversight.

New Jerusalem’s statement minimizes the significance of Acacia Elementary’s low level of reserves and the charter school’s deficit for its first year of operations as indicators of the charter school’s financial condition. New Jerusalem’s statement is inconsistent with the district’s requirements. Specifically, as we state on page 47, the district’s memorandum of understanding with Acacia Elementary required the charter school to maintain a minimum level of reserves. Thus, we disagree with New Jerusalem’s justification for its lack of action in response to Acacia Elementary’s initial indicators of financial difficulties and we stand by our conclusion that the district should have taken action sooner in response to these indicators.

⑪

As we describe on page 33, the district did not update its charter school policy between September 2008 and February 2016, despite amendments to state charter school law in 2013. We look forward to the district’s 60-day response to clarify the specific procedure it has established to ensure that its policies are updated periodically to reflect changes in state law.

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Contrary to New Jerusalem’s statement, our report does not suggest that New Jerusalem’s review of Acacia Elementary’s petition would have revealed Tri-Valley’s financial mismanagement.

⑬

Although we acknowledge on pages 51 and 52 that New Jerusalem uses oversight matrices, our concern is that New Jerusalem could not demonstrate that it always reviewed these matrices or provided feedback to Acacia Elementary on identified issues. As such, the district is not using this tool in the most meaningful way, as we state on page 52.

⑭

We disagree with the district’s claim that Acacia Elementary qualified for an exception to being located within the district’s geographic boundaries. State law requires a charter petition to identify a single school to operate within the geographic boundaries of the authorizer, with limited exceptions. As the district noted in its response, the plain language of the law provides an exception if the charter school has attempted to locate a single site or facility to house the entire program, but such a facility or site is unavailable in the area in which the charter school chooses to locate. As we point out on page 22, Acacia Elementary’s petition stated that the school’s intention was to serve students within San Joaquin County, with particular attention to underserved students in Stockton.

⑮

Further, on that same page, we note that in fiscal year 2015–16 none of Acacia Elementary’s students lived within New Jerusalem’s boundaries. Therefore, we stand by our conclusion that it did not qualify for the legal exception and should have petitioned the district where the students it intended to serve were located.

- ⑩ As we point out on page 24, state law does not specify how far in advance the host district needs to be notified. However, because the district did not notify Stockton Unified until a few hours before it authorized Acacia Elementary’s petition, it is unclear how this constituted sufficient notice that would have allowed Stockton Unified an opportunity to object.
- ⑪ State law requires petitions to include all of the required signatures prior to being submitted to the district’s governing board for review. However, Acacia Elementary’s petition included only nine of the 10 teacher signatures it needed at the time it was authorized. Districts should strictly adhere to legal requirements related to charter school authorization.
- ⑫ We address specifics of the district’s comments related to financial oversight in Comments 19 through 25 below.
- ⑬ New Jerusalem misstates that Acacia Elementary’s reported ending balance amounted to \$58,000 for fiscal year 2013–14, when, in fact, Acacia Elementary actually reported a *deficit* of \$58,000, an amount \$116,000 lower than New Jerusalem cited in its response. We stand by our conclusion on page 47 that, in aggregate with other indicators present in Acacia Elementary’s financial reports, this deficit should have led New Jerusalem to start taking further action regarding Acacia Elementary’s financial condition.
- ⑭ We disagree with New Jerusalem’s argument that its reliance on Tri-Valley’s reputation as a successful CMO justified New Jerusalem’s lack of action in response to initial indicators of Acacia Elementary’s financial difficulties. As an authorizing district, New Jerusalem had a responsibility to monitor the fiscal condition of Acacia Elementary. As we show in Figure 3 on page 48, Acacia Elementary’s financial reports indicated that its financial condition was deteriorating. Hence, we believe that New Jerusalem should have taken action based on Acacia Elementary’s financial information, regardless of its perception of Tri-Valley’s reputation.
- ⑮ Our report does not suggest that New Jerusalem should have approved Acacia Elementary’s financial decisions and transactions, including its lease agreement. Instead, on page 52, we state that New Jerusalem could not demonstrate that it acted in response to the high rates in this lease agreement until April 2016, even though the district was aware that Acacia Elementary had relocated

to a new facility in September 2014. Had the district evaluated the related lease agreement in the fall of 2014, when Acacia Elementary notified the district of its relocation to a new facility, we believe New Jerusalem could have earlier recognized the impact of the lease agreement's higher rates on Acacia Elementary's financial condition.

On page 49 and in Figure 3 on page 48, we acknowledge that the district issued a formal notice of concern after receiving Acacia Elementary's unaudited financial report for fiscal year 2014-15, requested additional information from the school to assess its financial condition, and promptly commenced revocation proceedings against Acacia Elementary after identifying additional issues with Acacia Elementary's finances. Therefore, it is unclear with which aspect of our analysis New Jerusalem disagrees.

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Contrary to New Jerusalem's statement, our report does not suggest that New Jerusalem should have known about the financial issues pertaining to Tri-Valley's Livermore schools.

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As we show in Figure 3 on page 48, we recognize New Jerusalem's attempts to place a district representative on Tri-Valley's governing board. Our report does not suggest that placing a district representative on Tri-Valley's governing board sooner would have allowed New Jerusalem to identify Acacia Elementary's undisclosed loan or the fact that Tri-Valley pledged Acacia Elementary's revenue in a lease agreement for its Livermore schools.

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We disagree with New Jerusalem's assessment of its oversight of Acacia Elementary's financial condition. In its response, New Jerusalem asserted that it identified early indicators of Acacia Elementary's financial distress and responded quickly after reviewing the unaudited financial report for Acacia Elementary's second year of operations. However, as we state on page 47 and highlight in Figure 3 on page 48, prior to receiving Acacia Elementary's unaudited financial report for its second year of operations, New Jerusalem had received financial reports indicating that Acacia Elementary was experiencing financial difficulties. The district could not demonstrate that it responded to those initial indicators of Acacia Elementary's financial distress. As a result, we stand by our conclusion that New Jerusalem could have responded sooner to initial indicators of Acacia Elementary's financial difficulties.

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Contrary to New Jerusalem's statement, our report does not state that charter schools are required to assess measurable student outcomes each year. On page 58, we note that although state law requires charter schools to establish measurable student outcomes within their petitions, it does not require authorizing districts to assess annually whether charter schools are meeting those outcomes.

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- ②7 New Jerusalem is mischaracterizing a statement we made on page 57, which notes that state law requires authorizing districts to conduct annual site visits at their charter schools, but does not identify specific oversight activities that the districts must perform.
- ②8 We address specifics of the district's comments related to academic oversight in Comments 29 through 31 below.
- ②9 We note on page 59 that Acacia Elementary failed to meet some of its measurable student outcomes in fiscal year 2014–15 and 2015–16, such as having its students meet or exceed the average achievement of schools located in Stockton. We also include on page 59 the district's explanation that academic performance data for fiscal year 2014–15 was not available until fall 2015. Although the district states that it did not have two years of data to compare prior to revocation, the fall 2015 data would have been sufficient for the district to assess whether Acacia Elementary met its measurable student outcomes for fiscal year 2014–15. However, as we also note on that same page, the district did not report concerns about Acacia Elementary's academic performance until June 2016.
- ③0 Contrary to New Jerusalem's statement, our report accurately cites excerpts from the court's decision to issue the preliminary injunction. The court's decision states that "the resolutions and Finding of Facts #8 of each resolution do not constitute substantial evidence that the District considered increases in the students' academic achievement as the most important factor in the revocation decision. This court would expect that increases would be laid out and identified as to each group and sub-group with a statement about the impact of the increases for the students and the values of such increases for the students and the community."
- ③1 As we state on page 17 for Objective 6c in Table 3, we were asked to perform this analysis over this time frame by the Joint Legislative Audit Committee. Although the district notes that a measurement over four years provides a more accurate picture of academic performance, only two years of academic performance data was available.
- ③2 As we state on page 30, the board meeting minutes from May 2015 showed that Tri-Valley's board approved New Jerusalem's proposal for a fee increase to 3 percent; however, the minutes also indicate that the proposal did not include a breakdown describing what the school would receive in exchange. As we note on page 12, state law allows charter schools to purchase additional services from their authorizers; however, state law specifies that authorizers can only charge for the actual costs of supervisory oversight not to exceed 1 percent of a charter school's revenue, or 3 percent of its

revenue if the authorizer provides substantially rent-free facilities. Although Tri-Valley agreed to pay New Jerusalem oversight fees that exceeded the statutory cap, the agreement violated state law.

Although New Jerusalem notes that it is common practice for authorizers and charter schools to agree on a flat rate percentage for oversight fees, state law establishes a legal limitation that districts can only charge their actual costs up to 1 percent of charter school revenue. We believe that the implementation of time-reporting tools would allow staff to identify the cost of district activities related to oversight of each charter school.

The example that New Jerusalem provides in its response is not relevant to Acacia Elementary, which is the focus of our audit. New Jerusalem's response refers to another charter school that the district authorized.

We have made a legislative recommendation to amend state law to grant clear authority for a nonvoting member from an authorizing district to be on an out-of-district charter school's governing board and allow such a representative to attend all meetings of the charter school's governing board. We did not share this recommendation with the districts we audited because it was not made to them.

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