



A REPORT
TO THE
ARIZONA LEGISLATURE

Performance Audit Division

Performance Audit

Arizona State Board for Charter Schools

AUGUST • 2003
REPORT NO. 03 – 07



STATE OF ARIZONA
OFFICE OF THE
**AUDITOR
GENERAL**

Debra K. Davenport
Auditor General

The **Auditor General** is appointed by the Joint Legislative Audit Committee, a bipartisan committee composed of five senators and five representatives. Her mission is to provide independent and impartial information and specific recommendations to improve the operations of state and local government entities. To this end, she provides financial audits and accounting services to the State and political subdivisions, investigates possible misuse of public monies, and conducts performance audits of school districts, state agencies, and the programs they administer.

The Joint Legislative Audit Committee

Senator **Robert Blendu**, Chair

Senator **Gabrielle Giffords**

Senator **Peter Rios**

Senator **Thayer Verschoor**

Senator **Jim Weiers**

Senator **Ken Bennett** (*ex-officio*)

Representative **John Huppenthal**, Vice Chair

Representative **Tom Boone**

Representative **Ken Clark**

Representative **Ted Downing**

Representative **Steve Yarbrough**

Representative **Jake Flake** (*ex-officio*)

Audit Staff

Dale Chapman, Manager and Contact Person

Mark Haldane, Team leader

Danielle A. Mariano

Jesus Borboa

Copies of the Auditor General's reports are free.
You may request them by contacting us at:

Office of the Auditor General

2910 N. 44th Street, Suite 410 • Phoenix, AZ 85018 • (602) 553-0333

Additionally, many of our reports can be found in electronic format at:

www.auditorgen.state.az.us



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

August 11, 2003

Members of the Arizona Legislature

The Honorable Janet Napolitano, Governor

Ms. Kristen Jordison, Executive Director
Arizona State Board for Charter Schools

Transmitted herewith is a report of the Auditor General, A Performance Audit and Sunset Review of the Arizona State Board for Charter Schools. This report is in response to a May 14, 2002, resolution of the Joint Legislative Audit Committee. The performance audit was conducted as part of the Sunset review process prescribed in Arizona Revised Statutes §41-2951 et seq. I am also transmitting with this report a copy of the Report Highlights for this audit to provide a quick summary for your convenience.

As outlined in its response, the Arizona State Board for Charter Schools agrees with most of the findings and plans to implement all but one of the recommendations directed at it.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on August 12, 2003.

Sincerely,

Debbie Davenport
Auditor General

Enclosure

PROGRAM FACT SHEET

Arizona State Board for Charter Schools

Services:

The Arizona State Board for Charter Schools is one of three entities authorized to sponsor charter schools in Arizona.¹ The Board has the following responsibilities:

- Evaluate applications and grant charters to qualified applicants;
- Monitor the schools it charters to ensure they comply with federal and state laws and charter contract requirements;
- Take disciplinary action against charter schools that violate federal, state, or charter contract provisions;
- Investigate and resolve complaints from parents, students, charter school faculty and staff, and the public regarding charter contract provisions, or, depending on the nature of the complaint, refer the matter to the appropriate authority; and
- Provide consumer information to prospective and current school operators and the public.

Board membership and staffing

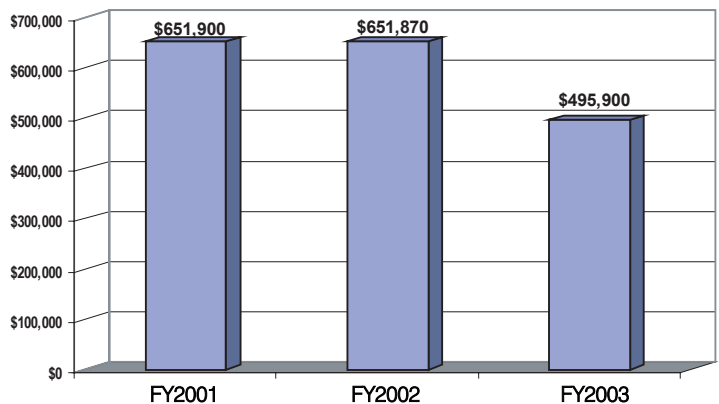
The Board comprises nine voting members and three nonvoting members:

- Three legislators who are nonvoting advisory members and the Superintendent of Public Instruction serve terms concurrent with their terms in office.
- Six members of the public and two members of the business community are appointed by the Governor and serve staggered 4-year terms.

As of May 2003, the Board had six staff, including an executive director, director of government affairs, and various specialists. For fiscal year 2003, the Board was authorized eight FTE.

Program Revenue:

State General Fund Appropriations



¹ The State Board of Education and local school district governing boards are also authorized to sponsor charter schools.

Facilities and equipment:

The Board leases space in the state-owned Executive Tower at 1700 West Washington Street in Phoenix. Its equipment includes typical office equipment such as office furniture and computers.

Mission:

The Board's mission is "to foster accountability in charter schools which will improve student achievement through market choice."

Program goals:

- To sponsor successful charter schools;
- To improve customer service; and
- To provide necessary oversight of sponsored charter schools.

Adequacy of performance measures:

Overall, the measures established by the Board are appropriate and appear to be generally aligned with the Board's goals. While the Board has established several input, output, outcome, efficiency, and quality measures, it should make some improvements to its measures. For example, the Board has established measures to track the number of charter school applications received and approved. However, the Board does not have an efficiency measure to report if applications were processed in a timely manner, or a quality measure to track applicant satisfaction with the charter school application process.

Additionally, the Board should establish measures that track the success of schools in operation. For example, the Board could include outcome measures regarding the number of charters granted to schools that failed within 1, 2, or 3 years; or the number of sponsored schools with a defined percentage of students who meet or exceed Arizona standards on achievement tests.

SUMMARY

The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona State Board for Charter Schools, pursuant to a May 14, 2002, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the Sunset review process prescribed in Arizona Revised Statutes (A.R.S.) §41-2951 et seq.

The Legislature established the State Board for Charter Schools (Board) in 1994. Under Arizona statute, the Board has authority to sponsor charter schools by entering into charter contracts specifying how the school will be operated. The Board is one of three entities authorized to grant charters in Arizona. The Arizona State Board of Education and local school district governing boards may also grant charters. Board responsibilities include evaluating charter school applications and granting charters, monitoring sponsored schools for compliance with applicable laws and charter contract requirements, handling complaints, and providing consumer information to the public. Although there are three sponsoring entities in the State, the Board sponsors over 70 percent of the State's charter schools. As of March 2003, the Board sponsored 329 charter schools serving approximately 54,000 students.

The Board should implement a more systematic monitoring approach (see pages 11 through 18)

The Board should implement a more systematic approach to monitoring charter schools, which would enable it to more effectively oversee the hundreds of schools it regulates. Monitoring charter schools is one of the Board's most critical functions, as it helps ensure that the schools abide by federal and state requirements and effectively educate Arizona's students.

However, the Board lacks a systematic and coordinated approach for monitoring the 329 charter schools it regulates. The Board uses periodic, targeted site visits, and statutorily required 5-year reviews, and partners with the Arizona Department of Education to monitor schools. Through its two types of visits, board staff reviewed a combined 158 charter schools in 2001 and 2002. Yet with 329 schools to monitor, no board staff assigned to conduct site visits full-time, and the estimated 2 to 3 hours it

takes to conduct a site visit, not including staff preparation time and travel time, board staff have not visited several schools. Additionally, when board staff conduct a site visit, staff do not always review and verify compliance with mandated educational requirements that are included in the Board's site visit procedures. Specifically, auditor review of all 87 site visits conducted in 2002 indicates that board staff reviewed charter school compliance with requirements such as fingerprinting and curriculum at fewer than half of the schools visited. Finally, board staff identified problems during 41 of its 87 site visits in 2002, but did not follow up on 31 of the schools to ensure they properly addressed the problems.

The Board has also partnered with the Arizona Department of Education (ADE) to monitor charter schools, but these efforts and associated followup are not well documented. For example, the Board relies on ADE to ensure that board-sponsored charter schools comply with federal and state special education requirements, but the Board's processes for interacting with ADE, documenting charter school compliance with these requirements, and continually being informed of a school's progress in addressing deficiencies are not documented in policy or procedure. Further, the Board works with ADE on compliance with "Arizona Learns" requirements, which implement the federal No Child Left Behind Act. Among other things, schools that are labeled as underperforming must submit a school improvement plan to both ADE and the Board. However, the Board has not established any policies or procedures for accepting improvement plans and following up on their implementation.

The Board should implement a more systematic approach to monitoring charter schools. At its June 2003 meeting, the Board expanded its monitoring efforts by now requiring each charter school's independent auditor to assess, as part of its annual audit of the school, compliance with some special education requirements, fingerprinting, open meeting laws, and some public records law requirements. Previously, the Board attempted to monitor much of this information through routine site visits. However, the Board should adopt administrative rules, and policies and procedures regarding these auditor reviews and their uses, as well as the monitoring partnerships it has with ADE and the use of that compliance information. In addition, the Board should require schools to submit corrective action plans for deficiencies, and board staff should be required to verify that schools have taken corrective action, using site visits where appropriate to follow up.

The Board should continue its efforts to more closely review schools' financial condition (see pages 19 through 27)

While the Board has taken steps to more closely review and monitor charter school finances, it can further enhance these efforts. Both research and the State's

experience with charter schools indicate that financial difficulties are a major reason for charter school closures or failures. In Arizona, 9 board-sponsored charter schools have closed between June 2000 and April 2003 due to financial reasons. Auditors' review of 43 charter school fiscal year 2001 and 19 fiscal year 2002 audited financial statements revealed another 12 schools in operation with financial problems.

To help address these deficiencies, the Board recently strengthened its application requirements and improved its application review process. Specifically, in May 2003, the Board adopted a new application process, which is in effect for charter school applicants for the 2004-05 school year. This new process enhances the requirements for revenue projections and requires applicants to include secured sources of projected revenues within their proposed budgets. Prior to this change, the Board approved applications with uncertain or unsupported projected revenues in their budgets. Additionally, the Board will now require applicants to adequately support its marketing plan by identifying the number of students and market growth in the area. Overestimating student enrollment is one reason that schools experience financial problems, as these estimates serve as the basis for most of an applicant's estimated revenues. Auditor review of 13 applications submitted in fiscal year 2003 identified several applications that did not have adequate support for the projected student enrollment. Finally, the Board enhanced its application review process by incorporating additional guidance for reviewers and revising the scoring. However, the Board still needs to adopt necessary administrative rules, and policies and procedures. The Board also should strengthen its application review committee by including lenders with nonprofit lending experience and educational program experts with school funding experience.

The Board should also further improve its monitoring of operating charter schools' finances. During the audit, the Board began to change its monitoring efforts to focus more resources on monitoring and reviewing the financial solvency of its charter schools. Specifically, the Board has assigned one of its staff to identify and monitor schools experiencing financial difficulties and contracted with a certified public accountant in March 2003 to assist in these efforts. However, in addition to these efforts, the Board should review financial information charter schools already submit to the Arizona Department of Education and require schools to submit corrective action plans detailing steps the school will take to address financial problems. Additionally, if the school's independent auditor identifies financial problems so severe that school closure is possible, to ensure the public is adequately informed, the Board should discuss this information at its meetings and include it in the school's public file.

Board needs additional disciplinary authority (see pages 29 through 34)

The Legislature should consider amending statute to provide the Board a wider range of disciplinary authority to appropriately respond to charter school violations. Currently, the Board is limited to two options: recommending the withholding of 10 percent of a charter school's state funding or revoking a charter. The Board uses the first option far more often than the second. However, these penalties may not be appropriate for some charter school violations. For example, withholding 10 percent of a school's monthly state funding may not be appropriate for minor offenses, such as those that do not affect the education and welfare of students. While the Board has taken action to request the withholding of state funding 55 times in 2001 and 2002 for violations, including school noncompliance with special education requirements and failure to submit annual audited financial statements within statutory time frames, the Board has not taken action against schools for lesser violations. These include failing to maintain teacher resumes on file for public review and failing to document governing board meeting minutes. Additionally, this penalty does not provide enough flexibility to respond adequately to violations that are more serious. As a result, the Board could benefit from additional nondisciplinary and disciplinary options. These options might include authority to issue nondisciplinary letters of concern, and disciplinary options such as requiring charter school operators to take additional training, placing a school on probation, or directing the withholding of any amount of state funding.

Regardless of whether the Legislature grants the Board additional disciplinary authority, the Board should develop administrative rules to govern its disciplinary process. The Board should also establish guidelines to assist it in making consistent and appropriate disciplinary decisions.

Sunset Factors (see pages 35 through 41)

As part of the Sunset review process, this audit makes the following additional recommendations:

- The Board should adopt administrative rules as required by statute to reflect its application, monitoring, disciplinary, and other processes.
- The Board should document its process for investigating and resolving complaints in policy and procedure, and use its accountability database to track complaint receipt, investigation, and resolution.

TABLE OF CONTENTS



Introduction & Background	1
Finding 1: The Board should implement a more systematic monitoring approach	11
Monitoring charter schools important	11
Some monitoring efforts ineffective	12
More systematic monitoring approach would maximize board efforts	16
Recommendations	18
Finding 2: The Board should continue its efforts to more closely review schools' financial condition	19
Children adversely affected when schools close	19
Board has improved application process	20
Oversight of operating school finances needs further improvement	23
Recommendations	27
Finding 3: Board needs additional disciplinary authority	29
Board has limited disciplinary options	29
Expanded options would assist Board	30
Board should adopt administrative rules	33
Recommendations	34
Sunset Factors	35
Agency Response	

• continued



TABLE OF CONTENTS

Figures:

1	Number of Charter Schools by Sponsor As of March 2003	1
2	Revenue Sources for Charter and District Schools for Fiscal Year 2002 (Unaudited)	3
3	Violations for Which the Board Requested That State Funding Be Temporarily Withheld 2001 and 2002	30

Table:

1	Arizona State Board for Charter Schools Schedule of Revenues, Expenditures, and Other Changes in Fund Balance Years Ended or Ending June 30, 2001, 2002, and 2003 (Unaudited)	7
---	---	---

concluded *

INTRODUCTION & BACKGROUND

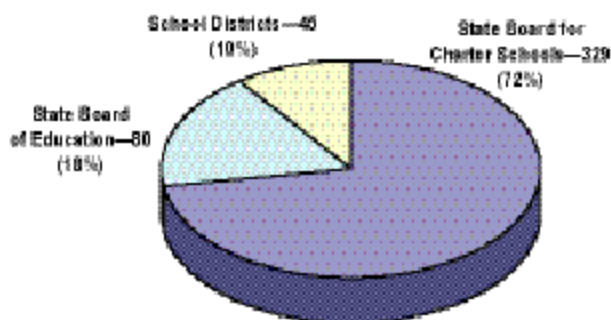
The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona State Board for Charter Schools, pursuant to a May 14, 2002, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the Sunset review process prescribed in Arizona Revised Statutes (A.R.S.) §41-2951 et seq.

Board history

The Legislature established the State Board for Charter Schools (Board) in 1994. Under Arizona statute, the Board has authority to sponsor charter schools by entering into charter contracts specifying how the schools will be operated. Among other things, this action gives the schools eligibility to receive state funding. The Board is one of three entities in Arizona authorized by statute to sponsor charter schools. The other two entities are the State Board of Education and local school district governing boards. However, as illustrated in Figure 1, the Board sponsors and regulates the majority of charter schools in the State. Specifically, as of March 2003, the Board sponsored 329 schools, or 72%

Mission
To foster accountability in charter schools which will improve student achievement through market choice.

Figure 1 Number of Charter Schools by Sponsor
As of March 2003



Source: Auditor General staff analysis of information provided by the Arizona Department of Education.

percent of all charter schools operating in the State, as compared to 125 schools for the two other sponsoring entities.

Charter schools provide alternatives to traditional public schools

Eight percent of Arizona's K-12 students attend charter schools.

Charter schools are public, state-funded schools that offer Arizona's children educational alternatives to traditional public schools. While charter schools only became available to Arizona parents and students in the mid-1990s, they have quickly become a popular and viable educational option. According to Department of Education student enrollment reports, as of October 2002, nearly 74,000 Arizona students attended charter schools. This represents about 8 percent of the over 910,000 students attending K-12 schools in the State. By comparison, the U.S. Department of Education, National Center for Education Statistics reports that slightly more than 1 percent of public school students in the country are enrolled in public charter schools for the 2001-02 school year.¹ Only Washington, D.C. has a larger percentage of its public school students enrolled in charter schools (9.2 percent) than Arizona, but Arizona has more charter schools than any other state.

One reason for charter schools' popularity is the alternatives to traditional public schools that these schools offer. Charter schools are generally smaller, can offer unique programs, and target specific populations. Similarities and differences between charter schools and individual schools within school districts (i.e., district schools) are discussed below:

- **Enrollment**—Charter schools tend to be smaller than district schools. The average enrollment at a charter school for fiscal year 2003 is approximately 160 students, and only 1 of the State's 454 charter schools has more than 1,000 students. In contrast, the average district school had more than 600 students, and 190 of the 1,401 district schools (13.6 percent) had more than 1,000 students in fiscal year 2002.

Similar to district schools, charter schools must enroll all eligible students who submit timely applications. If a charter school has more applications than openings available, it must have an equitable manner for enrolling students, such as a lottery or waiting list. Unlike district schools, however, charter schools recruit and market their schools to prospective students.

- **Funding**—Charter schools have several of the same revenue sources as district schools, including federal and state funding, grants, loans, and donations. Similar to district schools, charter schools receive state funding based on student enrollment and reported attendance. However, charter schools' state

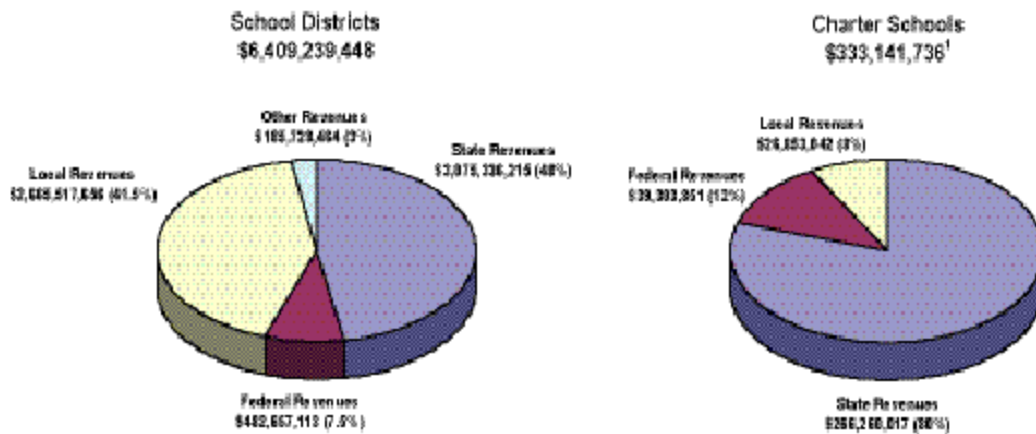
¹ U.S. Department of Education, National Center for Education Statistics. *Overview of Public Elementary and Secondary Schools and Districts: School Year 2001-02*, NCES 2003-411, by Lee McGraw Hoffman. Washington, D.C.: 2003.

funding is based on current year attendance, while district schools' payments are based on the previous year's attendance. Under this funding approach, district schools can plan for and receive consistent payments throughout the school year from the State, whereas charter school payments can fluctuate dramatically, as initial monthly payments are based on estimated student enrollments and later payments on actual enrollments. If a charter school has overestimated enrollment, the Department of Education will adjust the school's monthly state funding to account for the difference and recover any overpayments. Additionally, charter schools do not receive capital funding from the State. As a result, charter schools have to seek their own funding to build or lease school facilities, maintain existing facilities, or bring facilities up to minimum standards.

State funding accounts for the majority of charter school revenues. As illustrated in Figure 2, charter schools received 80 percent of their funding from the State in fiscal year 2002. In contrast, district schools received approximately 48 percent of their funding from the State in fiscal year 2002. The remainder of charter school revenues consisted of federal and local monies, and other revenues, such as grants and donations.

State funding accounts for 80 percent of charter school revenues.

Figure 2 Revenue Sources for Charter and District Schools for Fiscal Year 2002 (Unaudited)



¹ Total also includes Other Revenues totaling \$724,826, which is less than 1 percent.

Source: Fiscal Year 2001-2002 Annual Report for the Arizona Department of Education.

- Organizational structure**—Charter schools are organized and operated in a variety of ways. They must have a governing board, which is similar to a school district governing board, that it is statutorily authorized to make policy decisions

for the school. However, unlike district schools, charter schools can be structured as nonprofit or for-profit corporations, partnerships, or sole proprietorships. Additionally, charter schools are independent public schools and make most operational decisions at the school level. For example, each charter school develops its own policies related to discipline, personnel, and other matters. Conversely, school district governing boards set these types of policies for the multiple schools within their districts.

- **Educational structure**—Although charter schools, like district schools, must meet federal and state educational and academic requirements, every charter school has its own individual mission or vision. As a result, charter school operators can structure these requirements into various educational programs that target specific student populations. For example, one Tempe charter school attracts students who have interest and talent in the arts with an integrated academic and arts program. Other schools offer educational programs that may not be available in district schools, including agricultural or science and technology programs, programs targeted to pregnant or parenting students, or programs targeted for college-bound students.

Charter school requirements

Charter schools must comply with the academic, financial, and general requirements imposed by state and federal law, as well as with the requirements specified in their charter contract. These requirements include:

- **Academic requirements**—All charter schools must align their curricula with Arizona’s academic standards. For example, schools must design a method to measure progress toward the student outcomes adopted by the State Board of Education, participate in Arizona’s Instrument to Measure Standards (AIMS) test at the prescribed grade levels and the nationally standardized achievement tests, and complete the elements required by the annual report card. Schools must provide clear student achievement performance objectives and account for student achievement to the Department of Education.
- **Financial requirements**—Each charter school must submit a detailed business plan, including start-up and operational budgets, with its application. Additionally, in accordance with statute, schools must submit an annual financial report to the Arizona Superintendent of Public Instruction. Further, state laws require charter schools to annually provide audited financial statements to the Board and comply with the Uniform System of

Arizona Department of Education Annual Report Card

Annual report cards provide standard information about each Arizona school to allow comparisons to be made among schools, and show school accomplishments from year to year. Report cards include a school overview, staffing information, student enrollment, transportation policy, school resources and honors, and academic achievement indicators.

Source: Arizona Department of Education.

Financial Records for Charter Schools (USFRCS) or, if exempt, generally accepted accounting principles (GAAP). The Board has granted USFRCS exemptions to most schools it sponsors.

- **General requirements**—Each charter school must comply with its charter contract, as well as all applicable state, federal, and local laws, and regulations. These include laws regarding health, safety, and civil rights, as well as local ordinances related to the quality and location of facilities. In addition, schools must comply with the Individuals with Disabilities Education Act, which mandates that all public schools provide special education services and regulations related to acceptance of federal funding. Further, schools must be nonreligious in their programs, admission policies, and employment practices. Finally, each charter school must submit data to the Department of Education, including annual demographic and ethnicity data, teacher qualifications, and money spent in the classroom.

Board responsibilities

To help assess charter school compliance with these requirements and fulfill its statutory responsibilities, the Board performs the following activities:

- Evaluates applications and grants charters to qualified applicants. While the Board sponsors 329 schools, it actually has approximately 250 charter contracts, as some operators operate multiple school sites. In accordance with statute, the Board grants charters for 15-year terms;
- Monitors schools to help ensure they comply with federal and state laws, and charter contract requirements;
- Disciplines schools that violate statutory or contractual requirements, such as failing to comply with special education or employee fingerprinting requirements;
- Receives complaints from parents, students, charter school faculty, and the public and, depending on the nature of the complaint, investigates and resolves the matter or refers the matter to the proper agency, such as the county attorney or Attorney General; and
- Provides consumer information to the public, school operators, and prospective operators.

The Board annually receives approximately 60 applications for new charters or charter school transfers from the districts or the State Board of Education. In fiscal

year 2003, the Board received 36 applications for new charters and approved 21 of them. In that same year, 14 charter schools applied to transfer their charter to the Board from the other two sponsoring entities. The Board granted charters to all 14 schools.

Organization and staffing

The Board consists of the Superintendent of Public Instruction, eight members appointed by the Governor (six public members and two members of the business community), and three legislators who are nonvoting advisory members. The superintendent and legislative members serve terms concurrent with their terms in office. The other board members serve staggered 4-year terms. The Board elects its president and other officers annually.

For fiscal year 2003, the Board was authorized eight full-time equivalent (FTE) positions. As of May 2003, its staff include an executive director, director of government affairs, and four specialists and support staff. The staff review charter school applications and make recommendations to the Board, monitor charter school compliance with laws and regulations, and provide information to the public.

Budget

The Legislature appropriates monies to the Board from the State General Fund. Table 1 (see page 7) illustrates the Board's actual and estimated revenues and expenditures for fiscal years 2001 through 2003. As shown, the Board received a State General Fund appropriation of \$495,400 in fiscal year 2003. This represented a more than \$150,000 decrease from its appropriation in fiscal year 2002. Additionally, the Board's appropriations have exceeded its expenditures in recent years, allowing it to return over 13.5 percent of its total appropriation to the State General Fund in both fiscal years 2001 and 2002. While the Board's largest expense is personal services and employee-related costs, it has also had a contract with a private firm to review charter school audited financial statements. However, this contract expired in February 2003, and the Board entered into a new contract that redefined the services requested and reduced the Board's contract costs from \$150 to \$65 per hour.

Table 1 Arizona State Board for Charter Schools
 Schedule of Revenues, Expenditures, and Other Changes in Fund Balance
 Years Ended or Ending June 30, 2001, 2002, and 2003
 (Unaudited)

	2001 (Actual)	2002 (Actual)	2003 (Estimated)
Revenues:			
State General Fund appropriations	\$651,900	\$651,116	\$495,400
Sales and charges for services		754	500
Total revenues	<u>\$651,900</u>	<u>\$651,870</u>	<u>\$495,900</u>
Expenditures and other uses:¹			
Personal services and employee related	\$246,627	\$272,754	\$346,800 ²
Professional and outside services	222,611	216,672	73,000 ²
Travel	11,105	7,828	10,000
Food	158	407	
Other operating	65,449	63,697	64,600
Equipment	<u>15,323</u>	<u>2,135</u>	<u>1,000</u>
Total expenditures	561,473	563,493	495,400
Reversion and remittances to the State General Fund	<u>90,427</u>	<u>89,337</u>	<u>500</u>
Total expenditures and other uses	<u>\$651,900</u>	<u>\$651,870</u>	<u>\$495,900</u>

¹ Includes the prior year's administrative adjustments.

² In 2003, the Board created a new position to provide additional charter school monitoring; consequently, the amount increased.

³ In 2003, the Board's expenditures decreased significantly because it spent less for a parent survey and certified public accountant services.

Source: Auditor General analysis of the Arizona Financial Information System Revenues and Expenditures by Fund, Program, Organization, and Object; Status of Appropriations and Expenditures; and Total Balances by Fund reports for the years ended June 30, 2001 and 2002, and financial information provided by the Board for the year ending June 30, 2003.

Scope and methodology

This audit focused on the Board's review of charter schools through its application and monitoring processes, oversight of schools including its review of charter school finances, and enforcement authority. This audit and Sunset review includes the following findings and associated recommendations:

- The Board should implement a more systematic approach to monitoring charter schools by coordinating its many monitoring efforts and adequately following up on identified problems.

- While the Board has improved its oversight of charter school financial operations, it should take additional steps in this area, including further enhancing its review of finances at existing schools.
- The Legislature should consider expanding the number of disciplinary options available to the Board, which would give the Board more flexibility to appropriately discipline charter schools.

In addition, within the Sunset Factors (see pages 35 through 41), the report recommends that the Board adopt administrative rules as required by law to reflect its application, monitoring, and disciplinary processes; and document its process for investigating and resolving complaints in policy and procedure, and use its accountability database to track complaint receipt, investigation, and resolution.

Auditors used a variety of methods to study the issues addressed in the audit. They attended eight board meetings and the Arizona Department of Education's "Arizona School Improvement Plan Orientation Workshops"; interviewed 5 of the 12 board members, management, and staff; reviewed board meeting minutes from January 2001 through March 2003; and reviewed applicable statutes, policies, and procedures. To perform more specific audit steps, they used the following methods:

- To evaluate the Board's charter school oversight and monitoring practices, auditors reviewed all 87 site visit reports for 2002, 42 of the Board's charter school public files, the Board's compliance records and its site visit checklist, and its accountability database. Additionally, auditors reviewed several studies regarding charter school accountability and monitoring, including three conducted by research organizations at the national level.¹
- To determine whether the Board adequately reviews and oversees charter school finances and financial operations, auditors reviewed and analyzed 43 fiscal year 2001 charter school audited financial statements, which consisted of a random sample of 30 and a risk-based sample of 13 financial statements, and 19 fiscal year 2002 charter school audited financial statements, reviewed the Board's contract for the review of charter school audits, interviewed a certified public accountant employed by the contractor who reviews school audits, and reviewed the fiscal year 2001 report of findings prepared by the contractor. In addition, auditors reviewed 8 charter school applications submitted during fiscal year 2003 and 5 applications submitted in fiscal year 2002, observed 3 application review meetings, and contacted 6 charter school authorizers in other states and the State Board of Education regarding their charter school

¹ Public Impact. *Charter School Accountability: A Guide to Issues and Options for Charter Authorizers*. Charlotte, N.C.:2000.

Hill, Paul T., Robin J. Lake, and Mary Beth Celio. *Charter Schools and Accountability in Public Education*. Washington, D.C.: Brookings Institution Press, 2002.

SRI International. *A Decade of Public Charter Schools*. Washington, D.C.: November 2002.

application and monitoring processes.¹ Finally, auditors reviewed two studies and one publication related to charter schools and charter school closures.²

- To analyze the disciplinary options available to the Board and how the Board has used these options, auditors reviewed all disciplinary actions taken by the Board in 2001 and 2002 and all 18 charter revocation actions initiated by the Board from 1996 through January 2003. Further, auditors reviewed four charter school settlement agreements resulting from revocation proceedings and attended two disciplinary board hearings held in September and November 2002. Finally, auditors reviewed the North Carolina State Board of Education and Washington, D.C., Public Charter School Board disciplinary authority, and policies and procedures.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the State Board for Charter Schools, its executive director, and staff for their cooperation and assistance throughout the audit.

¹ Auditors contacted the following six charter school authorizers because literature and a board manager identified them as authorizers either employing best practices or having similar operations to the Arizona State Board for Charter Schools: City of Chicago, Massachusetts, Minnesota, North Carolina, Texas, and Washington, D.C.

² Bowman, Darcia Harris. Charter Closings Come Under Scrutiny. *Education Week*, Feb. 28, 2001.

SouthEastern Regional Vision for Education. *The Charter School Review Process: A Guide for Chartering Entities*, March 1998.

The Center for Education Reform. *Charter School Closures: The Opportunity for Accountability*; Washington D.C., October 2002.

FINDING 1

The Board should implement a more systematic monitoring approach

The Board should implement a more systematic approach for monitoring charter schools, which would enable it to more effectively oversee the schools it regulates. The Board needs to actively monitor the schools it charters to help ensure they comply with statutory and charter contract requirements. However, the Board lacks a systematic and coordinated monitoring approach for the hundreds of schools it oversees. Its current approach, which uses site visits and other monitoring tools, is ineffective because some schools may not be visited, the reviews that do occur are often incomplete, and followup on identified problems is inadequate. Monitoring could be more effective and systematic if the Board adopted a coordinated monitoring approach and consistent followup to correct noncompliance.

Monitoring charter schools important

Monitoring charter schools is one of the most critical functions that the Board can perform, as it helps to ensure that the schools abide by federal and state requirements and effectively educate Arizona's students. According to a study commissioned by the Annie E. Casey Foundation, a national nonprofit organization that supports projects aimed at improving public education, providing ongoing oversight gives sponsors tools to close ineffective schools, and creates incentives for charter schools to improve.¹ Additionally, a Brookings Institution study notes that "Authorizers need to take their responsibilities toward charters seriously, which requires creating routines for monitoring and assessing schools... and providing ongoing assessments of schools. Authorizers must fulfill their public duties to ensure that charter schools are held accountable for performance and to protect students from failing schools."² Finally, the popularity of charter schools in Arizona is growing, with an enrollment of nearly 74,000 students as of fiscal year 2003 according to

Charter schools must be held accountable.

¹ Public Impact. *Charter School Accountability: A Guide to Issues and Options for Charter Authorizers*. Charlotte, N.C.:2000.

² Hill, Paul T., Robin J. Lake, and Mary Beth Celio, *Charter Schools and Accountability in Public Education*, Washington, D.C., Brookings Institution Press, 2002.

Arizona Department of Education (ADE) student enrollment reports, as compared to a student enrollment of fewer than 50,000 in fiscal year 2000, making it even more important to ensure that charter schools comply with federal and state educational requirements.

According to A.R.S. §§15-182(E)(1) and 15-183(R), the Board must exercise general supervision, oversight, and administrative responsibility over the schools it sponsors. Therefore, the Board is responsible for monitoring charter school compliance with statutory and charter requirements, including:

- **Fingerprinting**—Charter schools must ensure that all persons engaged in instructional work directly as a classroom, laboratory, or other teacher or indirectly as a supervisory teacher, speech therapist, or principal have a valid class 1 or 2 fingerprint clearance card. Charter school operators must also be fingerprinted.
- **Special Education**—Charter schools must make special education services available to their students, identify students who may need these services, evaluate student needs, and design and implement an individualized program to assist these students.
- **Public Records**—Charter schools must document governing board meeting minutes, comply with open meeting laws, and have a governing body responsible for making the school's policy decisions. Likewise, charter schools must have resumes available for public review in order to document each teacher's educational and teaching background and experience in a particular academic area.
- **Arizona Curriculum Standards**—Charter schools' administrators and principals must annually declare to the Board that their adopted curriculum is aligned with Arizona standards.
- **Annual Financial Report**—Charter schools must provide ADE with an annual summary of their financial activity, including beginning and ending balances, revenues and expenses, and budget-to-actual comparisons of expenses for the fiscal year.

Some monitoring efforts ineffective

Despite statutory responsibility for charter school oversight, some of the Board's monitoring efforts do not allow it to effectively monitor the hundreds of schools it regulates. For example, the Board uses on-site visits to monitor schools, but board staff have not visited all of the schools the Board regulates, nor were the site visits

staff conducted thorough. Additionally, the Board has not adequately followed up on deficiencies during its site visits. Further, while the Board conducts other monitoring efforts by partnering with ADE, these efforts and associated followup are not well documented.

Effectiveness of site visits as a monitoring tool has been limited—

Even though site visits can be useful for monitoring certain areas at charter schools, such as student counts, resource constraints and a lack of thoroughness limit the effectiveness of the Board's use of site visits. Board staff conduct two types of visits:

- **Site visits**—Each year, board staff conduct site visits at a number of schools. According to the Board's executive director, the Board targets new schools in their first year of operation or schools where a problem was brought to the Board's attention.¹ For example, board staff may conduct site visits at schools that have a pattern of parent complaints or receive negative media attention. Based on the Board's site visit procedures, site visits should focus on charter school compliance with statutory and contractual requirements, such as fingerprinting, student counts, and staffing numbers and qualifications. If these site visits identify problems, the Board reports that it requires schools to take corrective action. In 2002, board staff conducted compliance site visits at 87 schools, while in 2001, board staff conducted site visits at 40 schools.
- **Five-year reviews**—Additionally, A.R.S. §15-183(l) requires the Board to conduct 5-year reviews of all the schools it sponsors. While board staff visit schools to conduct these reviews, according to the Board's executive director, these reviews do not assess school compliance with statute and charter requirements, but instead focus on the school's mission and goals, as well as developing trend information, such as public demand for charter schools and the number of schools that conduct strategic planning. Board staff conducted 3 of these reviews in 2002 and another 36 reviews in 2001.

However, the effectiveness of site visits as a monitoring tool has been limited for two reasons:

- **Board lacks resources to visit all schools**—The Board does not have the necessary staff resources to conduct site visits at all of the 329 charter schools it sponsors. The Board has six staff available to conduct site visits in addition to their other responsibilities, but has not assigned any of its staff to conduct site visits full-time. Additionally, while site visits take an estimated 2 to 3 hours to conduct, not including travel time, the actual time to conduct a site visit varies depending on the staff preparation time for the visit, the school's location and associated travel time (51 percent of the charter schools the Board sponsors are outside of the Phoenix metropolitan area), the type of visit, and the number of reviewers. As a result, although the Board reports that it targets its visits to those

¹ The Board will also visit schools for open houses, graduations, and special presentations, and if a school is in close proximity to another school targeted for a visit.

schools where it believes monitoring is needed most, some schools with problems may go unmonitored.

- **Site visits lack thoroughness**—When board staff conduct a site visit at a school, staff do not always review and verify compliance with mandated educational requirements that are included in the Board’s site visit procedures. For example, based on auditor review of the 87 visits conducted in 2002, board staff reviewed charter school compliance with fingerprinting requirements in only 37 percent (31 of 87) of the visits, compliance with public access to teacher’s education and teaching background information in only 38 percent (33 of 87) of the visits, and compliance with curriculum requirements in only 34 percent (30 of 87) of the visits.

While the Board has developed site visit procedures to direct staff during these reviews, auditor review of the 87 visits found that staff inconsistently followed the procedures and inadequately documented the scope of their reviews. Additionally, the procedures do not provide adequate direction to staff, including direction on the items to review to verify compliance with critical areas such as fingerprinting, and does not direct board staff to evaluate several important areas. For example, it does not direct staff to review school policies and procedures for administering standardized tests.

Board staff do not always follow up on identified problems—In 2002, board staff identified problems during 41 of 87 site visits. These issues included missing fingerprint documentation, missing governing board meeting minutes that would demonstrate compliance with open meeting laws, and missing teacher qualification information. Although the Board does not have specific guidance about how the follow-up process should be conducted, including formally notifying schools of identified problems, it does maintain site visit reports indicating that when staff find infractions or cannot verify compliance with requirements, additional information should be requested or a follow-up visit conducted. However, auditors’ review of the Board’s files found that staff did not follow up on 31 of the 41 visits where problems were noted. For example:

- **Compliance information unavailable**—During a 2002 site visit to a Phoenix charter school, board staff could not review the school’s compliance with fingerprinting laws, and public records and open meeting requirements. Documentation needed to adequately review these areas, such as fingerprint clearance cards, teacher resumes, and governing board meeting minutes, was not available at the school. However, neither the Board’s site visit report nor the school’s public files indicate that board staff followed up on this missing documentation and obtained it for review.

Board did not follow up on 76 percent of site visits identifying problems.

Additional monitoring efforts not well documented—In addition to conducting site visits, the Board conducts other monitoring efforts, including partnering with ADE to monitor charter school compliance with special education, school achievement, and school finance requirements. However, while it appears appropriate for the Board to work with ADE to monitor charter schools, the Board lacks documented processes and policies and procedures for doing so, including any related to followup. For example:

- **Special education**—According to the Board’s executive director, the Board relies on ADE’s Exceptional Student Services (ESS) unit to help ensure that board-sponsored charter schools comply with state and federal special education requirements. ESS assigns each charter school a specialist who generally visits the school at least twice each year to provide information and receive feedback. ESS conducts monitoring visits once every 6 years, unless a charter school fails to submit its special education policies and procedures on time. Additionally, ESS assigns each school a mentor who provides up to 12 free hours of technical assistance and reports the status of each school’s special education program to ESS. Further, ESS investigates all parent complaints regarding special education. According to the director of this unit, the Board is copied on all correspondence between ESS and charter schools, including monitoring results, complaints, and corrective action plans. In addition, when ESS determines that a charter school is severely noncompliant with special education requirements, it informally notifies the Board via a meeting or telephone call. However, the Board’s processes for interacting with this unit and documenting charter school compliance with special education requirements is not documented in policy or procedure. Further, the Board does not have any procedures in place to ensure that it is continually notified of a school’s progress in implementing a corrective action plan or addressing the issue.
- **School achievement**—According to the Board’s executive director, the Board works with ADE on statutorily mandated compliance with the “Arizona Learns” requirements, which implement the federal No Child Left Behind Act. Specifically, A.R.S. §15-241 requires ADE to compile an annual achievement profile for each school, including scores for Arizona’s Instrument to Measure Standards (AIMS) test, graduation rates, dropout rates, and data to determine if schools are making adequate yearly progress. Schools are required to provide the data necessary to compile the achievement profile to ADE. Charter schools labeled as “underperforming” by ADE must submit a school improvement plan to both the Superintendent of Public Instruction and the Board, as well as notify parents of the designation and the public hearing at which the improvement plan will be presented. In response to the schools initially labeled as underperforming, the Board held a public meeting in February 2003, during which 26 schools submitted improvement plans. Schools that are underperforming for a second consecutive year are designated as “failing.” A.R.S. §15-241(R) requires the Board to take action to restore failing charter

schools to acceptable performance or revoke the charter. However, the Board has not established any processes or policies and procedures for accepting improvement plans and following up on their implementation. Additionally, according to the Board's executive director, the Board does not verify that schools are sending the required letters to parents.

- **School finance**—Based on a review of meeting agendas, the Board meets biweekly with staff from ADE's School Finance Division. Meetings have a standard agenda to discuss and review a variety of school finance and charter school issues, such as student count estimates and problems, school payment issues, and mid-year closings. However, the Board has no policies detailing how to follow up on information obtained at these meetings.

More systematic monitoring approach would maximize board efforts

The Board can maximize its limited resources and monitoring efforts by implementing a more systematic monitoring approach. The Board recently adopted a new requirement that will provide it with additional monitoring information beyond what it receives from ADE. To guide its monitoring approach, the Board should adopt needed administrative rules, and policies and procedures. Additionally, board staff should consistently follow up on deficiencies identified through its monitoring efforts and conduct site visits only if warranted by the lack of school progress in addressing identified deficiencies. Finally, to assist with its follow-up efforts, the Board should better use its existing accountability database.

Recent change will provide more monitoring information—In addition to the information the Board receives from ADE, the Board will soon begin to receive additional monitoring information. At its June 2003 board meeting, the Board adopted a legal compliance questionnaire that will require each school's independent auditor to assess charter school compliance with some special education requirements, fingerprinting and open meeting laws, and some public records law requirements. The auditors will be required to assess school compliance in these areas beginning with the fiscal year 2003 audits. This information, which the Board has previously sought to monitor using site visits, will assist the Board in monitoring school compliance with these requirements.

Administrative rules, and policies and procedures, needed to guide monitoring approach—To ensure its monitoring approach is systematic and comprehensive, the Board should reflect the various partnering relationships it maintains with ADE to monitor charter schools in administrative rules, and policies and procedures. At a minimum, the policies should provide a description of each

agency's monitoring responsibilities, specific guidelines for the Board's interactions with ADE, and procedures for documenting information provided by ADE. Further, the Board should establish policies and procedures for how it will use and track the information provided by ADE. Finally, the Board should adopt rules, and policies and procedures, reflecting its use of the newly adopted legal compliance questionnaire.

Adequate followup needed—To help ensure that schools address deficiencies identified through its monitoring efforts, the Board should adequately follow up on charter school actions to correct the deficiencies. The Board should establish administrative rules, and supporting policies and procedures, that specifically detail its follow-up process, including the steps schools must take to address deficiencies and the steps staff must follow when conducting follow-up activities. For example, the Board's rules and policies should require board staff to formally notify schools of identified deficiencies, require schools to submit corrective action plans noting how deficiencies will be addressed and the time frames for doing so, and require board staff to verify that schools have taken corrective action. Board rules and policies should also include guidelines for addressing schools that do not correct deficiencies in a timely manner, such as specifying the conditions under which the Board will pursue disciplinary action.

Finally, because much of the information previously monitored through site visits will now be monitored by the school's independent auditors, the Board should redirect its use of site visits from routine monitoring to followup. For example, if a school has not implemented corrective actions in a timely manner or if there is a need to verify the corrective action taken through a site visit, the Board could direct its staff to conduct such a visit. Using the site visits for these purposes would maximize the use of the Board's limited resources.

Site visits more effectively used as a follow-up tool.

Integrate database information to maximize monitoring—Finally, to assist with its follow-up efforts, the Board should better use its existing accountability database. While the Board uses this database on a limited basis, the database could make it easier for the Board to document the results of site visits and follow-up efforts. The database already contains the majority of the areas the Board is responsible for monitoring, such as compliance with special education and standardized testing requirements; however, the Board should modify it to reflect all areas of the Board's responsibility. For example, the Board should add data fields for compliance with fingerprinting and Arizona curriculum standards. The Board would also need to address problems with missing and/or out-of-date information related to statutory and charter compliance. For example, the database has no data regarding which schools submitted scores for the spring 2002 AIMS or Stanford 9 tests. To ensure that the Board maximizes the use of this database, it should establish policies and procedures that direct staff on the database's use, including entering data from ADE's monitoring efforts, follow-up efforts, and other relevant information sources. Additionally, the Board should provide training to its staff on how to integrate the database into their monitoring and follow-up efforts.

Recommendations

1. The Board should develop a systematic monitoring approach that is established in administrative rules, and policies and procedures. This approach should include:
 - a. Descriptions of the Board's and ADE's monitoring responsibilities; specific guidelines for the Board's interactions with ADE; documentation requirements for the Board's ongoing information exchanges with ADE; and requirements for the use of and tracking of information provided by ADE; and
 - b. Descriptions of and uses for any other monitoring method it uses, including the legal compliance questionnaire.
2. The Board should develop and implement administrative rules, and supporting policies and procedures, to govern its follow-up process. This process should include guidelines for:
 - a. Formally notifying schools of identified deficiencies;
 - b. Charter schools to submit corrective action plans identifying planned actions that will address deficiencies;
 - c. Time lines for submitting the corrective action plans;
 - d. Board staff to verify that schools have taken corrective action; and
 - e. Increasing its follow-up efforts by making greater use of site visits for followup rather than for routine monitoring.
3. The Board should effectively use its existing accountability database by establishing policies and procedures that direct staff on its use, including entering data from its document reviews and follow-up efforts.
4. The Board should train its staff how to use the accountability database and how the database can assist staff in their monitoring and follow-up efforts.

FINDING 2

The Board should continue its efforts to more closely review schools' financial condition

While the Board has taken steps to more closely review charter school applications and monitor charter school finances in an effort to help schools address financial problems, it can further enhance these efforts. Nine schools have closed since June 2001 due to financial insolvency, and a review of charter school fiscal year 2001 and fiscal year 2002 audited financial statements revealed continuing financial problems at several schools. To help address these concerns, the Board strengthened the financial requirements for charter school applicants in May 2003 and plans to enhance its review of charter school applicants' financial components. Additionally, while the Board has focused more resources on monitoring and reviewing the financial solvency of its charter schools in response to concerns raised during the audit, it can take further action to improve its monitoring of charter school finances.

Children adversely affected when schools close

Charter school closures are often due to financial difficulties, creating educational upheaval for parents and students. Viable financial plans and successful financial management of charter schools are key factors in opening and operating a charter school. In many respects, a charter school's financial operations are as important as its educational operations. According to a study conducted for the U.S. Department of Education by SRI International, an independent nonprofit research institute, financial weakness is one of the most important factors in the decision to reject a charter school application.¹ Additionally, *Education Week*, a newspaper published by a Washington, D.C. nonprofit organization that helps raise awareness and understanding of American educational issues, reported that financial problems are a major reason for charter school closures or failures.²

¹ *A Decade of Public Charter Schools*, SRI International, November 2002.

² Bowman, Darcia Harris. Charter Closings Come Under Scrutiny. *Education Week*, Feb. 28, 2001.

Charter school closures disrupt student education.

Since June 2001, nine Arizona charter schools closed due to financial problems.

When charter schools close, student education can be disrupted. Parents must find appropriate new schools for their children and student records may be difficult to obtain. Additionally, relocating students can be time- and resource-intensive, especially for parents of children with special needs or students who have not been successful in traditional public schools. Moreover, closed schools may not fulfill their legal obligations after closing. In one instance, an Arizona student was unable to obtain her official transcripts from a charter school that had closed and, as a result, a college scholarship was jeopardized because she was unable to provide proof of her academic credits. An Arizona Department of Education official wrote to the college to explain why the student's records were unavailable. Additionally, the official reported that she wrote similar letters to military recruiters on behalf of students who had attended the same school and wanted to enter the armed services.

In Arizona, financial difficulties resulting from a lack of student enrollment, mismanagement, and other reasons have affected board-sponsored charter schools. Specifically, 9 of the 13 schools that closed between June 2001 and April 2003 did so because of financial insolvency, and two of these schools closed after operating for less than 1 year. According to Department of Education student enrollment reports, the 9 closings displaced over 950 students.

Board has improved application process

To help reduce the potential for school closures due to financial problems, the Board recently strengthened its application requirements and improved its application review process. Prior to this change, while the Board required charter applicants to submit budget and financial information, the requested information often did not adequately address critical revenue sources. In addition, the Board's application review process lacked the necessary guidance to properly review and evaluate a charter applicant's financial information.

Stricter financial requirements now required for applicants—The Board has initiated changes to its application process to strengthen the financial requirements for applicants to qualify for a charter, but some additional improvements would be beneficial. To satisfy board application requirements for financial and budget information, charter school applicants must submit a business plan that includes both start-up and operational budgets. The start-up budget should reflect the applicant's projected revenues and expenditures for the first 12 months prior to opening, usually from the time the charter is granted by the Board to the first state funding payment, and the assumptions that support these projections. The first state funding payment is then made in July of the year the school opens. The operational budget should contain the applicant's projected revenues and expenditures for its first 3 years of operation after opening. However, the financial

information submitted in some budgets has been unrealistic or supported by invalid assumptions. Specifically,

- **Projected revenues were not always adequately supported**—The Board has approved some applications and granted charters without critically examining the sources of the applicant’s revenue or the likelihood of its receipt. These projected revenues have included grants not yet awarded, unapproved loans, and donations that have not yet been received. However, in some cases, applicants have not supported the realistic expectation of these revenues, either in their application or in testimony before the Board, and these revenues have comprised more than half of the projected revenues. For example, in an application approved in February 2003, a charter school projected a start-up budget of no more than \$50,000 with monies available from private sources, but provided no additional information or support for these monies. In another application approved in January 2003, a school included \$200,000 in donations and a \$1.57 million small business loan as revenue, constituting over 92 percent of its start-up budget, without providing any information on the source of the donations and their likely receipt, and the loan’s likely approval. Additionally, the Board approved a school’s application that included federal educational grants of \$165,000 in its first-year revenue projections, even though the school was ineligible for the grants because of its for-profit tax status. Finally, while the Board reports that it has required applicants to present realistic alternatives for funding in the event that the primary sources of projected revenues are not realized in verbal testimony before the Board, the Board has not required documentation of alternative funding sources in the application.
- **Enrollment estimates were not always supported**—Student enrollment estimates serve as the basis for most of an applicant’s estimated revenues. However, the operational budgets applicants submitted did not consistently contain enrollment estimates based on adequate research data. While the Board required charter school applicants to submit a marketing plan that supported enrollment estimates, it had no requirements for what the plan must contain and did not provide direction to applicants regarding how to adequately support student enrollment projections. Based on a review of 13 applications submitted in fiscal year 2003, auditors identified two applications that adequately detailed proposed marketing plans and how the plans would lead to the estimated student enrollment. One applicant’s plan included information on the demographics of the surrounding neighborhood, surveys of existing schools, and projections of homes with children in the area, and identified potential students for the school.

However, a review of the other 11 applications found that, more typically, schools provided information on their planned advertising and promotion efforts, but did not adequately support how these efforts will yield the projected student enrollment. As a result, some charter school operators have overestimated their

Board will begin to consider only revenues for which receipt has been guaranteed.

projected enrollment, upon which estimated state funding payment revenue is based. Additionally, since charter schools receive approximately 80 percent of their funding from the State, overestimating student enrollment can severely impact school budgets, planning, and estimated revenues.

To address many of these deficiencies, the Board recently changed the application requirements for charter school applicants. Specifically, at its May 2003 board meeting, the Board adopted application requirements that require start-up budgets to include only revenues for which receipt has been guaranteed. In addition, applicants' projected revenues cannot include grants or federal stimulus monies awarded by the U.S. Department of Education for the design and initial implementation of charter schools. Additionally, the Board will now evaluate applicants' marketing plans with respect to the number of potential students and growth in the target area, how parents will be attracted to the school, and implementation costs. These factors will enable the Board to better evaluate applicants' enrollment estimates. These changes will go into effect for applicants applying to open charter schools for the 2004-05 school year. However, even with these changes, the Board's application requirements and process are not supported by administrative rules, or policies and procedures. Therefore, the Board should codify its revised application process in administrative rules, and also adopt necessary policies and procedures to support its process.

Board improved application review process—The Board has also changed its application review process to incorporate some needed guidance to appropriately evaluate a charter applicant's financial information, but the review committee's composition should be strengthened. Prior to this change, the Board used a review tool to assist in reviewing and scoring applications that did not provide clear guidance or examples on how to evaluate and score an applicant's financial information. For example, the review tool asked raters to score financial information on a scale of zero to three, but did not explain the criteria for ranking an application at any of these levels. In addition, the review tool did not provide any criteria or examples of acceptable financial documentation, or acceptable support and assumptions for the financial information, including the projected budgets, submitted by the charter school applicant.

However, in May 2003, the Board adopted a new application review process that evaluates applicants' business plans and operating budgets in detail, including the marketing, management, and financial plans. For example, factors the Board considers to determine the adequacy of the marketing plan include determining if the applicant has identified the number of students and the market growth in the school's target area. Additionally, the Board reviews the corporate principals, organizational structure, governing board structure and composition, and personnel duties and qualifications in the applicant's management plan. Finally, the Board will evaluate start-up and operating budgets reviewing numerous items including policies and

procedures, timelines for acquiring supplies and equipment necessary to operate the school, budget assumptions, and other materials that indicate whether the school will be able to sustain itself.

The Board also revised its scoring criteria from a numeric zero-to-three scale to a descriptive range that includes “falls below the expectation,” “approaches the expectation,” “meets the expectation,” and “exceeds the expectation.” The criteria defines each expectation category and details items to score under each requirement; however, the Board still needs to codify the new process in administrative rules and policies.

In addition, the Board should strengthen the composition of its application review committees to include experts, such as lenders with nonprofit lending experience and educational program experts with school funding experience. Currently, the Board uses a peer review committee and in-house staff to review applications. While the peer reviewers have experience as charter school operators, they do not have specific expertise in lending, financing, and accounting to evaluate the financial documents and make expert assessments about the school’s financial viability.

Application review committees should include lending and school funding experts.

In contrast, the State Board of Education has promulgated rules that specify the qualifications and requirements for individuals serving on its review committee. For example, the State Board of Education’s rules require that the review committee consist of an individual knowledgeable in finance, accounting, and generally accepted accounting principles. Additionally, a study by the SouthEastern Regional Vision for Education (SERVE), a nonprofit educational organization that promotes the improvement of educational opportunities in the Southeastern United States, advocates having professionals from various disciplines, including experts in finance and representatives from community development financial institutions, to help review charter school applications.¹

Oversight of operating school finances needs further improvement

The Board should also more strongly monitor the finances of charter schools that are already operating. Auditors’ review of audited financial statements for 43 charter schools identified several operating schools with financial problems. Once auditors brought these problems to the Board’s attention, it began to enhance its oversight of charter school finances, but needs to do more. Specifically, the Board should increase its review of available financial information, focus its monitoring efforts on fiscally unstable schools, and require schools with financial problems to take corrective action.

¹ SouthEastern Regional Vision for Education. *The Charter School Review Process: A Guide for Chartering Entities*, March 1998.

Several schools have continuing financial problems—Auditors reviewed 43 charter schools' fiscal year 2001 financial statements audited by public accounting firms, and found evidence that 21 of the schools were experiencing financial difficulties. Eleven of these 21 schools had deficits resulting from liabilities in excess of assets. In four instances, the deficits were serious enough that the school's external auditor questioned the school's ability to continue operating. These deficits ranged from \$8,600 to nearly \$500,000. Ten of the 21 schools did not have sufficient cash or other readily available resources to satisfy obligations due within the next year.

To determine if any of the 21 schools continue to experience financial difficulties, auditors also reviewed the available fiscal year 2002 audited financial statements. Based on a review of the fiscal year 2002 statements, 12 of the 21 schools continue to have financial problems, including 6 with deficits resulting from liabilities in excess of assets. Seven of the 21 schools appear to have improved their financial situation, while 1 school closed because the Board revoked the school's charter.¹ One charter school had not submitted its fiscal year 2002 audited financial statements as of May 1, 2003, even though they were due on March 31, 2003.

Several schools have operating deficits.

Board changed focus of monitoring efforts—During the audit, the Board took some steps to improve its oversight of charter school financial solvency. Historically, the Board's financial oversight of charter school finances focused on whether charter schools' annual financial statements and audits complied with Generally Accepted Accounting Practices (GAAP) and Generally Accepted Auditing Standards (GAAS). The Board had retained a contractor to review each school's audited financial statements for compliance with GAAP and GAAS and to produce a report of the external auditor's findings from the audited financial statements for the Board's use. However, this contract did not require a review of the audited statements for solvency or financial weaknesses, nor did the Board consistently follow up on the report of findings.

In response to these problems, the Board has begun to change its monitoring approach. One step the Board took was to change the requirements of an existing staff position to identify and monitor schools experiencing financial difficulties. Specifically, with this staff position, the Board has begun to create a database of the 2001 charter school audited financial statements in an effort to identify financial trends and indicators of financially troubled schools. According to the executive director, board staff will also follow up on the findings reported in the school's annual audits, require schools to take corrective actions to address financial problems, and conduct financial assessments of financially at-risk schools.

A second step involved retaining the services of a certified public accountant (CPA) in March 2003, to help monitor the financial operations of charter schools and review school audits for solvency or other financial weaknesses. According to the contract, the CPA will help to follow up on any findings in the audits, train the Board's staff on

¹ The Board revoked this school's charter for its failure to give the AIMS test and submit its fiscal year 2001 audited financial statements in a timely manner.

reviewing financial information submitted by schools, and conduct a desk review of a sample of the charter school audited financial statements to determine compliance with financial requirements and evaluate operational stability.

Board has begun to monitor charter school finances.

Additional actions can further strengthen oversight—The Board can take additional steps to strengthen its oversight of school finances. These steps include:

- **Reviewing financial information charter schools already submit to the Arizona Department of Education (ADE)**—According to statute, charter schools must submit information required by the annual financial report to the ADE by October 15 of each year. This information includes beginning and ending balances, revenues and expenses, and budget-to-actual expenses for the prior fiscal year. The annual financial report presents condensed financial activity of charter schools for comparison purposes and includes information that can assist sponsors, school governing boards, ADE, legislators, and taxpayers in determining whether charter schools are meeting their stewardship responsibilities. The Board should review this information annually.

Other charter school authorizers also use financial reporting as a means of identifying fiscally unstable schools, as well as for closely monitoring schools with financial problems. For example, the Massachusetts Department of Education requires its schools to annually submit financial statements for the prior year and projections of income and expenses for the upcoming school year in order to examine differences between the projected year's budget and the previous year's actual performance. This practice helps identify financially troubled schools and triggers additional monitoring. Additionally, the Chicago Public Schools and the District of Columbia Public Charter School Board require that charter schools provide these authorizers with copies of their annual budgets and cash flow projections for each fiscal year.¹ Finally, the D.C. Board expects the schools it sponsors to provide it with interim financial statements.

- **Requiring schools to take corrective action to address financial problems**—For those schools with financial problems, the Board should require that these schools submit corrective action plans detailing steps the school will take to address the financial problems. Board staff should then review these corrective action plans and monitor school progress in implementing the plans. In addition, if the school's independent auditor identifies financial problems so severe that school closure is possible, to ensure the public is adequately informed, the Board should discuss these schools at its meetings and include this information in the school's public file. At least one other charter school authorizer does something similar. The North Carolina State Board of Education's Charter School Advisory Committee receives a "watch list" that contains schools having financial problems and they discuss this list at their meetings. The Board also

¹ Chicago public schools require that schools annually submit quarterly cash flow projections.

could consider publishing a list of schools experiencing financial problems on its Web site.

- **Developing needed administrative rules, and supporting policies and procedures regarding its fiscal oversight practices**—Currently, the Board lacks any guidance regarding its oversight practices for charter school finances. The Board should adopt needed administrative rules and generate policies and procedures that specify the type of financial information and documentation it should review and the frequency of reviews. Likewise, policies and procedures should also contain guidelines for following up on findings or concerns noted by board staff and schools' external auditors and ensuring that schools take corrective actions. These guidelines should be similar to the follow-up process and guidelines recommended in Finding I (see pages 11 through 18).

Recommendations

1. The Board should codify its application process by establishing necessary administrative rules, and supporting policies and procedures.
2. The Board should improve the review of financial information provided in charter school applications by:
 - a. Establishing necessary administrative rules, and supporting policies and procedures for the review and scoring of financial information in the charter school application; and
 - b. Restructuring the application review committee to include lenders with nonprofit lending experience and educational program experts with school funding experience.
3. The Board should improve its oversight efforts of operating schools by:
 - a. Annually reviewing the financial information submitted to the Arizona Department of Education as part of the annual financial report;
 - b. Requiring schools with financial problems to submit corrective action plans detailing steps the school will take to address the problems and monitoring school progress in implementing the plans;
 - c. Identifying at board meetings and in its public files schools whose independent auditor has found financial problems so severe that closure is possible; and
 - d. Developing necessary administrative rules, and supporting policies and procedures, to guide its financial oversight practices.

FINDING 3

Board needs additional disciplinary authority

The Legislature should consider amending statute to provide the Board with additional disciplinary authority to appropriately respond to charter school violations. Currently, the Board is limited to exercising two options: recommending the withholding of 10 percent of a charter school's state funding or revoking a charter. However, an expanded array of nondisciplinary and disciplinary options may be more appropriate for some charter school problems or violations. These options might include issuing a nondisciplinary letter of concern; or disciplinary actions such as requiring staff to take additional training, withholding a board-determined amount of state funding, or placing a school on probation. Regardless of whether the Board receives additional disciplinary authority, it should develop necessary administrative rules and supporting policies to govern its disciplinary process.

Board has limited disciplinary options

Statute currently makes two disciplinary options available to the Board. Specifically, when the Board finds that a charter school has violated state or federal law, or has violated the terms of its charter, A.R.S. §§15-183 and 15-185(H) allow the Board to take one of the following actions:

- **Withhold 10 percent of a school's funding**—The Board can request that the Arizona State Board of Education (SBE) withhold up to 10 percent of a school's monthly state funding for a violation of federal or state law, or contractual requirements. However, while SBE usually withholds funds as requested, the authority to withhold 10 percent of a school's state funding actually only delays these payments to the school. Once schools demonstrate that the violation has been corrected, the Board will direct SBE to forward any withheld monies to the schools.

Board has only two disciplinary options available.

- **Revoke a charter**—If the violation is severe, the Board can act to revoke a school’s charter. If the Board decides to pursue this course of action, statute requires the Board to schedule and hold a revocation hearing and send the school a Notice of Intent to Revoke 90 days prior to the scheduled hearing.

The Board uses the first action far more frequently than the second. As illustrated in Figure 3, during 2001 and 2002, the Board took action to request that SBE withhold state funding from charter schools 55 times, for infractions ranging from school noncompliance with special education requirements to schools not submitting their annual audited financial statements within statutory time frames. Prior to July 2000, the Board did not have authority to request the withholding of state monies and thus could not exercise this disciplinary option.

Until July 2000, the only disciplinary option available to the Board was revocation of a school’s charter. While the Board initiated revocation proceedings against six schools during its first 5 years of operation (1996-2000) and revoked one charter, it has initiated this action against more schools in 2001 and 2002. Specifically, the Board initiated revocation proceedings against ten schools in 2001 and 2002, but revoked only one charter. The Board initiated these proceedings in response to violations that have threatened the health or welfare of students, such as failing to fingerprint uncertified employees; or, if schools have multiple serious violations, including failing to provide special education services and not administering the Arizona’s Instrument to Measure Standards (AIMS) test. For these ten cases, two schools voluntarily surrendered their charter; the Board dismissed four notices once the schools remedied the violations; and the Board entered into agreements with the other schools to allow them to continue operating with certain restrictions.

Figure 3 Violations for Which the Board Requested That State Funding Be Temporarily Withheld 2001 and 2002¹

Type of Violation	Number of Violations
Failure to submit the Annual Financial Report to the Arizona Department of Education	2
Failure to submit independent auditor’s report on time	44
Failure to comply with special education provisions	5
Failure to administer the AIMS test	4
Total violations	55

¹ Numbers do not reflect violations committed by a school that resulted in the revocation of that school’s charter.

Source: Auditor General staff analysis and summary of information contained in the Arizona State Board for Charter Schools board meeting minutes for 2001 and 2002.

Expanded options would assist Board

The Board’s limited disciplinary options do not always provide an action that is equivalent to the level of the violation. The withholding of 10 percent of a school’s monthly state funding may be too harsh for minor offenses and may not provide enough flexibility in the case of more serious violations. Therefore, the Legislature should consider granting the Board expanded disciplinary options.

Current disciplinary options not appropriate for some offenses—For some incidents of noncompliance, withholding 10 percent of a school’s state funding

may be too strong of an action. For example, failing to have faculty resumes on file for public review or failing to document governing board meeting minutes are both a statutory and contract violation. However, charter school noncompliance with these requirements does not necessarily impair children's welfare or education, and in fact, the Board has not taken disciplinary action against schools that have not complied with these requirements.

Withholding state funding may be inappropriate for some offenses.

The limited number of disciplinary options available to the Board also may restrict its ability to take appropriate action when schools commit violations that are more serious. For example, if a school fails to administer the AIMS test, a primary tool for assessing pupil achievement, it not only violates statute, but also jeopardizes students' education and could prevent them from graduating. In fiscal year 2002, seven charter schools failed to give the AIMS test to their students. In response, the Department of Education withheld state monies from these schools, while the Board initiated revocation proceedings against two schools because these schools also had not submitted their annual audited financial statements. The Board recommended that 10 percent of four schools' state funding be withheld and took no further action against one school. However, for these five schools, more serious action may have been warranted.

Finally, the Board cannot increase the amount of state funding withheld or take increasingly severe action if schools have multiple violations or if violations become more serious. Instead, the Board can only add the additional violations to the original reason for withholding a school's funding. For example, in 2002 the Board was already withholding 10 percent of the state funding from three schools for their failure to comply with special education requirements. The schools later failed to submit their Annual Financial Report, a condensed summary of their financial activity for the fiscal year, to ADE. However, unless the Board decides to revoke a school's charter, it could not take additional or progressive disciplinary action against the schools because it does not have the authority to do so.

Board's limited options hamper progressive discipline.

Board needs greater range of nondisciplinary and disciplinary options—The Legislature should consider amending A.R.S. §§15-183 and 15-185(H) to provide the Board with additional nondisciplinary and disciplinary options. Expanded options would allow the Board to impose discipline that is more consistent with the charter school violation, provide the Board with greater flexibility, and allow for progressive discipline in the event of increasingly severe or multiple violations. Changes to statute could include:

- **Letters of concern**—Letters of concern act as nondisciplinary advisory letters that can be issued when there is insufficient evidence to support direct action against a charter school, but sufficient evidence for the Board to notify the charter school of its concern and require the school to take necessary corrective action. Letters of concern are not a disciplinary action, but as is the case with other Arizona regulatory agencies, can be used as a factor in determining future

disciplinary actions. For example, both the Arizona Medical Board and Arizona Board of Osteopathic Examiners in Medicine and Surgery have the authority to use nondisciplinary advisory letters or letters of concern when there is insufficient evidence to take action, but sufficient evidence to notify physicians of their concerns.

- **Mandatory training**—Mandatory training would also be an appropriate tool or action for the Board to address minor infractions. The Board could require charter school governing board members and administrators to take specific training that would address the school violation or concern. For example, if a school has not followed special education requirements, the Board could require the school operators to take additional special education training that the Department of Education currently provides. Similarly, the North Carolina Office of Charter Schools requires some charter school governing boards to obtain mandatory management training to address charter school violations or deficiencies. In these cases, schools can choose the necessary training from several training groups, such as the National Charter School Institute, which provides training on topics ranging from running a governing board meeting to developing appropriate personnel policies.
- **Increase amount of withholding**—Specific authority to increase the amount of state funding withheld would give the Board increased flexibility to take appropriate action, especially in circumstances where progressive discipline is warranted. In the 2003 legislative session, the Board sought this additional authority. Specifically, the Legislature considered House Bill 2097, which would have provided the Board with authority to direct ADE to withhold any portion of the school's state funds. Although defeated, this proposed legislation would have allowed the Board to impose withholdings greater than 10 percent for more serious or multiple violations. According to legislative analysts, other measures contained in the bill led to its defeat. However, the State Board of Education (SBE) has similar authority to withhold any portion of state funding from school districts. A.R.S. §15-272 authorizes the SBE to withhold any portion of state funding if a school district has failed to comply with the uniform system of financial records.
- **Probation**—Authority to impose probation would give the Board greater latitude to ensure violations are addressed by requiring that specific terms and conditions be met before the probation can be lifted. Other charter school authorizers also have the authority to use probation, including North Carolina, the District of Columbia (D.C.), and Texas. For example, the North Carolina State Board of Education has the authority to place charter schools on probation for a variety of violations. These violations include failure to submit required financial data, a nonfunctioning school governing board, and failure to comply with health and safety standards. While on probation, schools must correct any deficiencies within specific time frames. If a school has not corrected the noted deficiencies

while on probation, the North Carolina Board will take additional progressive disciplinary action.

If the Legislature amends statute to provide the Board with additional disciplinary options, it would have the effect of also providing the SBE and local school districts with this same authority. Statutes authorizing the use of current disciplinary options pertain to all three charter school authorizers in the State.

Board should adopt administrative rules

Regardless of whether the Board receives additional disciplinary authority, it should adopt necessary administrative rules and supporting guidelines to govern its disciplinary process. Pursuant to A.R.S. §15-182(E)(5), the Board must adopt rules for its own governance. Statute also requires the Board to establish rules for administrative hearings. However, the Board has not established these required rules. This failure could subject board actions to questions of appropriateness and validity. The Board should also establish guidelines that will assist it in making consistent and appropriate disciplinary decisions. Guidelines should include a hierarchy of disciplinary actions and specify factors, including the violation's severity, the charter school's history, and other aggravating or mitigating circumstances that the Board should consider when imposing disciplinary action.

Board should adopt required rules.

Other charter school authorizers maintain specific guidelines for disciplining noncompliant schools. For example, the North Carolina Charter Schools Advisory Committee has specific guidance that governs its disciplinary process. These guidelines outline violations and identify the actions that the Committee can recommend to the North Carolina State Board of Education, which is the state's only authorizer. Under this process, there are four phases of noncompliance. For each phase, the guidelines communicate how close the school is to having its charter revoked, require corrective action, and establish time lines for compliance. In addition, at any point in the process, the Charter School Advisory Committee may suggest to the North Carolina State Board of Education that a noncompliant school be moved more quickly toward revocation.

Recommendations

1. The Legislature should consider revising A.R.S. §§15-183 and 15-185(H) to grant the Board authority to impose a greater array of nondisciplinary and disciplinary options for charter school violations. Specifically, the Legislature should consider giving the Board authority to:
 - a. Issue nondisciplinary Letters of Concern and define when it would be appropriate for the Board to issue these letters, which can also be used in determining future disciplinary actions;
 - b. Impose mandatory training for charter school governing board members, and operators/administrators;
 - c. Direct the State Board of Education to withhold any portion of a charter school's state funding; and
 - d. Impose probation with specific terms.
2. Regardless of whether the Board receives additional disciplinary authority, the Board should adopt appropriate administrative rules to govern its disciplinary process.
3. The Board should develop and implement disciplinary guidelines that include consideration of the violation's severity, the charter school's violation history, any other aggravating or mitigating factors, and the disciplinary actions available to the Board.

SUNSET FACTORS

1. Objective and purpose in establishing the Arizona State Board for Charter Schools.

The Legislature established the Arizona State Board for Charter Schools (Board) in 1994 to sponsor and regulate charter schools. While the Board is one of three entities in the State authorized to grant charters, as of March 2003, the Board sponsored over 70 percent of the charter schools in the State. In addition to the Board, the State Board of Education and local school districts can grant charters.

The Board's mission statement is as follows:

"To foster accountability in charter schools which will improve student achievement through market choice."

In support of its mission, the Board performs the following functions:

- **Charter authorization**—The Board grants charters to qualified applicants for charter schools. It evaluates applications from new applicants, charter school operators wishing to transfer sponsorship to the Board, and board-sponsored operators seeking to expand their number of sites.
- **Oversight**—The Board exercises general supervision over charter schools it sponsors through its review of schools' annual financial audits, statutorily required 5-year reviews, and site visits.
- **Complaint resolution**—The Board receives complaints from parents, students, charter school faculty, and the public on a broad range of charter school issues. According to the Board's executive director, the Board investigates and resolves complaints or, depending on the nature of the complaint, refers the matter to the appropriate agency, such as the county attorney or the Attorney General.

- **Public information**—The Board provides information to the public and existing and prospective charter school operators regarding schools, operating requirements, and other useful information.

2. The effectiveness with which the State Board for Charter Schools has met its objectives and purposes and the efficiency with which it has operated.

The Board has generally met its objective and purpose through its sponsorship of over 300 charter schools. However, there are a number of ways in which the Board could improve its efficiency and effectiveness. First, while the Board monitors charter schools, including conducting statutorily required 5-year reviews and periodic site visits, the Board should implement a more systematic monitoring approach. This would enable the Board to more effectively oversee the schools it regulates with its available resources. Monitoring charter schools is one of the most critical functions that the Board can perform, as it helps ensure that schools comply with federal and state requirements, and effectively educate Arizona students. However, the Board's current monitoring approach, which uses charter school site visits and other monitoring tools, is not fully effective. The Board cannot visit all 329 schools in a timely manner with its limited number of staff, and the site visits it does conduct are not thorough. In addition, deficiencies are not adequately followed up. Further, its other monitoring efforts are not well documented.

Given the number of schools the Board regulates and its limited resources, it should adopt a more coordinated monitoring approach using its various monitoring methods. As part of this process, board staff should also consistently follow up on deficiencies identified through its monitoring efforts and use site visits as a follow-up tool (see Finding 1, pages 11 through 18).

Additionally, the Board should continue with its efforts to more closely review charter school applications and monitor charter school finances. Some charter schools in the State have closed for financial reasons, while several operating schools have significant financial problems. To begin addressing these concerns, the Board has strengthened the financial requirements for opening a school and plans to enhance its review of applicant financial information. Specifically, at its May 2003 board meeting, the Board adopted new charter school application requirements that require start-up budgets to include only revenues for which receipt has been guaranteed. The Board has also enhanced its application review process. Additionally, while the Board has improved its monitoring and review of operating charter schools' finances, it should increase its review of available charter school financial information and require schools with financial problems to take corrective action (see Finding 2, pages 19 through 27).

3. The extent to which the State Board for Charter Schools has operated within the public interest.

The Board has generally operated within the public interest by granting charters to qualified applicants and providing public information on charter schools. Consistent with its legislative mandate, the Board has granted hundreds of charters and regulated 329 charter schools as of March 2003. These schools provide educational alternatives to students and market choices to parents.

Additionally, the Board has processes in place to provide charter school information to current and prospective school operators and the public. For example, the Board provides prospective charter operators with information about the chartering process and referrals to other state and federal agencies dedicated to assist charter schools. The Board also works with the Arizona Charter Schools Association to provide operators with support and training. In addition, the Board maintains a Web site that informs operators of upcoming training and educational opportunities, as well as provides information to the public about charter schools, including a "Frequently Asked Questions" component. Finally, the Board publishes a newsletter that also provides useful information to the public and charter school operators.

4. The extent to which rules and regulations promulgated by the State Board for Charter Schools are consistent with legislative mandate.

While the Board is mandated by statute to promulgate administrative rules, it has failed to do so. Pursuant to A.R.S. §15-182(E)(5), the Board must adopt rules for its own governance. These rules pertain to the management of matters affecting charter schools' procedural or substantive rights. Statute also requires the Board to establish rules for administrative hearings. By not establishing rules regarding its various processes, including its application and chartering, oversight, and disciplinary processes, the Board has not provided the public with the opportunity to provide input and comment on them. Additionally, without rules, the Board's actions could be jeopardized.

Although the Board has undertaken efforts to adopt rules, it has never proceeded through the entire rule-making process. For example, the Board drafted proposed rules and submitted them to the Governor's Regulatory Review Council (GRRC) for courtesy reviews in 1999 and 2001. While not part of the formal rule-making process, GRRC performed the courtesy reviews, but found the Board's rules to be deficient in many areas. For example, GRCC stated that the proposed rules were duplicative of the Board's statute, that time lines for processing an application were nonexistent, and that the proposed rules failed to define the factors used to consider accepting or rejecting an

Board has failed to adopt any required rules.

application. According to the Board, it lacks sufficient expertise to redraft the rules, and has not discussed draft rules with GRRRC since May 2002.

The Board should initiate the rule-making process and adopt all necessary rules as required by statute. According to the Board's executive director, the Board plans to begin the formal rule-making process in fiscal year 2004, after it approves the proposed rules.

5. The extent to which the State Board for Charter Schools has encouraged input from the public before adopting its rules and the extent to which it has informed the public as to its actions and their expected impact on the public.

Since the Board has not promulgated rules, it has not requested public input regarding the proposed rules. While it filed a Notice of Proposed Rule Making with the Secretary of State in 2000, drafted proposed rules, and submitted those rules to GRRRC for informal courtesy reviews, it has never formally submitted rules to GRRRC. Soliciting public input is required only after the Board formally submits its rules to GRRRC. According to the Board, it will review proposed rules at a public meeting after it submits them to GRRRC for review. However, in addition to soliciting input at a public meeting, the Board should solicit input from its various constituent groups and stakeholders, such as the Arizona Charter Schools Association and the Arizona Regional Resource Center, while drafting proposed rules.

The Board has complied with open meeting laws by posting public meeting notices at least 24 hours in advance at the required locations and making meeting agendas available to the public, and having a statement of where meeting notices will be posted on file with the Secretary of State.

6. The extent to which the State Board for Charter Schools has been able to investigate and resolve complaints that are within its jurisdiction.

Statute authorizes the Board to receive and investigate complaints regarding charter schools, and while the Board has a process for doing so, this process is not supported by rules. According to the Board's executive director, the Board receives complaints from parents, students, charter school operators, and the public; and received 98 written complaints in fiscal year 2002. The Board categorizes the complaints it receives as follows:

- Physical or sexual abuse of a student by school staff or faculty;
- Failure to provide special education services;

- Fraud, such as failure to purchase books or equipment with grants or funds received for that purpose; and
- Contract and compliance-related issues, such as problems reporting Average Daily Membership, teaching religion, or failing to administer the required tests.

Based on the type of complaint it receives, the Board will either refer the complaint to the appropriate agency or investigate and resolve the complaint if it is within the Board's jurisdiction. According to the Board's executive director, the Board refers the first three categories to the appropriate law enforcement or state agency and provides any requested assistance and documentation to these agencies. For example, abuse complaints are referred to the appropriate law enforcement agency, special education complaints are referred to the Department of Education, and fraud complaints are referred to the Attorney General's Office.

The Board investigates and resolves contract or compliance-related complaints. The Board will also attempt to provide assistance in resolving noncontract-related complaints, such as complaints regarding school uniforms or unfair treatment by a teacher, even though it does not have jurisdiction in these matters. However, the Board lacks administrative rules regarding complaint processing and a reliable system to track the complaints it receives and their investigation and resolution. Currently, while the Board's staff maintain a list documenting the receipt of complaints, the Board does not track their investigation, referral, or disposition.

Therefore, the Board should adopt all necessary rules, and supporting policies and procedures, to guide its complaint receipt, investigation, and resolution process. Additionally, the Board should automate its complaint tracking by possibly incorporating the function into an existing board database, such as its accountability database, which already has the capability to track complaint processing.

Board should document its complaint-handling process.

7. The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation.

A.R.S. §41-192 authorizes the Attorney General to prosecute actions and represent the Board. The Board refers complaints alleging school involvement in fraudulent behavior directly to the Attorney General's Office for investigation and possible prosecution.

8. The extent to which the State Board for Charter Schools has addressed deficiencies in the enabling statutes, which prevents it from fulfilling its statutory mandates.

The Legislature has amended several board statutes in recent years, some of which have enhanced the Board's ability to fulfill its statutory mandate. For example:

- In 2000, the Board supported and the Legislature passed statutory changes that allow the Board to recommend to the Department of Education that 10 percent of a charter school's state funding be withheld for schools that fail to comply with federal and state law, or contractual requirements.
- In 2000, the Board also supported legislation that added misappropriation of charter school funds to the criminal code.
- In 2003, the Board supported and the Legislature considered House Bill 2097, which would have provided the Board with authority to direct the Department of Education to withhold up to 100 percent of a school's state funding for failure to comply with legal or contractual requirements. Although defeated, this proposed legislation would have allowed the Board to impose withholdings greater than 10 percent for more serious or multiple violations. According to legislative analysts, other measures contained in the bill led to its defeat.

Additionally, the fiscal year 2004 omnibus budget reconciliation bill (Laws 2003, Ch. 264 §20) suspended the State Board of Education's (SBE) authority to sponsor any additional charter schools in fiscal year 2004 and requires the SBE to enter into an intergovernmental agreement with the Arizona State Board for Charter Schools requiring the Board to provide oversight for SBE-sponsored charter schools in fiscal year 2004. This law eliminates the duplication of charter granting between the two state agencies and transfers approximately \$185,000 annually and three FTE to the Board.

9. The extent to which changes are necessary in the laws of the State Board for Charter Schools to adequately comply with the factors listed in the subsection.

Based on audit work, the Legislature should consider amending A.R.S §§15-183 and 15-185(H) to provide the Board with an expanded range of nondisciplinary and disciplinary options to more appropriately respond to both minor and major statutory and contract violations. The changes could include authority to use nondisciplinary letters of concern, and disciplinary options such as requiring

mandatory training, directing the withholding of any amount of state funding, and placing schools on probation. (see Finding 3, pages 29 through 34).

10. The extent to which the termination of the agency would significantly harm the public health, safety, or welfare.

Termination of the Board could potentially harm the public welfare since the Board oversees and monitors 329 charter schools that educate approximately 54,000 students. Without the Board to monitor and enforce charter school compliance with federal and state laws and accountability for student achievement and academic progress, students may not receive the education to which they are entitled. If the Board were terminated, other authorizers in the State, such as the State Board of Education and local school districts, may not be able to assume the regulation of these schools. Specifically, as indicated in Sunset Factor No. 8, Laws 2003, Ch. 264 §20 suspended the State Board of Education's authority to sponsor any additional charter schools in fiscal year 2004 and requires the SBE to enter into an intergovernmental agreement with the Arizona State Board for Charter Schools requiring the Board to provide oversight for SBE-sponsored charter schools in fiscal year 2004. Additionally, statute prohibits local schools districts from sponsoring charter schools outside of their districts, and only eight local school districts currently sponsor charters. As a result, other local school districts would need to agree to sponsor charter schools and establish the necessary regulatory systems and expertise in order to assume the regulation of the hundreds of charter schools sponsored by the Board.

11. The extent to which the level of regulation exercised by the State Board for Charter Schools is appropriate and whether less or more stringent levels of regulation would be appropriate.

The audit found that the current level of regulation exercised by the State Board for Charter schools is generally appropriate.

12. The extent to which the State Board for Charter Schools has used private contractors in the performance of its duties and how effective use of private contractors could be accomplished.

The Board has relied on private contractors to perform activities beyond its staff resources. For example, the Board had contracted with a private certified public accounting firm to annually review each charter school's audited financial statements for compliance with accounting and auditing standards and to forward a report of audit findings to the Board. This contract ended in February

2003, and the Board's staff now perform many of this contractor's functions. However, the Board revised the scope of services requested from a certified public accountant and entered into a new contract with a different contractor in March 2003. The contractor will review charter school audited financial statements for financial solvency concerns and other financial weaknesses, in addition to compliance with accounting and auditing standards. Additionally, the Board has a contract with the Department of Administration for accounting services.

This audit did not identify any further uses for private contracts.

AGENCY RESPONSE

Arizona State Board for Charter Schools



August 6, 2003

Debbie Davenport
Auditor General
Office of the Auditor General
2910 North 44th Street, Suite 410
Phoenix, Arizona 85018

Dear Ms. Davenport,

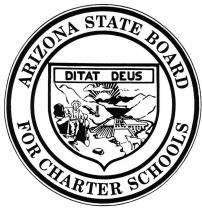
Thank you for the opportunity to provide comments on the evaluation of the Arizona State Board for Charter Schools that was conducted as part of the Sunset review process prescribed in Arizona Revised Statutes (A.R.S.) § 41-2951 et seq. We are pleased with the Auditor General's report that supports some of the Board's current practices and directions, as well as providing observations and recommendations that will help the Board refine some processes and policies that will help strengthen Arizona's Charter School system. The success of Arizona's charter school movement is a result of the commitment, dedication and extraordinary hard work of past and present legislators, policy makers, board members, charter operators, and staff who work together to embrace public school choice for parents and students.

The Board appreciates and respects the professionalism of the team of auditors who have worked on this report. We take the recommendations seriously and have deliberated and discussed at length each and every one. The Board's goal is to glean from this audit all possibilities that will make the Board more responsive and effective and our schools more successful.

Please feel free to contact me at (602) 364-3080 if additional information is needed.

Sincerely,

Kristen Jordison
Executive Director



Arizona State Board for Charter Schools

Response to the Auditor General's Performance Audit

INTRODUCTION

Less than a decade ago the Arizona State Legislature passed a law (A.R.S. § 15-181 and 15-182) that allowed for the establishment of charter schools and created the Arizona State Board for Charter Schools (the "Board") as one of three possible charter school sponsors in the state. Pursuant to this law (A.R.S. 15-182.E) the Board is responsible for granting charters to qualified applicants, exercising general supervision over these schools, making recommendations to the legislature, determining the policy of the Board, and delegating the execution of this policy to its staff and the Superintendent of Public Instruction. As a public service, the Board provides information to schools and the public through the Board's website, the public charter files, and monthly publications of the Board's activity. Additionally, the Board receives complaints from parents, students, charter school faculty and the public that are processed and made public.

Arizona has created an education marketplace with the creation of charter schools. A marketplace where parents and students, the "customer", have many choices to satisfy their differing needs. Unlike school districts that have students automatically assigned to them, charter schools must attract their students to survive. Thus, their "product" or educational service must meet the needs of the customer and the regulatory body in order to sustain their business. If the educational program that is offered is not desired on the market or does not meet the standards laid out by the state, the business will close.

So how is this working in Arizona? The answer is simple, the vast majority of charter schools in Arizona have been successful.

- According to a study of parent satisfaction conducted in the spring of 2002 sixty-seven percent of parents graded their charter school an A+ or an A.¹
- According to a national survey conducted by the Thomas B. Fordham Institute, Arizona ranked 1st in the nation in state policies for charter schools; 3rd in the nation for overall policies and practices, and 9th in the nation for charter school sponsors. In terms of grades, Arizona received an A+ for financial audits and progress reports required; an A for clear special-needs students provisions; an A for reports reviewed, problems

¹ Solmon, Lewis C. (2003). Findings from the 2002 Survey of Parents with Children in Arizona Charter Schools: How Parents Grade Their Charter Schools. *Prepared for the Arizona State Board for Charter Schools.*

flagged and school notified, and an A- for charter school sponsors making decisions on merit, not politics.²

- When compared to Arizona district school students, Arizona charter school students are making greater gains in reading and are making about the same gains in math. Additionally, the academic gains are greater the longer a student attends a charter school.³
- The closure rate for charter schools is very small. A rate significantly lower than the rate of small business closures.
- The Arizona charter school law has repeatedly been named the strongest charter school law in the nation by the Center for Education Reform.⁴

The Board appreciates the professionalism of the team of auditors who worked on this audit for the past year. The audit supports some of the Board's current practices and directions, as well as providing observations and recommendations that will help the Board refine some processes and policies that will help strengthen Arizona's charter school system.

² Palmer, L. B., & Gau, R. (June 2003). Charter School Authorizing: Are States Making the Grade? *Published by the Thomas B. Fordham Institute with support from the Walton Family Foundation.*

³ Solmon, L., Garcia, D., & Paark, K. (March 2001). Does Charter School Attendance Improve Test Scores? The Arizona Results. *A Project of the Goldwater Institute's Center for Market-Based Education.*

⁴ Charter School Laws Across the States Ranking Scorecard. *Center for Education Reform*
[http://www.edreform.org/charter_schools/states/arizona.htm].

AUDITOR GENERAL FINDING 1

The Board should implement a more systematic monitoring approach

Oversight of charter school compliance includes many variables such as academic achievement, fiscal accountability, and general compliance with federal, state, and local laws and regulations. The Board is not the governing body of the charter school and thus is not responsible for the daily operations of the school. The Board is not the Arizona Department of Education and thus is not responsible to Department's state and federal statutory requirements. And the Board is another agency or entity, such as a local municipality dictating the zoning requirements for charter schools. The Board is, however, responsible for the general oversight of charter schools much like the other state agencies that oversee private contracts. Thus, the Board needs to respect their role and work cooperatively with each body to ensure proper communication between these entities and charter schools and provide the discipline when the charter school fails to properly follow the statutory requirements, if necessary.

For example, the audit notes that the Board has not established any policies or procedures for accepting school improvement plans and following up on their implementation. The Board did require each school to submit a copy of their school improvement plan to the Board as outlined in statute. It is appropriate to say that the Board has not followed-up on the implementation of these plans. However, this is due to the fact that the Board does not have the authority to do so. This authority has been given to the Department of Education for the development of solutions teams and includes a specific state appropriation to do so. As another example, Arizona Learns outlines the Board's responsibilities and the Board has established a study committee to develop recommendations for implementation of this role.

Existing Effective Monitoring Approach

The audit report indicates that the Board utilizes three monitoring tools to assess school compliance with laws and charter requirements (i.e., site visits, five year reviews, and partnering with Department of Education). While these three methods are utilized effectively in oversight, many other methods are also used to monitor compliance of charter schools. Some of the specific examples of oversight methods, as provided to the auditors, are outlined below:

Academic Accountability

- Requires each governing board, charter administrator, and charter principal to submit their respective declaration indicating that the adopted/implemented curriculum is aligned with the Arizona Academic Standards.
- Prior to the approval of any new charter, the curriculum must demonstrate alignment with the Arizona Academic Standards.

- Review curriculum samples for alignment to the Arizona Academic Standards for every school adding grade levels to their contract.
- Hold schools accountable for properly administering required tests by withholding 10% of monthly state aid.
- Work with Department of Education, Exceptional Student Services Unit to hold schools accountable for special education policies and services.
- Work with the Department of Education to hold schools accountable for the proper and timely submission of their School Improvement Plans.
- Work with the Department of Education on statutorily mandated compliance with Arizona Learns and No Child Left Behind.

Fiscal Accountability

- Constantly monitor individual schools state aid revenues through meetings and data analysis with the Department of Education School Finance Unit.
- Established policy to safeguard the estimated enrollment list by requiring schools to maintain specific documentation for each student submitted for payment.
- Hold schools accountable for timely submission of their annual audit.
- Developed new legal compliance questionnaire and audit guidelines.
- Moved up the annual audit submission deadline from March 30 to November 15th starting with the FY 2004 audits.
- Follow-up with audit findings.
- Work with the Department of Education Audit Unit on Average Daily Membership audits.
- Work cooperatively with the Attorney General's School Fraud division.

General Compliance

- Work closely with the State Fire Marshal's office, local municipalities, and county health departments to ensure that all schools meet all health and safety requirements prior to and during operation of the school. These documents are in each charter school's respective file.

Site Visits and Five-Year Reviews

In addition to the oversight examples outlined above, the Board routinely conducts site visits and five-year reviews. Site visits help inform and supplement oversight that is occurring throughout the year and is not meant to be a comprehensive review of compliance for the school. The Board believes site visits are an effective oversight tool and provides a different perspective than what can be found on paper alone.

Although it is not possible to visit every school each year, the Board has historically visited approximately fifty percent of the schools. Specifically, in school year 2001 the Board visited 44% or 65 schools (40 site visits and 25 five-year reviews) out of 147 charters and in school year 2002 the Board visited 55% or 105 schools (87 site visits and 18 five-year reviews) out of 192 charters.

The site visit logs reviewed by the auditors are maintained to document the date of the visit but have not been a comprehensive description of all activity that occurred during or after the site visit. Thus, these logs may not have provided enough information to accurately draw conclusions on the effectiveness of the visits themselves. The Board does follow up on those issues that impact the safety, health or quality of education the children are receiving.

Responsibilities and Relationships of the Board

The statutorily assigned responsibilities of the Board as described above are important to keep in mind when reviewing the audit findings. Additionally, according to Arizona law, charter schools are designated as local education agencies (LEA) and, as such, bear many of the same responsibilities as traditional school districts (e.g. special education, state and federal grant reporting, curriculum standards, fingerprinting, open meeting law, etc.) and are legally and financially autonomous entities. Thus, just like traditional school districts, charter schools work closely with various units within the Arizona Department of Education (Department of Education) to submit required data for state and federal funding and statutory reporting compliance. The Board works closely with the Department of Education to help communicate information and deadlines to charter schools and provides disciplinary action for non-compliant schools if necessary. Besides the Department of Education, the Board has developed this type of supportive relationship with many other entities such as the Arizona State Fire Marshal, county health departments, and local municipalities that require information and compliance from charter schools.

Finding 1 Board Response:

Auditor General's Recommendation 1: The Board should develop a systematic monitoring approach that is established in administrative rules, and policies and procedures. This approach should include (please see Auditor General's report for full list).

Auditor General's Recommendation 2: The Board should develop and implement administrative rules, and supporting policies and procedures, to govern its follow-up process.

Auditor General's Recommendation 3: The Board should effectively use its existing accountability database by establishing policies and procedures that direct staff on its use, including entering data from its document reviews and follow-up efforts.

Auditor General's Recommendation 4: The Board should train its staff how to use the accountability database and how the database can assist staff in their monitoring and follow-up efforts.

Board Response

The Board consistently seeks ways to make processes more efficient, understandable and transparent to our schools and the public within the framework of the statutes that govern our operation (A.R.S. § 15-182). The Board will continue these efforts to improve and find better, more efficient ways of operating. It is for this reason that although the Board does not agree with the Auditor General's finding on the current process of monitoring charter schools, the Board does agree that a more systematic approach established in administrative rules, and policies and procedures would more clearly articulate this responsibility to charter schools and to the public. Thus, these recommendations will be implemented.

AUDITOR GENERAL FINDING 2

The Board should continue its efforts to more closely review school's financial condition

A charter school's business operations are as important as its educational operations and each one influences the other. It is for this reason and others that charter school closures are extremely difficult to predict, even when a school's financial condition is poor. Although some of the schools that have closed did so because of financial difficulty, there are many schools that have sustained severe financial difficulties and are now in good financial health.

Additionally, the closure rate for charter schools in Arizona is very small and the rate of closure for financial reasons is even smaller. However, the Board agrees that financial oversight of charter schools is an important function and this is evident from past and recent changes made to the oversight process. Specific examples of oversight of charter schools' financials are listed below:

Application Process:

- The Board requires a start-up budget, a first year cash flow budget and a three year operational budget
- Projected revenue sources, outside of equalization and Classroom Site Funds, must be supported with documentation. Although the Board has always questioned unsecured revenues, the Board has not had a specific requirement to provide documentation in the application until this year.
- Marketing plans will be evaluated with respect to the number of potential students and growth in the target area
- Developed a comprehensive scoring rubric with cut scores to be used by the applicants, the reviewers, and the Board

Annual Financial Audit

- Charter schools are required to submit an annual financial statement and compliance audit conducted by an Independent Certified Public Accountant to the Board.
- All charter schools have always been required to submit an Annual Finance Report to the Department of Education by October 15 of each year.
- The Board developed and adopted audit guidelines that include specific details on the level of audit to be conducted and a new audit deadline of November 15.
- The Board developed and adopted a new compliance questionnaire that includes more detail on fingerprinting, special education, and open meeting law compliance.

Oversight of State Aid/Student Counts

- The Board developed a policy to reinforce the accuracy of each schools estimated enrollment submission by requiring specific data elements be on file for each student submitted to the Department of Education.
- The Board's staff, on each site visit, validates the accuracy of the student count submitted to the Department of Education by comparing the number of students in class to the number submitted to the Department of Education.
- The Board's staff meets with the Department of Education's School Finance Unit on a bi-weekly basis to monitor the student counts submitted.

Oversight of school finances

Although the audit cites that the Board took steps to improve its oversight of charter school financial solvency the Board believes it has no statutory authority to take action against a school because of poor financial health. The financial health of a charter school is the responsibility of the school's governing board. The Board has, and will further develop, methods for overseeing compliance with Generally Accepted Accounting Principles (GAAP), Generally Accepted Auditing Standards (GAAS), and where applicable, the Uniform System of Financial Records for Charter Schools (USFRCS). The Board is in the process of following up on the findings reported in the school's annual audits and will require schools to take corrective action to address these compliance concerns. Additionally, as noted by the audit, the Board is in the process of evaluating trend data but the purposes of this evaluation, at least in the short term, will be to inform policy decisions.

Finding 2 Board Response

Auditor General's Recommendation 1: The Board should codify its application process by establishing necessary administrative rules, and supporting policies and procedures.

Auditor General Recommendation 2: The Board should improve the review of financial information provided in charter school application by:

- a. Establishing necessary administrative rules, and supporting policies and procedures for the review and scoring of financial information in the charter school application; and*
- b. Restructuring the application review committee to include lenders with non-profit lending experience and educational program experts with school funding experience.*

Auditor General, Recommendation 3 a-d: The Board should improve its oversight efforts of operating schools by:

- a. Annually reviewing the financial information submitted to the Arizona Department of Education as part of the annual financial report;*

- b. Requiring schools with financial problems to submit corrective action plans detailing steps the school will take to address the problems and monitoring school progress in implementing the plans;*
- c. Identifying at board meetings and in its public files schools whose independent auditor has found financial problems so severe that closure is possible; and*
- d. Developing necessary administrative rules, and supporting policies and procedures, to guide its financial oversight practices.*

Board Response

Recommendation 1

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 2

The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented. As the audit notes the Board has established a scoring rubric that specifically addresses the scoring of the financial information in the charter school application and will take the next step to establish the necessary administrative rules, and supporting policies and procedures for the review and scoring of this information. Additionally, the Board has incorporated educational program experts with school funding experience into the review process and will continue to do so. The Board will take steps to include other financial experts into this application review process but does not want to limit the scope to only individuals with non-profit lending experience. The Board believes individuals knowledgeable in running a small business for example, would make a good representative. Thus, the Board will make efforts to diversify its review panel to include individuals with financial expertise.

Recommendation 3a.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation 3b.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The Board has, and will further develop, methods for overseeing compliance with Generally Accepted Accounting Practices (GAAP), Generally Accepted Auditing Standards (GAAS), and where applicable, the Uniform System of Financial Records for Charter Schools (USFRCS). The Board is in the process of following up on the findings reported in the school's annual audits and will require schools to take corrective action to address these compliance concerns. Additionally, as noted by the audit, the Board is in the process of evaluating trend data but the purposes of this evaluation, at least in the short term, will be to inform policy decisions.

Recommendation 3c.

The finding of the Auditor General is agreed to and the recommendation will not be implemented. Financial information is public and available to parents should they want to learn about the financial condition of their school. Because of the difficulty in predicting closure, this type of notification could unfairly alarm the parents of the school and make the school's financial situation worse by causing an exodus of students from the school.

Recommendation 3d.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

AUDITOR GENERAL FINDING 3

Board needs additional disciplinary authority

The audit report correctly characterizes the two statutorily defined disciplinary options that are available to the Board: recommending the withholding of up to 10 percent of the charter school's state funding or revoking a charter. In addition to developing disciplinary options, the Board would like to develop some type of reward or recognition system for the hundreds of charter schools that are in compliance.

Finding 3 Board Response

Auditor General, Recommendation 1 a-d The Legislature should consider revising A.R.S. 15-183 and 15-185(H) to grant the Board authority to impose a greater array of non-disciplinary and disciplinary options for charter school violations. Specifically, the Legislature should consider giving the Board the authority to:

- a. Issue non-disciplinary Letters of Concern and define when it would be appropriate for the Board to issue these letters, which can also be used in determining future disciplinary actions;*
- b. Impose mandatory training for charter school governing board members, and operators/administrators;*
- c. Direct the State Board of Education to withhold any portion of a charter school's state funding; and*
- d. Impose probation with specific terms.*

Board Response:

The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented.

Recommendation a: The Board agrees that, given a defined set of circumstances, the issuance of a letter of concern could be an added step in the disciplinary process. However, the Board feels that this could be implemented within our current statutory authority and codified in rules, policies, and procedures. Thus, the Board does not agree that the Legislature needs to act on this matter.

Recommendation b. Although the Board requires new charter operators to attend a one-day workshop hosted by the Department of Education, Exceptional Student Services Unit, the Board does not feel that there are great enough training opportunities where this could be used to address disciplinary matters.

Recommendation c. As the audit notes, the Board sought the authority to increase the amount of state withholding in the 2003 legislative session and thus, supports this added authority. In addition to having the flexibility to increase the amount of state funding withheld, the Board would also like to have the authority to direct the Department of Education to take the funds without having to go through the State Board of Education. The added step of forwarding the request to the State Board of Education to forward to the Department of Education delays the timing of this sanction and makes it less effective.

Recommendation d. The Board feels that other disciplinary measure could be implemented within our current statutory authority and codified in rules, policies, and procedures. This could include the imposition of corrective action plans with specific timeframes with increasing disciplinary sanctions for failure to meet the requirements of the plan. Thus, the Board does not agree that probation should be imposed.

Performance Audit Division reports issued within the last 12 months

02-03	Department of Economic Security—Kinship Foster Care and Kinship Care Pilot Program	02-12	HB2003 Children’s Behavioral Health Services Monies
02-04	State Parks Board—Heritage Fund	02-13	Department of Health Services—Office of Long Term Care
02-05	Arizona Health Care Cost Containment System—Member Services Division	03-L1	Competitive Electric Metering, Meter Reading, and Billing and Collections
02-06	Arizona Health Care Cost Containment System—Rate Setting Processes	03-01	Government Information Technology Agency—State-wide Technology Contracting Issues
02-07	Arizona Health Care Cost Containment System—Medical Services Contracting	03-02	Registrar of Contractors
02-08	Arizona Health Care Cost Containment System—Quality of Care	03-03	Water Infrastructure Finance Authority
02-09	Arizona Health Care Cost Containment System—Sunset Factors	03-04	State Board of Funeral Directors and Embalmers
02-10	Department of Economic Security—Division of Children, Youth and Families, Child Protective Services	03-05	Department of Economic Security—Child Protective Services—Foster Care Placement Stability and Foster Parent Communication
02-11	Department of Health Services—Health Start Program	03-06	Arizona Board of Appraisal

Future Performance Audit Division reports

Department of Commerce

Department of Economic Security—Child Protective Services—Caseloads and Training