

Extraordinary Audit

of the
**Mexican American Community
Services Agency's (MACSA's)
El Portal Leadership Academy
and Academia Calmecac
Charter Schools**



**Commissioned by the Santa Clara
County Office of Education**

August 27, 2009

**Administrative Agent
Christine Lizardi Frazier
Office of Kern County
Superintendent of Schools**

Chief Executive Officer
Joel D. Montero



August 27, 2009

Dr. Charles Weis, Superintendent
Santa Clara County Office of Education
1290 Ridder Park Drive
San Jose, CA 95131

Dear Superintendent Weis:

In April 2009, the Santa Clara County Office of Education and the Fiscal Crisis and Management Assistance Team (FCMAT) entered into an agreement for FCMAT to conduct an AB 139 extraordinary audit of the Mexican American Community Services Agency (MACSA) Academia Calmecac and El Portal Leadership Academy charter schools. The study agreement specifies that FCMAT will complete the following scope of work:

1. The COE requests the Team to conduct a review of the business practices of two direct funded charter schools, the MACSA Academia Calmecac, sponsored by the East Side Union High School District, and the MACSA El Portal Leadership Academy, sponsored by the Gilroy Unified School District. Specifically, the review is requested to determine if there is evidence of illegal fiscal practices or misappropriation of employee CalPERS and CalSTRS payroll deductions.

It is alleged that approximately \$400,000 in employee deductions (\$150,000 for the Gilroy-sponsored charter and \$250,000 for the East Side-sponsored charter employees) have not been processed and sent to the retirement agencies for a period in excess of one year; and that the employer portion has also not been processed. It is alleged that MACSA, the Mexican American Community Services Agency, has used the retirement contributions to pay operating costs.

The Team's review will verify whether there is sufficient evidence of illegal fiscal practices or misappropriation in the processing of payrolls and handling of employee deductions and employer contributions for the county superintendent to contact local law enforcement for further investigation.

The attached final report contains the study team's findings and recommendations.

We appreciate the opportunity to serve you and we extend our thanks to all the staff and administration of the Santa Clara County Office of Education, MACSA, and the East Side Union High and Gilroy Unified school districts.

FCMAT

Joel D. Montero, Chief Executive Officer

1300 17th Street - CITY CENTRE, Bakersfield, CA 93301-4533 • Telephone 661-636-4611 • Fax 661-636-4647

422 Petaluma Blvd North, Suite. C, Petaluma, CA 94952 • Telephone: 707-775-2850 • Fax: 707-775-2854 • www.fcmat.org

Administrative Agent: Christine Lizardi Frazier - Office of Kern County Superintendent of Schools

Sincerely,

A handwritten signature in black ink, appearing to read 'Joel D. Montero', with a stylized flourish at the end.

Joel D. Montero
Chief Executive Officer

c: Cathy Grovenburg, Assistant Superintendent Business Services

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Foreword

FCMAT Background

The Fiscal Crisis and Management Assistance Team (FCMAT) was created by legislation in accordance with Assembly Bill 1200 in 1992 as a service to assist local educational agencies in complying with fiscal accountability standards.

AB 1200 was established from a need to ensure that local educational agencies throughout California were adequately prepared to meet and sustain their financial obligations. AB 1200 is also a statewide plan for county offices of education and school districts to work together on a local level to improve fiscal procedures and accountability standards. The legislation expanded the role of the county office in monitoring school districts under certain fiscal constraints to ensure these districts could meet their financial commitments on a multiyear basis. AB 2756 provides specific responsibilities to FCMAT with regard to districts that have received emergency state loans. These include comprehensive assessments in five major operational areas and periodic reports that identify the district’s progress on the improvement plans.

Upon request, FCMAT also provides extraordinary audits in accordance with Assembly Bill 139 and Education Code Section 1241.5 (b) and (c), which authorize county superintendents of schools to conduct or request a review or audit of the expenditures and

internal controls of any school district or charter school in their county if there is reason to believe that fraud, misappropriation of funds, or other illegal fiscal practices have occurred.

Since 1992, FCMAT has been engaged to perform more than 700 reviews for local educational agencies, including school districts, county offices of education, charter schools and community colleges. Services range from fiscal crisis intervention to management review and assistance. FCMAT also provides professional development training. The Kern County Superintendent of

Total Number of Studies..... 743

Total Number of Districts in CA 982

● Management Assistance..... 705 (94.886%)

● Fiscal Crisis/Emergency 38 (5.114%)

Note: Some districts had multiple studies.

● Districts (7) that have received emergency loans from the state.

(Rev. 1/22/09)

Study Agreements by Fiscal Year

Fiscal Year	Number of Studies
92/93	10
93/94	15
94/95	23
95/96	29
96/97	26
97/98	26
98/99	27
99/00	47
00/01	48
01/02	58
02/03	34
03/04	71
04/05	74
05/06	78
06/07	71
07/08	54
08/09	59 (Projected)

Santa Clara County Office of Education – MACSA Charter Schools

Schools is the administrative agent for FCMAT. The agency is guided under the leadership of Joel D. Montero, Chief Executive Officer, with funding derived through appropriations in the state budget and a modest fee schedule for charges to requesting agencies.

Introduction

Background

California Education Code Section 47600, also known as the Charter Schools Act of 1992, was enacted “to provide opportunities for teachers, parents, pupils, and community members to establish and maintain schools that operate independently from the existing school district structure.” Charter schools are a part of the public school system but differ from traditional public schools because they are exempt from many state laws relating to specific educational programs. Specific goals and operating procedures for the charter school are detailed in an agreement, or charter, between the authorizing agency and the charter school organizers. Charter schools may elect to operate as corporations organized under the Nonprofit Public Benefit Corporation Law of the Internal Revenue Code [26 U.S.C. Sec. 501(c)(3)].

Charters offer a more flexible school governance model but are accountable for student achievement and fiscal management. The chartering agency is responsible for adequate and appropriate oversight, including determining if a charter is following prudent business practices and generally accepted accounting principles (GAAP) in accounting for revenues and expenditures and preparing financial reports. The chartering agency may be a school district, county office of education, or the California State Board of Education.

The Mexican American Community Services Agency (MACSA) Academia Calmecac charter school was authorized by the East Side Union High School District and opened in 2001. The MACSA El Portal Leadership Academy charter school was authorized by the Gilroy Unified School District. Its charter petition was approved on February 21, 2000, and the school opened in 2001. Both authorizing districts are in Santa Clara County.

Both schools are direct-funded and are operated by MACSA, which is a nonprofit corporation. MACSA provides all of the administrative functions for the two charter schools. Academia Calmecac serves approximately 190 students in grades 9-12, and El Portal serves approximately 158 students in grades 9-12. Both schools offer a site-based instructional program.

Based on the provisions of Education Code section 1241.5(c), a county superintendent may review or audit the expenditures and internal controls of any charter school in his or her county if he or she has reason to believe that fraud, misappropriation of funds, or other illegal fiscal practices have occurred that merit examination. The review or audit conducted by the county superintendent shall be focused on the alleged fraud, misappropriation of funds, or other illegal fiscal practices and shall be conducted in a timely and efficient manner. The basis of the review is to determine if sufficient documentation exists to further investigate the findings. Education Code section 42638(b) states:

If the county superintendent determines that there is evidence that fraud or misappropriation of funds has occurred, the county superintendent shall notify the

governing board of the school district, the State Controller, the Superintendent of Public Instruction, and the local district attorney.

In March 2009, the Fiscal Crisis and Management Assistance Team (FCMAT) received a request from the Santa Clara County Office of Education for an Assembly Bill (AB) 139 extraordinary audit of the two MACSA charter schools. The county office had received information regarding the charter schools' alleged nonpayment of California State Teachers' Retirement System (STRS) and California Public Employees' Retirement System (PERS) contributions.

In April 2009, FCMAT and the county office entered into a study agreement which specifies that FCMAT will complete the following:

1. The COE requests the Team to conduct a review of the business practices of two direct funded charter schools, the MACSA Academia Calmecac, sponsored by the East Side Union High School District, and the MACSA El Portal Leadership Academy, sponsored by the Gilroy Unified School District. Specifically, the review is requested to determine if there is evidence of illegal fiscal practices or misappropriation of employee CalPERS and CalSTRS payroll deductions.

It is alleged that approximately \$400,000 in employee deductions (\$150,000 for the Gilroy sponsored charter and \$250,000 for the East Side sponsored charter employees) have not been processed and sent to the retirement agencies for a period in excess of one year; and that the employer portion has also not been processed. It is alleged that MACSA, the Mexican American Community Services Agency, has used the retirement contributions to pay operating costs.

The Team's review will verify whether there is sufficient evidence of illegal fiscal practices or misappropriation in the processing of payroll and handling of employee deductions and employer contributions for the county superintendent to contact local law enforcement for further investigation.

Study Guidelines

FCMAT visited the county office, MACSA, the East Side Union High School District and the Gilroy Unified School District on May 12-14, 2009 to conduct interviews, collect data and review documents. This report is the result of those activities and is divided into the following sections:

- I. Executive Summary
- II. PERS and STRS Contributions
- III. Financial Trends and Analysis
- IV. Appendix

Study Team

The FCMAT study team was composed of the following members:

Diane Branham
FCMAT Fiscal Intervention Specialist
Bakersfield, California

Deborah Deal
FCMAT Fiscal Intervention Specialist
Bakersfield, California

John Lotze
FCMAT Public Information Specialist
Bakersfield, California

Executive Summary

During 2008-09, the Santa Clara County Office of Education received information alleging that, for more than a year, employee deductions and employer contributions to the Public Employees' Retirement System (PERS) and the State Teachers' Retirement System (STRS) had not been paid for employees of the Academia Calmecac and the El Portal Leadership Academy charter schools. It was also alleged that these funds had been used by MACSA to pay operating costs.

Education Code section 47605 gives charter schools the option to participate in PERS and STRS, and the MACSA board of directors approved participation in both retirement systems at its January 10, 2002 meeting. Charter schools that choose to participate must follow the regulations for each program. Payments include a contribution from employees and from employers on all creditable earnings.

When charter school employees became aware that the required retirement contributions were not being made to PERS and STRS, a grievance was filed. As a result, MACSA agreed to a schedule for payment of all current and past due contributions.

Academia Calmecac owed \$249,909.76 for past due payments from April 2007 through January 2009. Payments were also not made for the March and April 2009 payrolls, leaving a total unpaid balance of \$267,777.91 as of May 12, 2009.

El Portal Leadership Academy owed \$140,139.85 for past due payments from August 2007 through January 2009. As of May 12, 2009, \$103,394.56 had been paid, but no payment was made for the April 2009 payroll, leaving a total unpaid balance of \$41,400.01.

Failure to report creditable earnings and pay the required contributions to PERS and STRS on time can result in late penalties and interest. Amounts withheld from employees' salaries are to be treated as a trust fund and not used for other purposes. The creditable earnings and past due employee deductions and the employer contribution amounts should be reported and paid to PERS and STRS immediately, and all future payments should be reported and paid on time.

A review of the financial trends and cost variances for the charter schools indicated that both schools face substantial fiscal challenges that will require making difficult decisions immediately to balance the budgets, pay all of the past due PERS and STRS contributions, and allow them to continue as a going concern.

Enrollment at both charter schools has decreased in 2008-09, and the historical average daily attendance (ADA) to enrollment ratios are lower than the statewide average for high schools. Because the majority of the charter schools' funding is based on ADA, it is imperative that ADA be increased or expenses be reduced.

Academia Calmecac's revenues exceeded expenditures each year after 2004-05, and the school has maintained a positive ending balance since that time. However, it is not clear

whether the entire PERS and STRS liabilities were recorded in the financial statements. If not, the charter school's fund balance will be reduced.

The large increase reported in other local revenue for 2008-09 had not yet been received as of the second interim reporting period. This item should be reviewed to ensure that funds will be received in 2008-09. Increases or decreases in annual revenues appear to have kept pace with annual expenses over time; however, this may be due largely to the increase in other local revenue reported in 2008-09.

El Portal Leadership Academy's revenues have exceeded expenditures in only two years since 2004-05; deficit spending occurred in the other three years. The charter school also reported a negative ending balance each year except 2008-09. As is the case with Academia Calmecac, it is not clear whether the entire PERS and STRS liabilities were recorded in the financial statements. If not, the charter school's fund balance will be reduced. The charter school has also reported a negative cash balance in each of the prior three years.

The charter school included large increases in unrestricted federal revenue and other local revenue in its 2008-09 second interim budget. These should be reviewed to ensure that the funds are unrestricted and that the projected amounts will be received in 2008-09.

MACSA provides all administrative services for the charter schools. MACSA staff indicated that one bank account is kept for the entire MACSA organization, including the two charter schools. Best practice would be for MACSA to maintain a separate bank account for each charter school to ensure that funds are not commingled.

Interviews with staff members at MACSA and the authorizing school districts did not reveal that charter school funds had been used for items unrelated to charter school expenses. However, the failure to make timely retirement system payments appears to be an illegal fiscal practice, and the failure to set the funds aside in a trust and, instead, use the funds to pay for operational costs is an apparent misappropriation of funds. The authorizing school districts and the county office should ensure that MACSA pays all past due PERS and STRS contributions immediately and reports and pays all future monthly contributions on time. In accordance with Education Code section 42638(b), action by the county superintendent shall include the following:

If the county superintendent determines that there is evidence that fraud or misappropriation of funds has occurred, the county superintendent shall notify the governing board of the school district, the State Controller, the Superintendent of Public Instruction and the local district attorney.

Subsequent Events

Following FCMAT's field work, the county office and MACSA reported that the El Portal Leadership Academy charter was rescinded by the authorizing school district in June, 2009. A resolution dated June 11, 2009 and adopted by the MACSA board of directors indicates that MACSA relinquished the El Portal Leadership Academy charter school. The county office and MACSA also reported that the Academia Calmecac charter was revoked by the authorizing school district effective June 30, 2009.

MACSA staff further indicated that all current and past due PERS and STRS contributions have been paid for employees of the El Portal Leadership Academy. All past due contributions have not been paid for employees of Academia Calmecac.

Findings and Recommendations

PERS and STRS Contributions

The California Public Employees' Retirement System (PERS) provides retirement benefits to eligible classified employees, and the California State Teachers' Retirement System (STRS) provides retirement benefits to eligible certificated employees, if their employers participate in these retirement systems. Education Code section 47605 gives charter schools the option to participate in these retirement programs. If a charter school chooses to provide this benefit for its employees, it must follow the regulations for each program in which it participates. The PERS regulations are included in Government Code sections 20000-22970, and the regulations for STRS are included in Education Code sections 22000-28101.

Payments for eligible STRS members include an 8% contribution from employees and an 8.25% contribution from employers on all creditable earnings. Payments for eligible PERS members include a 7% contribution from employees and an annual actuarially determined contribution from employers on all creditable earnings. The PERS contribution from employers was 9.306% for 2007-08 and 9.428% for 2008-09. The amounts withheld from employees' salaries are to be treated as a trust fund and deposited with STRS or PERS. Failure to pay the required contributions to PERS and STRS on time can result in late penalties and interest.

At its January 10, 2002 meeting, the MACSA board of directors adopted a resolution approving participation in PERS and STRS for the employees of El Portal Leadership Academy and Academia Calmecac charter schools.

The five-year renewal charter petition for the MACSA El Portal Leadership Academy, dated April 18, 2007, states the following on page 72:

Staff at MACSA El Portal Leadership Academy will participate in the federal social security system and will have access to other school-sponsored retirement plans according to policies developed by the Board of Directors and adopted as the school's employee policies. The school retains the option for its Board to elect to participate in the State Teachers Retirement System and/or Public Employees Retirement System and coordinate such participation as appropriate, with the social security system or other reciprocal systems in the future, should it find that participation enables the school to attract and retain a higher quality of staff.

MACSA El Portal Leadership Academy will enter into negotiations with the Santa Clara County Office of Education for STRS reporting services for the certificated employees of the school.

The charter petition for MACSA Academia Calmecac, dated December 1, 2005 (revised November 20, 2008), states the following on page 34:

Staff at MACSA Academia Calmecac will participate in the federal social security system and will have access to other school-sponsored retirement plans according to policies developed by the Board of Directors and adopted as the school's employee policies. The school retains the option for its Board to elect to participate in the State Teachers Retirement System and/or Public Employees Retirement System and coordinate such participation as appropriate, with the social security system or other reciprocal systems in the future, should it find that participation enables the school to attract and retain a higher quality of staff. MACSA Academia Calmecac will enter into negotiations with the Santa Clara County Office of Education for STRS reporting services for the certificated employees of the school.

Education Code section 47611.3 states the following:

- (a) At the request of a charter school, a school district or county office of education that is the chartering authority of a charter school shall create any reports required by the State Teachers' Retirement System and the Public Employees' Retirement System. The county superintendent of schools, employing agency, or school district that reports to those systems pursuant to Section 23004 of this code or Section 20221 of the Government Code shall submit the required reports on behalf of the charter school. The school district or county office of education may charge the charter school for the actual costs of the reporting services.

MACSA processes payroll for the employees of Academia Calmecac and El Portal Leadership Academy. MACSA staff members are responsible for submitting the employee earnings and PERS and STRS retirement information to each of the respective authorizing school districts, accompanied by payment for both the employee and employer contributions. The districts' payroll staff are then responsible for entering the employee earnings and retirement information into the financial accounting software and for ensuring that the information reported is monitored, accurate and on time. The county office audits the retirement information and then submits it to PERS and STRS with payment.

The applicable education code and government code sections provide the reporting and payment deadlines that must be followed and the penalties and interest that may be assessed if the deadlines are not followed. These requirements are also outlined in the PERS and STRS procedure manuals available online at <http://www.calpers.ca.gov/> and <http://www.calstrs.com/>, respectively.

Staff members from the East Side Union High School and Gilroy Unified school districts reported that retirement information for the charter schools is entered into the financial system and reported to PERS and STRS only when the charter schools submit the payroll report and payment of the contributions.

MACSA staff indicated that retirement contributions for the charter school employees were not made for several months because the schools were not meeting their enrollment and ADA projections and an ongoing lack of cash flow necessitated late payments for

items in addition to STRS and PERS. Staff also indicated that cash flow has been an ongoing issue for the entire MACSA organization and that MACSA had planned to sell a piece of property to meet its obligations. However, MACSA has been unable to sell the property because of the severe downturn in the real estate market.

When charter school employees became aware that the required retirement contributions were not being made to PERS and STRS, a grievance was filed. As a result of the grievance, MACSA agreed to a payment schedule that provides for payment of all current and past due contributions by the dates specified below for each charter school.

MACSA Academia Calmecac

The MACSA board of directors' meeting minutes dated March 12, 2009 indicate that the chief financial officer provided an update on STRS and PERS and state, "The payments for STRS and PERS (for AC) had been delayed from April 2007 through January 2009. It is MACSA's intent to repay all PERS and STRS employee contributions by March 31, 2009; and pay all PERS and STRS employer contributions by the end of September 2009."

East Side Union High School District staff verified that the last payment for STRS and PERS contributions was for March 2007 and was received by the district in February 2008.

In response to a grievance filed by an employee on June 27, 2008 regarding the nonpayment of retirement contributions and union dues, MACSA developed a payment plan for PERS and STRS. The payment plan indicated that \$249,909.76 was owed for contributions through January 2009, that MACSA would make monthly payments beginning in March 2009, and that all past due contributions would be paid by September 2009. However, MACSA and East Side UHSD staff members reported that no payments had been made as of May 12, 2009.

MACSA's accounts payable records indicate that the February 2009 contribution has been paid; however, payments have not yet been made for March and April 2009. This leaves a total balance owed of \$267,777.91 through April 2009.

A review of the fiscal year 2007-08 Benefits History – PERS Report revealed that an incorrect employer contribution rate was applied each month. Corrections should be made to indicate the rate of 9.306%. The fiscal year 2008-09 Benefits History – PERS Report also indicates that an incorrect rate was used for July 2008. This should be corrected to indicate the rate of 9.428%.

The annual independent audit for fiscal year 2007-08 did not recognize that the charter school had chosen to participate in the PERS and STRS retirement systems. A revised audit for 2007-08, presented by the audit firm on March 23, 2009, recognizes that the charter school has chosen to participate in PERS but does not recognize participation in STRS. The revised audit states the following:

The school contributes to the School Employer Pool under the California Public Employees' Retirement System (CalPERS); a cost-sharing multiple-employer public employer retirement system defined benefit pension plan administered by CalPERS. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by State statutes, as legislatively amended, within the Public Employees' Retirement Laws. A payable in the amount of \$172,885 was due at June 30, 2008.

The audits for fiscal years 2004-05, 2005-06 and 2006-07 recognize that the charter contributes to PERS; however, they do not recognize participation in STRS.

Based on the charter's fiscal year 2007-08 unaudited actuals report and annual independent audit, it is not known if the entire amount of unpaid contributions were included in the financial reports. The 2007-08 employer contribution was recognized as an expense. However, based on the information provided, FCMAT was not able to determine if the amount owed for 2006-07 and the amount withheld from the employees' pay were recognized as liabilities.

MACSA El Portal Leadership Academy

The MACSA board of directors' meeting minutes dated March 12, 2009 indicate that the chief financial officer provided an update on STRS and PERS and state, "The payments for PERS (for EPLA) had been delayed from October 2007 through January 2009. The payments for STRS (for EPLA) had been delayed from August 2007 through January 2009. MACSA is committed to paying all outstanding PERS and STRS employer contributions by the end of June 2009."

In response to a grievance filed by an employee on June 27, 2008 regarding the non-payment of retirement contributions and union dues, MACSA developed a payment plan for PERS and STRS. The payment plan indicated that \$140,139.85 was owed for contributions through January 2009, that MACSA would make monthly payments beginning in February 2009, and that all past due contributions would be paid by June 2009. As of May 12, 2009, the accounts payable records provided to FCMAT indicated that \$103,394.56 had been paid.

MACSA's accounts payable records indicate that the contributions for February and March 2009 have been paid, but not the contribution for April 2009. This leaves a total balance owed of \$41,400.01 through April 2009.

A review of the fiscal year 2007-08 Benefits History – PERS Report revealed that an incorrect employer contribution rate was applied each month. Corrections should be made to indicate the rate of 9.306%. The fiscal year 2008-09 Benefits History – PERS Report also indicates that an incorrect rate was used for July 2008. This should be corrected to indicate the rate of 9.428%.

The annual independent audit for fiscal year 2007-08 does not recognize that the charter school has chosen to participate in the PERS and STRS retirement systems. The audits for fiscal years 2004-05, 2005-06 and 2006-07 recognize that the charter school contributes to PERS; however, they do not recognize participation in STRS.

Based on the charter school's fiscal year 2007-08 unaudited actuals and annual independent audit, it is not known if the entire amount of the unpaid contributions was included in the financial reports. The 2007-08 employer contribution was recognized as an expense. However, based on the information provided, FCMAT was not able to determine if the amount withheld from the employees' pay was recognized as a liability.

Recommendations

The charter schools should:

1. Report service credit and pay the required employee and employer contributions to PERS and STRS on the required schedule.
2. Immediately pay all past due amounts owed to PERS and STRS. If PERS and STRS will not waive the penalties and interest accrued to date, the payment should include those costs.
3. Ensure that the correct employer contribution percentages for PERS have been applied at each payroll reporting period.
4. Ensure that all applicable financial reports recognize the liability for the unpaid PERS and STRS contributions.
5. Work with the county office and PERS and STRS to determine if a separate account can be established for each charter school so that retirement information can be reported directly to the county office.

If a separate account cannot be established, work with the authorizing school district to develop a system to ensure that payroll reports for each pay period are submitted to the district and that the district is monitoring submissions monthly.

The districts and county office should:

6. Take all steps necessary to ensure that MACSA pays all past due PERS and STRS contributions immediately and reports and pays all future monthly contributions in accordance with the required time lines.

The county superintendent should:

7. Notify the governing board of the charter school, the State Controller, the Superintendent of Public Instruction, and the local district attorney that retirement contributions have not been paid or set aside in a trust.

Financial Trends and Analysis

Financial planning is crucial for every local educational agency, regardless of its size or structure. Long-term financial planning helps a charter school strategically align its budget with its instructional goals and programs, and should be part of annual budget development. In addition, recognizing financial trends is essential to maintaining a charter school's fiscal health. Reviewing and analyzing year-over-year trends in key budget areas is helpful in evaluating the charter's budget direction and in highlighting possible areas of concern.

Fiscal year 2008-2009 has been an unprecedented budget year for California's local educational agencies. In November, the governor called for a special session when it became clear that financial projections showed a growing multibillion-dollar deficit. During the emergency session, the governor released the 2009-2010 proposed budget in December, a month earlier than normal.

On February 20, 2009, after months of delays, the governor signed a 17-month budget, Senate Sill (SB) 1, Chapter 1, Statutes of 2009, which runs through June 2010 and included revisions to the 2008-09 budget and approval of the 2009-10 state budget. The enacted budget is devastating to K-12 education, reducing education spending by \$8.6 billion over the next 17 months.

The enacted budget depended on the passage of several ballot measures that went before the voters on May 19, 2009. All failed with the exception of Proposition 1F. Therefore, the governor's May revise included further cuts to education funding. In July, the governor called for another special session to address the additional \$26 billion deficit in the state's budget.

Given these enacted and proposed cuts to education funding, it is critical that local education agencies monitor their spending and cash flow and make reductions as needed to maintain reserves and weather the state's fiscal crisis.

Because of the charter schools' outstanding PERS and STRS contributions, the county office of education requested that FCMAT review financial trends and cost variances for each of the charter schools. FCMAT reviewed Academia Calmecac's and El Portal Leadership Academy's unaudited actuals and annual independent audits for fiscal years 2004-05 through 2007-08 and the 2008-09 second interim reports. The review compared year-over-year trends in general fund revenues, expenditures, deficit spending, ending fund balance and ending cash balance.

Because the charter schools' primary funding is based on the total number of student attendance days, monitoring and projecting student enrollment and analyzing average daily attendance (ADA) are essential to budget planning. When enrollment and related ADA decline, the charter school must consider the effect on the budget and teacher-to-student ratios and plan accordingly. FCMAT reviewed the charters schools' enrollment and ADA for 2003-04 through 2008-09 and compared the October California Basic

Educational Data System (CBEDS) enrollment counts to the second period (P-2) principal apportionment as presented in the annual independent audit.

The tables below compare this data.

MACSA Academia Calmecac

Table 1: Enrollment/ADA for Academia Calmecac

	2004-05	2005-06	2006-07	2007-08	2008-09
CBEDS Enrollment*	142	191	205	207	190
P-2 ADA**	153	167	180	275	171.25
Gain/Loss - # of Students	16	49	14	2	-17
Gain/Loss - % of Students	12.70%	34.51%	7.33%	0.98%	-8.21%
Enrollment/ADA Ratio	107.75%	87.43%	87.80%	132.85%	90.13%

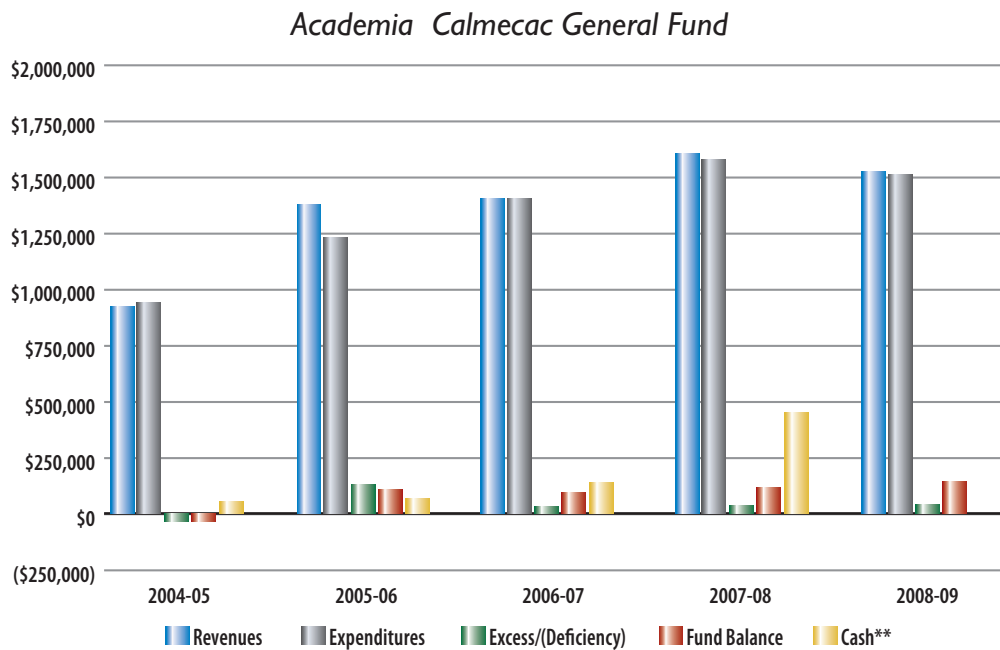
*Source: CDE Dataquest Web site

**Source: Annual Independent Audit; 2008-09 CDE

The Academia Calmecac's enrollment increased in the previous four years but declined by 8% in 2008-09. Because it is highly unusual for the P-2 ADA to be higher than the October CBEDS enrollment count, it appears that the audit report does not contain the correct ADA for 2004-05 and 2007-08. Excluding these two years, the school's average historical ADA is 88.45% of total enrollment. As reported by School Services of California (SSC), the 2006-07 statewide average ratio of ADA-to-enrollment for grades 9-12 was 91.56%. Thus the ratio for Academia Calmecac is less than the statewide average. Because the majority of the school's funding is based on ADA, it is essential to investigate all means of increasing ADA.

Table 2: Academia Calmecac General Fund

	2004-05	2005-06	2006-07	2007-08	2008-09*
Revenues	\$921,326	\$1,364,301	\$1,406,063	\$1,635,935	\$1,530,077
Expenditures	\$947,752	\$1,232,421	\$1,402,723	\$1,612,279	\$1,510,289
Excess/(Deficiency)	(\$26,426)	\$131,880	\$3,340	\$23,656	\$19,788
Fund Balance	(\$31,465)	\$100,415	\$103,755	\$127,411	\$129,923
Cash**	\$36,874	\$49,845	\$136,730	\$441,005	unknown



Source: Annual Independent Audit

*Source: Second Interim Report; report includes beginning balance that doesn't match prior year ending balance

**Source: Unaudited Actuals Report

A review of the charter school's revenues, expenditures, deficit spending, fund balance and cash balances from 2004-05 through the 2008-09 second interim reporting period indicates that revenues have exceeded expenditures in each year following 2004-05 and the school has maintained a positive ending balance since that time. However, based on the documentation received, it is not clear whether the entire liabilities for PERS and STRS have been recorded in the charter school's financial statements.

The charter school's unaudited actuals reports indicate that the cash balance at the end of each fiscal year has been positive. However, this could not be verified by the annual independent audit reports because cash was reported at zero for each fiscal year except 2007-08.

Table 3: Academia Calmecac General Fund – Variance Analysis

Description	2004-05	2005-06	2006-07	2007-08	2008-09*
Revenues					
State Aid	387,593.00	561,983.46	487,704.25	637,662.00	554,168.00
In Lieu of Property Taxes	488,969.00	656,404.00	749,273.21	677,572.00	527,741.00
Federal Revenue	10,240.00	104,776.00	111,501.00	97,361.00	98,000.00
Other State Revenue	23,613.90	30,407.14	57,044.50	216,250.27	100,168.00
Other Local Revenue	10,910.05	10,730.14	540.33	7,089.41	250,000.00
TOTAL REVENUES	921,325.95	1,364,300.74	1,406,063.29	1,635,934.68	1,530,077.00
Expenditures					
Certificated Salaries	504,246.95	576,266.85	595,131.03	835,785.59	590,086.00
Non-Certificated Salaries	131,488.54	168,714.54	257,901.99	92,137.85	223,818.00
Employee Benefits	170,789.64	208,241.38	256,989.91	280,666.50	274,934.00
Books and Supplies	73,045.02	39,290.34	44,157.80	36,325.41	43,304.00
Services and Other Operating Expenditures	55,007.18	237,054.88	247,208.89	367,363.13	378,147.00
Capital Outlay	0.00	0.00	0.00	0.00	0.00
Other Outgo	13,174.71	2,852.60	1,333.33	0.00	0.00
TOTAL EXPENDITURES	947,752.04	1,232,420.59	1,402,722.95	1,612,278.48	1,510,289.00
Other Financing Sources/Uses					
Transfers In	0.00	0.00	0.00	0.00	0.00
Transfers Out	0.00	0.00	0.00	0.00	0.00
Contributions	0.00	0.00	0.00	0.00	0.00
TOTAL, OTHER FINANCIAL SOURCES/USES	0.00	0.00	0.00	0.00	0.00
Net Increase/(Decrease) in Fund Balance	(26,426.09)	131,880.15	3,340.34	23,656.20	19,788.00
Fund Balance					
Beginning Fund Balance	74,961.00	(31,465.09)	100,415.06	103,755.40	110,135.01
Adjustments/Restatements	(80,000.00)	0.00	0.00	0.00	0.00
Total Ending Fund Balance	(31,465.09)	100,415.06	103,755.40	127,411.60	129,923.01

Source: Unaudited Actuals • *Source: Second Interim Report; report includes a beginning balance that doesn't match the prior year ending balance

A review of the above variance analysis indicates that the charter school reported a substantial increase in other state revenue in 2007-08. This appears to have been caused by a change in the reporting of revenue for the charter school's categorical block grant; in 2006-07 this revenue was included in state aid rather than in other state revenue. A large increase is also reported in other local revenue in 2008-09. Because these funds had not yet been received at the second interim reporting period, this item should be reviewed to ensure that funds will be received in 2008-09.

Expenses for the charter school include salaries and benefits for a school principal, nine teachers and five support staff members. Ten percent of the MACSA chief executive officer's salary and benefits and 7.4% of ADA funding are paid to MACSA for administrative services. Also, 1% of the general purpose and charter school block grant funding is paid to East Side UHSD for its oversight; this is in addition to a monthly lease payment for the use of school facilities.

The increase and/or decrease in annual revenues appears to have kept pace with the increase/decrease in annual expenses over time; however, this may be due in large part to the increase in other local revenue reported in 2008-09.

MACSA El Portal Leadership Academy

Table 4: Enrollment/ADA for El Portal Leadership Academy

	2004-05	2005-06	2006-07	2007-08	2008-09
CBEDS Enrollment*	168	140	181	164	158
P-2 ADA**	131	129	157	137.44	142.51
Gain/Loss - # of Students	35	-28	41	-17	-6
Gain/Loss - % of Students	26.32%	-16.67%	29.29%	-9.39%	-3.66%
Enrollment/ADA Ratio	77.98%	92.14%	86.74%	83.80%	90.20%

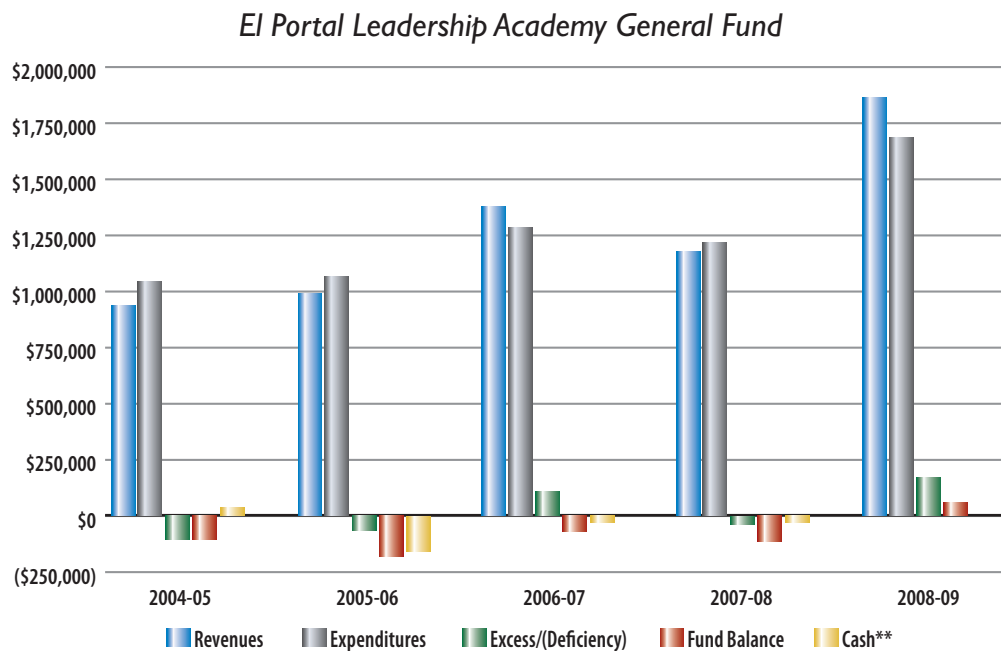
*Source: CDE Dataquest Web site

**Source: Annual Independent Audit; 2008-09 CDE

The El Portal Leadership Academy has experienced declining enrollment in three of the last five years, and an overall enrollment decline of 6% since 2004-05. The charter school's five-year historical ADA average is 86.17% of total enrollment. As reported by School Services of California (SSC), the 2006-07 statewide average ratio of ADA-to-enrollment for grades 9-12 was 91.56%. Thus the ratio for El Portal is significantly less than the statewide average. Because the majority of the school's funding is based on ADA, it is essential to investigate all means of increasing ADA.

Table 5: El Portal Leadership Academy General Fund

	2004-05	2005-06	2006-07	2007-08	2008-09*
Revenues	\$934,331	\$990,081	\$1,373,952	\$1,176,559	\$1,848,230
Expenditures	\$1,020,665	\$1,060,663	\$1,278,041	\$1,215,086	\$1,699,147
Excess/(Deficiency)	(\$86,334)	(\$70,582)	\$95,911	(\$38,527)	\$149,083
Fund Balance	(\$90,085)	(\$160,667)	(\$64,756)	(\$103,283)	\$45,800
Cash**	\$2,866	(\$137,067)	(\$13,803)	(\$16,732)	unknown



Source: Annual Independent Audit

*Source: Second Interim Report

**Source: Unaudited Actuals Report

A review of the charter school's revenues, expenditures, deficit spending, fund balance and cash balances from fiscal year 2004-05 through the 2008-09 second interim reporting period indicates that revenues exceeded expenditures in only two years. Deficit spending is shown in each of the other three years. The charter school has also reported a negative ending fund balance each fiscal year except 2008-09. In addition, based on the documentation received, it is not clear whether the entire liabilities for PERS and STRS have been recorded in the charter school's financial statements.

The school's unaudited actuals reports indicated that the cash balance has been negative at the end of three of the prior four fiscal years. However, this could not be verified by the annual independent audit reports because the cash balance was not reported in the audit prior to 2007-08.

Table 6: El Portal Leadership Academy General Fund – Variance Analysis

Description	2004-05	2005-06	2006-07	2007-08	2008-09*				
Revenues									
State Aid	309,829.00	86%	267,676.08	194%	520,079.00	66%	345,053.10	107%	369,043.00
In Lieu of Property Taxes	551,639.96	105%	576,790.34	111%	641,333.82	91%	584,844.25	102%	595,083.00
Federal Revenue	46,982.00	249%	117,212.00	106%	124,815.00	81%	100,660.00	346%	348,000.00
Other State Revenue	11,835.62	202%	23,924.96	347%	83,052.73	172%	143,147.55	60%	86,104.00
Other Local Revenue	14,044.23	32%	4,476.66	104%	4,671.69	61%	2,854.32	15766%	450,000.00
TOTAL REVENUES	934,330.81	106%	990,080.04	139%	1,373,952.24	86%	1,176,559.22	157%	1,848,230.00
Expenditures									
Certificated Salaries	504,541.06	91%	459,422.09	124%	571,098.50	110%	628,631.16	81%	510,138.00
Non-Certificated Salaries	129,153.41	102%	131,486.19	128%	168,633.37	40%	66,750.59	438%	292,073.00
Employee Benefits	184,758.52	99%	182,678.35	124%	226,208.79	97%	219,839.13	118%	259,479.00
Books and Supplies	42,226.39	92%	38,878.25	148%	57,638.34	60%	34,684.87	324%	112,482.00
Services and Other Operating Expenditures	92,863.27	263%	244,632.06	103%	252,795.14	105%	265,180.10	198%	524,975.00
Capital Outlay	0.00	0%	0.00	0%	0.00	0%	0.00	0%	0.00
Other Outgo	67,122.46	5%	3,565.76	47%	1,666.67	0%	0.00	0%	0.00
TOTAL EXPENDITURES	1,020,665.11	104%	1,060,662.70	120%	1,278,040.81	95%	1,215,085.85	140%	1,699,147.00
Other Financing Sources/Uses									
Transfers In	0.00		0.00		0.00		0.00		0.00
Transfers Out	0.00		0.00		0.00		0.00		0.00
Contributions	0.00		0.00		0.00		0.00		0.00
TOTAL, OTHER FINANCIAL SOURCES/USES	0.00		0.00		0.00		0.00		0.00
Net Increase/(Decrease) in Fund Balance	(86,334.30)		(70,582.66)		95,911.43		(38,526.63)		149,083.00
Fund Balance									
Beginning Fund Balance	96,249.26		(90,085.04)		(160,667.70)		(64,756.27)		(103,282.90)
Adjustments/Restatements	(100,000.00)		0.00		0.00		0.00		0.00
Total Ending Fund Balance	(90,085.04)		(160,667.70)		(64,756.27)		(103,282.90)		45,800.10

Source: Unaudited Actuals • *Source: Second Interim Report

The above variance analysis indicates that the El Portal Leadership Academy charter school reported a substantial increase in other state revenue in 2007-08. This appears to have been caused by a change in the reporting of revenue for the charter school's categorical block grant; in 2006-07 this revenue was included in state aid rather than in other state revenue. Large increases are also reported in federal revenue and other local revenue in 2008-09. The 2008-09 second interim report indicates that 70% of these funds had been received as of January 31, 2009, and that these increased funds are unrestricted. This information should be reviewed to ensure that these additional funds are unrestricted and that the projected amounts will be received in 2008-09.

The charter school's expenses include salaries and benefits for a school principal, eight teachers and one support staff member. As with the Academia Calmecac, 10% of the MACSA chief executive officer's salary and benefits and 7.4% of ADA funding are paid to MACSA for administrative services. In addition, 3% of the general purpose and charter school block grant funding is paid to the Gilroy Unified School District for its oversight and the use of its school facilities.

The charter school's 2008-09 second interim report indicates large increases in classified salaries, books and supplies, and services and other operating expenditures. While these increases appear to be driven by the increase in federal and local revenues, the expenditures should be reviewed to ensure that they are consistent with the provisions of the additional funding.

Going Concern

The term "going concern," means that an agency, business or organization is fiscally healthy and able to meet its financial obligations. When its fiscal health is suspect or it is deemed to have risk of insolvency, an organization is referred to as "not a going concern" or "lack of a going concern." Education Code section 42127.6, often referred to as the "going concern" section, was amended to include the provisions of AB 2756.

A review of the two charter school's financial trends indicates that MACSA will need to make difficult choices about which expenditures and programs to continue funding and which to scale back, reconfigure or eliminate so that it can balance the schools' budgets, pay all of the past due PERS and STRS contributions, and continue as a going concern. The charter schools face substantial fiscal challenges that will require them to make and implement difficult decisions immediately.

Financial Reporting

Education Code section 47604.33 states, in part, the following:

- (a) Each charter school shall annually prepare and submit the following reports to its chartering authority and the county superintendent of schools:
 - (1) On or before July 1, a preliminary budget.

- (2) On or before December 15, an interim financial report. This report shall reflect changes through October 31.
- (3) On or before March 15, a second interim financial report. This report shall reflect changes through January 31.
- (4) On or before September 15, a final unaudited report for the full prior year.

Although MACSA is completing these reports, a review of the 2007-08 and 2008-09 charter school board of directors' meeting minutes did not indicate that the reports were provided to the board for review and approval, nor did they indicate that the annual independent audits for the charter schools were presented to the board.

MACSA provides all administrative services for the charter schools. MACSA staff members indicated that one bank account is kept for the entire MACSA organization, including the two charter schools, and that funds are coded into the accounting system by division and program. Funds are then distributed throughout the entire organization as needed.

Page 67 of the charter petition for El Portal Academy charter school, dated April 18, 2007, states the following:

MACSA shall keep separate accounts for those funds received by the state and from other sources, which relate to the Academy. Any budget deficit will be covered by MACSA and all surpluses generated by the Academy will return directly to the Academy's account. El Portal Leadership Academy shall provide GUSD with quarterly reports, which will include MACSA El Portal Leadership Academy's financial information.

Page 31 of the charter petition for Academia Calmecac charter school, dated December 1, 2005, states the following:

MACSA shall keep separate accounts for those funds received by the state and from other sources, which relate to the Academy. Any budget deficit may be covered by MACSA and all surpluses generated by the Academy will return directly to the Academy's account. Academia Calmecac shall provide the District with monthly financial reports of the Academy.

Best practices would be for MACSA to maintain a separate bank account for each charter school to ensure that funds provided for these public schools are not commingled with funds for the parent organization's other programs.

Recommendations

The charter schools should:

1. Review budget variances on an on-going basis, and make budget adjustments as necessary.
2. Investigate methods to improve the ratio of ADA to enrollment.
3. Review the projected increases in federal and other local revenue for fiscal year 2008-09 to ensure that they are accurate and that the funds are unrestricted.
4. Ensure that the cash balance for each charter school is included in that school's annual independent audit.
5. Make and implement the decisions necessary to ensure that each charter school is able to continue as a going concern.
6. Present all required state budget reports and the annual independent audit to the board of directors for approval within the required time lines.
7. Consider keeping a separate bank account for each charter school.

Appendix A

Study Agreement

FCMAT

FISCAL CRISIS & MANAGEMENT
ASSISTANCE TEAM

CSIS California School Information Services

FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM AB 139 SERVICES AGREEMENT *April 16, 2009*

The FISCAL CRISIS AND MANAGEMENT ASSISTANCE TEAM (FCMAT), hereinafter referred to as the Team, and the Santa Clara County Office of Education, hereinafter referred to as the COE, mutually agree as follows:

1. BASIS OF AGREEMENT

The Team provides a variety of services to school districts and county offices of education upon request. Based on the provisions of Education Code Section 1241.5 (c), a County Superintendent of Schools may review or audit the expenditures and internal controls of any charter school in his or her county if he or she has reason to believe that fraud, misappropriation of funds, or other illegal fiscal practices have occurred that merit examination. The review or audit conducted by the county superintendent shall be focused on the alleged fraud, misappropriation of funds, or other illegal fiscal practices and shall be conducted in a timely and efficient manner.

The COE has requested that the Team provide for the assignment of professionals to study specific aspects of the MACSA Academia Calmecac and El Portal Leadership Academy charter schools. These professionals may include staff of the Team, County Offices of Education, the California State Department of Education, school districts, or private contractors. All work shall be performed in accordance with the terms and conditions of this Agreement.

2. SCOPE OF THE WORK

A. Scope and Objectives of the Study

The scope and objectives of this study pursuant to the provisions of Education Code Section 1241.5 (c):

- 1) The COE requests the Team to conduct a review of the business practices of two direct funded charter schools, the MACSA Academia Calmecac, sponsored by the East Side Union High School District, and the MACSA El Portal Leadership Academy, sponsored by the Gilroy Unified School District. Specifically, the review is requested to determine if there is evidence of illegal fiscal practices or misappropriation of employee CalPers and CalSTRS payroll deductions.

It is alleged that approximately \$400,000 in employee deductions (\$150,000 for the Gilroy sponsored charter and \$250,000 for the East Side sponsored charter employees) have not been processed and sent to the retirement agencies for a period in excess of one year; and that the employer portion has also not been processed. It is alleged that MACSA, the Mexican American Community Services Agency has used the retirement contributions to pay operating costs.

The Team's review will verify whether there is sufficient evidence of illegal fiscal practices or misappropriation in the processing of payrolls and handling of employee deductions and employer contributions for the county superintendent to contact local law enforcement for further investigation.

B. Services and Products to be Provided

- 1) Orientation Meeting - The Team will conduct an orientation session with the COE/Charter/District(s) to brief COE/Charter/District(s) management and supervisory personnel on the procedures of the Team and on the purpose and schedule of the study, if requested.
- 2) On-site Review - The Team will conduct on-site visits to the appropriate sites to conduct interviews and gather documentation relevant to the scope of work. The Team will continue to review pertinent documents off-site.
- 3) Progress Reports - The Team will inform the COE of material issues as the review is performed.
- 4) Draft Reports - Sufficient copies of a preliminary draft report will be delivered to the COE administration for review and comment.
- 5) Final Report - Sufficient copies of the final report will be delivered to the COE following completion of the review.
- 6) Follow-Up Support - Subsequent to the completion of the study, the Team will meet with the COE as requested by the COE to discuss the findings and recommendations of the report

3. PROJECT PERSONNEL

The study team will be supervised by Anthony L. Bridges, Deputy Executive Officer, Fiscal Crisis and Management Assistance Team, Kern County Superintendent of Schools Office. The study team may also include:

- A. Diane Branham, FCMAT Fiscal Intervention Specialist
- B. Debi Deal, FCMAT Fiscal Intervention Specialist

Other equally qualified FCMAT staff or independent consultants will be substituted in the event one of the above noted individuals is unable to participate in the study.

4. PROJECT COSTS

The cost for studies requested pursuant to E.C. 1241.5 (c) shall be:

- A. A daily rate of \$1,100 per Team member to complete the scope of work listed in section 2 A.
- B. The estimated cost of the study is \$22,000 for up to ten (10) days of services by each Team member. The COE will be invoiced for the actual number of full and/or partial days necessary to complete the review, with 50% of the cost due following the completion of the on-site review and the remaining amount due upon acceptance of the final report by the COE.
- C. Any change to the scope will affect the cost estimate, and will be documented in an amended agreement. The COE will be notified if, for reasons outside the control of the Team, additional days charged at the agreed upon daily rate are necessary. Advance approval in writing by the COE and FCMAT for additional days to complete the review is required.
- D. The COE is eligible for 100% reimbursement of its expenditures for an AB 139 review. The procedure to file a claim is posted on FCMAT's website at www.fcmat.org and all claims are subject to approval by the California Department of Education and Department of Finance.

Payments for FCMAT services are payable to Kern County Superintendent of Schools-Administrative Agent.

5. RESPONSIBILITIES OF THE COE

- A. The COE will provide office and conference room space while on-site reviews are in progress.
- B. The COE will provide the following (if requested):
 - 1) A map of the local area
 - 2) Existing policies, regulations and prior reports addressing the study

- request
- 3) Current organizational charts
- 4) Current and four (4) prior year's audit reports
- 5) Any documents requested on a supplemental listing

C. The COE Administration will review a preliminary draft copy of the study. Any comments regarding the accuracy of the data presented in the report or the practicability of the recommendations will be reviewed with the Team prior to completion of the final report.

Pursuant to EC 45125.1(c), representatives of FCMAT will have limited contact with District pupils. The COE shall take appropriate steps to comply with EC 45125.1(c).

6. PROJECT SCHEDULE

The following schedule outlines the planned completion dates for key study milestones:

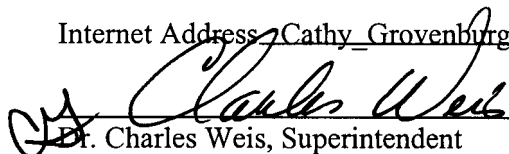
Orientation:	(estimated) First week of May 2009
Staff Interviews:	To be determined
Exit Interviews:	To be determined
Preliminary Report Submitted	To be determined
Final Report Submitted	To be determined
Board Presentation	To be determined

7. CONTACT PERSON

Please print name of contact person: Cathy Grovenburg.
Assistant Superintendent, Business Services

Telephone (408) 453-6832 FAX (408) 453-6571

Internet Address: Cathy_Grovenburg@sccoe.org

 4/20/09
 Dr. Charles Weis, Superintendent Date
 Santa Clara County Office of Education



April 16, 2009

Barbara (Dean) Murphy, Deputy Administrative Officer Date
 Fiscal Crisis and Management Assistance Team