

CALIFORNIA VIRTUAL ACADEMIES AND INSIGHT SCHOOLS OF CALIFORNIA

Audit Report

July 1, 2014, through June 30, 2016



BETTY T. YEE
California State Controller

October 2017



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California State Controller

October 9, 2017

The Honorable Tom Torlakson
Superintendent of Public Instruction
California Department of Education
1430 N Street
Sacramento, CA 95814

Dear Superintendent Torlakson:

The State Controller's Office audited 14 charter schools—11 California Virtual Academies and three Insight Schools of California (together, CAVA)—for the period of July 1, 2014, through June 30, 2016, to verify whether CAVA: (1) complied with its contractual agreements with authorizing entities; (2) accurately reported attendance, enrollment, and cohort dropout/graduation outcome data results to the California Department of Education (CDE); (3) appropriately allocated and reported shared expenses; (4) appropriately identified, accounted for, and disclosed related-party relationships and transactions in its independent audit report; and (5) is organizationally independent from K12 Inc.

Our audit identified no issues regarding enrollment and cohort dropout/graduation outcome data reported to the CDE, disclosure of related-party relationships and transactions in the schools' independent audit reports, or allocation of shared expenses reported to the CDE.

Our audit did not find any issues related to CAVA's organizational independence from K12 Inc. that were not previously addressed in the July 8, 2016 settlement agreements that the 14 schools entered into with the California State Attorney General. To that point, in the course of our audit fieldwork, we determined that CAVA and K12 Inc. were not organizationally independent during the audit period. Specifically, we found that CAVA assigned significant authority to a K12 Inc. employee, that the fee structure CAVA agreed to with K12 Inc. bound the entities together, and that CAVA agreed to provide check-writing authority to K12 Inc., among other issues. However, as previously indicated, the settlement agreement addressed each of the issues we identified. For example, the agreement required that no CAVA employees report to any K12 Inc. employees, that CAVA and K12 Inc. modify their fee structure, and that K12 Inc. remove itself from check-writing authority over CAVA's bank accounts.

Our audit found that CAVA did not fully comply with the schools' contractual agreements with authorizing entities, lacked sufficient documentation to support that pupil attendance was accurately reported to the CDE, lacked sufficient documentation to support satisfactory progress of students between 19 to 22 years old, and may have miscalculated its pupil-teacher ratio.

Our audit also identified issues that were not specifically defined in the audit objectives, but were related. These issues are discussed in the Observations section of this report.

If you have any questions, please contact Jim L. Spano, CPA, Assistant Division Chief, by telephone at (916) 323-5849.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/rg

cc: Kimberly Tarvin, Director
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Audit Report

Summary

The State Controller's Office (SCO) audited 14 charter schools—11 California Virtual Academies and three Insight Schools of California (together, CAVA)—for the period of July 1, 2014, through June 30, 2016, to verify whether CAVA: (1) complied with its contractual agreements with authorizing entities; (2) accurately reported attendance, enrollment, and cohort dropout/graduation outcome data results to the California Department of Education (CDE); (3) appropriately allocated and reported shared expenses; (4) appropriately identified, accounted for, and disclosed related-party relationships and transactions in its independent audit report; and (5) is organizationally independent from K12 Inc.

Our audit identified no issues regarding enrollment and cohort dropout/graduation outcome data reported to the CDE, disclosure of related-party relationships and transactions in the schools' independent audit reports, or allocation of shared expenses reported to the CDE.

Our audit did not find any issues related to CAVA's organizational independence from K12 Inc. that were not previously addressed in the July 8, 2016 settlement agreements the 14 schools entered into with the California State Attorney General.

However, our audit found that CAVA did not fully comply with the schools' contractual agreements with authorizing entities, lacked sufficient documentation to support that pupil attendance was accurately reported to the CDE, lacked sufficient documentation to support satisfactory progress of students between 19 to 22 years old, and may have miscalculated its pupil-teacher ratio.

Our audit also identified issues that were not specifically defined in the audit objectives, but were related. These issues are discussed in the Observations section of this report.

Background

CAVA is a group of online charter schools that operate in 45 of California's 58 counties. CAVA offers an online educational alternative to a traditional brick-and-mortar school building. This learning environment provides students an online curriculum through which they can receive assignments, complete lessons, and interface with teachers through a computer or telephone.

CAVA schools are organized as non-profit public-benefit corporations; its first schools began operations in 2002. Each school's charter is authorized by a school district (authorizing entity) and governed by a separate board of directors. However, the schools operate collectively by sharing teachers, administrators, and some costs.

In fiscal year (FY) 2015-16, CAVA consisted of 14 charter schools: eight independent charter schools and three management organizations (MO), each with two charter schools. The 14 charter schools are as follows:

- CAVA @ Fresno
- CAVA @ Jamestown
- CAVA @ Kings
- CAVA @ Los Angeles
- CAVA @ Maricopa
- CAVA High @ Maricopa
- CAVA @ San Diego
- CAVA @ San Joaquin
- CAVA @ San Mateo
- CAVA @ Sonoma
- CAVA @ Sutter
- Insight @ Los Angeles
- Insight @ San Diego
- Insight @ San Joaquin

The three MOs consisted of: (1) CAVA @ Los Angeles and Insight at Los Angeles; (2) CAVA @ Maricopa and CAVA High @ Maricopa; and (3) CAVA @ San Diego and Insight @ San Diego.

In FY 2014-15, there were only 13 charter schools (seven independent charter schools) as Insight @ San Joaquin did not begin operations until the 2015-16 school year.

CAVA is funded principally through State of California public education funds. The State allocates funding based on CAVA's self-reported average daily attendance (ADA) for a designated period during the school year. CAVA calculates its ADA by dividing the total days of attendance reported for each student during the period by the total number of students enrolled during the period. Although CAVA is an online program, students may generate attendance only on school days as indicated by CAVA's academic calendar, and may earn only one day's attendance per calendar day, regardless of the hours spent or amount of work performed.

Each school has contracted with K12 Inc. as its sole curriculum provider, and the schools pay K12 Inc. an annual per-student fee for this curriculum. The schools also purchase management, accounting, operational, and recordkeeping services from K12 Inc.

K12 Inc. charges CAVA schools throughout each fiscal year for educational products and services. At the end of each fiscal year, K12 Inc. allows the schools to reduce expenses in the amount equal to the schools' spending deficit to prevent the schools' net assets from having a negative balance. As a result of this fee structure arrangement, "balanced budget credits" were accumulated by the schools. On July 8, 2016, a California Superior Court approved the settlement agreement between the California Department of Justice and K12 Inc. that expunged all CAVA schools' balanced budget credits, totaling approximately \$160 million that the

schools incurred from 2005 through 2016. K12 Inc. also agreed to expunge all balanced budget credits incurred by any of the CAVA schools at the end of every subsequent year.

CAVA maintains an administrative office, located in Simi Valley, which is responsible for the operation of the 14 charter schools. The administrative office's functions include the collecting, compiling, and reporting of attendance, enrollment, dropout, and graduation data to the CDE; developing agendas for board meetings; coordinating audits; and storing and compiling student records. One individual, to whom each school's board of directors has delegated authority, has oversight responsibilities for the 14 charter schools. During the audit period, this individual was the Head of Schools, an employee of K12 Inc. The schools' agreement with K12 Inc. that created this position designated the Head of Schools to function as the superintendent for all 14 CAVA schools during the audit period.

Objectives, Scope, and Methodology

The objectives of our audit were to determine whether CAVA: (1) complied with its contractual agreements with authorizing entities; (2) accurately reported attendance, enrollment, and cohort dropout/graduation outcome data results to the CDE; (3) appropriately allocated and reported shared expenses; (4) appropriately identified, accounted for, and disclosed related-party relationships and transactions in its independent audit report; and (5) is organizationally independent from K12 Inc.

We conducted this performance audit of CAVA for the period of July 1, 2014, through June 30, 2016, to address specific concerns identified by the CDE.

To achieve our audit objectives, we performed the following procedures in reference to the five bolded objectives:

Determine whether the CAVA schools complied with their contractual agreements with authorizing entities

- Reviewed the independent audit reports and note disclosures of each CAVA school to assess organization structure, financing arrangements, and potential related-party activities as applicable;
- Conducted site visits of the 14 authorizing entities;
- Reviewed signed contractual documentations, agreements, and amendments between CAVA schools and K12 Inc.;
- Reviewed each Memorandum of Understanding (MOU) between the CAVA schools and their authorizing entities to gain an understanding of the authorizing entities' processes and controls related to approval and oversight responsibilities for charter schools; and
- Verified compliance with the MOUs by: (1) identifying significant terms within each MOU and (2) assessing whether CAVA fulfilled the terms as stated in the MOU.

Determine whether the CAVA schools accurately reported attendance, enrollment, and cohort dropout/ graduation outcome data results to the CDE

- Interviewed CAVA staff and reviewed training materials provided to teachers to gain an understanding of processes and controls established by individual charter schools to accurately report attendance, enrollment, and cohort dropout/graduation outcome data results to the CDE; and
- Verified the accuracy of attendance, enrollment, dropout, and graduation data reported to the CDE by: (1) obtaining and reviewing a sample of independent study agreements; (2) verifying that charter schools maintained documentation supporting compliance with such agreements; and (3) verifying that the above data reported to the CDE is supported.

Determine whether the CAVA schools appropriately allocated and reported shared expenses

- Interviewed CAVA staff and reviewed shared expenses to gain an understanding of processes and controls established by CAVA to ensure that shared costs, such as teacher salaries, rent, and utilities, were appropriately allocated and reported among the charter schools; and
- Assessed whether shared expenses were appropriately allocated and reported by individual charter schools.

Determine whether the CAVA schools appropriately identified, accounted for, and disclosed related-party relationships and transactions in its independent audit report

- Interviewed CAVA staff and requested CAVA's policies and procedures regarding processes and controls established by individual charter schools to: (1) identify, account for, and disclose related-party relationships and transactions; and (2) authorize and approve significant transactions and arrangements with related parties and transactions outside the normal course of business; and
- Reviewed whether all related-party relationships and transactions were properly identified and disclosed in the independent audit reports.

Determine whether the CAVA schools are organizationally independent from K12 Inc.

- Reviewed contractual agreements that individual charter schools have with K12 Inc. for: (1) curriculum and instructional materials; (2) administrative and technology services; (3) management services; (4) accounting services; (5) operations services; and (6) record-keeping services;

- Assessed the organizational independence of individual charter schools and K12 Inc. by identifying, reviewing, and comparing key personnel and their roles at CAVA, at CAVA boards of directors, and at K12 Inc.; and
- Assessed potential conflicts of interest in the contractual agreements between individual charter schools and K12 Inc. for services identified on the previous page.

The legal authority to conduct this audit is provided by interagency agreement CN 150487 between the CDE and the SCO dated June 17, 2016. We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We limited our review of the internal controls to understanding processes and controls related to the five objectives necessary to develop appropriate auditing procedures. Our audit scope did not assess the efficiency or effectiveness of program operations. We did not audit the financial statements of the CAVA schools.

Conclusion

Our audit identified no issues regarding enrollment and cohort dropout/graduation outcome data reported to the CDE or allocation of shared expenses reported to the CDE.

Our audit also did not identify any related-party relationships and transactions that were not disclosed in the charter schools' independent audit reports. Although we did not identify any additional transactions that should have been reported, related-party transactions could exist that we did not identify.

Our audit did not find any issues related to CAVA's organizational independence from K12 Inc. that were not previously addressed in the July 8, 2016 settlement agreements the 14 schools entered into with the California State Attorney General.

However, our audit found that CAVA did not fully comply with the schools' contractual agreements with authorizing entities, lacked sufficient documentation to support that pupil attendance was accurately reported to the CDE, lacked sufficient documentation to support satisfactory progress of students between 19 to 22 years old, and may have miscalculated its pupil-teacher ratio.

Our audit did find instances of noncompliance with the requirements outlined in the Objectives section. These instances are described in the accompanying Findings and Recommendations section of this report.

Our audit also identified issues that were not specifically defined in the audit objectives, but were related to them. These issues are discussed in the Observations section.

**Views of
Responsible
Officials**

We issued a draft report on June 2, 2017. Lisa A. Corr, Esq., on behalf of CAVA, responded by letter dated June 12, 2017, disagreeing with the audit results. This final audit report includes CAVA's response.

Restricted Use

This report is solely for the information and use of CAVA, the CDE, the California Department of Finance, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

October 9, 2017

Findings and Recommendations

**FINDING 1—
Inaccurate calculation
of supervisory
oversight fees the
schools paid to
authorizing entities**

Each school entered into an MOU with its authorizing entity in which it agreed to pay between 2% and 3% of total revenues for supervisory oversight. The MOUs between the schools and their authorizing entities did not clarify the specific revenue sources used in calculating the oversight fees. Based on CAVA’s calculation, the schools understated the oversight fees paid to the authorizing entities for the audit period by \$64,000 (\$3,971 understatement in FY 2014-15 and \$60,029 understatement in FY 2015-16).

CAVA provided us with a worksheet that reconciled the calculation of the oversight fees. The worksheet showed inconsistencies between amounts calculated and revenues reported by the schools.

The specific revenues used in the calculations varied between the schools. CAVA’s worksheet shows that the fees were calculated using the following revenue sources:

- For nine of the 13 schools in FY 2014-15 and 10 of the 14 schools in FY 2015-16: revenue limit state aid, in-lieu property taxes, and education protection account
- For two of the schools: revenue limit state aid and education protection account
- For one of the schools: revenue limit state aid, in-lieu property taxes, education protection account, Lottery-restricted, and Lottery-unrestricted
- For one of the schools: revenue limit state aid, in-lieu property taxes, education protection account, one-time mandate grant, and mandated block grant

CAVA indicated that it relied on the calculations of the authorizing entities, which may have had their own interpretations of the revenue sources. CAVA further indicated that CAVA @ San Diego and Insight @ San Diego appear to have miscalculated the amounts CAVA owed, and that CAVA paid these schools according to these miscalculations.

The dollar variances identified above are not significant, but are indicative that billings may not be adequately monitored.

In an email dated April 4, 2017, for FY 2016-17 and after, the CAVA schools agreed to “establish a reconciliation process for review of each of the oversight invoices provided by each charter authorizer to ensure alignment with the MOUs and ensure that payments equal the contractual amounts approved in the MOUs between the parties.”

With the exception of the discussion above and the issue identified in Observation 2, we found that CAVA generally complied with the terms of the MOUs.

Recommendation

We recommend that the CAVA schools follow up to ensure that they establish a reconciliation process for the supervisory oversight fee billings to ensure the accuracy of the calculations.

CAVA's Response

The Charter Schools paid all amounts due as requested via invoice generated by each charter authorizer ("Authorizers"). The slight underpayment of fees per the MOU's spread across all the Charter Schools was approximately 1% of the total amount invoiced by the Authorizers. This difference is immaterial under auditing standards. Moreover, as a matter of law, the Charter Schools and their authorizing school districts are not required to pursue enforcement for such immaterial discrepancies. Such non-enforcement of the MOU is not a violation of law and thus not a basis for an audit finding.

SCO's Comment

Auditing standards allow us to include significant matters in our audit findings. The underpayment is significant because it represents a potential lack of oversight.

Section 6.04 of the Government Auditing Standards states, in part:

The concept of significance assists auditors throughout a performance audit, including when... developing the report and related findings and conclusions. Significance is defined as the relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors. Such factors include the magnitude of the matter in relation to the subject matter of the audit, the nature and effect of the matter, the relevance of the matter, the needs and interests of an objective third party with knowledge of the relevant information, and the impact of the matter to the audited program or activity.

FINDING 2— Lack of sufficient documentation to support claimed average daily attendance

CAVA does not maintain adequate documentation to support attendance claimed for all students. The schools claimed some attendance without evidence of daily engagement or judgement by a certificated employee of the time value of work produced.

Teachers determine ADA by reviewing the amount of time students log into the K12 Inc. school software, as well as time the students' learning coaches self-report. The K12 Inc. software, On-Line School (OLS), automatically records the amount of time a student spends logged into the system. Learning coaches self-report offline work in a separate system that the teachers can review. Time logged in both systems is compiled into a separate system where teachers can certify that each day of attendance represented by the time values is eligible to be claimed as ADA. Teachers verify that the amount of time reported in this system is supported by work produced by reviewing activity reported in the students' Progress Tracker.

From the spreadsheets CAVA prepared to calculate ADA, we selected a sample of 289 students (152 from FY 2014-15 and 137 from FY 2015-16) and evaluated whether the attendance reported for the student was

supported by hours logged into the OLS and daily activity identified on the Progress Tracker report. We noted that attendance for 40 students (23 in FY 2014-15 and 17 for FY 2015-16) was not supported by evidence of daily engagement or students' work samples (points earned in the Progress Tracker). These students had no hours or very few hours logged into the system and had earned few or no points in the Progress Tracker. CAVA's attendance records did not explain the disparities.

Training materials CAVA provided to teachers instructed them to document a description of the work reviewed and whether or not it justifies awarding a day's worth of attendance. We reviewed this documentation, but were unable to verify attendance without additional support. We requested documentation to support the teachers' determination of the time value of schoolwork for each student; however, we received no additional documentation.

Education Code section 47612.5(a)(2) states that charter schools shall "maintain written contemporaneous records that document all pupil attendance and make these records available for audit and inspection."

Education Code section 51747.5(b) states that charter schools "may claim apportionment credit for independent study only to the extent of the time value of pupil work products, as personally judged in each instance by a certificated teacher."

The documentation CAVA provided us did not support the teachers' determination of ADA.

Recommendation

We recommend that CAVA maintain attendance documents to support claimed ADA.

CAVA's Response

The Charter Schools reached a Settlement Agreement with the California Attorney General's Office (CA-AG) which addressed the attendance documentation issue raised in Finding 2. The Charter Schools maintain contemporaneous records of attendance as required by Title 5 Section 11960 of the California Code of Regulations ("daily engagement") and the time value of the student's work product as personally judged by the credentialed teacher as required by Education Code Section 51747.5 ("time value"). The law does not provide any required form of documentation of "daily engagement" or "time value". In fact, the CDE, in its independent study manual fails to even provide a sample contemporaneous record of attendance.

Teachers at the Charter Schools utilize activity reports to determine daily engagement (days where the student engaged in an educational activity required by the school on days that the school is actually taught at the school). The Charter School teachers then personally judge the time value of the work produced by the student over the attendance period, which will result in a reduction in attendance if the time value is not equal to the days of daily engagement. Ultimately, the teachers are trained to take the lower of the "daily engagement" or the "time value" in determining the days of attendance. Accordingly, the Charter School

meets the legal requirements established by Section 11960 of Title 5 of the California Code of Regulations and Education Code Section 51747.5 for claiming student attendance in a nonclassroom-based charter school.

The Charter Schools' attendance procedures also directly align with Section 6(g) of the Settlement Agreement with the CA- AG that requires "CAVA teachers to examine the "time value" of the student's work products over the whole learning period. Teacher must report the lower value as between the number of days of daily engagement and the number of days of time value."

SCO's Comment

Our finding does not concern CAVA's process of determining attendance, but rather the attendance CAVA assigned to specific students whose records we reviewed. We found a number of instances in which the documentation supporting students' attendance did not agree with the attendance CAVA claimed. For example, we found some instances in which a student's total progress throughout the academic period was unreasonably low when compared to the total attendance CAVA claimed, with no explanation for the disparities. In other instances, we noted that the days of attendance CAVA claimed were not supported by evidence of a student's daily engagement on instructional days, either in the online system or in learning coach logs, with no teacher explanation to justify attendance on these days. CAVA did not provide us with any documentation showing how the teachers made attendance determinations in these instances.

In our finding, we discuss 40 students for whom CAVA did not maintain sufficient documentation to support daily engagement. We determined this figure by evaluating attendance records over a one-month period for one percent of all CAVA students who reported attendance during that period. During this period, CAVA claimed 363 days of attendance with no documentation supporting student activity. The students did not log into the online school, their learning coaches did not report offline activity, and the teachers did not note any other daily engagement. For the attendance records reviewed, ADA was overstated by 1.53 in FY 2014-15 and 1.49 in FY 2015-16. We did not extrapolate the overstated ADA to the total ADA that CAVA claimed for these students during the audit period, or for students whose attendance records we did not review.

FINDING 3— Lack of sufficient documentation to support satisfactory progress of students between 19 and 22 years old

CAVA claimed ADA for students 19 years of age and older, yet it did not provide evidence that the students are making satisfactory progress toward obtaining a diploma.

CAVA did not provide us documentation supporting that it has a system in place to monitor students 19 years of age and older to ensure satisfactory progress toward a diploma. Although CAVA teachers provide academic support to struggling students and track each student's progress, CAVA guidelines to teachers for reporting attendance do not mention the potential disallowance of attendance for students who are not making progress. We requested CAVA's policy regarding students making satisfactory progress toward a diploma, but did not receive any such policy.

We noted that two students 19 years of age or older were classified as grade 12 students for four years. For example, we noted that:

- For FY 2014-15, CAVA @ Kings claimed attendance for a pupil over 22 years old who was enrolled in grade 12 for 4 ½ years.
- For FY 2015-16, CAVA @ Kings claimed attendance for a 22-year-old pupil who had enrolled in CAVA in September 2008, eight years earlier, at 14 years 5 months old.

CAVA staff provided us with the ultimate disposition of the two students noted above, showing that one graduated and one withdrew from the school. However, CAVA did not provide us with documentation showing that teachers monitored these students to ensure that the students made satisfactory progress throughout their tenures.

Education Code section 47612(b) states:

. . . to remain eligible for generating charter school apportionments, a pupil over 19 years of age shall be continuously enrolled in public school and make satisfactory progress towards award of a high school diploma.

Title 5, *California Code of Regulations*, section 11965(h) defines satisfactory progress as:

For each charter school, “satisfactory progress,” as that term is used in Education Code section 47612, means uninterrupted progress (1) towards completion, with passing grades, of the substance of the course of study that is required for graduation from a non-charter comprehensive high school of the school district that authorized the charter school’s charter, that the pupil has not yet completed, (2) at a rate that is at least adequate to allow the pupil to successfully complete, through full-time attendance, all of that uncompleted coursework within the aggregate amount of time assigned by the chartering agency for the study of that particular quantity of coursework within its standard academic schedule. If the chartering authority is not a school district having at least one non-charter comprehensive high school, the applicable high school graduation requirements and associated time assignments shall be those for the comprehensive high school(s) of the largest unified school district, as measured by average daily attendance, in the county or counties in which the charter school operates.

Recommendation

We recommend that CAVA update its attendance reporting guidelines to ensure that it claims apportionment for students between the ages 19 and 21 only when those students show measurable progress toward graduation.

CAVA’s Response

The SCO provides no facts to support its finding that the Charter Schools fail to monitor students to ensure that they are making satisfactory progress toward high school graduation. Indeed, to the contrary, the record demonstrates the graduation of pupils over the age of 19 and/or the withdrawal of students failing to pass courses that are required for graduation. The SCO fails to provide any law which requires the adoption of a formal policy or guidelines regarding students over the age

of 19. In fact, the regulations sufficiently address the definition of “satisfactory progress” and the Charter Schools align their practices accordingly.

During the enrollment process, the Charter Schools verify that the student has maintained continuous enrollment in a public school after the age of 18 via the student’s transcript. Supervising and homeroom teachers are continuously monitoring those students that are not making progress. Counselors also notify the lead guidance counselor if they have a student that is over-age and not making satisfactory progress. In addition, the Charter Schools tracker notes all 5th year seniors and monitors them closely to ensure that they would have the ability to graduate by age 22.

SCO’s Comment

As CAVA did not have any policies for monitoring satisfactory progress of students between the ages of 19 and 22—which we acknowledge are not required—we sought to evaluate CAVA’s actual monitoring of these students. CAVA provided us with the ultimate outcome for students in this age group, but did not provide any documentation that teachers or any other CAVA staff actively monitored these students to ensure they were making satisfactory progress. Therefore, we are unable to conclude that CAVA did so.

FINDING 4— Pupil-teacher ratio may have been inaccurately calculated

CAVA claimed employees working less than 175 days as full-time equivalent (FTE) instead of calculating FTE on a proportional basis. To accurately calculate its pupil-teacher ratio, the schools should have considered FTE teachers on a proportional basis so that each teacher was represented in the ratio only to the extent that he or she worked at the school throughout the entire reporting period. The calculation used by the schools increases the risk of noncompliance with state law.

We compared the teachers represented in the schools’ pupil-teacher ratios with payroll records and found that 112 teachers were not employed for at least 175 days during our audit period, but were counted as FTE. These teachers should have been counted only as partial FTE in calculating the pupil-teacher ratio. In FY 2014-15, 63 employees who were not employees as of November 30, 2015, but hired prior to March 30, 2016, were claimed as FTE. During FY 2015-16, 49 employees who were not employees as of November 30, 2015, but hired prior to March 30, 2016, were claimed as FTE.

Title 5, *California Code of Regulations*, section 11704, Pupil – Teacher Ratio states:

In a charter school, for the purposes of Education Code section 51745.6, the ratio of average daily attendance for independent study pupils to full-time equivalent (FTE) certificated employees responsible for independent study shall not exceed a pupil-teacher ratio of 25:1 or the ratio of pupils to full-time equivalent certificated employees for all other educational programs operated by the largest unified school district, as measured by average daily attendance, as reported at the second principal apportionment in the prior year, in the county or counties in which the charter school operates. Units of average daily

attendance for independent study that are ineligible for apportionment as provided in subdivision (b) of Education Code section 51745.6 shall also be ineligible for funding pursuant to Chapter 6 (commencing with section 47630) of Part 26.8 of the Education Code. For purposes of this section, a “full-time certificated employee” means an employee who is required to work a minimum six-hour day and 175 days per fiscal year. Part-time positions shall generate a partial FTE on a proportional basis.

CDE confirmed that this regulation considers a teacher’s full-time equivalence to the extent that they were employed throughout the school year. CDE’s Education Fiscal Services Consultant stated “if [teachers] don’t work the full year they would be considered less than 100% FTE... [I]f an employee... was hired during the school year and only worked 100 days, not 175, they should be calculated as .57 FTE (100/175).”

We are uncertain as to whether CAVA’s pupil-teacher ratio complied with state law. The information CAVA provided us to support its ratio was insufficient for us to recalculate the ratio using FTE teachers on a proportional basis. Therefore, we did not verify CAVA’s actual pupil-teacher ratio. CAVA informed us that it generally only hires teachers mid-year to replace teachers who have left, so its count of teachers at one point could approximate the proportional number of FTE teachers. However, CAVA did not provide detailed employment records that would allow us to make this calculation.

Recommendation

We recommend that CAVA establish procedures to ensure that employees working less than the minimum six hour days, 175 days per year, are calculated at the appropriate fraction of a FTE for the purpose of calculating the pupil-teacher ratio.

CAVA’s Response

The Charter Schools complied with the statute, the regulation, and the instructions set forth by the CDE in calculating their pupil to teacher ratio (“PTR”) all of which tie calculations to the period 2 attendance report (“P2”) and defines a full time equivalent (“FTE”) in accordance with the contract of the teacher. [CAVA cites law and CDE guidance regarding calculating the pupil-teacher ratio.]

Here, the Charter School’s calculated the pupil to teacher using the P2 attendance period as directed in Section 11704 and Education Code Section 51745.6(a)(2). In doing so, the Charter Schools determined FTE on the teacher’s contract (the contract requires the teacher to work for at least 175 days per year and at least 6 hours per day). The Charter Schools calculated its PTR based upon FTE at P2 against the ADA at P2.

The Charter Schools disagree with the Report’s methodology as it contradicts the law and the instructions published by the CDE. Nevertheless, the Charter Schools note that under either methodology, the Charter Schools maintain a pupil to teacher ratio that is far under the maximum level of 25:1. The PTR range among the Charter Schools was far below 25:1 set in law. For Fiscal Year 2015, the range among the Charter Schools was 10.71:1 – 22.84:1 and the range among the Charter Schools for Fiscal Year 2016 was 9.89:1 – 19.15:1.

SCO's Comment

Our finding describes a methodology for calculating the pupil-teacher ratio that the CDE agrees with, which is consistent with state law and regulation. The methodology we describe more accurately compares the average number of students throughout the attendance period with the teachers that were available during this period, when compared with CAVA's methodology. The number of teachers in the pupil-teacher ratio should represent how many were available to the students throughout the attendance period, not at a static point of CAVA's choosing. While the CDE guidance that CAVA references in its response does state that the pupil-teacher ratio should be calculated in connection with the second principal apportionment report, it does not state that the ratio should include a count of teachers at one point in time.

Although CAVA claims that its pupil-teacher ratio complied with state law, it did not provide us with sufficient records to verify that was the case. As we describe in our finding, we noted that CAVA hired teachers throughout the school year. CAVA told us that it did so only to replace teachers who left during the school year, but did not provide us with personnel records that we could use to verify this position. Without this information, and in the absence of CAVA calculating its pupil-teacher ratio according to the methodology we describe in our finding, we are unable to evaluate whether CAVA actually met the appropriate pupil-teacher ratio throughout the attendance period.

Observations

OBSERVATION 1 — Schools contracted to pay their authorizing entities oversight fees in excess of legal limits

The MOUs between the schools and their authorizing entities provide for a supervisory oversight fee that exceeds what is allowed by state law. This resulted in the schools overpaying the authorizing entity by \$1,218,753 for the audit period.

State law limits the actual costs of supervisory oversight fees to 1% of Local Control Funding Formula (LCFF) revenues if the charter school is unable to obtain a substantially rent-free facility from the authorizing entity. If substantial rent-free facilities are provided, the oversight fee increases to 3%. State law also indicates that oversight fees for supervision include fiscal oversight and that the oversight fee is calculated based on the school's LCFF revenues.

Two of the 13 schools in FY 2014-15 and three of the 14 schools in FY 2015-16 contracted to use facilities of their authorizing entity, through their MOUs, and agreed to pay the entities 3% of revenues.

The schools that did not contract to use facilities of their authorizing entity agreed to pay them the following percentages based on revenues:

- Ten schools agreed to pay 2%: 1% for supervisory oversight and 1% for fiscal oversight.
- One school agreed to pay 3%: 1.5% for supervisory oversight and 1.5% for fiscal oversight.

The schools that used facilities of their authorizing entity agreed to pay a supervisorial oversight fee within the 3% maximum percentage allowed by statute. However, the schools that did not use facilities of their authorizing entity agreed to pay an oversight fee in excess of the 1% supervisorial oversight fee allowed by statute.

Education Code section 47613 states, in part:

- (a) Except as set forth in subdivision (b), a chartering authority may charge for the actual cost of supervisorial oversight of a charter school not to exceed one percent of the revenue of the charter school.
- (b) A chartering authority may charge for the actual costs of supervisorial oversight of a charter school not to exceed 3 percent of the revenue of the charter school if the charter school is able to obtain substantially rent free facilities from the chartering authority.
- (f) For purposes of this section, "revenue of the charter school" means the amount received in the current fiscal year from the local control funding formula....

Education Code section 47604.32 states, in part:

- (a) Each chartering authority... shall do all of the following with respect to each charter school under its authority:
 - (4) Monitor the fiscal condition of each charter school under its authority...

- (b) The cost of performing the duties required by this section shall be funded with supervisory oversight fees collected pursuant to Section 47613.

Title 5, *California Code of Regulations*, section 11969.5 states:

The space allocated for use by the charter school, subject to sharing arrangements, shall be available for the charter school's entire school year regardless of the school district's instructional year or class schedule and may not be sublet or used for purposes other than those that are consistent with school district policies and practices for use of other public schools of the school district without permission of the school district.

We obtained the amount of LCFF revenue the schools received from the CDE's website. We calculated supervisory oversight fees based on 1% of LCFF revenues for schools that did not contract for their authorizing entity to provide facilities and 3% of LCFF revenues for schools that did. We found that the schools overpaid the authorizing entities in oversight fees by \$630,614 for FY 2014-15 and by \$588,139 for FY 2015-16, totaling \$1,218,753 for the audit period. This amount excludes any payments CAVA made to the authorizing entities for additional administrative services.

The calculation of overpaid supervisory oversight fees based on the statutorily allowed percentage of LCFF revenues is as follows:

Fiscal Year 2014-15:

School	Percent of LCFF Revenues¹	Schools Paid	Over (Under) Payment
CAVA @ Fresno	\$ 39,630	\$80,858	\$ 41,228
CAVA @ Jamestown	10,166	24,188	14,022
CAVA @ Kings	39,598	82,699	43,101
CAVA @ Los Angeles	745,372	745,822	450
CAVA @ Maricopa	90,697	166,272	75,575
CAVA @ Maricopa High	48,641	89,158	40,517
CAVA @ San Diego	205,713	417,236	211,523
CAVA @ San Joaquin	314,975	324,534	9,559
CAVA @ San Mateo	56,535	109,898	53,363
CAVA @ Sonoma	49,989	104,007	54,018
CAVA @ Sutter	64,135	125,625	61,490
Insight @ Los Angeles	12,321	41,310	28,989
Insight @ San Diego	4,837	1,616	(3,221)
Total			<u>\$ 630,614</u>

Fiscal Year 2015-16:

School	Percent of LCFF Revenues¹	Schools Paid	Over (Under) Payment
CAVA @ Fresno	\$ 37,323	\$74,634	\$ 37,311
CAVA @ Jamestown	9,599	19,178	9,579
CAVA @ Kings	38,673	81,540	42,867
CAVA @ Los Angeles	724,107	674,026	(50,081)
CAVA @ Maricopa	90,780	163,404	72,624
CAVA @ Maricopa High	49,391	88,904	39,513
CAVA @ San Diego	192,820	385,484	192,664
CAVA @ San Joaquin	322,054	322,152	98
CAVA @ San Mateo	59,105	133,039	73,934
CAVA @ Sonoma	47,466	94,947	47,481
CAVA @ Sutter	63,934	127,875	63,941
Insight @ Los Angeles	23,181	69,192	46,011
Insight @ San Diego	12,717	25,108	12,391
Insight @ San Joaquin ²	18,030	17,836	(194)
Total			<u>\$ 588,139</u>

¹ State law limits the amount a charter schools can pay its authorizing entity for oversight to 1% of LCFF revenues, or 3% of LCFF revenues when the school contracts to use the authorizing entity's facilities. The following schools contracted to use facilities: CAVA @ Los Angeles, CAVA @ San Joaquin, and Insight @ San Joaquin.

² Insight @ San Joaquin did not begin operations until FY 2015-16.

Recommendation

We recommend that the schools amend the MOUs with their authorizing entities to ensure that payments of oversight fees are consistent with state law.

CAVA's Response

The Charter School negotiates its MOU's with its Authorizers by taking into consideration the Authorizer's oversight costs, additional services provided to the Charter Schools beyond oversight and the provision of facilities. Education Code Section 47613 prevents an authorizing school district from unilaterally imposing oversight fees that are higher than the maximum amount set forth in the Section, but does not prevent the Charter Schools and their authorizers from contracting for a higher amount.

Education Code Section 47604.32 does direct specific minimum activities a charter authorizer is required to do with respect to each of its charters and requires these activities to be funded by supervisorial oversight fees. But the law does not prevent a granting agency from determining that additional oversight services are necessary to fulfill their obligations in the law; for example, under Education Code section 47607 all charter authorizers are required to monitor the charter school's compliance with its charter, the law, and academic outcomes as part of the renewal process. In order to meet this obligation under law the charter authorizer will be required to perform services that go beyond the minimum oversight obligations stated in Education Code Section 47604.32. There is express statutory authority for a charter school and

granting agency to negotiate additional fees and services. [CAVA quotes Education Code Section 47613(d).]

Further, Education Code Section 47633(c) allows a charter school to use its funding for any “public school purpose as “determined by the governing board of the charter school.” And Education Code section 35160 and 47610 allows a school district and charter school, respectively, to take any and all actions they deem necessary as long as not expressly precluded by law.

The Charter Schools’ Authorizers provide the Charter Schools with the minimum oversight requirements as described in Education Code Section 47604.32 and additional fiscal services, superintendent/administrative consultation, and access to facilities for testing, labs, special education services, professional development, graduation and promotion ceremonies, board meetings and other instructional needs. The Charter Schools are confident that the MOUs reflect charges that fairly compensate the Authorizer for the benefits received.

SCO’s Comment

The statutory cap on fees a chartering authority may charge an authorized charter school is a clear limit on such fees, regardless of whether the charter school wishes to pay more. We disagree with CAVA’s position that a charter school and its chartering authority may agree to a higher amount. The Education Code is not intended solely for the benefit of CAVA and its authorizing entities; it also serves to the public interest with respect to providing quality education and safeguarding taxpayer monies. CAVA cites no legal authority that allows it to waive the payment provisions we cite in our finding.

We acknowledge that state law allows CAVA to procure additional services from its authorizing entities, which it can pay for separately from its capped oversight fees. During audit fieldwork, we noted that several CAVA schools contracted to procure additional services from its authorizing entities. These services were specifically defined in the MOUs as services in addition to the authorizing entities’ oversight responsibilities. We excluded this information from our analysis as it is irrelevant to the amounts CAVA can pay its authorizing entities for oversight. All of our calculations reflect amounts CAVA paid for oversight, and exclude amounts CAVA paid for additional services. CAVA did not provide us any information during the audit that supported a position that the percentages of revenue they agreed to pay their authorizing entities included payment for additional services.

OBSERVATION 2— The restatement of prior years’ financial statements may have violated the schools’ memoranda of understanding with the authorizing entities

The schools restated prior-year financial statements for FY 2013-14 in the amount of \$261,954 and for FY 2014-15 in the amount of \$1,733,194 by applying \$1,995,148 in unspent deferred revenues against Common Core expenses that were included in balanced budget credits. Balanced budget credits represent the cumulative annual amounts that K-12 Inc. charged the schools for educational products and services in excess of available revenues at the end of each fiscal year. This restatement may have violated the MOUs of 12 of the 13 schools in FY 2014-15 and 13 of the 14 schools in FY 2015-16.

In preparing this observation, we reviewed the audit work papers prepared by the external auditors who prepared CAVA's audited financial statements. Those work papers show that CAVA did not encumber the Common Core funds by the deadline and prior expenses were not classified as being funded with Common Core funds until CAVA adjusted its books in October 2016. The external auditors' work papers also show that CAVA increased its payable to K12 Inc. in October 2016 in order to reduce balanced budget credits. Increasing the payable to K12 Inc. after the end of the school year appears to have violated the terms of the MOUs between CAVA and its authorizing entities.

Allowable Use of Common Core Funds

The prior-period adjustment was made in October 2016, when closing out FY 2015-16 financial statements. The adjustment reduced prior years' balanced budget credits for all 14 schools and increased the payables to K12 Inc. by \$1,995,148.

CAVA did not provide support that it had encumbered the Common Core funds by June 30, 2015, a prerequisite to being eligible to spend such funds. Therefore, these funds were no longer available to be applied against FY 2013-14 and FY 2014-15 balanced budget credits. Common Core funds not encumbered by June 30, 2015, are required to be returned to the CDE.

Memoranda of Understanding

Of the \$1,995,148 in restated amounts, \$1,893,632 was forgiven by K12 Inc. through the MOUs for 13 of the 14 CAVA schools. The 14th school, CAVA @ Fresno, did not have a MOU requirement to forgive balanced budget credits at the end of each school year.

The MOUs between all CAVA schools and their authorizing districts, except that of CAVA @ Fresno, state:

Any contract or arrangement between the Charter School and K12 Inc. for services or materials and equipment shall provide that any charges to or obligation of the Charter School in any fiscal year in excess of the amounts available for payment at the end of such fiscal year will be forgiven by K12 Inc. and shall not be carried over as an obligation in the next succeeding fiscal year.

The Notes to the 2014-15 financial statements for all schools disclosed an ongoing financial obligation to K12 Inc. at the end of the fiscal year.

The Notes to the 2015-16 financial statement for all schools disclosed:

[M]anagement noted that the [schools], in prior years, had incurred eligible expenses toward Common Core revenues, which had initially been classified as deferred revenues... rather than being recognized as revenues in the period that these eligible costs were expended... Accordingly, a prior adjustment... resulted in an increase in the cumulative prior year revenues... which was offset by a reduction in the cumulative prior year balanced budget credits.

The MOUs restricted CAVA from recovering balanced budget credits in subsequent years as the excess charges (expenses) would have been forgiven. Further, as noted above, the Common Core funds were not encumbered by the deadline to use such funds and thus were required to be returned to the CDE.

Recommendation

We recommend that the CDE follow up with CAVA to address and resolve the possible violation of the MOUs of 13 of the 14 schools. We also recommend that the CDE take appropriate action related to \$1,995,148 in Common Core funds not encumbered by June 30, 2015.

CAVA's Response

Common Core Implementation funds were properly spent during the audit period, and thus there is no issue of whether they were timely encumbered as they were appropriately spent prior to June 30, 2015 in alignment with the requirements for Common Core Implementation funds. As explained below, this conclusion has been affirmed by an independent auditing firm and their opinion is attached hereto.

[CAVA quotes Assembly Bill 83 concerning Common Core Implementation Funds and the California School Accounting Manual's definition of an encumbrance, concluding "'expenditures' meet the definition of 'encumbrance.'"]

During fiscal year 2016 audit, CAVA discovered that in fiscal years 2015 and 2014, CAVA had Common Core expenditures that it could claim against Common Core revenue. CAVA originally had recorded that revenue in fiscal year 2016. During the fiscal year 2016 audit, the timing of recognition of the Common Core revenues was corrected to shift them to fiscal years 2015 and 2014 to match the timing when the related expenditures were incurred (in accordance with Generally Accepted Accounting Principles). The correction was audited by CAVA's independent auditors and they agreed with the prior period restatement. Larger deficits were recorded in fiscal year 2016 and smaller deficits were recorded in fiscal years 2015 and 2014. As such Common Core funds were spent by June 30, 2015 and thus no further encumbrance was required by June 30, 2015. Please see attached letter from Green, Hasson & Janks, the Charter Schools' independent auditor affirming the procedures it undertook to audit the proper expenditure of Common Core Implementation funds. Further, our Office sent the Green, Hasson & Janks letter to a separate independent auditor to review the validity of restating financials to account for common core expenditures. Please see attached letter from Wade McMullen, Principal from CliftonLarsonAllen confirming the opinion of Green, Hasson & Janks. The restatement of the financial statements aligned with guidance provided by the CDE and the Charter School's independent auditors to reflect the expenditure and/or encumbrance of Common Core Implementation funding by June 30, 2015.

[CAVA inserts an email between K12 Inc. and the CDE.]

In letters to each of the school boards dated September 13, 2016, K12 stated it "shall forego its right to collect, and shall fully expunge" all prior year accumulated balanced budget credits issued since the schools' inception through the 2014/2015 school year and that those from fiscal

year 2015/2016 being foregone and expunged upon completion of the schools' final fiscal year 2016 audit. Prior period adjustments were not done with the objective of recouping balanced budget credits. These adjustments were done to reflect that the Schools had appropriately spent and exhausted Common Core Implementation funds by June 30, 2015.

SCO's Comment

We disagree with CAVA's position. CAVA did incur expenses prior to June 30, 2015, but these expenses were not categorized as Common Core until October 2016. As CAVA did not classify these funds as Common Core prior to the June 30, 2015 deadline, it was improper for CAVA to subsequently claim them as valid expenditures. We also disagree that prior period adjustments are a valid reason to repay K12 Inc. for obligations that were previously forgiven.

In preparing this observation, we reviewed the work papers in which Green Hasson Janks analyzed this issue in preparing CAVA's audited financial statements. Those work papers show that CAVA did not actually encumber the Common Core funds by the deadline; CAVA's expenses were not classified as being used for Common Core until CAVA adjusted its books in October 2016. These work papers show that CAVA increased its payable to K12 Inc. in October 2016 while increasing its revenue due to the Common Core adjustment. Instead of applying Common Core revenues to the schools' net position, CAVA applied these revenues to balanced budget credits. Increasing the payable to K12 Inc. after the end of the school year appears to violate the terms of the MOUs between CAVA and its authorizing entities, which state that no obligation to K12 Inc. should continue after the end of the school year.

OTHER ISSUE— CAVA claims that “Observations” are outside of the scope of the audit

CAVA's Response

[T]he Charter Schools object to the “Observations” as they are beyond the scope of the Audit and thus not lawfully included in the Report under Generally Accepted Government Auditing Standards.

SCO's Comment

We framed these issues as “Observations” to be transparent that they were not specifically within the scope of the audit. However, their inclusion in our report is reasonable and appropriate.

The two observations are based on information we found relevant to disclose while analyzing the audit objectives. They directly relate to audit work we conducted in analyzing the audit objectives, and are therefore appropriate to include in our report. Observation 1 adds context to our analysis of whether CAVA complied with the terms of the agreements it entered into with its authorizing entities. It shows that the amounts CAVA pays its authorizing entities is not only inconsistent with the terms of the MOUs, but also with state law. Observation 2 combines our analysis of CAVA's noncompliance with the terms of the MOUs. We present details about the Common Core funds in order to explain how the prior period adjustments occurred; this supports our analysis of the MOU, which is within the scope of the audit.

**Attachment—
CAVA's Response to
Draft Audit Report**



LAW OFFICES OF YOUNG, MINNEY & CORR, LLP
THE CHARTER LAW FIRM

June 12, 2017

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Re: Response to Draft Audit Report – California Virtual Academies and Insight Schools of California

Dear Mr. Spano:

Our Office serves as legal counsel for the fourteen (14) above-referenced charter schools¹ audited by the State Controller's Office ("SCO") under contract with the California Department of Education ("CDE") for the period July 1, 2014 through June 30, 2016 ("Audited Years"). The purpose of this letter is to provide comments on behalf of the Charter Schools concerning the Draft Audit Report ("Report") provided to our clients on June 2, 2017.

The Charter Schools welcome the opportunity to comment on the Report, and acknowledge the efforts of the Financial Audits Bureau to understand and apply the multitude of regulations applicable to the nonclassroom-based independent study charter school programs offered by the Charter Schools. The Charter Schools' respectfully request your consideration of their joint comments provided herein.

Finding 1: Inaccurate Calculation of Supervisory Oversight Fees the Schools Paid to Authorizing Entities.

Response

MOU Enforcement Falls to the Authorizer and Discrepancies Were Immaterial but Future Reconciliation Will Occur Annually.

¹ CAVA @ Fresno, CAVA @ Jamestown, CAVA @ Kings, CAVA @ Los Angeles, CAVA @ Maricopa, CAVA High @ Maricopa, CAVA @ San Diego, CAVA @ San Joaquin, CAVA @ San Mateo, CAVA @ Sonoma, CAVA @ Sutter, Insight @ Los Angeles, Insight @ San Diego, Insight @ San Joaquin (15-16 only) (collectively referred herein as "Charter Schools").

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The Charter Schools paid all amounts due as requested via invoice generated by each charter authorizer (“Authorizers”). The slight underpayment of fees per the MOU’s spread across all the Charter Schools was approximately 1% of the total amount invoiced by the Authorizers. This difference is immaterial under auditing standards. Moreover, as a matter of law, the Charter Schools and their authorizing school districts are not required to pursue enforcement for such immaterial discrepancies. Such non-enforcement of the MOU is not a violation of law and thus not a basis for an audit finding.

Nevertheless, in response to the recommendation action made by the Report, the Charter Schools will establish an annual reconciliation process for review of each of the oversight invoices provided by each charter authorizer to ensure alignment with the MOUs and ensure that payments equal the contractual amounts approved in the MOUs between the parties.

Finding 2: Lack of Sufficient Documentation to Support Claimed Average Daily Attendance

Response

The Charter Schools Maintain Legally Required Documentation to Support Accurate Reporting of Attendance. Attendance Documentation Complies with a Prior Settlement Agreement with the California Attorney General’s Office.

The Charter Schools reached a Settlement Agreement with the California Attorney General’s Office (CA-AG) which addressed the attendance documentation issue raised in Finding 2. The Charter Schools maintain contemporaneous records of attendance as required by Title 5 Section 11960 of the California Code of Regulations (“daily engagement”) and the time value of the student’s work product as personally judged by the credentialed teacher as required by Education Code Section 51747.5 (“time value”). The law does not provide any required form of documentation of “daily engagement” or “time value”. In fact, the CDE, in its independent study manual fails to even provide a sample contemporaneous record of attendance.

Teachers at the Charter Schools utilize activity reports to determine daily engagement (days where the student engaged in an educational activity required by the school on days that the school is actually taught at the school). The Charter School teachers then personally judge the time value of the work produced by the student over the attendance period, which will result in a reduction in attendance if the time value is not equal to the days of daily engagement. Ultimately, the teachers are trained to take the lower of the “daily engagement” or the “time value” in determining the days of attendance. Accordingly, the Charter School meets the legal requirements established by Section 11960 of Title 5 of the California Code of Regulations and Education Code Section 51747.5 for claiming student attendance in a nonclassroom-based charter school.

The Charter Schools’ attendance procedures also directly align with Section 6(g) of the Settlement Agreement with the CA- AG that requires “CAVA teachers to examine the “time value” of the student’s work products over the whole learning period. Teacher must report the



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lower value as between the number of days of daily engagement and the number of days of time value.”

In response to the recommendation made in the Report, the Charter Schools will continue to maintain contemporaneous attendance documentation to support claimed ADA and the Settlement with the CA-AG.

Finding 3: Lack of Sufficient Documentation to Support Satisfactory Progress of Students.

Response

The Charter Schools Will Abide by Strict Attendance Guidelines Limiting Apportionment for Students Over the Age of 19 to Those Who Remain Continuously Enrolled in a Public School, Making Satisfactory Progress Toward a High School Diploma, and Who are Not Over the Age of 22.

The SCO provides no facts to support its finding that the Charter Schools fail to monitor students to ensure that they are making satisfactory progress toward high school graduation. Indeed, to the contrary, the record demonstrates the graduation of pupils over the age of 19 and/or the withdrawal of students failing to pass courses that are required for graduation. The SCO fails to provide any law which requires the adoption of a formal policy or guidelines regarding students over the age of 19. In fact, the regulations sufficiently address the definition of “satisfactory progress” and the Charter Schools align their practices accordingly.

During the enrollment process, the Charter Schools verify that the student has maintained continuous enrollment in a public school after the age of 18 via the student’s transcript. Supervising and homeroom teachers are continuously monitoring those students that are not making progress. Counselors also notify the lead guidance counselor if they have a student that is over-age and not making satisfactory progress. In addition, the Charter Schools tracker notes all 5th year seniors and monitors them closely to ensure that they would have the ability to graduate by age 22.

In response to the recommendation action made by the Report, the Charter Schools will adopt attendance guidelines codifying current practice for the monitoring of satisfactory progress for students over the age of 19.

Finding 4: Pupil Teacher Ratio May Have Been Inaccurately Calculated

Response

The Charter Schools Calculate Pupil-Teacher Ratio in Accordance with Statute, Regulation, and the Instructions Published by the CDE.



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The Charter Schools complied with the statute, the regulation, and the instructions set forth by the CDE in calculating their pupil to teacher ratio ("PTR") all of which tie calculations to the period 2 attendance report ("P2") and defines a full time equivalent ("FTE") in accordance with the contract of the teacher.

Section 11704 of Title 5 of the California Code of Regulations state as follows:

"In a charter school, for the purposes of Education Code section 51745.6, the ratio of average daily attendance for independent study pupils to full-time equivalent (FTE) certificated employees responsible for independent study shall not exceed a pupil-teacher ratio of 25:1 or the ratio of pupils to full-time equivalent certificated employees for all other educational programs operated by the largest unified school district, as measured by average daily attendance, as reported at the second principal apportionment in the prior year ...For purposes of this section, a "full-time certificated employee" means an employee who is required to work a minimum six-hour day and 175 days per fiscal year. Part-time positions shall generate a partial FTE on a proportional basis." (emphasis added).

The CDE is tasked with providing annual instructions for calculating pupil teacher ratio. For example, please see <http://www.cde.ca.gov/sp/eo/is/iscalc15inst.asp#Charters> for the 2015-2016 school year and you will note the independent study ratio calculation is done annually at the time of, and in connection with the second principal apportionment (P-2) report.

Here, the Charter School's calculated the pupil to teacher using the P2 attendance period as directed in Section 11704 and Education Code Section 51745.6(a)(2). In so doing, the Charter Schools determined FTE on the teacher's contract (the contract requires the teacher to work for at least 175 days per year and at least 6 hours per day). The Charter Schools calculated its PTR based upon FTE at P2 against the ADA at P2.

The Charter Schools disagree with the Report's methodology as it contradicts the law and the instructions published by the CDE. Nevertheless, the Charter Schools note that under either methodology, the Charter Schools maintain a pupil to teacher ratio that is far under the maximum level of 25:1. The PTR range among the Charter Schools was far below 25:1 set in law. For Fiscal Year 2015, the range among the Charter Schools was 10.71:1 – 22.84:1 and the range among the Charter Schools for Fiscal Year 2016 was 9.89:1 – 19.15:1.

In response to the recommendation made in the Report, the Charter Schools will continue to follow applicable law and CDE instructions in calculating its PTR.

Observation 1: Schools Contracted to Pay Their Authorizing Entities Oversight Fees in Excess of Legal Limits



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Response

The Charter Schools Compensate Authorizers for Oversight, Services, and Facilities through Lawfully Negotiated and Executed MOUs.

As an initial matter, the Charter Schools object to the “Observations” as they are beyond the scope of the Audit and thus not lawfully included in the Report under Generally Accepted Government Auditing Standards.

The Charter School negotiates its MOU’s with its Authorizers by taking into consideration the Authorizer’s oversight costs, additional services provided to the Charter Schools beyond oversight and the provision of facilities. Education Code Section 47613 prevents an authorizing school district from unilaterally imposing oversight fees that are higher than the maximum amount set forth in the Section, but does not prevent the Charter Schools and their authorizers from contracting for a higher amount.

Education Code Section 47604.32 does direct specific minimum activities a charter authorizer is required to do with respect to each of its charters and requires these activities to be funded by supervisorial oversight fees. But the law does not prevent a granting agency from determining that additional oversight services are necessary to fulfill their obligations in the law; for example, under Education Code section 47607 all charter authorizers are required to monitor the charter school’s compliance with its charter, the law, and academic outcomes as part of the renewal process. In order to meet this obligation under law the charter authorizer will be required to perform services that go beyond the minimum oversight obligations stated in Education Code Section 47604.32. There is express statutory authority for a charter school and granting agency to negotiate additional fees and services.

Education Code Section 47613(d) provides:

“(d) This section does not prevent the charter school from separately purchasing administrative or other services from the chartering authority or any other source.”

Further, Education Code Section 47633(c) allows a charter school to use its funding for any “public school purpose as “determined by the governing board of the charter school.” And Education Code section 35160 and 47610 allows a school district and charter school, respectively, to take any and all actions they deem necessary as long as not expressly precluded by law.

The Charter Schools’ Authorizers provide the Charter Schools with the minimum oversight requirements as described in Education Code Section 47604.32 and additional fiscal services, superintendent/administrative consultation, and access to facilities for testing, labs, special education services, professional development, graduation and promotion ceremonies, board meetings and other instructional needs. The Charter Schools are confident that the MOUs reflect charges that fairly compensate the Authorizer for the benefits received. However, in response to



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the recommendation in the Report, the Charter Schools will review the recommendation in the Report with each of their Authorizers to consider negotiation of amendments to each of the MOUs.

Observation 2: The Restatement of Prior Year's Financial Statements May Have Violated The Memoranda of Understanding With the Authorizing Entities.

Response

The Charter School's Restatement of Prior Years' Financial Statements had no Impact on Compliance with MOUs.

Common Core Implementation funds were properly spent during the audit period, and thus there is no issue of whether they were timely encumbered as they were appropriately spent prior to June 30, 2015 in alignment with the requirements for Common Core Implementation funds. As explained below, this conclusion has been affirmed by an independent auditing firm and their opinion is attached hereto.

Per Assembly Bill 86 ("AB 86") (2013), Common Core Implementation funds were to be utilized for qualifying expenditures as follows:

- " (1) Professional development for teachers, administrators, and paraprofessional educators or other classified employees involved in the direct instruction of pupils that is aligned to the academic content standards adopted pursuant to sections 60605.8, 60605.11, and 60605.85 of the Education Code, and former Education Code Section 60811.3 as that section read until June 30, 2013.
- (2) Instructional materials aligned to the academic content standards adopted pursuant to sections 60605.8, 60605.11, and 60605.85 of the Education Code, and former Education Code Section 60811.3 as that section read until June 30, 2013 including, but not limited to, supplemental instructional materials as provided in sections 60605.86, 60605.87, and 60605.88 of the Education Code.
- (3) Integration of these academic content standards through technology-based instruction for purposes of improving the academic performance of pupils, including, but not necessarily limited to, expenditures necessary to support the administration of computer-based assessments and provide high-speed, high-bandwidth Internet connectivity for the purpose of administration of computer-based assessments.

AB 86 required all funds to be encumbered by June 30, 2015:



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(c) A school district, county office of education, charter school, or state special school may encumber funds apportioned pursuant to this section at any time during the 2013–14 or 2014–15 fiscal year.

The 2016 California School Accounting Manual (“CSAM”) defines an encumbrance as follows:

“Encumbrances. Obligations in the form of purchase orders, contracts, salaries, and other commitments chargeable to an appropriation for which a part of the appropriation is reserved.” (CSAM Glossary-7)

Clearly, “expenditures”, meet the definition of “encumbrance”.

During fiscal year 2016 audit, CAVA discovered that in fiscal years 2015 and 2014, CAVA had Common Core expenditures that it could claim against Common Core revenue. CAVA originally had recorded that revenue in fiscal year 2016. During the fiscal year 2016 audit, the timing of recognition of the Common Core revenues was corrected to shift them to fiscal years 2015 and 2014 to match the timing when the related expenditures were incurred (in accordance with Generally Accepted Accounting Principles). The correction was audited by CAVA’s independent auditors and they agreed with the prior period restatement. Larger deficits were recorded in fiscal year 2016 and smaller deficits were recorded in fiscal years 2015 and 2014. As such Common Core funds were spent by June 30, 2015 and thus no further encumbrance was required by June 30, 2015. Please see attached letter from Green, Hasson & Janks, the Charter Schools’ independent auditor affirming the procedures it undertook to audit the proper expenditure of Common Core Implementation funds. Further, our Office sent the Green, Hasson & Janks letter to a separate independent auditor to review the validity of restating financials to account for common core expenditures. Please see attached letter from Wade McMullen, Principal from CliftonLarsonAllen confirming the opinion of Green, Hasson & Janks. The restatement of the financial statements aligned with guidance provided by the CDE and the Charter School’s independent auditors to reflect the expenditure and/or encumbrance of Common Core Implementation funding by June 30, 2015. Please see guidance from the CDE to Marguerite Violassi, then K12 Director of Finance:



THE CHARTER LAW FIRM

Jim L. Spano

Re: Response to Draft Audit Report – California Virtual Academies and Insight Schools of California

June 12, 2017

Page 8 of 9

From: Julie Klein Briggs [mailto:JBriggs@cde.ca.gov]
Sent: Tuesday, October 11, 2016 3:14 PM
To: Violassi, Marguerite <mviolassi@k12.com>
Cc: Ruthann Munsterman <RMunsterman@cde.ca.gov>
Subject: RE: Common Core Spending Clarification

Hi Marguerite,

Thank you for your email below. As clarification, based on Section 85 of Assembly Bill 86 (Chapter 48, 2013) local educational agencies may encumber funds at any time during the 2013-14 or 2014-15 fiscal year. This means that the end date to spend or encumber the Common Core Implementation Funds was June 30, 2015. As of July 1, 2015, all expenditures or encumbrances should have been reported to CDE. While perhaps there might be a little wiggle room for amounts that might be immaterial, we would want to look at unspent amounts for your schools to make a determination. If amounts are material we would most likely issue an invoice to collect the unspent amounts. If you believe you can make adjustments for other 2013-14 and 2014-15 allowable expenditures that were charged to other resources, please let me know.

Thanks,
Julie

Julie A. Klein Briggs, Fiscal Consultant
School Fiscal Services Division
California Department of Education
1430 N Street, Suite 3800
Sacramento, CA 95814
916-323-6191 Phone
916-327-6157 FAX
jbriggs@cde.ca.gov
www.cde.ca.gov

In letters to each of the school boards dated September 13, 2016, K12 stated it “shall forego its right to collect, and shall fully expunge” all prior year accumulated balanced budget credits issued since the schools’ inception through the 2014/2015 school year and that those from fiscal year 2015/2016 being foregone and expunged upon completion of the schools’ final fiscal year 2016 audit. Prior period adjustments were not done with the objective of recouping balanced budget credits. These adjustments were done to reflect that the Schools had appropriately spent and exhausted Common Core Implementation funds by June 30, 2015.

In response to the recommendation in the Report, no further action is required here as all Common Core funds were expended appropriately, audited, and all balanced budget credits have been expunged per the terms of each Charter School’s MOU.

Reservation of Rights

The Charter Schools expressly reserve the right to make new or additional arguments in any administrative proceeding and/or subsequent litigation resulting from the Report.

* * *



THE CHARTER LAW FIRM

Jim L. Spano

Re: Response to Draft Audit Report – California Virtual Academies and Insight Schools of California

June 12, 2017

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If you should have any questions regarding this letter, please do not hesitate to contact me for more information.

Sincerely,

LAW OFFICES OF YOUNG,
MINNEY & CORR, LLP



LISA A. CORR
ATTORNEY AT LAW

ENCLOSURE



THE CHARTER LAW FIRM

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June 8, 2017

To the Head of Schools
California Virtual Academies

Re: Audit of Common Core Expenditures of
California Virtual Academies

At your request, we are providing this letter to inform you that in connection with our audits for the year ended June 30, 2016, we performed audit procedures on common core expenditures in accordance with auditing standards generally accepted in the United States of America and the audit guide for Annual Audits of K-12 Local Education Agencies and State Compliance Reporting published by the Education Audit Appeals Panel. Based on our procedures we determined that the California Virtual Academies have fairly presented, in all material respects, the common core expenditures in the appropriate period and there were no audit findings with respect to these expenditures. Based on our audits for the year ended June 30, 2016, we determined that the management had appropriately restated the common core expenditures for amounts expended prior to June 30, 2015 and accordingly, did not have unspent amounts that needed to be encumbered at June 30, 2015.

Green Hasson & Janks LLP

Los Angeles, California

An independent member of HLB International, a worldwide network of accounting firms and business advisors.



CliftonLarsonAllen

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June 21, 2017

Ms. Lisa Corr, Partner
Young, Minney & Corr
655 University Ave #150
Sacramento, CA 95825

Dear Ms. Corr:

At your request, we are providing this letter to affirm your understanding of common core expenditures regulations and the restatement of prior year expenditures as determined by CAVA management and their auditor for common core expenditures made or encumbered prior to June 30, 2015. Based upon the communications provided to us, we would concur with the auditor with respect to this matter.

Sincerely,

CliftonLarsonAllen LLP

Wade N. McMullen, CPA
Principal

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874**

<http://www.sco.ca.gov>