

**The Critical Role of the Charter School
Board Treasurer and Finance Committee –
The Top Ten Financial Management Mistakes to Avoid
and Ten Other Deadly Sins and Lesser Evils**

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Charter School Tools

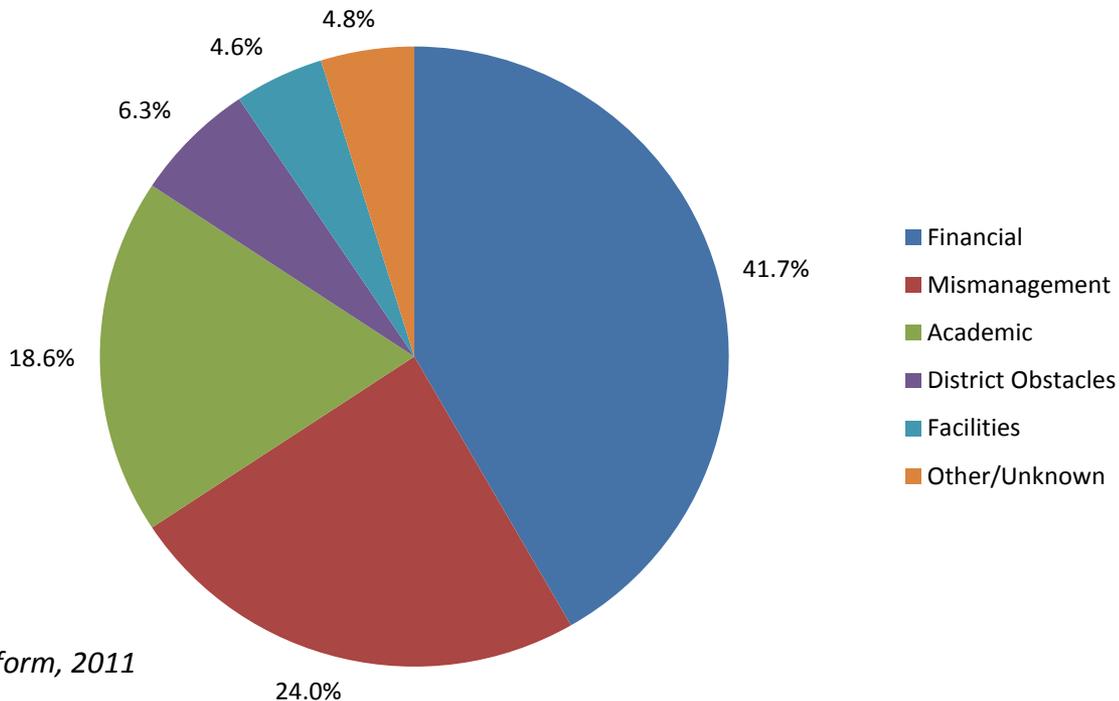
Agenda

- Why is it “critical”?
- What are the roles of the Treasurer and Finance Committee?
- Top 10 Financial Management Mistakes to Avoid.
- 10 other deadly sins and lesser evils.
- Financial management rubric

Why is it “critical”?

Because less than 1 in 5 charter schools have closed for academic reasons, but two-thirds closed because of financial or management failure.

National Charter Closures by Cause



Why is it “critical”?

Examples of financial failure -- accounting practices

Audit faults Academy’s accounting practices – *Times-Picayune*, 4/2/12:

“A private auditing firm found that...Academy didn’t properly track how a \$100,000 donation got spent, didn’t account for money left on pre-paid debit cards used by teachers on a school trip and gave out bonuses that were never approved by the school’s board....Charter schools around the country have drawn scrutiny of their finances, and financial mismanagement is one of the most common reasons they fail.”

→ EPILOGUE: SCHOOL CLOSED IN MAY 2012; ENTITY FILED FOR DISSOLUTION WITH APPROXIMATELY \$500,000 OF UNPAID LIABILITIES.

Why is it “critical”?

Examples of financial failure – budget mismanagement

Teachers protest cuts at charter school by cutting class – *WBRZ News 2, 4/25/12*: “More than half of the 22 teachers arranged to take the day off after their pay was cut 20% by the charter school’s board members...because of the more than \$1 million in cuts, teachers will now have to pay 50% of their health insurance.”

→ EPILOGUE: TEACHERS DID NOT RECEIVE LAST PAYCHECK; SCHOOL LOST CHARTER AND WAS TAKEN OVER.

Why is it “critical”?

Examples of financial failure – control failure

Police probe charter school – *News-Star Monroe, 6/22/12*: “...Charter School is facing both a police investigation for possible forgery and increased scrutiny by the [state] Legislative Auditors Office for ‘material weaknesses’....Among infractions are...not providing documentation for travel expenses, failing to record a fund raising account in the school’s ledger, purchasing items or loaning money for employees’ personal use...The audit report has nine findings including ‘significant deficiencies’ in the design and implementation of internal controls....’there was no evidence that any bank reconciliations had been completed during the audit year.’”

Why is it “critical”?

Examples of financial failure include embezzlement....

Charter School Employee Embezzled \$25,000 – Nola.com, 1/22/13: ““A high-ranking employee in the Business Office” forged signatures on five checks to pay herself \$25,000...In addition, the School did not keep all its accounts reconciled throughout the year, did not fully account for some grant transactions and lagged on requesting grant reimbursement from the [district] School Board.”

Former charter school administrator receives five-year sentence for stealing money from the school – Times-Picayune, 5/27/10: “She began stealing [\$660,000] from the school’s bank accounts as early as August 2008, a month after she was hired as business and human resources manager. She continued to write checks to herself and withdraw cash intended for school operations until she was fired in November 2009....[she] covered her tracks by making false entries in the school’s books.”

→ EPILOGUE: CEO RESIGNED. SCHOOL TAKEN OVER BY NEW OPERATOR.

Why is it “critical”?

- Because substantial public money is being spent.
- Because great educators are not necessarily great business people.
- Because the personal reputation of the board and leadership is associated with the school.
- Because the ultimate goal of any charter school is delivering great student achievement, and a financial failure can deny students that opportunity.

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What is the role of the Treasurer and Finance Committee?

“Sure, I’d be happy to be the Treasurer – but what does that mean?”

The role of the Treasurer and Finance Committee is defined in several places:

1. Bylaws of the corporation.
2. Charter application.
3. Charter review/renewal protocol.

What is the role of the Treasurer and Finance Committee?

Typical Description from By Laws

Range anywhere from....

“Treasurer. The Treasurer shall be a member of the Board of Trustees. The Treasurer shall perform all of the duties incident to the office of Treasurer and such other duties as from time to time may be assigned by the Board of Trustees.”

What is the role of the Treasurer and Finance Committee?

To....

Treasurer. The Treasurer and/or his or her designees shall have the custody of the corporate funds, securities, evidences of indebtedness, and other valuable documents; keep full and accurate accounts of receipts and disbursements in the corporate books; deposit all money and other valuables in the name and to the credit of the Corporation in such depositories as may be designated by the Board; disburse the funds of the Corporation as may be ordered or authorized by the Board and preserve proper vouchers for such disbursements; render to the President and Board at the regular meetings of the Board, or whenever they require it, an account of all transactions as Treasurer and of the financial condition of the Corporation; and render a full financial report at the annual meeting of the Corporation if so requested; be furnished by all corporate officers and agents at such Treasurer's request with such reports and statements as such Treasurer may require as to all financial transactions of the Corporation; and perform such other duties as from time to time may be prescribed by the Board or the President.

What is the role of the Treasurer and Finance Committee?

*Finance Committees are also typically specified in the by laws,
e.g.,*

“The Board of Trustees shall create and appoint a Finance Committee composed exclusively of Trustees to oversee the financial management of the organization. The Finance Committee shall recommend an annual budget for adoption by the Board of Trustees and may, by majority vote of the members of the Finance Committee, accept the annual audit of financial statements on behalf of the Board of Trustees.”

What is the role of the Treasurer and Finance Committee?

More detail is usually provided in the charter application (especially for newer schools) which typically include statements like:

The Board of Directors will exercise its oversight responsibilities by reviewing the periodic financial reports, requesting additional information as needed to understand the school's financial position fully and question any procedures or items on the financial statements. The Board of Directors will approve the annual budget and any large, non-standard purchases, as well as review the school's annual financial audit. The Board will select a Treasurer with professional experience in finance or accounting, and that person will oversee the Board's Finance Committee. The Treasurer and Finance Committee will ensure that the Board monitors the school's finances....

What is the role of the Treasurer and Finance Committee?

...continued....

The Board will utilize the following fiscal controls and financial management policies to remain informed regarding the school's financial position:

- Review and approval of the school's Fiscal Policies and Financial Procedures Manual.
- Review of monthly financial statements. These statements will include a balance sheet, income summary, detailed statements that compare actual versus budgeted expenses, statement of cash flows, and financial forecast.
- Monthly meetings with Treasurer and Finance Committee. The Board's Treasurer and Finance Committee will meet monthly with the Principal and Financial Manager to review the school's financial records, including the most recent reconciliation of accounts, and to present a variance report of actual versus budgeted expenditures.

What is the role of the Treasurer and Finance Committee?

...continued.

- Annual budget approval. The Board will review and approve the school's annual budget each year. In the third quarter, the Principal and Financial Manager will prepare and propose a detailed annual budget to the Finance Committee. The Finance Committee will then present the draft budget to the Board for review and approval at the end of each fiscal year.
- Annual report approval. The Principal and Financial Manager will prepare an annual report at the end of each fiscal year. The report will be approved by the Board, and will include a year-end balance sheet, including budgeted versus actual income and expense analysis.
- Audit compliance. The Board will hire an external auditor and ensure that an annual audit is completed. The Board Treasurer with support of the Finance Manager will prepare the management's response to each audit finding.

What is the role of the Treasurer and Finance Committee?

The annual review or charter renewal process may also establish evaluation criteria for financial management

Excerpt from Annual Authorizer Review

<i><u>Financial Performance</u></i>				
STANDARD #	COMPLIANCE INDICATOR	EVIDENT	NOT EVIDENT	N/A
Both budgets balanced using realistic and responsible assumptions	Prior and Current Year Budgets			
Unqualified opinion; no major findings	Financial Audit			
All in good standing	Financial Obligations			
Timely submission of all required financial reports.	Financial Reporting			
Complete and accurate filing of all required financial reports.	Financial Reporting			

What is the role of the Treasurer and Finance Committee?

State example

II. Financial Performance Framework – Financial Performance Score	
Rating	Score
Meets Expectations	80 – 100
Approaches Expectations	60 – 79
Fails to Meet Expectations	0 – 59

Financial Performance Score Indicators				
Indicators	Potential Points	Full Credit	Partial Credit	No Credit
Fund Balance	Full Credit – 30 points Partial Credit – 15 points No Credit – 0 points	Y1: >2% Y2: >3% Y3: >4% Y4: >5% Y5: >6% +Y5: >7.5%	Y1: 1-2% Y2: 1.5-3% Y3: 2-4% Y4: 2.5-5% Y5: 3-6% +Y5: 3.75-7.5%	Y1: <1% Y2: <1.5% Y3: <2 Y4: <2.5% Y5: <3% +Y5: <3.75%
Audit Findings	Full Credit – 30 points Partial Credit – 15 points No Credit – 0 points	Unqualified audit with no findings	Unqualified audit with no recurring or material findings	Unqualified audit with recurring or material findings Qualified audit
Debt to Assets Ratio	Full Credit – 20 points No Credit – 0 points	<0.9	N/A	>0.9
Timely Reporting	Full Credit – 20 points Partial Credit – 15 points Partial Credit – 10 points	All quarterly reports, AFR, and audit submitted timely	1 late – 15 points 2 late – 10 points	3-5 late

What is the role of the Treasurer and Finance Committee?

Recap

- Bylaws provide narrow definition.
- Charter application usually has more detail, and is typically part of the charter contract.
- Authorizer review and renewal criteria are very important, but by the time an issue rises to a level of non-compliance it is probably too late.
- Basic idea: Stay in operation, out of headlines, and deploy resources in a way that aligns with the school's accountability.

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- 10 other deadly sins and lesser evils.
- Financial management rubric.

Top Ten Financial Management Mistakes to Avoid

#10 – No finance expertise on the board

- Risk – can be “snowed”, either accidentally deliberately, by management.
- May not have foresight to see warning signs of trouble.
- Need not just expertise, but personality strength to ensure if you see something, you say something.
- Like legal expertise, if you don’t have it on board, hire it.

Top Ten Financial Management Mistakes to Avoid

#9 – No discipline around purchasing and contracts

- Public bidding requirements – examples.
- Policies and procedures should specify thresholds.
- Good idea for board approval of large contracts in addition to second signature.
- Example of good procurement practice:

Materials and Supplies

Less than \$1,000	Less than \$10,000	Greater than \$10,000 but less than \$30,000	Greater than \$30,000
<ul style="list-style-type: none">• No statutory requirement• Best Practice: Obtain 3 verbal quotes	<ul style="list-style-type: none">• No statutory requirement• Best Practice: obtain 3 written quotes	<ul style="list-style-type: none">• Obtain 3 telephone or fax quotes and give written confirmation of accepted offer.• If a lower quote is available than accepted offer, school must submit reason for rejection to lowest bidder.	<ul style="list-style-type: none">• Advertise and let by contract to lowest bidder according to specifications.• RFP must be published twice in a newspaper in the locality, at least 13 days before

Top Ten Financial Management Mistakes to Avoid

#9 – No discipline around purchasing and contracts (continued)

- Principals often sign crazy contracts – employment letters with guarantees, ridiculous copier leases, vending machine deals.
- All contracts should include:
 - Payment terms – upon delivery and acceptance of goods/services.
 - Hard cap or not-to-exceed amounts.
 - Termination right.

Top Ten Financial Management Mistakes to Avoid

#8 – Grants

- Categorical vs. competitive.
- The importance of maximizing FRL%.
- Can be hard to see leakage on categorical; money left on the table.
- Too many competitive grants can distract school from core mission.

Top Ten Financial Management Mistakes to Avoid

#7 – Looking for a superhero

- In 15 years, I have met one person who could do operations and finance well, and that was after five years on the job
- Schools that are operations intensive (e.g., own facility, transportation and foodservice) need a strong operations person. That person may even be able to do student data and human resources compliance reporting, but they are unlikely to be good at financial reporting, budget modeling and re-forecasting.

Top Ten Financial Management Mistakes to Avoid

#7 – Looking for a superhero (continued)

- A great operations person can pay for themselves

Top Ten Financial Management Mistakes to Avoid

#7 – Looking for a superhero (continued)

- A great operations person can pay for themselves:
 - Purchasing, contracts and vendor management.
 - Can stand up to principal – example.
 - Accurate SIS information can drive revenue.
 - Operations failures can lead to student disenrollment, or funding loss of ~\$50K per student (i.e., \$10K/student for the next ~5 years).

Top Ten Financial Management Mistakes to Avoid

#6 – Excessive management organization control

- Who employs the principal?
- Who employs the business manager?
- Can you hire an executive director?
- What do they *think* they are doing – roles and responsibilities, accountability.
- Building reserves
 - Example – budget 15% fee and charge 22%, carry the balance over
 - Example – shared operating surplus

Top Ten Financial Management Mistakes to Avoid

#5 – Bad facility deals

- We are in the best charter school financing market ever! (Notice who this conference sponsors are.) But...
- What is a reasonable percentage of revenue to spend on a facility lease or loan?
- Are financing fees reasonable?
- Managing risk – when yes means no, and when no means yes.
Tip: Be very wary of private developers.
- Ask for help!

Top Ten Financial Management Mistakes to Avoid

#4 – Late reporting

- First sign of a problem.
- Usually accompanied by its close friend, sloppy reporting.
- Get help at first sign of trouble.

Top Ten Financial Management Mistakes to Avoid

#3 – Failure to budget contingencies and build reserves

- Why?
- What is right level?

Top Ten Financial Management Mistakes to Avoid

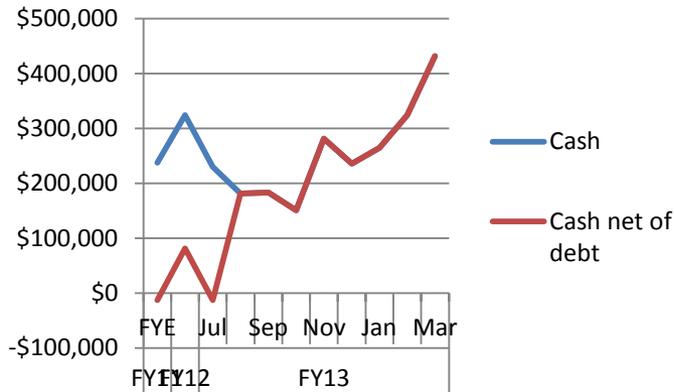
#2 – Lack of controls

- Cash.
- Bank reconciliations; copies of statements.
- Segregation of duties.

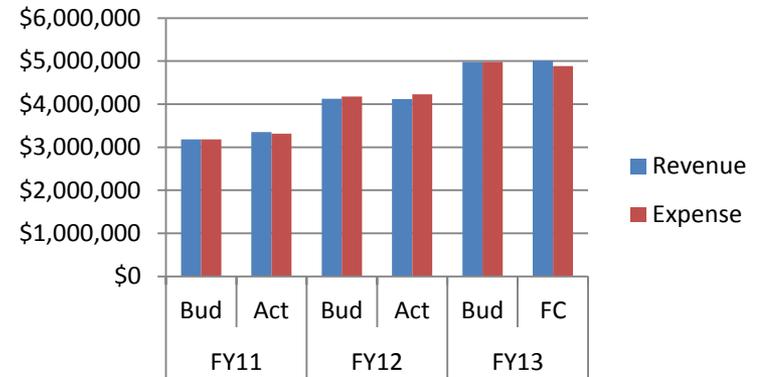
Top Ten Financial Management Mistakes to Avoid

Dashboard Example

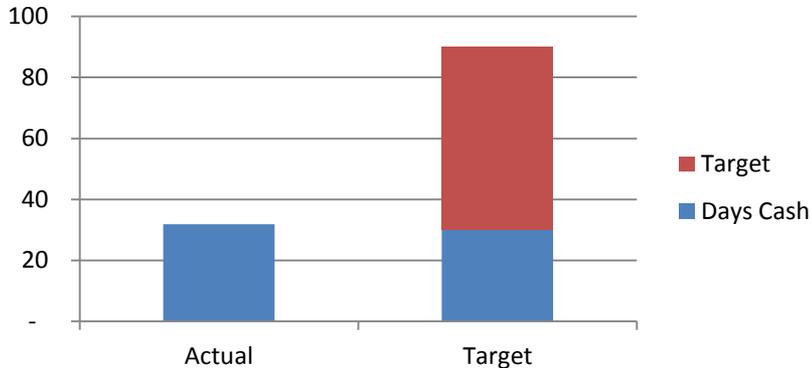
Cash Balances



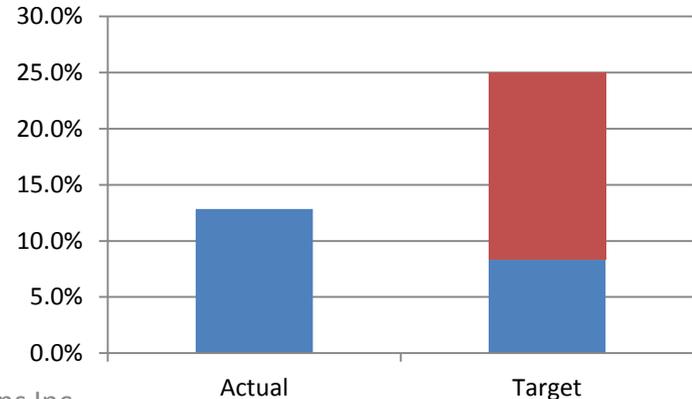
Income Statement FY11-FY13 Budget vs. Actual



Days Cash



Reserves as % of Revenue



Top Ten Financial Management Mistakes to Avoid

#1 – Inertia: failure to adjust

- Most critical time to reforecast is within first month of school.
- Staffing must be adjusted for enrollment reality.
- Never easy but always necessary.
- This is not the time to use your contingency.
- Typical variances – teacher attrition, benefits expense, funding changes, special education.
- Review and adjust monthly.
- Have a quality discussion about redeploying “good guys”.

Top Ten Financial Management Mistakes to Avoid

Recap – Top Ten Financial Management Mistakes to Avoid

- # 10 No finance experience on the board
- # 9 No discipline around purchasing and contracts
- # 8 Grants
- # 7 Looking for a superhero
- # 6 Excessive management organization control
- # 5 Bad facility deals
- # 4 Late reporting
- # 3 Failure to budget contingency and build reserves
- # 2 Lack of controls
- # 1 Inertia

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10 other deadly sins and lesser evils

#1 – The most important numbers are not financial

- The rigor of a school leader’s academic reporting should at least match the rigor of the finance leader’s report. E.g.,
 - “Academic balance sheet” = enrollment status, teacher evaluation, retention.
 - “Academic P&L and forecast” = interim assessment results, updated forecast vs. accountability targets.

10 other deadly sins and lesser evils

#1 – The most important numbers are not financial (continued)

Example

- 2012-13 Teacher Retention

	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
Opening	21	21	21	19	18	18	19	18	18	18
Term/Resign			(3)	(3)	(1)		(1)			(2)
New Hires			1	2	1	1				
Ending	21	21	19	18	18	19	18	18	18	16

10 other deadly sins and lesser evils

#2 – Accounting Method

Schools often use cash basis accounting or the “modified cash” method at their peril

Basis of Accounting	Cash	Modified Cash	Accrual
Characteristics	Record all revenues and expenses when received.	Record short-term revenues and expenses when received – no A/R, A/P.	Record revenue and accrue expenses in period in which they are earned or expended.
Pros/cons	Easy but not accurate; potential to run out of money	Easier but not GAAP; interim reports don't give accurate picture	Need more accounting expertise but accurate at all times.

10 other deadly sins and lesser evils

#3 – Unrelated business

Non-profits are subject to unrelated business tax (UBT) on revenues that are unrelated to their organizational purpose, material, and recurring. A key factor is whether they are competing with for-profit entities. Even worse than paying UBT is the risk of losing 501(c)3 status.*

Most highly-publicized example:
YMCAs competing with fitness centers

* With the exception of real estate.

10 other deadly sins and lesser evils

#3 – Unrelated business (continued)

Charter school examples:

1. School operates a coffee shop and convenience store open to students as well as the public.
2. School provides non-educational administrative services to other schools for a fee.

10 other deadly sins and lesser evils

#4 – Two leaders, no accountability

- First of all, when does a school need an Executive Director in addition to a principal? Ideas:
 - When there are three or more sites.
 - When there is a substantial fundraising program.
 - When there is a special academic program that is funded.
 - When there is a management organization.

10 other deadly sins and lesser evils

#4 – Two leaders, no accountability (continued)

- If there is one, how is budget responsibility assigned?
- Is it an evaluation factor?
 - *Tip: Key evaluation criteria in order of importance are (i) academic performance, (ii) financial performance, (iii) stakeholder satisfaction, (iv) fidelity to design or accountability framework, (v) external relations, and (vi) growth (if applicable).*

10 other deadly sins and lesser evils

#5 – Lawyering up when you don't need to

- Lawyers regularly attend meetings at about 15-20% of charter schools.
 - Advantage: They are in the loop on board dynamics and school issues.
 - Disadvantage: Cost.
 - Recommendation: Have a lawyer on your board and let them make the call when the school needs an attorney.

10 other deadly sins and lesser evils

#6 – “Let’s talk amongst ourselves”

- There should be a legal reason to go into executive session. The reason should be noted in the minutes. Examples:

Executive Session Requirements

- Executive Session can only be held for the following reasons:
 - To discuss the character, professional competence, physical or mental health of a person, provided that person is notified in writing at least 24 hours prior to the meeting and allowed to request that such discussion be held at an open meeting
 - Strategy sessions/negotiations about collective bargaining, or prospective litigation after formal written demand
 - Discussion related to security personnel, plans, or devices
 - Investigative proceedings regarding allegations of misconduct
 - Discussions with individual students or their parents regarding problems of that student or their parents; provided that the student or parent may request that such discussions be held in an open meeting

10 other deadly sins and lesser evils

#7 – Poor risk management

- Brokers have gotten aggressive in approaching charter market.
- Review coverage twice per year.
- Ensure training, e.g.,
 - Does every contractor stepping foot in the school provide a certificate naming the school as an additional insured?
 - Sexual harassment training
 - Incident reporting.
- Be aware of deductibles and fees.

10 other deadly sins and lesser evils

#8 – Asset control

- iPads and laptops tend to grow feet.
- When authorizing capex or major purchases, ask how assets will be protected.

Tip: Try not to purchase fixed assets with federal funds.

10 other deadly sins and lesser evils

#9 – Setting a low bar

- Top operations or finance staff should be roughly equivalent to school leader in stature and experience.
- Maybe even establish formal protocol for direct reporting to board.
- Good interview exercise for finance leader: give them your last two audits and ask them to prepare a presentation to the board based on that information.

10 other deadly sins and lesser evils

#10 – Stuff gets lost

- Use Dropbox to manage board documentation, agendas, minutes.
- Corporations and non-profits increasingly using tools like Board Vantage and Director's Desk to send board packages to board members' iPads, with easy updates. But expensive.

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Financial management rubric

Criterion	High Performing	Average	Unacceptable
Budgeting	Process starts in Dec. so teacher recruitment can commence in Jan. Principals highly engaged in process. At least 2 finance committee reviews. Includes capital budget.	First draft presented in March and two iterations before final approval. Principals engaged in process.	5 minute discussion prior to approval at late June board meeting.
Budget management	Monthly budget reviews with principals, discussion of risks, mitigating factors, and actions; followed by review with finance committee. Contingency = reserves.	Periodic adjustments based on accurate monthly statements and forecasts; clear explanation to finance committee and board.	No adjustments or “secret” adjustments to budget.
Financial reporting	Timely and accurate monthly reporting incl. variance analysis, forecast, balance sheets, cash flow, narrative and dashboard.	Monthly income statement with variance analysis and full year forecast; prior review with finance committee. Discussion of cash balance and reserves.	Income statement but no variance analysis, forecast, or narrative explanation. No balance sheet information.
Procurement	100% compliance with policies and procedures regarding approvals, solicitation and negotiation. Documentation easily auditable.	Approvals of major contracts generally obtained; email approvals can be produced. Two check signers.	No adherence to policies, no capital budget, frequent vendor conflicts and litigation.
Controls	Petty cash and student activities funds accounted for accurately and deposits made regularly. Bank reconciliations performed independently. Copies of bank statements to Treasurer.	Petty cash and student activities funds reconciled periodically. Bank statements reconciled monthly.	Cash all over the place, “separate” checking accounts under school control, no reconciliation of bank statements, reimbursement of credit card expenses without documentation.

Agenda

Thank you!

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Presentation will be uploaded to

www.charterschooltools.org