



Brighter Choice Charter Middle School for Boys Financial Operations

Report of Examination

Period Covered:

July 1, 2011 — July 31, 2013

2013M-348



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 2014

Dear School Officials:

A top priority of the Office of the State Comptroller is to help school officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support school operations. The Comptroller oversees the fiscal affairs of schools statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and School Board governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard school assets.

Following is a report of our audit of the Brighter Choice Charter Middle School for Boys, entitled Financial Operations. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Section 2854 [1][c] of the Education Law, as amended by Chapter 101 of the Laws of 2010.

This audit's results and recommendations are resources for school officials to use in effectively managing operations and in meeting the expectations of taxpayers, students and their parents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

A charter school is a public school financed by local, State and Federal resources that is not under the control of the local school board and is governed by Education Law Article 56. Charter schools have fewer legal operational requirements than traditional public schools. Many of a charter school's operational requirements are contained in Article 56, and in its by-laws, charter agreement and financial management plans. Charter schools are required to set both financial and academic goals. A school's renewal of its charter is dependent on meeting these goals. The Brighter Choice Charter Middle School for Boys' (School) current charter was issued in January 2010.

The School is located in the City of Albany, and is governed by a Board of Trustees (Board), which is currently comprised of seven members. The Board is responsible for the general management and control of the School's financial and educational affairs. The Principal of the School (Principal) is the School's chief executive officer and is responsible, along with other administrative staff, for the School's day-to-day management under the Board's direction. The Director of Finance (Director) is the chief accounting officer and is responsible for maintaining custody of, depositing and disbursing School funds; maintaining the financial records; and preparing the monthly and annual financial reports.

During the 2012-13 school year, the School had 144 students in grades five through seven, and 38 employees. The School's 2012-13 fiscal year budgeted expenses were approximately \$2.71 million, funded primarily with revenues derived from resident pupil tuition billings¹ and State and Federal aid. The School contracts with a not-for-profit foundation (Foundation) for various services. The Foundation provides start-up grants, School facilities, a revolving loan fund and technical assistance to a number of charter schools.

Objective

The objective of our audit was to evaluate the effectiveness of the School's compact² contract with the Foundation. Our audit addressed the following related question:

- Did the School receive all the services from the Foundation as outlined in a compact agreement and is the fee structure of the compact agreement reasonable?

¹ The School bills various local school districts tuition charges to provide educational services to students residing in the respective districts.

² An official contract or formal agreement between two or more parties

**Scope and
Methodology**

We reviewed the School's relationship and contracts with the Foundation for the period July 1, 2011 through July 31, 2013.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit is included in Appendix B of this report.

**Comments of
School Officials and
Corrective Action**

The results of our audit and recommendations have been discussed with School officials and their comments, which appear in Appendix A, have been considered in preparing this report. School officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Board to make this plan available for public review in the Secretary's office.

Compact Contract

Schools require a number of services to adequately conduct business. A school can choose to obtain these services by using an employee to perform the service or hiring an independent service provider. Ultimately, it is the board's responsibility to choose a method that provides the school with the required services in the most reasonably efficient manner possible. As part of this responsibility, all board members must disclose in writing to the school board any interest they or their spouse have in an actual or proposed school contract.³

The School entered into a three-year compact agreement with the Foundation in June 2011. All Board members voted in favor of the compact agreement, except for the Board Chairman, who recused himself from voting because he is also the Foundation's Executive Director. The compact does not describe in detail the services that the Foundation will provide. For example, according to the compact, the Foundation will provide legal and financial assistance, technical support and advocacy at State and local levels to the School. When asked to describe the specific services being provided to the School, the Board Chairman stated that the School receives access to short-term loans from the Foundation and access to educational software, among other services. The fee for these services is 1 percent of total pupil revenue from the prior academic year. The total 2012-13 fiscal year fee due to the Foundation was \$14,801.

As a result of the insufficient detail about the exact services provided, we reviewed all expenses from seven select account codes to determine if there were duplicate services being provided by the Foundation or another entity. We did not find any duplicate services.

In January 2013, the School revised the compact contract with the Foundation; the revised compact supersedes the prior one. The revised compact provides further detail about the specific services that the Foundation could provide the School and increases the fee from 1 percent of total pupil revenue for the 2012-13 fiscal year to 1.5 percent for the following year, and 2 percent for the contract's final year. The increase in the fee percentage over the next two years will place an additional financial burden on the School.

We reviewed the revised compact document and could not determine how delivery of services will be measured because the revised

³ Effective May 28, 2010, Chapter 101 of the Laws of 2010 made applicable to charter schools the disclosure requirements of Section 802 of the General Municipal Law.

compact was insufficiently detailed. Therefore, School officials do not have a means to determine whether the School received the services. The fee structure, based on a percentage of per pupil revenue, does not appear to be reasonable, as the services being provided do not have any bearing on the number of students at the School or the State Education Department's Charter School Tuition rate.⁴ Per a discussion with the Board Chairman, a percentage of per pupil revenue was used because the Foundation wanted to have the School pay a known amount that was based on total revenue. The fee increases in the revised compact because the Foundation intends to expand the services it provides to the School.

In addition, General Municipal Law (GML) requires Board members to disclose their interests in School contracts, in writing, to the Board, with the written disclosure being made a part of the record of the Board's proceedings. During the audit period, there were two Board members who were also officers or directors of the Foundation.⁵ While both filed financial disclosure forms, neither disclosed their relationship with the Foundation on these forms. Although the Board members did not have a prohibited interest in either the 2011 or 2013 compacts between the School and the Foundation,⁶ both individuals were required to provide written disclosure of their interests in the compact to the Board.

When the School enters into contracts that do not provide sufficient detail about the services being provided and do not have a reasonable fee structure – and decision makers have not provided all information regarding potential conflicts of interest – the School is susceptible to incurring costs that are greater than necessary for the services it receives.

Recommendations

1. The Board should ensure that contracts with the Foundation contain sufficient descriptions to determine the benefits, rights and responsibilities of all parties to the contract, and the Board should use this information to monitor compliance with the contract.

⁴ The tuition rate to be used by public school districts with resident students attending charter schools

⁵ One Board member resigned in March 2012 and was not a Board member when the revised compact agreement was approved in January 2013. The other Board member is the Foundation's Executive Director, a position he currently holds.

⁶ As an officer or director of the Foundation, each Board member would be deemed to have an "interest" in the School's contracts with the Foundation (see, GML Section 800[3][c]). As Board members, even if these individuals possessed one or more powers or duties that could give rise to a prohibited interest in the contracts between the School and the Foundation, the Board members' interests in these contracts are not prohibited because there is a statutory exception for interests in contracts with a voluntary non-profit corporation or association, such as the Foundation (see GML Section 802[1][f]).

2. The Board should determine if there is a more cost-effective means to receive the desired services currently being provided by the Foundation.
3. Board members should disclose their interests in School contracts, in writing, to the Board, with the written disclosure being made a part of the record of the Board's proceedings.

APPENDIX A
RESPONSE FROM SCHOOL OFFICIALS

The School officials' response to this audit can be found on the following pages.



February 3, 2014

[REDACTED]
[REDACTED]

NYS Office of the State Comptroller
Division of Local Government and School Accountability
One Broad Street Plaza
Glens Falls, NY 12801

Dear [REDACTED]:

The Board of Directors and school leadership has reviewed the draft report of your examination of the financial operations of the Brighter Choice Charter Middle School for Boys. Accountability is one of the hallmarks of a charter school and it pushes us toward our goal of providing the best educational opportunities to students and families. We appreciated your thorough review of our fiscal operations and are encouraged that it yielded limited findings. We have reviewed the draft report and prepared the following responses.

The audit first highlighted the compact contract with the Brighter Choice Foundation to achieve high-quality instruction and operations at our school. It is common practice for district schools, private schools and charter schools to contract educational service providers in the areas of curriculum design and consulting, student benchmarking and performance, staff professional development, legal services and board governance training, financial management, accounting, human resources, strategic planning and regulatory affairs. As noted in the report, we received these types of services through our compact agreement with no duplicate services received from another entity.

The Foundation has supported the school since inception, beginning with the complex real estate development services to assemble 26 parcels of land for our facility. They also secured an \$8 million bridge loan to ensure that the building opened on time and provided a \$150,000 grant to help fund first-year expenses. In 2011 the school and Foundation recognized that the school would benefit from a more formal arrangement for on-going services to ensure the long-term success of the school. The spirit of the relationship was not intended to be purely transactional, as with an attorney or consultant. Rather, it was intended to be a partnership where both parties are pursuing

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the same goal of academic and operational excellence on behalf of our Brighter Choice students and their families.

The Board signed an amended and expanded compact agreement in 2013 to provide more clarity to the relationship after identifying a growing need for services. In the past two years, the Foundation has more than doubled the size of their staff available to service the needs of our school. Those individuals are now in our schools regularly, consulting with our teachers and administrative leaders to develop and improve our implementation of the Common Core Standards, community engagement, organizational capacity, and fiscal management.

The board considered that the cost of acquiring those services from individual providers (attorneys, educational consultants, testing services, marketing consultants, etc.) would likely exceed the \$14,801 charged in 2012-2013. We also recognized that the need for such services also increases with every new student the school enrolls, as does the relative need for classrooms, teachers, administrative staff, and so forth. Similar educational service providers offer a suite of services for fees ranging from 1% to 12% of per-pupil revenues, depending on the level of service and degree of management provided. With these considerations, the board determined that the 1% to 2% per-pupil revenue fee structure was the most cost-effective method of providing these services on a gradually increasing scale. This structure also allows the school some relief should enrollment and revenues decline.

Your report also noted the disclosure requirements of our board members who were also officers or directors of the Foundation, a relationship which always been very transparent to all involved parties. As stated in your report, those members did not have a prohibited interest in these agreements, though they did recuse themselves from voting on the compact agreement. We will work to ensure the board minutes and disclosure forms are completed appropriately to reflect these circumstances in writing.

The board has carefully monitored the level of service provided by the Foundation and believes that the school has benefited greatly from this partnership. We have ensured the Foundation has complied with the terms and the spirit of the contract to strengthen our school. We also determined that this was a very cost-effective method of acquiring the necessary support services for the school. We appreciate the disclosure recommendations and will implement them immediately.

Thank you for this opportunity to participate in this review process and respond to your findings.

Sincerely,

Marcus Puccioni
Director of School Quality
Brighter Choice Charter Middle School for Boys

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

The objective of our examination was to assess the School's financial operations. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: general governance, financial oversight, third-party relationships, inventory controls, control environment, cash receipts and disbursements, purchasing, payroll and information technology.

During the initial assessment, we interviewed appropriate School officials, performed limited tests of transactions, and reviewed pertinent documents such as the School's charter, financial policies and procedures manuals, Board minutes and financial records and reports. In addition, we reviewed the School's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we determined that controls appeared to be adequate and limited risk existed in most of the financial areas we reviewed. We then decided upon the reported objective and scope by selecting for audit areas that appeared to have weak controls in place. We selected compact contracts for further audit testing.

To accomplish our audit objective and obtain valid audit evidence, our procedures included the following steps:

- We reviewed compact contracts, Board minutes and invoices, and we interviewed School officials to determine the compact contract terms.
- We judgmentally selected expense codes where services outlined in the compact contract would be recorded. Next, we reviewed all claims for the expenses for the selected codes to determine what service was provided and whether the service should be provided by the Foundation as part of the compact contract. The expense codes selected were accounting and auditing services, staff recruitment, student recruitment, consultant, legal, staff development and other.
- We reviewed Board minutes to determine when the Board approved the compact contract. Next, we determined which Board members were present at the Board meeting when the compact contract was approved.
- We reviewed the Board members' conflict of interest forms submitted to the Charter School Institute⁷ to determine if any Board member had a conflict of interest with the Foundation and if a Board member did, whether that Board member voted on the compact contract.
- We interviewed School officials to determine if any Board member with a conflict of interest was involved in the presentation and discussion regarding the compact contract.

⁷ The Institute, created by the State University of New York Board of Trustees, is charged with monitoring of overall charter school operations.

We conducted this performance audit in accordance with GAGAS. 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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