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ACTION MEMORANDUM

To: SPCSA Board

From: Mark Modrcin, Director of Authorizing
Mike Dang, Manager of Organizational and Financial Performance

Subject: Agenda Item No. 6: Recommendations under the SPCSA Financial Performance Framework for FY21

Date: January 28, 2022

Background

As the Authority is aware, NAC 387.775 requires that all public charter schools undergo an annual financial audit conducted by an independent third-party. These audits must be submitted to governing boards no later than November 1 of each calendar year, and subsequently must be submitted to the SPCSA by December 1 of each year.

The results of these annual audits are then analyzed against the SPCSA Financial Performance Framework, which is a critical tool in evaluating a charter schools' financial well-being, health, and performance as part of ongoing monitoring and the renewal decision making process. Charter schools have the autonomy to manage their finances consistent with state and federal law; however, sponsors must ensure that the schools they sponsor are financially stable and meeting SPCSA board approved financial performance standards.

As a reminder, the SPCSA Financial Performance Framework includes eight indicators, four aimed at assessing the near-term health of a school and four aimed at assessing the long-term sustainability and viability of a school. These indicators are as follows:

Near Term Indicators	**Sustainability Indicators**
Current Ratio	Total Margin and Aggregated Three-Year Total Margin
Unrestricted Days Cash-On-Hand Ratio	Debt to Asset Ratio
Enrollment Variance[1]	Cash Flow
Debt (or Lease) Default	Debt or Lease Service Coverage Ratio

For each indicator, schools receive one of three ratings: Meets the Standard, Does Not Meet the Standard, or Falls Far Below Standard.

As stated in the SPCSA Financial Performance Framework technical guide, poor financial performance measure ratings may result in intervention by the SPCSA. Generally, a school with a financial framework profile results that include at least one indicator rated at Falls Far Below Standard and/or at least three indicators rated at Does Not Meet Standard may be recommended to enter the intervention process.

The Authority has three levels of intervention when schools do not meet financial standards. These levels are as follows: Notice of Concern, Notice of Breach and Notice of Intent to Terminate.

Analysis

SPCSA staff have reviewed all Fiscal Year Ending June 30, 2021 (FYE 21) independent financial audits received through January 4, 2022, and schools were provided preliminary ratings against the SPCSA Financial Performance Framework standards on December 22, 2021. SPCSA staff provided schools a three-week window to review and confirm or comment on performance against the established standards as adopted by the Authority.

Overall, results under the SPCSA Financial Performance Framework were strong, with the vast majority earning a 'Meets Standard' rating in the majority of indicators. Specifically, of the 37 sponsored charter schools in the SPCSA portfolio for FYE 21, this memo regards SPCSA staff reviews, ratings and recommendations regarding 25 of those schools which submitted their audits. It is staff's intent to present the other schools at the Special February 15th Board Meeting held for the purpose of reviewing the financial performance of the other schools. Of those audits presented today, 22 earned "Meets Standard" ratings in at least six of the seven (normally eight) measured indicators for FYE 21. Of the 22, 15 schools met performance standards under all seven measured indicators (including GALS which met standards on all six of their six measurable indicators[2]). All SPCSA-sponsored schools met the performance standard under the Debt Default measure.

A small number of schools earned a Does Not Meet Standard rating in three or more indicators, and/or earned one or more Falls Far Below Standard ratings under any of the eight financial

[1] Enrollment Variance was adopted by the Authority at its June 25, 2021 board meeting for FYE 22. As such, no results for FYE 21 will be presented.

[2] The Cash Flow measure formula factors in two years of surplus (deficit) margins. GALS's only had one year of operation at the time of this review, which was FYE 21. GALS had a positive margin of $419,000 for FYE 21.

rating indicators. SPCSA staff have consulted with each of these schools to gather any explanatory context and additional evidence about their financial standing since releasing preliminary data in mid-December. The schools, along with their results under the financial framework as well as staff analysis are as follows[3]:

Beacon Academy

Current Ratio	UDCOH	Enrollment Forecast	Debt Default	Total Margin	Debt to Asset Ratio	Cash Flow	Debt Coverage Ratio
MS	MS	NR	MS	MS	MS	FFBS	DNMS

Beacon Academy's negative Cash Flow means that its ending cash balance for FYE 21 was less than its ending cash balance for FYE 20. This reduction in Beacon's ending cash balance, which was approximately $2.5 million, is reflected in the Cash Flow measure. The school had notified SPCSA staff over the past two years that it was planning to acquire a new campus and was building its cash reserves for that planned usage. Consequently, the drawdown is primarily attributable to the planned and SPCSA-approved purchase and rehabilitation of a new "East" campus facility which required the use of these funds.

The school's Debt Coverage Ratio measure is rated as DNMS. The school has indicated that the amount showing and being counted as the current portion of its Note Payable is not the current portion but is the total balance of over $1 million. The effect of this is to overstate the current portion and to show a higher expense than the school is scheduled to incur. Consequently, the school is working with its auditor now to correct this and to submit to the SPCSA the corrected figures. Even with the amount now named by the school as the total balance being treated as a planned payment amount, the rating is a DNMS. Consequently, the "outside risk" regarding this measure appears to be the DNMS and, if the school is able to submit the paperwork it is working on, the rating should only qualify to improve to a MS.

In conclusion, the SPCSA Financial Framework technical guide allows for the Authority to consider mitigating circumstances for the Cash Flow measure, particularly in cases of a large capital investment. Beacon Academy of Nevada has provided sufficient evidence that this has occurred, and the school has also provided a potentially reasonable explanation regarding the Debt Service Coverage Ratio. The school otherwise has ratings reflecting a healthy financial position. *Consequently, staff does not recommend any action with regard to Beacon Academy.*

[3] MS = Meets Standard; DNMS = Does Not Meet Standard; FFBS = Falls Far Below Standard

Equipo Academy

Current Ratio	UDCOH	Enrollment Forecast	Debt Default	Total Margin	Debt to Asset Ratio	Cash Flow	Debt Coverage Ratio
MS	DNMS	NR	MS	MS	MS	FFBS	MS

Equipo Academy earned a DNMS rating for the UDCOH measure due to its having 37 Unrestricted Days of Cash on Hand. That is below the UDCOH threshold required of having 60 days of cash on hand for a MS rating. Staff considered Equipo's Accounts Receivable (AR) balance in its analysis to understand if the school would meet the 60-day threshold if this figure were included. Staff calculated that Equipo would have had to convert just over $500,000 of its receivables into cash to have met the 60 day or greater threshold. Staff noted that the school had $455,000 in federal grant related AR which the school indicated could have helped the school move it closer to the 60-day threshold. Staff analyzed this and noted it would have lifted the measure to 58 days, or much closer to the published standard.

The Cash Flow measure for Equipo received a FFBS, which reflects a decrease in the Cash Balance of the school on a year over year basis. Essentially the cash balance for the SYE 21 was $824,000 which reflects a decline of $470,000 from its cash balance of $1.3 million for the SYE 20. Regarding the FFBS rating, the school indicated that the decline was anticipated by the school. This is because the school received additional funds in one period which lifted its cash balance and then used those funds especially in the following year, the SYE 21.

The additional funds included a Paycheck Protection Program (PPP) loan of $863,000. Equipo stated that these dollars were used for some of its programs which naturally drew down the cash and resulted in the lower cash balance at SYE 21. Equipo used the critical PPP funding to, among other things, underwrite their childhood nutrition programs, and according to the school, this enabled them to openly serve the broader East Vegas community with summer and school-year breakfast and lunch services. Equipo also indicated it "received that funding in FY 20 and then expended it largely in FY 21" and that this use of funds "was something [the] board and [principal] were aware of that [Equipo] would be spending more than usual during the pandemic, but especially in the case of this unique emergency award it skewed [their] cash in the bank since the cash was received in one year and largely spent in another."

Consequently, staff does not recommend any action with regard to Equipo Academy as a result of the above ratings and information.

Nevada Connections Academy

Current Ratio	UDCOH	Enrollment Forecast	Debt Default	Total Margin	Debt to Asset Ratio	Cash Flow	Debt Coverage Ratio
MS	MS	NR	MS	DNMS	MS	DNMS	DNMS

SPCSA staff have reviewed the circumstances around Nevada Connections Academy's financial performance. The negative total margin for the year can be attributed to a 60% reduction in revenue pursuant to a contractual reduction in the school's enrollment. The school explained it could only be offset by a 42% reduction in expenses, and the school indicated it continues to aggressively reduce costs to be in line with their new enrollment levels. The negative cash flow from a drawdown of cash through FYE 21 was a result of the school using cash reserves to close the gap created when the decrease in revenue could not be matched by the decrease in expenses. According to NCA, the debt service coverage ratio not meeting standards is also a consequence of the negative total margin.

Given the progress the school has made in mitigating the causes of these shortfalls, SPCSA staff does not recommend any action with regard to Nevada Connections Academy.

Quest Preparatory Academy

Current Ratio	UDCOH	Enrollment Forecast	Debt Default	Total Margin	Debt to Asset Ratio	Cash Flow	Debt Coverage Ratio
DNMS	MS	NR	MS	MS	DNMS	MS	DNMS

During the school year ending (SYE) 21, Quest Preparatory Academy was operating under a Notice of Concern due to their SYE 20 financial performance SPCSA staff recognizes the significant improvement of Quest as it relates to the school's financial performance. One area of significant improvement was to Quest's Total Margin. The school had run a deficit in each of its prior three years but turned in a surplus for FYE 21. Another area of significant improvement was to Quest's Unrestricted Days of Cash On Hand (UDCOH). During the fiscal year, Quest improved its UDCOH to 36 days, more than doubling its prior year ratio of 16 days. This means it doubled the number of days it could pay expenses at the average daily expense level of the school during FYE 21. The standard is 60 or more days of UDCOH or "Greater than or equal to (>=) 30 and less than (<) 60 UDCOH and one-year trend is positive."[4] While this improvement is a sign that the school is on the right track, Quest has yet to meet the MS performance standards under three of the eight measures within the framework. *Consequently, SPCSA staff recommend no action with regards to Quest and that the Authority keep the school under an active Notice of Concern.*

Discovery Charter School

Current Ratio	UDCOH	Enrollment Forecast	Debt Default	Total Margin	Debt to Asset Ratio	Cash Flow	Debt Coverage Ratio
MS	MS	NR	MS	MS	DNMS	MS	MS

During the school year ending (SYE) 21, Discovery Charter School was operating under a Notice of Concern due to their SYE 20 financial performance. During SYE 21, the school shared that they undertook many efforts to improve their overall financial health and were able to improve their finances significantly. For these efforts, they received "Meets Standards" on every rating except for the Debt to Asset ratio. It is noteworthy that this ratio did improve to "Does

[4] SPCSA Financial Performance Framework Technical Guide (FPF Technical Guide SPCSA 2021.06.25 posted 07 02.docx), page 10.

Not Meet Standards" from "Falls Far Below Standards" the prior year. *In light of these improvements, staff recommends that Discovery's Notice of Concern be lifted.*

Conclusion and Recommendations

After considering the results above, as well as additional information provided by the staff review process, which included discussions with several schools, SPCSA staff has tailored recommendations so as to be responsive to the available performance data while also considering the individual context for each school.

The Financial Performance Framework technical guide states that a school earning at least one Falls Far Below rating and/or at least three Does Not Meet Standard ratings may be recommended for intervention. SPCSA staff has performed further review and analysis on each school that received at least one Falls Far Below and/or at least three Does Not Meet Standard ratings as commented on above.

Consequently, SPCSA staff recommends that the Authority:

1. Remove the Notice of Concern from Discovery Charter School.
2. Keep Quest Preparatory Academy under an active Notice of Concern.

Proposed Motion:

Adopt the presented financial performance framework results for the schools listed in the attached ratings summary document for FY21 for all indicators except the Enrollment Forecast Accuracy measure, which was not rated; and

Rescind the Notice of Concern for Discovery Charter School, removing them from the Financial Performance Framework intervention ladder as the school is Meeting Standards as described in the technical guide.

NOTE: SPCSA staff anticipates presenting results for the following schools at the Authority board meeting scheduled for February 15, 2022:

- Doral Academy of Nevada
- Doral Academy of Northern Nevada
- Explore Academy
- Legacy Traditional Schools – Nevada
- Mater Academy of Nevada
- Mater Academy of Northern Nevada
- Nevada Virtual Academy
- Pinecrest Academy of Nevada
- Pinecrest Academy of Northern Nevada
- Signature Preparatory Academy
- Somerset Academy of Las Vegas
- Sports Management and Leadership Academy of Nevada (SLAM!)