

ARIZONA COURT OF APPEALS

DIVISION ONE

LEGACY EDUCATION GROUP DBA EAST VALLEY HIGH SCHOOL, an Arizona non-profit corporation; and TUCSON PREPARATORY SCHOOL, an Arizona non-profit corporation,

Plaintiffs/ Appellants,

v.

ARIZONA STATE BOARD FOR CHARTER SCHOOLS,

Defendant/ Appellee.

Court of Appeals
Division One
No. 1 CA-CV 17-0023

Maricopa County
Superior Court
No. CV2016-051845

**PLAINTIFFS/APPELLANTS'
COMBINED OPENING BRIEF AND APPENDIX**

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INTRODUCTION

This is a case about whether a state agency must follow the Administrative Procedure Act (“**APA**”) and promulgate rules to implement policies that affect all entities regulated by the agency.

This Court has addressed this same situation—an agency that thinks its actions are exempt from rulemaking—many times before. The previous cases confirm that under the plain text of the APA, all state agencies must promulgate rules unless the legislature has enacted an express exemption.

This case, involving Defendant/Appellee Arizona State Board for Charter Schools (the “**Board**”), should be no different. When the Board adopts policies that affect all the charter schools regulated by the Board, the Board must follow the APA. The superior court erred in holding otherwise, and its ruling should be reversed.

STATEMENT OF FACTS AND CASE*

I. Background on charter schools and the Board.

In Arizona, a charter school is a public, state-funded school designed to “provide additional academic choices for parents and pupils” and “to provide a learning environment that will improve pupil achievement.”

[A.R.S. § 15-181\(A\)](#).

A charter school must obtain a charter from an authorized sponsor.

[A.R.S. § 15-183\(A\)](#). A charter school must comply with some, but not all of the state laws that govern traditional school districts. *Id.* at [§ 15-183\(E\)\(5\)](#).

In addition, it must comply with the terms of its charter contract (an agreement between the school and its sponsor), any laws that apply specifically to charter schools, and any policies adopted by the school’s sponsor. *Id.* [§ 15-183\(E\)](#) (listing the charter contract requirements). A charter school’s sponsor is primarily responsible for regulating the school, including ensuring that the school is improving student performance and

* Selected record items cited are included in the Appendix attached to the end of this brief, cited by page numbers (e.g., [APP123](#)), which also match the PDF page numbers and function as clickable links. Other record items are cited with “IR-” followed by the record number. Page citations to record items refer to the PDF page numbers of the electronic record, not the page numbers at the bottom of filings.

using state funding appropriately. Arizona has more than 600 charter schools.

The Board sponsors the vast majority of charter schools.¹ The Board is an Arizona state agency formed by the legislature in 1994, at the same time as the legislature first authorized charter schools. *See* 1994 Ariz. Sess. Laws 2515, 2517, ch. 2, § 2 (H.B. 2002, 41st Leg., 9th Sp. Sess.). The Board has the authority to “[d]etermine . . . policy” and can “[s]ue and be sued.” [A.R.S. §§ 15-182\(E\)\(6\), \(F\)\(2\)](#). [*See also* [APP129](#), ¶ 5 (“Defendant Arizona State Board for Charter Schools is an agency of the State of Arizona . . .”).]

Plaintiffs/Appellants Legacy Education Group and Tucson Preparatory School (the “**Schools**”) operate two charter schools, both of which are sponsored by the Board: East Valley High School and Tucson Preparatory School. [[APP128-29](#), ¶¶ 1-3.]

II. Pre-2012 supervision of charter schools.

For nearly two decades (from 1994 to 2012), the Board and other sponsors had the power and responsibility to supervise charter schools. In particular, by statute each sponsor (including the Board) had “oversight

¹ The other sponsors are the State Board of Education or an Arizona public university or community college district. *See* [A.R.S. § 15-183\(C\)](#).

and administrative responsibility for the charter schools” that it sponsored. A.R.S. § 15-183(R).[†] As part of that “oversight and administrative responsibility,” the sponsor was required to review every charter school “at five year intervals.” *Id.* §§ 15-183(R),[†] 15-183(I)(3).[†] In addition, the sponsor had the express power to “revoke a charter at any time.” *Id.* § 15-183(I)(3). In addition to those powers and responsibilities applicable to all sponsors, the Board also had specific authority and obligation to “[e]xercise general supervision over charter schools” it sponsored. A.R.S. § 15-182(E)(1). [See also APP129, ¶ 9 (“Pursuant to statute and the terms of the charter contracts, the Board exercises general supervision . . .”).]

Since its inception, the Board has exercised that authority and those obligations through two types of administrative activities: (1) codified rules applicable to all schools, and (2) individual adjudications specific to a particular school. The rules applicable to all charter schools appear in the Arizona Administrative Code and went through the ordinary administrative rulemaking process applicable to all agencies. See [Ariz.](#)

[†] Statutes in this section marked with the “†” symbol refer to the version in place before August 1, 2012. A copy of that historical version is attached at [APP068-69](#).

[Admin. Code R7-5-101](#) to [R7-5-504](#) (Board rules for charter schools). For individual adjudications, the Board must follow specific statutory procedures, including notice to the school, an opportunity “to correct the problems,” and “a public hearing.” A.R.S. § 15-183(I)(3).[†]

III. The legislature requires the Board to create frameworks.

In 2012, the legislature sought to bring more formality to the standards by which the Board and other charter schools would be measured. The 2012 legislation created A.R.S. § 15-183(R), which requires the Board to “adopt[]” a “performance framework” to govern charter schools. 2012 Ariz. Sess. Laws 733, 741, ch. 155, § 1 (S.B. 1424, 50th Leg., 2d Reg. Sess.) (codified at [A.R.S. § 15-183\(R\)](#)). The performance framework must address three broad topics: (1) “academic performance,” (2) “operational expectations,” and (3) “[i]ntervention and improvement.” *Id.* The 2012 legislation did not exempt the Board from following the APA or its rulemaking requirements.

Then, in 2013, the legislature amended A.R.S. § 15-183(R). The sole amendment to that subsection required the Board to make the frameworks publicly available on the internet. *See* 2013 Ariz. Sess. Laws 327, 336, ch. 68, § 1 (S.B. 1204, 51st Leg., 1st Reg. Sess.) (adding “shall be publicly available,

shall be placed on the sponsoring entity's website" to [A.R.S. § 15-183\(R\)](#)).

The 2013 legislation, like the 2012 legislation, did not exempt the Board from following the APA or its rulemaking requirements.

IV. The Board creates frameworks and begins the rulemaking process.

Following that new legislation, in 2012 the Board created an Academic Framework and a Financial Framework (together the "Frameworks" at issue in this case). [[APP136](#) (Academic Performance Framework and Guidance (originally eff. Oct. 9, 2012), June 13, 2016 rev.); [APP154](#) (Financial Performance Framework and Guidance (originally eff. Aug. 13, 2012), June 13, 2016 rev.); *see also* [APP129](#), ¶ 10.]²

About a year after first issuing the Frameworks, the Board began the formal rulemaking process to codify the Frameworks as rules. It opened a rulemaking docket in September 2013. *See* 19 Ariz. Admin. Reg. 2857 (Sept. 20, 2013).

Meanwhile, the Auditor General issued a report recommending that the Board formally promulgate the Frameworks as rules. Arizona Auditor

² While this case was pending the Board issued new Frameworks. This brief refers to the latest versions presented to the superior court. [[APP136-76](#).] The Frameworks that applied when the complaint was filed are available at IR-8.

General, Report No. 13-12 (2013) at 33 [copy at [APP070-122](#)] (“**Auditor General Report**”) (“Specifically, the Board should adopt rules to define board standards for academic, financial, and operational performance. . . .”); *see also id.* at 20-21 [[APP096-97](#)].³ The Board responded to the Auditor General and expressly committed to implementing the recommendation to promulgate rules:

[Auditor General recommendation:] 1.7 To ensure that it can exercise appropriate oversight of charter schools based on its performance standards, the Board should *adopt rules* to define board standards for academic, financial, and operational performance

[Board response:] The finding of the Auditor General *is agreed to* and the audit recommendation *will be implemented*.

[[APP119](#) (emphasis added).]

After receiving that recommendation from the Auditor General, the Board issued a notice of proposed rulemaking. *See* 20 Ariz. Admin. Reg. 307 (Feb. 14, 2014). The notice specifically purported to implement A.R.S. § 15-183(R). *Id.* at 308, § 2. The notice further explained, “[t]hree new

³ The complaint referenced the Auditor General Report, so it may be considered in connection with the motion to dismiss. [[APP132](#), ¶ 25.] *See Coleman v. City of Mesa*, [230 Ariz. 352, 356](#), ¶ 9 (2012) (“[P]ublic records regarding matters referenced in a complaint, are not ‘outside the pleading’ . . .”).

Sections added by this rulemaking establish the Board’s academic and financial performance expectations for charter holders *as required by* A.R.S. § 15-183(R).” *Id.* at § 5 (emphasis added; citations omitted). The Board never took any further action on that rulemaking, however, and the rulemaking therefore expired without the Board ever finalizing the proposed rules.

Although the first rulemaking died for lack of Board action, the Board opened another rulemaking docket two years later. *See* 22 Ariz. Admin. Reg. 823 (Apr. 15, 2016). The 2016 rulemaking docket confirmed that the rulemaking would cover the Frameworks. The notice stated that “the Board intends to place in rule Board guidance regarding performance, financial, and operational standards. . . .” *See* 22 Ariz. Admin. Reg. at 824, § 2.

V. The Schools sue the Board for violating the rulemaking process.

In the meantime, the Board continued to apply the Frameworks to charter schools even though the Board never promulgated them using the APA’s rulemaking process. [[APP131](#), ¶¶ 20-24.] As a result, the Schools sued the Board in superior court, contending that the Board violated the

APA by creating and using the Frameworks without complying with the rulemaking requirements. [[APP128-34.](#)]

The Board moved to dismiss, arguing essentially that the Board did not have to follow the APA in promulgating the Frameworks, and that in any event the existing rulemaking docket effectively mooted the case. [IR-5.] That motion was briefed in parallel with summary judgment motions and cross-motions filed by the Schools and the Board. [IR-6 to IR-12; IR-15 to IR-16; IR-19 to IR-20.]

Before oral argument, the Board asked the court to take judicial notice of the 2016 proposed rulemaking. [IR-24.] The Board's 2016 proposed rules, like the 2014 proposed rules, cited A.R.S. § 15-183(R) and incorporated many elements of the Frameworks into the proposed rules. *See* 22 Ariz. Admin. Reg. 3057 (Oct. 28, 2016).

The superior court held argument and ruled from the bench at argument. The court (Hon. John R. Hannah) granted the Board's motion to dismiss. It explained that "the Administrative Procedure[] Act does not apply to the frameworks – the performance framework that is described in ARS Section 15-183(R)." [[APP230](#) at 54:6-11.]

The superior court entered judgment [IR-29], and the Schools filed a timely notice of appeal. [IR-30.]

STATEMENT OF THE ISSUE

1. Agency action qualifies as a “rule” that triggers rulemaking requirements if it is “an agency statement of general applicability that implements, interprets or prescribes law or policy, or describes the procedure or practice requirements of an agency.” [A.R.S. § 41-1001\(19\)](#). The Board’s Frameworks apply to all charter schools it sponsors and implement and interpret the laws and procedures that apply to charter schools. Did the superior court err in ruling that the APA does not apply to the Frameworks?

STANDARD OF REVIEW

“Dismissal of a complaint under Rule 12(b)(6) is reviewed de novo.” *Coleman*, [230 Ariz. at 355](#), ¶ 7. This Court also reviews de novo whether action “is a rule within the meaning of the APA.” *Ariz. State Univ. v. Ariz. State Ret. Sys.*, [237 Ariz. 246, 250](#), ¶ 14 (App. 2015) (“*ASU*”).

ARGUMENT

I. The Frameworks are invalid because the Board acted contrary to law by implementing rules without complying with the APA.

The Frameworks satisfy the APA’s definition of a rule, and as a result the Board acted contrary to law by promulgating them outside the required APA process. This issue is controlled by statute; this Court has repeatedly enforced the rulemaking requirements and rejected agencies’ attempts to evade the statutory requirements.

For these reasons, the superior court erred in dismissing the Schools’ complaint. “Dismissal is appropriate under Rule 12(b)(6) only if as a matter of law [] plaintiffs would not be entitled to relief under any interpretation of the facts susceptible of proof.” *Coleman*, 230 Ariz. at 355-56, ¶ 8 (quotation marks omitted; alteration in original). “[C]ourts must assume the truth of all well-pleaded factual allegations and indulge all reasonable inferences from those facts” *Id.*, ¶ 9.

A. The APA requires agencies to follow specific rulemaking procedures.

The APA broadly defines a “rule” as any generally applicable agency statement that implements a statute or describes agency procedure:

“Rule” means an agency statement of general applicability that implements, interprets or prescribes law or policy, or describes the procedure or practice requirements of an agency.

[A.R.S. § 41-1001\(19\)](#). An agency must create a rule when, for example, a law “does not set forth the calculations to be made and leaves much to [the agency’s] discretion.” *Carondelet Health Servs., Inc. v. AHCCCS*, [182 Ariz. 221, 228](#) (App. 1994). In such circumstances, if a rule is not “promulgated in accordance with the provisions of the APA, . . . it is invalid.” *Id.*

Among other things, the APA’s provisions require the agency to create a public docket for the rule and publish a notice in the Arizona Administrative Register, including the “exact wording of the rule.” See [A.R.S. §§ 41-1021, 41-1022](#). These notice requirements allow the public and affected entities to meaningfully participate in the regulatory process. By statute, the public has a right to submit comments about the proposed rule and even call for an oral proceeding about the proposed rule. [A.R.S. § 41-1023\(B\)–\(C\)](#). The agency must then consider the comments of the public, the rule’s economic impact (including a cost-benefit analysis), and any comments about the economic impact. [A.R.S. §§ 41-1024\(C\), 41-1055](#). The agency must also maintain a complete record of this process in order to

facilitate judicial review. [A.R.S. § 41-1029\(A\)](#) (“An agency shall maintain an official rule making record.”).

Following these procedures helps to create a transparent and fair regulatory process. Public participation in the process helps to ensure that the rules operate fairly and provides opportunities for others to point out deficiencies in the substance of the rules. In light of these goals, the legislature created a “[r]egulatory bill of rights” “[t]o ensure fair and open regulation.” [A.R.S. § 41-1001.01\(A\)](#). This bill of rights guarantees the public’s right to “participate in the rule making process.” [A.R.S. § 41-1001.01\(A\)\(5\), \(6\), \(17\)](#).

B. The Frameworks satisfy the APA’s definition of “rule.”

The Frameworks are and purport to be (1) “an agency statement of general applicability,” that (2) “implements, interprets or prescribes law or policy, or describes the procedure or practice requirements of an agency.” [A.R.S. § 41-1001\(19\)](#). Consequently, they are rules. *See, e.g., ASU, 237 Ariz. at 250, ¶ 16* (“Thus, barring any exemptions, an agency statement is a rule, subject to the APA’s rulemaking procedure, if it, first, is generally applicable, and, second, implements, interprets or prescribes law or policy, or describes the procedure or practice requirements of an agency.”).

1. The Frameworks satisfy the first requirement.

The complaint alleged that “[t]he Frameworks are generally applicable to all charter schools sponsored by the Board” [APP130, ¶ 13; *see also id.*, ¶ 14.] The terms of the Frameworks confirm that they satisfy the general applicability requirement. Both the Academic and Financial Frameworks expressly apply to “all Charter Holders in [the Board’s] portfolio.” [APP138 (Academic Framework); APP156 (Financial Framework).]

In other words, they apply to every entity to which they could possibly apply. The Board did not dispute this below. Consequently, the Frameworks are “statement[s] of general applicability” and meet the first requirement. [A.R.S. § 41-1001\(19\)](#); *see also Carondelet*, 182 Ariz. at 227 (“The first element is met since AHCCCS admits that its methodology is generally applied to all hospitals.”).

2. The Frameworks satisfy the second requirement.

The Frameworks also satisfy the second element because they “implement[], interpret[] or prescribe[] law or policy, or describe[] the procedure or practice requirements of an agency.” [A.R.S. § 41-1001\(19\)](#).

That list is disjunctive, so agency action qualifies as a rule if it satisfies any of the conditions. The Frameworks satisfy all of them.

(a) The Frameworks implement law and policy.

The Frameworks *implement* the Board’s statutory directive to measure and evaluate charter schools’ performance under A.R.S. §§ 15-183(I) and 15-183(R), which require the Board to adopt frameworks. The Academic Framework even says so, expressly referencing A.R.S. § 15-183(R):

As the authorizer or sponsor of charter schools, the State Board for Charter Schools must adopt a performance framework that includes the academic performance expectations of the charter school and the measurement of sufficient progress toward the academic performance expectations (*A.R.S. § 15-183(R)*).

[[APP138](#) (emphasis added).] The statute further specifies that the Board will rely on the Frameworks “[i]n *implementing* its oversight and administrative responsibilities” [A.R.S. § 15-183\(R\)](#) (emphasis added).

(b) The Frameworks interpret and prescribe law and policy.

The Frameworks also *interpret* A.R.S. § 15-183(R). Agency action “interprets” a statute when “the statute leaves open questions.” [ASU, 237 Ariz. at 251, ¶ 18](#). For example, this Court has held that ambulance rate schedules qualify as rules because they “specify such things as how a fraction of an hour is to be charged, how mileage is to be charged, the

assessment of charges for the transport of multiple patients, what constitutes a minimum charge, when the rate for advanced life support may be charged, and other items which are generally applicable to all ambulance companies statewide.” *Sw. Ambulance, Inc. v. Ariz. Dep’t. of Health Servs.*, [183 Ariz. 258, 261](#) (App. 1995) (superseded by statute on other grounds).

Here, rather than set forth all of the details, § 15-183(R) instead “leaves much to the [agency]’s discretion.” *See ASU*, [237 Ariz. at 251, ¶ 19](#) That statute sets forth only the broad categories that the Frameworks must address. The Board necessarily must interpret the statute to flesh out the details. It did so through the Frameworks.

For example, both the Academic Framework and the Financial Framework specify specific indicators, measures, metrics, targets, and ratings. [[APP139](#) (Academic Framework); [APP156-57](#) (Financial Framework).] The Financial Framework creates specific thresholds and financial metrics. It specifies three different levels of liquidity (more than 30 days, between 15 and 30 days, or fewer than 15 days). [[APP162.](#)] It creates a complicated financial ratio:

Fixed Charge Coverage Ratio = (Change in Net Assets + Depreciation + Amortization + Interest Expense + Lease Expense)/(Current Portion of Long-Term Debt and Capital Leases + Interest + Lease Expense)

[APP164-66.] And it sets an arbitrary threshold value for that ratio (1.10).

[APP166.]

In creating those financial metrics and thresholds, the Board interpreted the statute in at least three ways: (1) by selecting which measures to use (none of them appear in the statute), (2) by defining how to compute the measures (also not in the statute), and (3) by determining the threshold values for the measures (likewise not in the statute). All three steps involve substantial policy questions. Thus, like in *ASU*, “to implement [the statute], one must first interpret it.” *Id.* And like in *Southwest Ambulance*, here the agency specified all of those criteria and made them apply to all charter schools that it sponsors. Thus, the Board implemented the statute through the Frameworks, as it was required to do.

(c) The Frameworks describe procedure and practice.

In addition, the Frameworks describe the *procedure* or *practice requirements* of the Board. The Academic Framework, for example, specifies the details of how the Board conducts its on-site reviews,

including the length of visit, the typical arrival time, and the specific questions the Board staff will use. [APP151-52.] It also specifies when findings will be presented to the Board. [APP144.]

The Financial Framework has similar provisions. It explains the specific information the Board will use. [APP158 (noting that “information from the annual audit” will be used in the following categories: “Independent Auditor’s Report on the financial statements; Audited statement of financial position; Audited statement of activities and changes in net assets; Audited statement of cash flows; Notes to the audited financial statements; Applicable compliance questionnaire”).] It further explains how the Board will use the information it collects: i.e., to waive requirements or impose additional requirements. [APP159.] And when the information will be considered (e.g., at renewal, interval reviews, failing school designations, and in connection with the Academic Framework). [*Id.*]

For these reasons, the Frameworks satisfy the second element because they “implement[]” and “interpret[]” law or policy, and “describe[] the procedure or practice requirements of an agency.” A.R.S. § 41-1001(19).

C. The rulemaking requirements of the APA apply to the Board.

The APA's rulemaking requirements apply to the Board. By statute, the APA and its rulemaking mandate "apply to all agencies and all proceedings not expressly exempted." [A.R.S. § 41-1002\(A\)](#). This background principle applies even when the legislature does not expressly require rulemaking to enact a particular statute, as *Carondelet* and *ASU* confirm.

In *Carondelet*, AHCCCS argued that "it can be inferred from [the statute's] silence that the legislature never envisioned the need for an explanatory rule." *Carondelet*, [182 Ariz. at 228](#). This Court stated, "we disagree." *Id.* As *Carondelet* correctly explained, under A.R.S. § 41-1002(A), "[a]ll agencies are subject to the APA unless they are expressly exempted." *Id.*

This Court again confirmed that principle in *ASU*. See *ASU*, [237 Ariz. at 252](#), ¶¶ 23-25 ("Neither [specific statute] nor the APA exempt the [agency] from rulemaking; therefore, rulemaking is required before the Policy can be given effect." (citations omitted)) Thus, because the legislature has not given the Board a specific exemption from rulemaking, the APA applies.

Moreover, the Board has already followed the APA and promulgated rules on a variety of topics. See [Ariz. Admin. Code R7-5-101](#) to [R7-5-504](#). Since 1994, the Board has completed the formal rulemaking process three different times. See 10 Ariz. Admin. Reg. 1141 (Mar. 26, 2004); 12 Ariz. Admin. Reg. 577 (Feb. 24, 2006); 20 Ariz. Admin. Reg. 437 (Feb. 21, 2014).

Indeed, the Board even started to follow the APA *twice* on this very topic: it issued a notice of proposed rulemaking in 2014, let that die on the vine, and then opened *another* rulemaking docket in 2016. See 20 Ariz. Admin. Reg. 307 (Feb. 14, 2014); 22 Ariz. Admin. Reg. 823 (Apr. 15, 2016).

The Board thus (correctly) never considered itself to be exempt from the APA.

D. The Board did not follow the APA.

In 2012, after the legislature required the Board to create frameworks under A.R.S. § 15-183(R), the Board did so that same year. But in creating the Frameworks, the Board did not follow the rulemaking requirements set forth in the APA. [[APP130](#), ¶ 12.]

Unsurprisingly, the independent Auditor General determined that the Board should formally promulgate the Frameworks as rules. It listed the Frameworks as the “one exception” to the Board’s otherwise favorable

rulemaking report card. It then specifically recommended rulemaking on the Frameworks' subjects ("academic, financial, operational performance"):

General Counsel for the Auditor General has analyzed the Board's rulemaking statutes and believes that the Board has established rules required by statute, with *one exception*. Specifically, the Board *should adopt rules* to define board standards for *academic, financial, and operational performance*, sufficient progress toward standards, and consequences for not meeting or making progress toward standards.

Auditor General Report at 33 [[APP109](#)] (emphasis added).

Elsewhere in the Report, the Auditor General expressly cited the legislation authorizing the "performance frameworks" ("Laws 2012, Ch. 155" (codified at A.R.S. § 15-183(R)) and cited the lack of rulemaking. Auditor General Report at 20-21 [[APP096-97](#)]. The Auditor General then suggested that "the Board may have difficulty taking action" to enforce the Frameworks because of the lack of rules. Auditor General Report at 21 [[APP097](#)]. Consequently, the Auditor General recommended that "the Board should adopt rules." *Id.*, § 1.7; *see also id.*, § 1.2(a) (recommending rules for financial frameworks) [[APP097-98](#)].

E. This Court has repeatedly invalidated agency action that violated the APA.

Failing to follow the rulemaking requirements renders the Frameworks void. By statute, “[a] rule is invalid unless it is made and approved in substantial compliance with” the APA. [A.R.S. § 41-1030\(A\)](#). This Court has repeatedly voided agency action for failure to follow the APA.

In *ASU*, [237 Ariz. 246](#), the Arizona State Retirement System created a “Policy” “to memorialize how [it] would implement” a statutory requirement to charge an employer for the unfunded liability created by the employer’s termination incentive program. *Id.* at 249, ¶ 6. The Retirement System wrote and implemented the Policy without following the APA. This Court held that “the Policy was a rule within the meaning of the APA,” and consequently invalidated the Policy. *Id.* at 252, ¶ 22; *id.* at 254, ¶ 32.

In *Southwest Ambulance*, [183 Ariz. 258](#), the Department of Health Services issued a schedule of rates and charges for ambulance services without following the APA. *Id.* at 260. This Court held that the schedules

“contain the elements of a rule, and should have been adopted in accordance with the rule-making procedure.” *Id.* at 261.

And in *Carondelet*, 182 Ariz. 221, AHCCCS adopted a methodology to adjust factors that would in turn be used to determine hospital payment rates without following the APA. *Id.* at 226. This Court held that the methodology “constitutes a rule under the APA,” and consequently invalidated the methodology. *Id.* at 229-230.

This Court should do the same. The Frameworks fit the APA’s definition of a “rule,” but the Board did not follow the APA in promulgating them. As a result, they must be invalidated.

II. The superior court erred by holding that the Frameworks do not violate the APA.

In dismissing the complaint, the superior court’s written ruling stated that the motion to dismiss “is granted for the reasons stated on the record.” [APP126.] The small amount of explanation in the written ruling further stated, “This ruling is a legal interpretation of A.R.S. § 15-183(R) that does not depend on the facts.” [*Id.*] In the comments at oral argument, the superior court explained that “the Administrative Procedures [sic] Act does

not apply to the frameworks—the performance framework that is described in ARS Section 15-183(R).” [APP230, lines 6-11.]

The superior court did not articulate any valid reason for its ruling. It did not hold that the Frameworks failed to satisfy the statutory definition of “rule,” nor did it identify any specific rulemaking exemption for the Board (either in general or for the Frameworks in particular). Instead, the superior court appeared to base its ruling on one or more of several concerns it expressed on the record. But as addressed below, none of them justify dismissing the complaint or holding that the Board did not violate the APA.

A. Promulgating the Frameworks through rulemaking would not be impracticable.

At argument, the superior court commented, “[I]t’s impracticable. You can’t—they can’t create a rule for every aspect of overseeing a charter school any more than a school board can create a rule for overseeing every aspect of a school.” [APP231, lines 20-23.] But writing rules in this case would not be impracticable, and in any event that is no excuse.

1. Contrary to the superior court's suggestion, promulgating the Frameworks as rules is not impracticable.

The superior court's impracticability comment is wrong because writing rules in this case would not be impracticable.

First, the Board's own actions show that writing rules would not be impracticable. The Board has already written the Frameworks and apparently is capable of committing such concepts to paper. As in the tort doctrine *res ipsa loquitur*, the thing speaks for itself: the Board's ability to draft the existing Frameworks shows that writing them down is not "impracticable."⁴ Cf. *Black's Law Dictionary* 1503 (10th ed. 2014) (entry for "res ipsa loquitur").

Second, [A.R.S. § 15-183\(R\)](#) expressly requires the Board to make its frameworks publicly accessible. There is no reason that the Board cannot promulgate those very same frameworks under the APA. Thus, contrary to the superior court's suggestion, complying with the APA is not "impracticable" in this case.

⁴ Although the Schools take no position on whether the Board would have satisfied all of its statutory obligations had it merely promulgated the existing Frameworks through the rulemaking process, the point remains that the Board violated the APA by drafting and applying the Frameworks without following the rulemaking process.

2. Contrary to the superior court’s suggestion, the Board need not promulgate rules covering every aspect of a school’s operations.

The superior court apparently misapprehended the scope of the APA’s requirements. Nothing requires the Board to “create a rule for *every aspect* of overseeing a charter school,” as the superior court said. [APP231, lines 21-22 (emphasis added).]

First, this case does not require such a broad holding. To resolve this case, the Court need look only at what the Board has already done. This case challenges the specific documents the Board issued as the Academic Framework and the Financial Framework. The case presents the question of whether the Board had to promulgate *those documents* as rules.

Second, as a matter of law the Board need not write rules for “every aspect” of the school. The Board remains free to exercise its oversight responsibilities through individual adjudications of individual schools, just as it did between 1994 and 2012. But once it adopts policies that apply to *all* schools (such as the frameworks required by A.R.S. § 15-183(R)), the APA requires it to promulgate rules. *Cf. Shelby Sch. v. Ariz. State Bd. of Educ.*, 192 Ariz. 156, 164, ¶ 29 (App. 1998) (noting that an agency may “proceed in making policy by regulation or by ad hoc adjudication”).

3. Difficulty in drafting rules does not excuse APA compliance.

In addition, and also contrary to the superior court's suggestion, the APA provides no exception for rules that are complicated or difficult. To the contrary, Arizona agencies routinely write extremely complex rules:⁵

- In the education space alone, the State Board of Education has published 154 pages of rules. *See* [Ariz. Admin. Code R7-2-101](#) et seq.
- The Department of Health Services has published 261 pages of rules covering topics as complicated as quality management for hospitals ([Ariz. Admin. Code R9-10-204](#)) and qualifications for hospital medical staff ([Ariz. Admin. Code R9-10-207](#)).
- The Radiation Regulatory Agency has 277 pages of rules detailing how to calculate radiation exposure ([Ariz. Admin. Code R12-1-408](#) to [R12-1-416](#)) and covering mobile radiographic equipment ([Ariz. Admin. Code R12-1-608](#)). That agency even promulgated rules specifically addressing topics as specific as "Safety Precautions for Remote Afterloader Units, Teletherapy Units, and Gamma Stereotactic Radiosurgery Units" ([Ariz. Admin. Code R12-1-732](#)).
- Unsurprisingly, the Department of Revenue has complicated tax rules. *See* [Ariz. Admin. Code R15-2A-103](#) et seq.
- The Department of Environmental Quality has codified standards for air pollution covering everything from "existing nonferrous metals industry sources" to dry cleaning plants, cotton gins, and sulfuric acid plants. *See* [Ariz. Admin. Code R18-2-701](#) et seq.

⁵ Not all of the rules listed here were necessarily required to be adopted in compliance with the APA, but the rules' very existence nevertheless demonstrates that agencies routinely issue formal rules on very complicated topics.

- There are even 35 pages of rules devoted specifically to school buses. See [Ariz. Admin. Code R13-13-101](#) et seq.

Complexity does not excuse an agency from the APA. For these reasons, the superior court’s “impracticability” standard has no basis in the law and would not apply to this case in any event.

B. The APA applies even when the rules adopted apply to another governmental entity.

The superior court also expressed concern that the rules would involve “the State dealing with itself” (i.e., that one state agency would be writing rules for another public entity). [[APP185](#), lines 3-24.] This Court has already rejected an identical argument.

In *ASU*, a state university sued a state agency for failing to promulgate rules. The state agency argued “that forcing it to comply with the APA under the circumstances here would be ‘absurd’ because the APA was not intended to protect the rights of ‘one division of state government,’ the University, from the actions of another, the System.” *ASU*, [237 Ariz. at 253](#), ¶ 31. This Court expressly rejected that argument, concluding that the APA “makes no exception for agencies whose decisions affect the rights of divisions and political subdivisions of the state.” *Id.* Citing another case with a similar posture, the Court explained, “we have held that rules

promulgated without following the rulemaking procedure of the APA are unenforceable against political subdivisions of the state.” *Id.* (citing *Cochise Cty. v. AHCCCS*, 170 Ariz. 443, 445 (App. 1991)).

C. The superior court mistakenly believed that if rules are required now, they would have been required since 1994.

The superior court asserted that “[t]he implication of” the Schools’ position is that rules “should have existed since 1994.” [APP232, lines 11-15.] Not so. Agencies may exercise their oversight functions through individual adjudications without going through rulemaking. The rulemaking obligation arises only when the agency creates something with “general applicability.” A.R.S. § 41-1001(19).

Here, rulemaking was not required before 2012 because before then the legislature had not required the Board to set out written frameworks. The Board could regulate charter schools through individual oversight against particular schools; the legislature gave the Board the authority to “[e]xercise general supervision over charter schools” it sponsored, A.R.S. § 15-182(E)(1), including “oversight and administrative responsibility,” and the power to “revoke a charter.” A.R.S. §§ 15-183(R), 15-183(I)(3).[†] And for

[†] Version in place before August 1, 2012. [Copy at APP068-69.]

years the Board exercised its supervisory authority in that manner, through individual adjudications.

That changed in 2012, when the legislature apparently decided that individual adjudications were no longer sufficient for the topics covered by the frameworks, and instead required the Board to issue written frameworks under A.R.S. § 15-183(R). Once the Board wrote the Frameworks, which have “general applicability” and apply to all Board-sponsored charter schools (as required by A.R.S. § 15-183(R)), the rulemaking obligation arose.

Thus, contrary to the superior court’s assumption, charter schools did not exist in an unregulated, lawless state in the 18 years between 1994 and 2012. But the legislatively-required increase in formality of oversight and regulation triggered the Board’s obligation to follow the APA and promulgate rules.

D. Contrary to the superior court’s assertion, this is “a rule-making situation.”

By statute and under well-established precedent, an agency must follow the APA unless expressly exempted by the legislature. (*See* [Argument § I.C.](#)) The superior court dodged that requirement, explaining:

“the usual rule that says the legislature has to exempt an agency from rule-making that doesn’t apply because this isn’t a rule-making situation in the first place.” [APP232, lines 8-10.] That flies in the face of the APA, which gives the legislature the exclusive power to exempt agencies from rulemaking. Declaring that “this isn’t a rule-making situation in the first place” unlawfully usurps the legislative power and has no basis in Arizona law.

E. The Board’s role as a sponsor does not excuse it from APA compliance.

The superior court also questioned how the Board’s role as a sponsor of charter schools affects its obligations under the APA. Although those questions did not appear to drive the court’s decision, the Schools nevertheless address them here.

1. The Board’s only role is to serve as a sponsor, yet it must still follow the APA.

The superior court asked about “the distinction between the Charter Board as a state agency and the Charter Board as a sponsor.” [APP225, lines 15-17.]

No one disputes that the Board is a state agency with the ability to promulgate rules. Its status as a sponsor does not change its obligations

because the Board has only one administrative role—to sponsor and regulate charter schools—and it fulfills that role as a sponsor. That role does not prevent the Board from following the APA, as demonstrated by the many rules the Board has already promulgated in its capacity as a sponsor.

Saying that the Board has a dual role as a state agency and a sponsor has no more meaning than saying that the Department of Revenue has a dual role as a state agency and tax collector. The Department of Revenue is a state agency that exists solely to collect and distribute tax money, just like the Board is a state agency that exists solely to sponsor charter schools. The Department of Revenue promulgates rules to fulfill its obligation to collect taxes, just like the Board must promulgate rules to fulfill its obligations as a sponsor.

Moreover, in other areas the Board apparently had no issue following the APA, as demonstrated by the Board's existing rules, all of which relate to its obligations as a sponsor of charter schools. See [Ariz. Admin. Code R7-5-101](#) to [R7-5-504](#).

2. Rulemaking exemptions for other sponsors are legally irrelevant and practically meaningless.

The superior court also asked questions about “other entities that have the authority to sponsor a charter school [that] don’t have to go through all this [the APA].”⁶ [APP189, lines 24-25.] For example, a public university may sponsor a charter school, [A.R.S. § 15-183\(C\)](#), but the legislature expressly exempted the universities from rulemaking. *See* [A.R.S. § 41-1005\(D\)](#).

That the legislature exempted some other sponsors does not mean that all sponsors are exempt from rulemaking on the *subject matter* of frameworks. The legislature may create rulemaking exemptions either by subject matter or by agency:

- **By subject matter:** For example, by statute, rules concerning the *subject matter* of maintaining agency property need not follow the APA, regardless of the agency. [A.R.S. § 41-1005\(A\)\(6\)](#).
- **By agency:** Some agencies (like the Board of Regents and its universities) enjoy a blanket statutory exemption. *See* [A.R.S. § 41-1005\(D\)](#).

⁶ The superior court used school districts as an example, but school districts may no longer sponsor charter schools. *See* 2014 Ariz. Sess. Laws 122, 124, ch. 17, § 1 (S.B. 1488, 51st Leg., 2d Reg. Sess.) (“[A] school district governing board shall not grant a charter to a new charter school that begins initial operations after June 30, 2013 . . .”).

That means that for some subject matters, one agency need not follow the APA, while a different agency nevertheless must follow the APA, *even on the exact same subject matter*. For example, the Board has promulgated several existing rules that apply *only* to the charter schools it sponsors, not to other charter schools sponsored by the universities or community college districts. See [Ariz. Admin. Code R7-5-101](#) to [R7-5-504](#). That is the result the legislature intended by reserving for itself the power to create exemptions, and by choosing to exempt entire agencies in some instances and specific subject matters in other instances. Here, there is nothing inconsistent with requiring the Board to follow the APA while respecting the statutory rulemaking exemption given to the universities.

Moreover, in reality this concern has no meaningful impact because the Board sponsors the vast majority of all charter schools, and essentially all of the non-captive charter schools. Giving weight to the rulemaking exemptions enjoyed by other sponsors would let the tail wag the dog. The universities, for example, sponsor very few schools, and they only sponsor charter schools run by the universities themselves. Those captive, university-run schools do not need the same kinds of procedural protections as independent schools sponsored and regulated by the Board.

The fact that those few, largely captive schools may not benefit from the APA's protections has no legal relevance, and in any event it makes almost no practical difference.

And with no evidence in the record concerning any other charter schools, the superior could not rely on this issue in granting the motion to dismiss. See *Coleman*, 230 Ariz. at 355, ¶ 9 (“[C]ourts look only to the pleading itself when adjudicating a Rule 12(b)(6) motion.”); *id.*, ¶ 8 (“Dismissal is appropriate under Rule 12(b)(6) only if as a matter of law [] plaintiffs would not be entitled to relief under any interpretation of the facts susceptible of proof.” (quotation marks omitted; alteration in original)).

F. Contrary to the Board’s contention, the Board uses the Frameworks to do more than merely collect information.

In briefing below, the Board made an additional argument that the superior court apparently did not find persuasive.⁷ The Schools address it here.

Below, the Board relied on *Shelby* to claim that the Frameworks are not rules because they merely collect information. [IR-15 at 9.] In *Shelby*, the State Board of Education evaluated the creditworthiness of a charter school applicant. The unsuccessful applicant contended a “creditworthiness requirement” should have been promulgated as a rule. [192 Ariz. at 167, ¶ 48](#). The Court dismissed that argument in three sentences, concluding that creditworthiness “was a part of the information-gathering process necessary to enable the Board [of Education] to make

⁷The Board made several other arguments below that would not support dismissal. For example, it cross-moved for summary judgment on the basis that the Board substantially complied with the APA under A.R.S. § 41-1030(A). [IR-15 at 11.] The Board expressly relied on material outside the pleadings for this point, and noted that it “cross-moves for summary judgment on this point.” [IR-15 at 11 n.7.] The superior court did not ask any questions on this topic. And because the Board relied on material outside the pleadings, the superior court could not dismiss the complaint on this basis. Because this and other arguments are irrelevant on appeal from the dismissal, the Schools do not address them.

decisions. It was not procedural but instead was a method of obtaining data.” *Id.*⁸

The opinion in *Shelby* does not explain what form the “creditworthiness requirement” took or how the agency used the information generally (beyond the application at issue in the case). If anything, the opinion suggests that the “creditworthiness requirement” was really a “credit check requirement” imposed in an ad hoc manner. *Id.* at 164, ¶ 30. The school applied “in the first year” charter school applications were accepted. *Id.* The requirement apparently did not specify any particular metrics for determining creditworthiness or any particular thresholds for meeting the requirement. Thus, in contrast to the Frameworks at issue here, the credit check requirement appears to have been a loose, undefined tool without prescribed thresholds or consequences. (The same analysis applies to the other cases the Board cited

⁸ The plain text of the APA does not exempt information-gathering processes for rulemaking, and thus *Shelby* does not faithfully interpret the APA. If the Board of Education imposed a creditworthiness requirement applicable to all applicants (as opposed to merely in individual adjudications of applications), then it necessarily interpreted a statute as supporting the requirement and therefore should have promulgated a rule. This Court need not reach the continuing validity of *Shelby* because so many other bases support reversal.

below in summary fashion [in IR-15 at 9]: *Canyon Ambulatory Surgery Ctr. v. SCF Ariz.*, 225 Ariz. 414, 420, ¶ 22 (App. 2010); *Duke Energy Arlington Valley, LLC v. Ariz. Dep't. of Revenue*, 219 Ariz. 76, 78, ¶ 11 (App. 2008.)

Moreover, and in contrast to *Shelby*, the Frameworks do far more than merely collect information. First, the complaint explains how the Frameworks have been used, and the superior court had to “assume the truth of all well-pleaded factual allegations and indulge all reasonable inferences from those facts.” *Coleman*, 230 Ariz. at 355, ¶ 9.

In particular:

- The Frameworks “have been used and are used by the Board to make substantive decisions regarding charter schools’ operations.”
- “[T]he Board has based its determinations regarding whether charter school contracts will be renewed or revoked in large part on the Frameworks and the dashboards generated by the Frameworks.”
- “In the past two years, the Board has relied on the Frameworks to require charter schools to enter into conditional renewal agreements that impose onerous, additional requirements on the schools in order to obtain renewal of their charters.”
- “The Board has also based other decisions regarding charter schools and their charter terms on the Frameworks, and has imposed additional requirements [on] charter schools based at least in part on the Frameworks.”
- “[T]he Board has relied on the Frameworks to require charter schools that are not meeting the standards established by the Frameworks to agree to ‘performance management plans’ and enter into onerous

consent agreements on penalty of losing funding or having their charters revoked; to deny requests by charter schools to increase the grade levels they serve, even when demand for those grades exists; to deny requests by charter schools to expand their enrollment, even when demand exists; and to force non-traditional charter schools to comply with standards and metrics designed for more traditional schools.”

[APP131, ¶¶ 20-24; *see also* APP130-31, ¶¶ 15-19.]

The text of the Frameworks themselves confirm that they go beyond mere information gathering. The Academic Framework specifically states that it will “be used in high-stakes decisions.” [APP138.] It specifies the threshold for finding that a charter holder “has failed to demonstrate sufficient progress.” [APP144.] And it defines the matrices for how the Board will use information it collects to determine whether a school meets the Board’s standards. [APP140-44.]

The standards set forth in the Academic Framework have serious consequences. The Board uses them when evaluating a school during the five-year review, as well as when a school seeks to expand its operations. [APP145.] As just one example, a school may engage in specifically identified expansions (e.g., adding a grade level or increasing enrollment) only if the school meets a specific threshold identified in the Academic Framework (i.e., only if 75% of all of the charter holder’s schools “have an

Overall Rating of ‘Meets Standard’ or ‘Exceeds Standard’”). [*Id.*] Likewise, the Financial Framework prescribes consequences for falling short in two or more of the many metrics in the Framework: at a minimum, the school is “required to submit a financial performance response” as described in the Framework. [APP160.]

For these reasons, the Board’s argument concerning information-gathering does not apply to this case (and apparently was not the basis for the superior court’s ruling, in any event).

REQUEST FOR COSTS & ATTORNEYS’ FEES

Pursuant to ARCAP 21, A.R.S. §§ 12-342, 12-348, and 12-1840, the Schools request their fees and costs.

CONCLUSION

The Court should vacate the judgment, reverse the dismissal, and remand for further proceedings.

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RESPECTFULLY SUBMITTED this 18th day of April, 2017.

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* The appendix page number matches the electronic PDF page number. Counsel has added emphasis to selected pages in this appendix using yellow highlighting to assist the Court with its review of the record. Some record items included in the appendix contain only a limited excerpt. This appendix complies with the bookmarking requirements of ARCAP 13.1(d)(3).

¹ This document is also in the superior court record at IR-9 to IR-11.

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A.R.S. § 15-183
(Current version)
(Excerpts)

§ 15-183. Charter schools; application; requirements; immunity; exemptions;
renewal of application; reprisal; fee; funds; annual reports

A. An applicant seeking to establish a charter school shall submit a written application to a proposed sponsor as prescribed in subsection C of this section. The application, application process and application time frames shall be posted on the sponsor's website and shall include the following, as specified in the application adopted by the sponsor:

1. A detailed educational plan.
2. A detailed business plan.
3. A detailed operational plan.
4. Any other materials required by the sponsor.

B. The sponsor of a charter school may contract with a public body, private person or private organization for the purpose of establishing a charter school pursuant to this article.

C. The sponsor of a charter school may be either the state board of education, the state board for charter schools, a university under the jurisdiction of the Arizona board of regents, a community college district or a group of community college districts, subject to the following requirements:

1. An applicant may not submit an application for sponsorship to any person or entity other than those prescribed in this subsection.
2. The applicant may submit the application to the state board of education or the state board for charter schools. Notwithstanding any other law, neither the state board for charter schools nor the state board of education shall grant a charter to a school district governing board for a new charter school that begins initial operations after June 30, 2013 or for the conversion of an existing district public school to a charter school that begins initial operations after June 30, 2013. The state board of education or the state

board for charter schools may approve the application if the application meets the requirements of this article and may approve the charter if the proposed sponsor determines, within its sole discretion, that the applicant is sufficiently qualified to operate a charter school and that the applicant is applying to operate as a separate charter holder by considering factors such as whether:

(a) The schools have separate governing bodies, governing body membership, staff, facilities and student population.

(b) Daily operations are carried out by different administrators.

(c) The applicant intends to have an affiliation agreement for the purpose of providing enrollment preferences.

(d) The applicant's charter management organization has multiple charter holders serving varied grade configurations on one physical site or nearby sites serving one community.

(e) It is reconstituting an existing school site population at the same or new site.

(f) It is reconstituting an existing grade configuration from a prior charter holder with at least one grade remaining on the original site with the other grade or grades moving to a new site. The state board of education or the state board for charter schools may approve any charter schools transferring charters. If the state board of education or the state board for charter schools rejects the preliminary application, the state board of education or the state board for charter schools shall notify the applicant in writing of the reasons for the rejection and of suggestions for improving the application. An applicant may submit a revised application for reconsideration by the state board of education or the state board for charter schools. The applicant may request, and the state board of education or the state board for charter schools may provide, technical assistance to improve the application.

3. The applicant may submit the application to a university under the jurisdiction of the Arizona board of regents, a community college district or a group of community college districts. A university, a community college district or a group of community college districts shall not grant a charter to

a school district governing board for a new charter school that begins initial operations after June 30, 2013 or for the conversion of an existing district public school to a charter school that begins initial operations after June 30, 2013. A university, a community college district or a group of community college districts may approve the application if it meets the requirements of this article and if the proposed sponsor determines, in its sole discretion, that the applicant is sufficiently qualified to operate a charter school.

4. Each applicant seeking to establish a charter school shall submit a full set of fingerprints to the approving agency for the purpose of obtaining a state and federal criminal records check pursuant to § 41-1750 and Public Law 92-544. If an applicant will have direct contact with students, the applicant shall possess a valid fingerprint clearance card that is issued pursuant to title 41, chapter 12, article 3.1. The department of public safety may exchange this fingerprint data with the federal bureau of investigation. The criminal records check shall be completed before the issuance of a charter.

5. All persons engaged in instructional work directly as a classroom, laboratory or other teacher or indirectly as a supervisory teacher, speech therapist or principal shall have a valid fingerprint clearance card that is issued pursuant to title 41, chapter 12, article 3.1, unless the person is a volunteer or guest speaker who is accompanied in the classroom by a person with a valid fingerprint clearance card. A charter school shall not employ a teacher whose certificate has been surrendered or revoked, unless the teacher's certificate has been subsequently reinstated by the state board of education. All other personnel shall be fingerprint checked pursuant to § 15-512, or the charter school may require those personnel to obtain a fingerprint clearance card issued pursuant to title 41, chapter 12, article 3.1. Before employment, the charter school shall make documented, good faith efforts to contact previous employers of a person to obtain information and recommendations that may be relevant to a person's fitness for employment as prescribed in § 15-512, subsection F. The charter school shall notify the department of public safety if the charter school or sponsor receives credible evidence that a person who possesses a valid fingerprint clearance card is arrested for or is charged with an offense listed in § 41-1758.03, subsection B. Charter schools may hire personnel that have not yet received a fingerprint clearance card if proof is provided of the submission of an application to the department of public safety for a fingerprint clearance card and if the charter school that is seeking to hire the applicant does all of the following:

(a) Documents in the applicant's file the necessity for hiring and placement of the applicant before receiving a fingerprint clearance card.

(b) Ensures that the department of public safety completes a statewide criminal records check on the applicant. A statewide criminal records check shall be completed by the department of public safety every one hundred twenty days until the date that the fingerprint check is completed or the fingerprint clearance card is issued or denied.

(c) Obtains references from the applicant's current employer and the two most recent previous employers except for applicants who have been employed for at least five years by the applicant's most recent employer.

(d) Provides general supervision of the applicant until the date that the fingerprint card is obtained.

(e) Completes a search of criminal records in all local jurisdictions outside of this state in which the applicant has lived in the previous five years.

(f) Verifies the fingerprint status of the applicant with the department of public safety.

6. A charter school that complies with the fingerprinting requirements of this section shall be deemed to have complied with § 15-512 and is entitled to the same rights and protections provided to school districts by § 15-512.

7. If a charter school operator is not already subject to a public meeting or hearing by the municipality in which the charter school is located, the operator of a charter school shall conduct a public meeting at least thirty days before the charter school operator opens a site or sites for the charter school. The charter school operator shall post notices of the public meeting in at least three different locations that are within three hundred feet of the proposed charter school site.

8. A person who is employed by a charter school or who is an applicant for employment with a charter school, who is arrested for or charged with a

nonappealable offense listed in § 41-1758.03, subsection B and who does not immediately report the arrest or charge to the person's supervisor or potential employer is guilty of unprofessional conduct and the person shall be immediately dismissed from employment with the charter school or immediately excluded from potential employment with the charter school.

9. A person who is employed by a charter school and who is convicted of any nonappealable offense listed in § 41-1758.03, subsection B or is convicted of any nonappealable offense that amounts to unprofessional conduct under § 15-550 shall immediately do all of the following:

- (a) Surrender any certificates issued by the department of education.
- (b) Notify the person's employer or potential employer of the conviction.
- (c) Notify the department of public safety of the conviction.
- (d) Surrender the person's fingerprint clearance card.

D. An entity that is authorized to sponsor charter schools pursuant to this article has no legal authority over or responsibility for a charter school sponsored by a different entity. This subsection does not apply to the state board of education's duty to exercise general supervision over the public school system pursuant to § 15-203, subsection A, paragraph 1.

E. The charter of a charter school shall do all of the following:

1. Ensure compliance with federal, state and local rules, regulations and statutes relating to health, safety, civil rights and insurance. The department of education shall publish a list of relevant rules, regulations and statutes to notify charter schools of their responsibilities under this paragraph.
2. Ensure that it is nonsectarian in its programs, admission policies and employment practices and all other operations.
3. Ensure that it provides a comprehensive program of instruction for at least a kindergarten program or any grade between grades one and twelve, except that a school may offer this curriculum with an emphasis on a specific

learning philosophy or style or certain subject areas such as mathematics, science, fine arts, performance arts or foreign language.

4. Ensure that it designs a method to measure pupil progress toward the pupil outcomes adopted by the state board of education pursuant to § 15-741.01, including participation in the Arizona instrument to measure standards test and the nationally standardized norm-referenced achievement test as designated by the state board and the completion and distribution of an annual report card as prescribed in chapter 7, article 3 of this title.

5. Ensure that, except as provided in this article and in its charter, it is exempt from all statutes and rules relating to schools, governing boards and school districts.

6. Ensure that, except as provided in this article, it is subject to the same financial and electronic data submission requirements as a school district, including the uniform system of financial records as prescribed in chapter 2, article 4 of this title, procurement rules as prescribed in § 15-213 and audit requirements. The auditor general shall conduct a comprehensive review and revision of the uniform system of financial records to ensure that the provisions of the uniform system of financial records that relate to charter schools are in accordance with commonly accepted accounting principles used by private business. A school's charter may include exceptions to the requirements of this paragraph that are necessary as determined by the university, the community college district, the group of community college districts, the state board of education or the state board for charter schools. The department of education or the office of the auditor general may conduct financial, program or compliance audits.

7. Ensure compliance with all federal and state laws relating to the education of children with disabilities in the same manner as a school district.

8. Ensure that it provides for a governing body for the charter school that is responsible for the policy decisions of the charter school. Notwithstanding § 1-216, if there is a vacancy or vacancies on the governing body, a majority of the remaining members of the governing body constitute a quorum for the transaction of business, unless that quorum is prohibited by the charter school's operating agreement.

9. Ensure that it provides a minimum of one hundred eighty instructional days before June 30 of each fiscal year unless it is operating on an alternative calendar approved by its sponsor. The superintendent of public instruction shall adjust the apportionment schedule accordingly to accommodate a charter school utilizing an alternative calendar.

F. A charter school shall keep in the personnel file of all current employees who provide instruction to pupils at the charter school information about the employee's educational and teaching background and experience in a particular academic content subject area. A charter school shall inform parents and guardians of the availability of the information and shall make the information available for inspection on request of parents and guardians of pupils enrolled at the charter school. This subsection does not require any charter school to release personally identifiable information in relation to any teacher or employee, including the teacher's or employee's address, salary, social security number or telephone number.

G. The charter of a charter school may be amended at the request of the governing body of the charter school and on the approval of the sponsor.

H. Charter schools may contract, sue and be sued.

I. The charter is effective for fifteen years from the first day of the fiscal year as specified in the charter, subject to the following:

1. At least eighteen months before the expiration of the charter, the sponsor shall notify the charter school that the charter school may apply for renewal and shall make the renewal application available to the charter school. A charter school that elects to apply for renewal shall file a complete renewal application at least fifteen months before the expiration of the charter. A sponsor shall give written notice of its intent not to renew the charter school's request for renewal to the charter school at least twelve months before the expiration of the charter. The sponsor shall make data used in making renewal decisions available to the school and the public and shall provide a public report summarizing the evidence basis for each decision. The sponsor may deny the request for renewal if, in its judgment, the charter holder has failed to do any of the following:

(a) Meet or make sufficient progress toward the academic performance expectations set forth in the performance framework.

(b) Meet the operational performance expectations set forth in the performance framework or any improvement plans.

(c) Complete the obligations of the contract.

(d) Comply with this article or any provision of law from which the charter school is not exempt.

2. A charter operator may apply for early renewal. At least nine months before the charter school's intended renewal consideration, the operator of the charter school shall submit a letter of intent to the sponsor to apply for early renewal. The sponsor shall review fiscal audits and academic performance data for the charter school that are annually collected by the sponsor, review the current contract between the sponsor and the charter school and provide the qualifying charter school with a renewal application. On submission of a complete application, the sponsor shall give written notice of its consideration of the renewal application. The sponsor may deny the request for early renewal if, in the sponsor's judgment, the charter holder has failed to do any of the following:

(a) Meet or make sufficient progress toward the academic performance expectations set forth in the performance framework.

(b) Meet the operational performance expectations set forth in the performance framework or any improvement plans.

(c) Complete the obligations of the contract.

(d) Comply with this article or any provision of law from which the charter school is not exempt.

3. A sponsor shall review a charter at five-year intervals using a performance framework adopted by the sponsor and may revoke a charter at any time if the charter school breaches one or more provisions of its charter or if the sponsor determines that the charter holder has failed to do any of the following:

(a) Meet or make sufficient progress toward the academic performance expectations set forth in the performance framework.

(b) Meet the operational performance expectations set forth in the performance framework or any improvement plans.

(c) Comply with this article or any provision of law from which the charter school is not exempt.

4. In determining whether to renew or revoke a charter holder, the sponsor must consider making sufficient progress toward the academic performance expectations set forth in the sponsor's performance framework as one of the most important factors.

5. At least sixty days before the effective date of the proposed revocation, the sponsor shall give written notice to the operator of the charter school of its intent to revoke the charter. Notice of the sponsor's intent to revoke the charter shall be delivered personally to the operator of the charter school or sent by certified mail, return receipt requested, to the address of the charter school. The notice shall incorporate a statement of reasons for the proposed revocation of the charter. The sponsor shall allow the charter school at least sixty days to correct the problems associated with the reasons for the proposed revocation of the charter. The final determination of whether to revoke the charter shall be made at a public hearing called for such purpose.

J. The charter may be renewed for successive periods of twenty years.

K. A charter school that is sponsored by the state board of education, the state board for charter schools, a university, a community college district or a group of community college districts may not be located on the property of a school district unless the district governing board grants this authority.

L. A governing board or a school district employee who has control over personnel actions shall not take unlawful reprisal against another employee of the school district because the employee is directly or indirectly involved in an application to establish a charter school. A governing board or a school district employee shall not take unlawful reprisal against an educational program of the school or the school district because an application to establish a charter school proposes the conversion of all or a portion of the educational program to a charter school. For the purposes of this subsection, "unlawful reprisal" means an action that is taken by a governing board or a school district employee as a direct result of a lawful

application to establish a charter school and that is adverse to another employee or an education program and:

1. With respect to a school district employee, results in one or more of the following:

- (a) Disciplinary or corrective action.
- (b) Detail, transfer or reassignment.
- (c) Suspension, demotion or dismissal.
- (d) An unfavorable performance evaluation.
- (e) A reduction in pay, benefits or awards.
- (f) Elimination of the employee's position without a reduction in force by reason of lack of monies or work.
- (g) Other significant changes in duties or responsibilities that are inconsistent with the employee's salary or employment classification.

2. With respect to an educational program, results in one or more of the following:

- (a) Suspension or termination of the program.
- (b) Transfer or reassignment of the program to a less favorable department.
- (c) Relocation of the program to a less favorable site within the school or school district.
- (d) Significant reduction or termination of funding for the program.

M. Charter schools shall secure insurance for liability and property loss. The governing body of a charter school that is sponsored by the state board of education or the state board for charter schools may enter into an intergovernmental agreement or otherwise contract to participate in an insurance program offered by a risk retention pool established pursuant to § 11-952.01 or 41-

621.01 or the charter school may secure its own insurance coverage. The pool may charge the requesting charter school reasonable fees for any services it performs in connection with the insurance program.

N. Charter schools do not have the authority to acquire property by eminent domain.

O. A sponsor, including members, officers and employees of the sponsor, is immune from personal liability for all acts done and actions taken in good faith within the scope of its authority.

P. Charter school sponsors and this state are not liable for the debts or financial obligations of a charter school or persons who operate charter schools.

Q. The sponsor of a charter school shall establish procedures to conduct administrative hearings on determination by the sponsor that grounds exist to revoke a charter. Procedures for administrative hearings shall be similar to procedures prescribed for adjudicative proceedings in title 41, chapter 6, article 10. Except as provided in § 41-1092.08, subsection H, final decisions of the state board of education and the state board for charter schools from hearings conducted pursuant to this subsection are subject to judicial review pursuant to title 12, chapter 7, article 6.

R. The sponsoring entity of a charter school shall have **oversight and administrative responsibility** for the charter schools that it sponsors. In implementing its oversight and administrative responsibilities, the sponsor shall ground its actions in evidence of the charter holder's performance in accordance with the performance framework adopted by the sponsor. The performance framework shall be publicly available, shall be placed on the sponsoring entity's website and shall include:

1. The academic performance expectations of the charter school and the measurement of sufficient progress toward the academic performance expectations.
2. The operational expectations of the charter school, including adherence to all applicable laws and obligations of the charter contract.
3. Intervention and improvement policies.

S. Charter schools may pledge, assign or encumber their assets to be used as collateral for loans or extensions of credit.

T. All property accumulated by a charter school shall remain the property of the charter school.

U. Charter schools may not locate a school on property that is less than one-fourth mile from agricultural land regulated pursuant to § 3-365, except that the owner of the agricultural land may agree to comply with the buffer zone requirements of § 3-365. If the owner agrees in writing to comply with the buffer zone requirements and records the agreement in the office of the county recorder as a restrictive covenant running with the title to the land, the charter school may locate a school within the affected buffer zone. The agreement may include any stipulations regarding the charter school, including conditions for future expansion of the school and changes in the operational status of the school that will result in a breach of the agreement.

V. A transfer of a charter to another sponsor, a transfer of a charter school site to another sponsor or a transfer of a charter school site to a different charter shall be completed before the beginning of the fiscal year that the transfer is scheduled to become effective. An entity that sponsors charter schools may accept a transferring school after the beginning of the fiscal year if the transfer is approved by the superintendent of public instruction. The superintendent of public instruction shall have the discretion to consider each transfer during the fiscal year on a case by case basis. A charter holder seeking to transfer sponsors shall comply with the current charter terms regarding assignment of the charter. A charter holder transferring sponsors shall notify the current sponsor that the transfer has been approved by the new sponsor.

W. Notwithstanding subsection V of this section, a charter holder on an improvement plan must notify parents or guardians of registered students of the intent to transfer the charter and the timing of the proposed transfer. On the approved transfer, the new sponsor shall enforce the improvement plan but may modify the plan based on performance.

X. Notwithstanding subsection Y of this section, the state board for charter schools shall charge a processing fee to any charter school that amends its contract to participate in Arizona online instruction pursuant to § 15-808. The charter Arizona online instruction processing fund is established consisting of fees collected and administered by the state board for charter schools. The state board for charter

schools shall use monies in the fund only for the processing of contract amendments for charter schools participating in Arizona online instruction. Monies in the fund are continuously appropriated.

Y. The sponsoring entity may not charge any fees to a charter school that it sponsors unless the sponsor has provided services to the charter school and the fees represent the full value of those services provided by the sponsor. On request, the value of the services provided by the sponsor to the charter school shall be demonstrated to the department of education.

Z. Charter schools may enter into an intergovernmental agreement with a presiding judge of the juvenile court to implement a law related education program as defined in § 15-154. The presiding judge of the juvenile court may assign juvenile probation officers to participate in a law related education program in any charter school in the county. The cost of juvenile probation officers who participate in the program implemented pursuant to this subsection shall be funded by the charter school.

AA. The sponsor of a charter school shall modify previously approved curriculum requirements for a charter school that wishes to participate in the board examination system prescribed in chapter 7, article 6 of this title.

BB. If a charter school decides not to participate in the board examination system prescribed in chapter 7, article 6 of this title, pupils enrolled at that charter school may earn a Grand Canyon diploma by obtaining a passing score on the same board examinations.

CC. Notwithstanding subsection Y of this section, a sponsor of charter schools may charge a new charter application processing fee to any applicant. The application fee shall fully cover the cost of application review and any needed technical assistance. Authorizers may approve policies that allow a portion of the fee to be returned to the applicant whose charter is approved.

DD. A charter school may choose to provide a preschool program for children with disabilities pursuant to § 15-771.

EE. Pursuant to the prescribed graduation requirements adopted by the state board of education, the governing body of a charter school operating a high school may approve a rigorous computer science course that would fulfill a mathematics course required for graduation from high school. The governing body may approve

a rigorous computer science course only if the rigorous computer science course includes significant mathematics content and the governing body determines the high school where the rigorous computer science course is offered has sufficient capacity, infrastructure and qualified staff, including competent teachers of computer science.

FF. A charter school may permit the use of school property, including school buildings, grounds, buses and equipment, by any person, group or organization for any lawful purpose, including a recreational, educational, political, economic, artistic, moral, scientific, social, religious or other civic or governmental purpose. The charter school may charge a reasonable fee for the use of the school property.

GG. A charter school and its employees, including the governing body, or chief administrative officer, are immune from civil liability with respect to all decisions made and actions taken to allow the use of school property, unless the charter school or its employees are guilty of gross negligence or intentional misconduct. This subsection does not limit any other immunity provisions that are prescribed by law.

HH. Sponsors authorized pursuant to this section shall submit an annual report to the auditor general on or before October 1. The report shall include:

1. The current number of charters authorized and the number of schools operated by authorized charter holders.
2. The academic and operational performance of the sponsor's charter portfolio as measured by the sponsor's adopted performance framework.
3. For the prior year, the number of new charters approved, the number of charter schools closed and the reason for the closure.
4. The sponsor's application, amendment, renewal and revocation processes, charter contract template and current performance framework as required by this section.

II. The auditor general shall prescribe the format for the annual report required by subsection HH of this section and may require that the annual report be submitted electronically. The auditor general shall review the submitted annual reports to ensure that the reports include the required items in subsection HH of this section and shall make the annual reports available upon request. If the auditor general

finds significant noncompliance or if a sponsor fails to submit the annual report required by subsection HH of this section, on or before December 31 of each year the auditor general shall report to the governor, the president of the senate, the speaker of the house of representatives and the chairs of the senate and house education committees or their successor committees, and the legislature shall consider revoking the sponsor's authority to sponsor charter schools.

(Footnotes omitted.)

A.R.S. § 15-183
(Version effective to Aug. 1, 2012)
(Excerpts)

§ 15-183. Charter schools; application; requirements; immunity; exemptions;
renewal of application; reprisal; fee; fund

A. An applicant seeking to establish a charter school shall submit a written application to a proposed sponsor as prescribed in subsection C of this section. The application shall include a detailed business plan for the charter school and may include a mission statement for the charter school, a description of the charter school's organizational structure and the governing body, a financial plan for the first three years of operation of the charter school, a description of the charter school's hiring policy, the name of the charter school's applicant or applicants and requested sponsor, a description of the charter school's facility and the location of the school, a description of the grades being served and an outline of criteria designed to measure the effectiveness of the school.

* * *

I. An approved plan to establish a charter school is effective for fifteen years from the first day of the fiscal year the charter school is in operation, subject to the following:

* * *

3. A sponsor shall review a charter at five year intervals and may **revoke a charter** at any time if the charter school breaches one or more provisions of its charter. At least ninety days before the effective date of the proposed revocation the sponsor shall give written notice to the operator of the charter school of its intent to revoke the charter. Notice of the sponsor's intent to revoke the charter shall be delivered personally to the operator of the charter school or sent by certified mail, return receipt requested, to the address of the charter school. The notice shall incorporate a statement of reasons for the proposed revocation of the charter. The sponsor shall allow the charter school at least ninety days to correct the problems associated with the reasons for the proposed revocation of the charter. The final determination of whether to revoke the charter shall be made at a public hearing called for such purpose.

* * *

R. The sponsoring entity of a charter school shall have oversight and administrative responsibility for the charter schools that it sponsors.

* * *



A REPORT
TO THE
ARIZONA LEGISLATURE

Performance Audit Division

Performance Audit and Sunset Review

Arizona State Board for Charter Schools

September • 2013
REPORT NO. 13-12



Debra K. Davenport
Auditor General

APP070

The **Auditor General** is appointed by the Joint Legislative Audit Committee, a bipartisan committee composed of five senators and five representatives. Her mission is to provide independent and impartial information and specific recommendations to improve the operations of state and local government entities. To this end, she provides financial audits and accounting services to the State and political subdivisions, investigates possible misuse of public monies, and conducts performance audits of school districts, state agencies, and the programs they administer.

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DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

MELANIE M. CHESNEY
DEPUTY AUDITOR GENERAL

September 25, 2013

Members of the Arizona Legislature

The Honorable Janice K. Brewer, Governor

Mr. Jake Logan, President
Arizona State Board for Charter Schools

Ms. Deanna Rowe, Executive Director
Arizona State Board for Charter Schools

Transmitted herewith is a report of the Auditor General, *A Performance Audit and Sunset Review of the Arizona State Board for Charter Schools*. This report is in response to an October 26, 2010, resolution of the Joint Legislative Audit Committee. The performance audit was conducted as part of the sunset review process prescribed in Arizona Revised Statutes §41-2951 et seq. I am also transmitting within this report a copy of the Report Highlights for this audit to provide a quick summary for your convenience.

As outlined in its response, the Arizona State Board for Charter Schools agrees with all of the findings and plans to implement all of the recommendations.

My staff and I will be pleased to discuss or clarify items in the report.

Sincerely,

Debbie Davenport
Auditor General

Attachment

cc: Arizona State Board for Charter Schools Members



REPORT HIGHLIGHTS PERFORMANCE AUDIT

Our Conclusion

The Arizona State Board for Charter Schools (Board) was established in 1994 to authorize and oversee the operations of charter schools. The Board has increased charter schools' accountability but can further enhance its oversight by continuing to implement its academic performance intervention policy, taking action to address charter holders with poor financial performance, assessing whether it should require charter holders to submit corrective action plans that address a broader range of internal control weaknesses or deficiencies, and establishing an operational framework. Additionally, although the Board provides information about charter schools on its Web site, it can do more to provide comparative information and guidance to better explain academic performance accountability.



2013

Board can further enhance its oversight of charter schools

Charter schools are publicly funded and are subject to many of the same state and federal educational requirements as school districts, such as using state-mandated tests and employing highly qualified teachers. However, charter schools are exempt from some requirements, such as hiring certified teachers. In the 2012-2013 school year, about 145,000 students were enrolled in charter schools throughout the State. As of August 2013, the Board oversaw 511 charter schools, including 503 charter schools sponsored directly by the Board and 8 charter schools sponsored by the Arizona State Board of Education.

The Board's responsibilities include approving charter school applications and renewals, overseeing charter school performance and accountability, and taking corrective action when necessary. Historically, the Board's oversight has focused on charter schools' compliance with financial, legal, and contractual requirements. Board staff reviewed schools' annual financial audits to assess charter schools' performance in these compliance areas, and the Board would take some action for repeated noncompliance. However, prior to 2010, the Board had not historically held charter schools accountable for their academic performance.

Board has improved academic performance oversight—In 2011, the Board worked with the National Association of Charter School Authorizers to enhance its oversight of charter school academic and financial performance. In addition, 2012 legislation required the Board to develop a charter school performance framework that includes academic performance and operational expectations and measures sufficient progress toward those expectations.

Adopted in the fall of 2012, the Board's academic performance framework incorporates more rigorous academic standards than required by the State and evaluates academic performance based on data that the Arizona Department of Education (ADE) already collects. The framework's performance measures give an overall performance rating of exceeds, meets, does not meet, or falls far below for each charter school. The Board used these ratings to conduct an initial analysis of its charter schools, based on ADE's academic performance data for the 2011–2012 school year, and determined that 269, or 60 percent, of its charter schools would have exceeded or met academic standards; 156, or 35 percent, would not have met standards; and 21, or about 5 percent, would have fallen far below standards.

Key charter school definitions

Charter authorizer—Entity authorized to sponsor public charter schools. In Arizona, the Arizona State Board for Charter Schools, the Arizona State Board of Education, the state universities, eligible community colleges, and school districts can sponsor charter schools.

Charter school—A public school that serves as an alternative to school districts. Charter schools receive public monies and cannot charge tuition.

Charter holder—A public body, private person, or private organization that contracts with a charter authorizer to operate one or more charter schools.

In August 2013, the Board adopted an academic intervention policy that guides its annual review of charter school academic performance and the possible intervention the Board may take to address charter schools that do not meet standards. If a charter holder's schools meet or exceed academic performance standards in successive years, they can be waived from annual reviews during certain years. If a charter holder's schools do not meet standards, the Board will consider disciplinary or corrective action.

Board can provide more financial oversight—The Board has also adopted a financial framework based on best practices. The measures for this framework will help the Board assess the financial condition of a charter school. For example, if a charter holder does not have at least 30 days of cash on hand, the holder would not meet the Board's standard for this measure. Board staff will annually calculate the measures for this framework, which the Board will review during its 5-year reviews of charter holders, contract renewals, and requests for certain contract changes. However, the Board does not plan to take action based on poor financial performance alone, but will consider this information when also reviewing a school's academic performance.

Board can better oversee financial, legal, and contractual requirements—The Board relies on the annual financial statement audits and legal compliance checklists completed by certified public accountants to assess charter holders' compliance with financial, legal, and contractual requirements. The Board requires charter holders to submit corrective action plans to address only two types of internal control weaknesses or deficiencies identified in the audits. In addition, although the Board oversees many of the compliance and operational areas suggested by best practices, it has not adopted an operational framework with additional operational indicators and standards that are helpful for evaluating charter holders' operational performance.

Recommendations

The Board should:

- Continue to implement its academic performance intervention policy;
- Adopt rules and develop and implement policies and procedures to guide its actions for addressing poor financial performance;
- Assess whether it should require corrective action plans to address other types of internal control findings; and
- Develop and implement an operational framework.

Board should improve public information about charter schools

The Board makes some information about charter schools available on its Web site, such as some charter holder applications and academic performance. However, some information can only be found in files at the Board's office. Additionally, some information, such as disciplinary action information, is difficult to find on the Board's Web site. The Board has plans to put more information about charter holders on its Web site, such as the academic and financial performance information based on its frameworks. The Board should also determine the feasibility of providing comparative charter school information on its Web site, which can help the public compare charter school performance. In addition, the Board should also provide some guidance on its Web site to help the public understand the differences between the Board's and ADE's assessments of charter school academic performance. For example, in fiscal year 2012, 252 charter schools received B and C (passing) grades from ADE, but 99 of these schools did not meet the Board's academic performance standards.

Recommendations

The Board should:

- Follow through with its plans to improve the information on its Web site;
- Determine the feasibility of providing comparison information about charter schools on its Web site; and
- Provide guidance on its Web site to help explain academic performance measures.

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concluded •

INTRODUCTION

Scope and Objectives

The Office of the Auditor General has conducted a performance audit and sunset review of the Arizona State Board for Charter Schools (Board) pursuant to an October 26, 2010, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the sunset review process prescribed in Arizona Revised Statutes (A.R.S.) §41-2951 et seq.

This performance audit and sunset review addresses (1) the Board's oversight of charter school performance, and (2) improvements the Board should make related to the information it provides to the public about charter schools. The report also includes responses to the statutory sunset factors.

History of Board and charter schools in Arizona

The Legislature established the Board in 1994 by enacting A.R.S. §15-181, which also authorized the formation of charter schools in Arizona to provide a learning environment that will improve student achievement through providing additional academic choices for parents and students. As a charter authorizer, the Board sponsors charter holders who operate charter schools (see textbox for definitions of these terms). The Board's mission is to improve public education by sponsoring quality educational choices in Arizona.

Although charter schools share some similarities with school districts, they have some operational flexibility that school districts do not have. Similar to school districts, charter schools are publicly funded and are subject to state and federal requirements, such as testing students against state-wide standards using state-mandated tests, reporting student attendance to the Arizona Department of Education (ADE), employing highly qualified teachers, and providing a program of instruction that includes core academic subjects mandated by the federal No Child Left Behind Act.¹ However, in contrast to school districts, A.R.S. §15-183(E)(5) exempts charter schools from some statutes and rules relating to schools, governing boards, and school districts.² For example, although charter schools must hire teachers who meet the State's definition of "highly qualified," they are not required to hire certified teachers. In addition, charter schools can apply to their charter authorizer for exemption from the school district procurement rules, providing them more flexibility in purchasing and procuring services. The Board has developed specific eligibility criteria for this exemption, such as being in good standing

Key charter school definitions

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Charter school—A public school that serves as an alternative to school districts. Charter schools receive public monies and cannot charge tuition.

Charter holder—A public body, private person, or private organization that contracts with a charter authorizer to operate one or more charter schools.

Source: Auditor General staff summary of information from the National Alliance of Public Charter Schools' Web site and A.R.S. §§15-181 and 15-183.

¹ Charter schools receive state monies based on student attendance. In addition, charter holders can receive a grant of federal monies from ADE to assist with start-up costs. In calendar years 2010 through 2012, 57 charter holders were awarded start-up grants.

² In contrast to school districts where statute regulates the disposition of school property, A.R.S. §15-183 provides closed charter schools the authority to retain all property it accumulates during operation, which includes any property purchased with state aid, such as textbooks or desks.

Table 1: Top ten states in the percentage of students attending charter schools School year 2011-2012

State	Percent of students
Washington, DC	40.8%
Arizona	12.4
Colorado	9.8
Delaware	7.9
Michigan	7.7
Utah	7.6
Ohio	7.2
Florida	6.8
California	6.7
Louisiana	6.4

Source: Auditor General staff analysis of data from the National Alliance for Public Charter Schools' Web site.

with the Arizona Corporation Commission, and provides this exemption to eligible charter schools that apply.

Arizona has experienced steady growth in the number of charter schools in the State, with more than 134,000 students enrolled in these schools in the 2011-2012 school year. According to a 2013 study by the Center for Student Achievement, the number of charter schools in Arizona has grown steadily since the 1996-1997 school year, including an average 8 percent annual increase between the 2007-2008 and 2011-2012 school years.¹ As shown in Table 1, in the 2011-2012 school year, approximately 12.4 percent of Arizona kindergarten through high school students attended charter schools. Of the 41 states and Washington, DC, that allow charter schools, only Washington, DC, had a higher percentage of students enrolled in charter schools. In the 2012-2013 school year, the number of students attending charter schools in Arizona continued to increase to approximately 145,000 students. According to the Center for Student Achievement, if similar student enrollment trends continue for charter schools, the number of Arizona students attending charter schools could double by 2020.

Board responsibilities

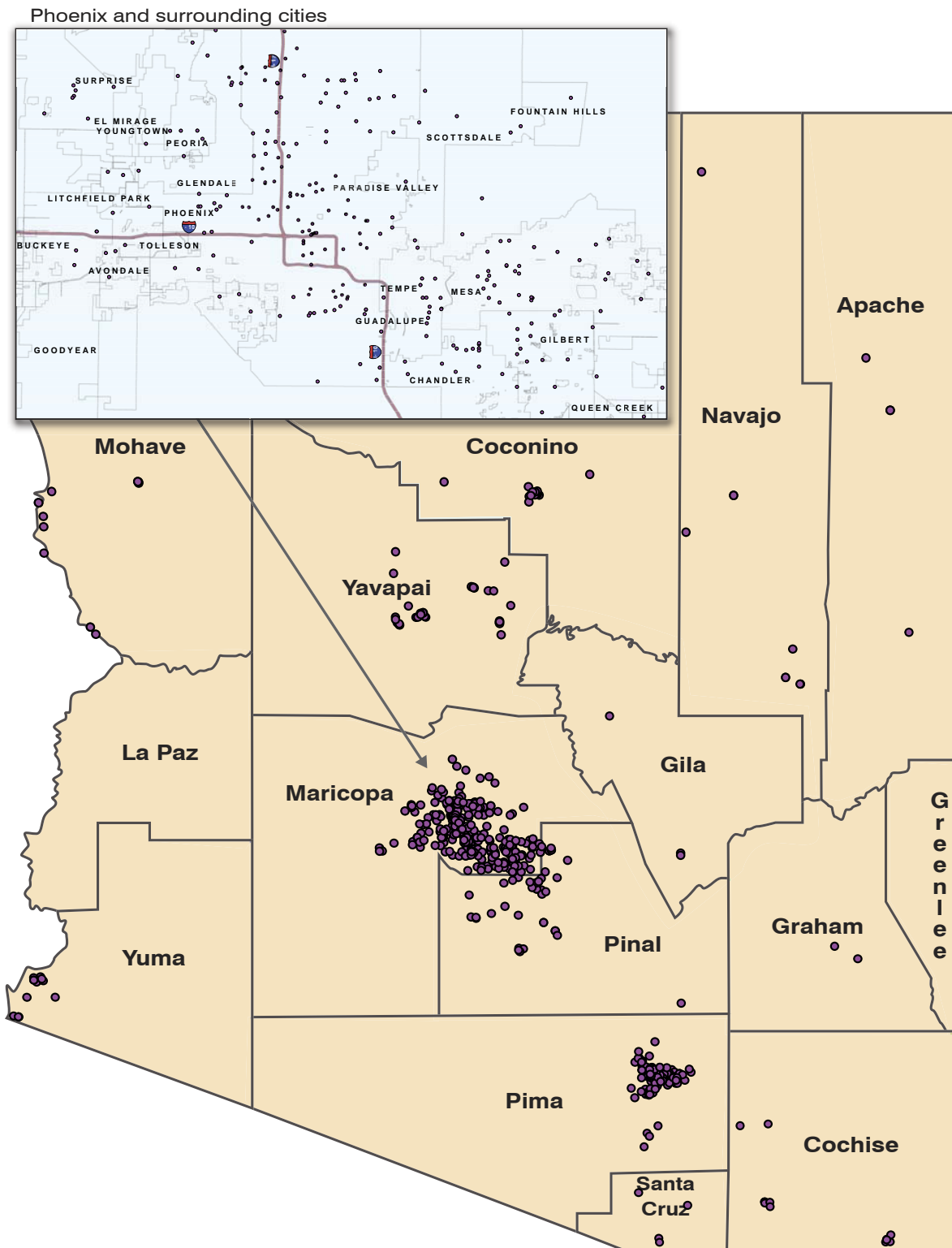
The Board is Arizona's primary charter school authorizer and oversees most charter schools in the State. According to the Board's database, as of August 2013, the Board provided oversight for 511 charter schools, including 503 charter schools sponsored directly by the Board and 8 charter schools sponsored by the Arizona State Board of Education.² In addition, according to ADE's Web site, Arizona school districts and Arizona State University sponsored 76 charter schools as of September 2013. As shown in Figure 1 (see page 3), although most charter schools are in Maricopa and Pima Counties, the Board sponsors charter schools throughout the State.

In addition to being the largest authorizer in Arizona, the Board is also the nation's largest independent state authorizer, according to the National Association of Charter School Authorizers (National Association). Similar to Arizona, most states employ a combination of authorizing entities, such as Local Education Agencies (LEAs) and state education agencies, to sponsor charter schools. LEAs are by far the most common authorizer, but authorize on average about 1 school (see

¹ Center for Student Achievement (2013). *Oh, the places they'll go: Arizona public school choice and its impact on students*. Phoenix, AZ: Author. The Center for Student Achievement's mission is to improve student achievement in all schools with a focus on the publication of rigorous and transparent research and evaluation. The Center provides national consulting services to educators in other states about how to use student data analysis for accountability purposes.

² In fiscal year 2004, the Board entered into an agreement with the Arizona State Board of Education to provide oversight for all of the charter schools the Arizona State Board of Education sponsors. In 2010, the Arizona State Board of Education decided not to renew the charter holders it sponsored, which resulted in many charter holders applying for charter contracts with the Board. As a result, the Board's database contains charter school information for both board-sponsored charter schools, which includes charter schools previously sponsored by the Arizona State Board of Education, as well as charter schools currently sponsored by the Arizona State Board of Education.

Figure 1: Board-sponsored charter schools throughout Arizona
As of April 2013



Source: Auditor General staff compilation of information from the Board's database for fiscal year 2013.

textbox). By contrast, 21 states rely on a state education agency to sponsor charter schools in addition to any charter schools authorized by LEAs. Texas, for example, through its state education agency, authorizes 504 schools.

The Board's charter school oversight responsibilities include approving applications and renewals, monitoring schools' performance, and taking corrective action when necessary. Specifically, the Board:

- **Reviews and approves or denies initial, renewal, and replication applications**—The Board considers and grants charter contracts to qualified applicants through its initial, renewal, and replication application processes. As shown in Table 2, in fiscal year 2012, the Board received 49 initial charter applications, reviewed 14 applications, and approved 9 applications. The Board did not review applications that its staff determined were incomplete. According to board staff, a common reason for incomplete applications is the applicant's failure to provide all required documentation. The Board considers complete applications at a public hearing (see Sunset Factor 2, pages 30 through 31, for more information on auditors' review of the Board's application processes). Once approved by the Board, the applications become a part of the charter contract. The Board's application processes are as follows:
 - **Initial charter**—Applicants for a charter contract, which is granted for a 15-year term, must submit detailed information on charter school operations, such as educational, organizational, and business plans. For example, application materials include sample curriculums and 3-year operational budgets. To review the applications, the Board uses a panel of volunteers, including current charter holders and others who have expertise in charter school development, curriculum, and finance. In 2011, the National Association conducted a review of several board operations and, in its 2011 report to the Board, indicated that the Board's initial application review and approval practices contained most aspects of a well-developed practice but made some recommendations for improvement. The Board has since implemented a change to its initial charter application review practices in response to the National Association's recommendations.¹ Specifically, in fiscal year 2013, the Board added an applicant interview to enhance the Board's ability to evaluate the applicant's capacity to

Charter school oversight—According to the National Association, fewer than 1 percent of authorizers (8 out of 974) nation-wide oversee more than 100 charter schools. In contrast, 85 percent (825 authorizers) oversee 5 or fewer charter schools, including 53 percent (516 authorizers) that only oversee 1 charter school.

Source: National Association of Charter School Authorizers. (2013). *The state of charter school authorizing 2012* (5th Annual Report on NACSA's Authorizer Survey). Chicago, IL: Author.

Table 2: Number of applications submitted and approved by Board Fiscal year 2012

Application type	Submitted	Reviewed	Approved
New	49	14	9
Renewal	43	43	40
Replication	6	6	6

Source: Auditor General staff analysis of the *State of Arizona Five-year Strategic Plans of State Agencies and The Master List of State Government Programs fiscal years 2012-2015* report.

¹ The National Association of Charter School Authorizers is a national organization committed to advancing excellence and accountability in the charter school sector. Through its evaluation grants, the National Association conducts authorizer evaluations across the nation with the purpose of identifying strengths and opportunities for improvement in an authorizer's policies and procedures. The National Association also offers grants to help authorizers implement any changes recommended during the evaluation. The Board received an implementation grant in the fall of 2011 to help develop an initial applicant interview as well as the academic, financial, and organizational performance frameworks (see Finding 1, pages 9 through 22, for more information on the frameworks).

operate a charter school. The Board uses the interview to ask follow-up questions based on the application materials.

- **Renewal**—Within 15 months prior to the expiration of a 15-year charter contract, the charter holder must submit a renewal application to extend the contract for another 20 years. At renewal, the Board considers the academic performance of the charter holder’s school or schools and the charter holder’s financial sustainability. If academic performance has not met board standards, the charter holder must submit an improvement plan. If financial performance does not meet two or more performance standards or falls far below one standard, the charter holder must submit additional information explaining its financial situation. The Board will use this additional information to help it decide whether or not to renew the charter contract. As shown in Table 2 (see page 4), in fiscal year 2012, the Board reviewed 43 charter contract renewal applications and approved 40 of these applications.
- **Replication**—According to the National Alliance for Public Charter Schools, an effective way to increase the number of quality charter holders in an authorizer’s portfolio is to allow high-performing charter schools to replicate their charters—in effect, to create additional schools under the same charter holder.¹ In Arizona, charter holders that meet board academic and financial performance standards can expand their operations by applying for a separate charter contract through a streamlined process by submitting a replication application. The charter holder does not need to submit all the materials required of a new applicant. In making its decision whether or not to allow a replication, the Board considers the charter holder’s past performance and its plans for the school that will be included in the new contract. As shown in Table 2 (see page 4), the Board approved all six replication applications it received and reviewed in fiscal year 2012.
- **Monitoring charter schools**—To monitor the charter schools for which it is responsible, the Board conducts site visits, reviews schools’ academic and financial performance, and requires annual financial audits. Board staff conduct site visits of all of its charter schools during their first year of operation, and in subsequent years for charter schools that do not meet board performance standards. As shown in Table 3, in fiscal year 2012, the Board conducted 124 charter school site visits. During these visits, board staff use a checklist to examine compliance issues, such as confirming that staff resumes are available for parent review, that the charter school maintains up-to-date fingerprint clearance cards for instructional staff, and that the school maintains accurate student attendance records, which are consistent with the school’s ADE reports.

**Table 3: Monitoring activities
Fiscal year 2012**

Monitoring activity	Number conducted by board staff
Site visits	124
Interval reviews	63
Annual financial audit reviews	364

Source: Auditor General staff review of the *State of Arizona Five-year Strategic Plans of State Agencies and The Master List of State Government Programs Fiscal Years 2012-2015* report.

In addition to conducting site visits, statute requires the Board to conduct reviews—called interval reviews—of charter holders every 5 years and requires charter holders to submit to the Board annual audit reports prepared by a certified

¹ National Alliance for Public Charter Schools. (2009). *A new model law for supporting the growth of high-quality public charter schools*. Washington, DC: Author.

public accountant (CPA).¹ As shown in Table 3 (see page 5), in fiscal year 2012, board staff conducted 63 interval reviews and reviewed 364 annual audit reports. During a charter holder's 5th- and 10th-year-interval reviews, board staff review academic performance, such as students' performance on state standardized tests. If a charter holder does not meet the Board's academic standards, board staff may conduct site visits to provide technical assistance and require the charter holder to take corrective action. Board staff use the annual audit reports to assess the charter holder's compliance with financial and legal requirements. These audits are statutorily required to ensure that the charter holder complies with state law, charter contractual requirements, and accounting standards. Specifically, in addition to auditing the charter school's financial statements, the CPA completes a checklist to ensure compliance with legal and contractual requirements, such as fingerprinting personnel, instructional hours, and student attendance (see Finding 1, pages 9 through 22, for additional information about the Board's oversight practices).

- Corrective and disciplinary action**—The Board has several actions it can take to ensure that charter schools comply with statutory, federal, contractual, and board requirements. Specifically, the Board has statutory authority to assign a corrective action plan and to request that ADE withhold up to 10 percent of the charter school's state funding if the Board determines a charter school is not complying with state or federal laws, charter contractual requirements, or board academic performance standards.² As shown in Table 4, in fiscal year 2012, the Board assigned 123 corrective action plans, which included requests to withhold funds from 24 charter holders. The Board may also issue a letter of intent to revoke a charter, which may result in entering into a consent or settlement agreement to resolve the areas of the noncompliance, or to revoke the charter. In fiscal year 2012, the Board issued 3 notices of intent to revoke and entered into 3 consent or settlement agreements (see Table 4).

**Table 4: Disciplinary actions
Fiscal year 2012**

Board action	Number
Corrective action plans assigned: ¹	
Audit-related	59
Withholding of funds	24
Academic-related	40
Total	<u>123</u>
Notices of intent to revoke issued	3
Consent or settlement agreements entered into	3
Charter revoked ²	0

¹ The Board requires corrective action for noncompliance with charter contracts or state and federal laws. According to board staff, there are three areas that will result in corrective action. These areas include noncompliance issues found in the annual financial audits, the Board requesting withholding of state funds, and academic performance that does not meet board standards.

² Charter revocation hearings may span fiscal years but are reported only once.

Source: Auditor General staff analysis of *State of Arizona Five-Year Strategic Plans of State Agencies and The Master List of State Government Programs for Fiscal Years 2012-2015* report and information provided by board staff.

¹ According to Arizona Administrative Code R7-5-502, the Board approves charter schools' audit contracts with an audit firm that meets the criteria for approval. For example, the Board may disapprove an audit contract with an audit firm that does not maintain good standing with an accounting industry regulatory body or if the regulatory body determines the audit firm failed to comply with auditing standards.

² ADE is responsible for distributing state funds to charter schools. A.R.S. §15-185(H) requires ADE to withhold monies from a charter school when requested by the charter authorizer.

Organization and staffing

The Board consists of 11 members, including the superintendent of public instruction or the superintendent's designee. The Governor appoints the remaining members, who serve 4-year staggered terms, as follows:

- Six members of the general public, two of whom must reside in a public school district where at least 60 percent of the children attending schools in the district meet the eligibility requirements for the federal Free and Reduced Lunch Program, and one of whom must reside on an Indian reservation;
- Two members of the business community;
- One charter school operator; and
- One charter school teacher.

In addition, three members of the Legislature, jointly appointed by the President of the Senate and the Speaker of the House, serve as advisory members to the Board. To assist it in its duties, the Board has been appropriated funding by the Legislature for eight full-time staff member positions including an Executive Director, three program directors, and four program specialists and support staff. All positions were filled as of June 2013. Staff are responsible for reviewing applications and making sponsorship recommendations to the Board, monitoring charter school performance and compliance with laws and contracts, and providing information to the public. According to board staff, the Board will receive a full-time fellow through the National Association for a year-long placement beginning in September 2013.¹

Budget

As shown in Table 5 (see page 8), the Board received approximately \$764,000 in fiscal year 2013 from the State General Fund. Most of the Board's expenditures are for personnel and employee-related costs, which totaled approximately \$631,000 in fiscal year 2013. Effective on August 2, 2012, the Board was allowed to collect fees for processing initial charter applications. Laws 2013, Ch. 68, authorized the Board to assess this fee without a rulemaking. As a result, the Board established a \$6,500 initial application fee and began collecting this fee for new charter school applications for the 2014-2015 school year. The Board was also awarded an \$87,500 grant from the National Association in fiscal year 2012 to develop and implement an applicant interview as part of the application process for new charter holders and to develop a new evaluation framework for measuring charter school performance (see Finding 1, pages 9 through 22, for more information about the framework).

¹ The National Association's fellowship program provides placement for a salaried professional with an interest in education reform with charter school authorizers that have a large portfolio of charter schools to maximize the fellow's impact on students. Fellows for the 2012-2013 program worked in New Jersey, New York City, and Philadelphia and placements for the 2013-2014 program include Arizona, North Carolina, and Washington, DC.

**Table 5: Schedule of revenues, expenditures, and changes in fund balance
Fiscal years 2011 through 2013
(Unaudited)**

	2011	2012	2013
Revenues			
State General Fund appropriations	\$ 724,776	\$ 741,932	\$ 763,856
Licenses and fees ¹	57,000	15,000	6,000
Private grant		22,206	4,000
Other	768	1,248	889
Gross revenues	782,544	780,386	774,745
Remittances to the State General Fund ²	(768)	(1,248)	(889)
Net revenues	781,776	779,138	773,856
Expenditures			
Personal services and related benefits ³	484,084	602,771	630,640
Professional and outside services ⁴	106,518	45,423	16,762
Travel	2,182	8,903	8,572
Other operating ⁵	163,244	113,950	98,496
Equipment	16,748	319	17,417
Total expenditures	772,776	771,366	771,887
Net change in fund balance	9,000	7,772	1,969
Fund balance, beginning of year		9,000	16,772
Fund balance, end of year ⁶	\$ 9,000	\$ 16,772	\$ 18,741

¹ Amount is a processing fee paid by charter schools that amend their contracts to participate in Arizona online instruction. The fees can be used only for processing contract amendments for charter schools participating in Arizona online instruction.

² The Board charges publication and reproduction fees. These fees are required to be remitted to the State General Fund.

³ According to the Board, the amount increased between fiscal years 2011 and 2012 primarily because vacancies in fiscal year 2011 were filled and one position was reclassified, resulting in a slightly higher salary. Fiscal year 2013 is the first year since fiscal year 2011 in which the Board expects no vacancies or changes in staff. In addition, the fiscal year 2013 amount includes a 5 percent critical retention payment to all uncovered employees as authorized by Laws 2012, Ch. 294, §133.

⁴ Amount includes expenditures from the Board's online processing fees that were used to contract for amendment processing during fiscal year 2011 and part of 2012. In addition, according to the Board, it also contracted for services other than contract amendments in fiscal year 2011 because staffing shortages did not allow it to perform certain work and reviews internally.

⁵ According to the Board, the other operating expenditures for fiscal year 2011 include costs for database improvements that were made to increase operating efficiencies. In addition, the Arizona Department of Administration significantly lowered the Board's rental expenditures in fiscal year 2012.

⁶ The Board's ending fund balance for fiscal year 2011 comprises Arizona online instruction fees that were collected in fiscal year 2011 but not spent until fiscal year 2012. In addition, the fiscal years 2012 and 2013 ending fund balances comprised unexpended grant and Arizona online processing fee monies

Source: Auditor General staff analysis of the Arizona Financial Information System (AFIS) *Accounting Event Transaction File* and the AFIS Management Information System *Status of General Ledger-Trial Balance* screen for fiscal years 2011 through 2013.

FINDING 1

The Arizona State Board for Charter Schools (Board) has implemented academic and financial performance standards to improve charter school accountability but can further enhance its oversight practices to ensure that the charter schools it oversees meet performance standards and comply with legal and contractual requirements. Board oversight is important for ensuring that schools are accountable to board-established performance standards and comply with state and federal laws. Historically, the Board's oversight has focused on charter school compliance with laws and regulations, with some emphasis on schools' academic performance. However, the Board has taken steps to improve its oversight by establishing stronger academic and financial performance standards for charter schools and implementing various mechanisms to assess their performance against these standards. Even with these changes, auditors identified opportunities for further improvement. Specifically, the Board should further strengthen charter school accountability by continuing to establish oversight practices recommended by the National Association of Charter School Authorizers (National Association). The Board should also develop and implement administrative rules to help it enforce charter school compliance with the improved academic and financial performance standards it has established.

Board has increased charter schools' accountability, but can further enhance oversight

Oversight is important to ensure charter school accountability

To help ensure that the charter schools it oversees meet their statutory obligations, the Board needs to provide effective oversight of academic performance, financial stability, and compliance with contractual and legal requirements. Although charter schools are subject to several statutory requirements, including reporting student attendance and testing students against state-wide standards, charter schools are provided some flexibility in conducting their operations, including educating their students. For example, charter schools are exempt from hiring certified teachers and can receive an exemption from other statutory requirements, such as procurement and uniform reporting requirements.

Oversight of charter schools by the state authorizer, such as the Board, is a widely accepted accountability tool. For example, according to data obtained from the National Alliance of Public Charter Schools (National Alliance), most states require at least annual collection and analysis of student academic data and/or financial accountability information, including compliance with accounting standards and completing an annual independent audit.¹ According to the National Alliance, comprehensive charter school monitoring and data collection is one of four factors that can have the greatest impact on the quality of a state's charter school sector. Additionally, according to the National Association, monitoring and oversight are important to hold charter schools accountable for high achievement and to ensure legal compliance and effective management.²

¹ National Alliance for Public Charter Schools. (2012). *Measuring up to the model: A ranking of charter school laws* (3rd ed.). Washington, DC: Author.

² National Association of Charter School Authorizers. (2012). *Principles & standards for quality charter school authorizing*. Chicago, IL: Author.

Board oversight historically focused on financial and legal compliance; more limited on academic performance

Despite the importance of student achievement and academic performance, the Board's charter school accountability efforts have historically focused on financial, legal, and contractual compliance. Specifically, from 1999, when financial oversight responsibility transferred from the Office of the Auditor General to the charter school authorizer, until 2010, when the Board implemented additional oversight practices, the Board's accountability focus was limited mainly to compliance with financial, legal, and contractual requirements.¹ For example, the Board's contract with charter schools required schools to implement standard internal controls, such as ensuring that the same person does not both approve expenditures and write checks, and board staff reviewed annual certified public accountant (CPA) audits of charter holders to assess whether a charter holder's school instituted and followed these controls. Board staff also reviewed the annual audits to determine if the charter school's financial reporting complied with accounting standards. When conducting these audits, CPAs have also been required to complete a board-approved checklist to assist the Board in determining whether charter schools are complying with certain federal and state laws, regulations, and contractual requirements. If board staff found that a charter holder had deficiencies in the same legal or contractual compliance area requiring corrective action for 3 years, board policy requires that the school go to the Board for review and possible disciplinary action.

The Board has not historically held its charter schools accountable for their academic performance, even though information was available to do so. Prior to 2010, the Board obtained academic data from the Arizona Department of Education (ADE), but did not have policies in place to hold charter schools accountable for underperformance outside of ADE's school improvement process. Starting in 2010, the Board began using academic performance data that ADE collected to evaluate student growth and test scores. For example, the Board began using this academic performance data to determine whether to approve charter holders' requests for renewal, replication, and contract amendments. It also began reviewing this data during its 5-year interval reviews of charter holders to determine whether a charter holder needed to develop an improvement plan that specified actions it would take to improve its students' academic performance. Although the Board followed up on some of these plans to determine whether changes were made or the students' academic performance improved, according to board staff, they only followed up on improvement plans submitted by charter holders that had other noncompliance issues (see pages 14 through 15 for information on the Board's policies for following up on improvement plans).

ADE has assessed student and school academic performance—including charter schools—since 2001 to comply with federal requirements. Specifically, the federal No Child Left Behind Act (Act) requires states to establish academic standards and to assess students' and schools' performance against these standards. These standards apply to both school districts and charter schools. In response to Proposition 301, in 2001, ADE developed and implemented a system measuring student and school performance called AZ Learns that provided a snapshot of student achievement. In 2011, ADE established an A-F Letter Grade Accountability System in accordance with state law to measure student achievement that required all public schools to annually provide the information needed for ADE to assign a letter grade to the school (see textbox on page 11). Unlike the previous

¹ Laws 1999, 1st S.S., Ch. 4, §15

A-F Letter Grade Accountability System—The State of Arizona measures student achievement using the A-F Letter Grade Accountability System, which was implemented in 2011. ADE is responsible for annually collecting state-wide results, assigning a letter grade to each school based on student academic test scores and other factors, such as high school graduation rates, and annually reporting these results to the U.S. Department of Education. The system rates schools' performance as:

- A—excellent
- B—above average
- C—average
- D—below average
- F—failing

A D-rated charter school must submit an improvement plan to both ADE and its charter authorizer. A school receives an F, or failing, rating if it has received a D—or the equivalent under ADE's previous rating system—for 3 consecutive years. If a charter school receives an F, ADE notifies the authorizer, and the authorizer can either take action to restore the charter school to acceptable performance or revoke the charter.

Source: Auditor General staff analysis of Arizona Revised Statutes (A.R.S.) §15-241 and information on state-wide standards published on ADE's Web site.

system, which provided a snapshot of student achievement, the A-F Letter Grade Accountability System also measures a school's students' academic growth over time.

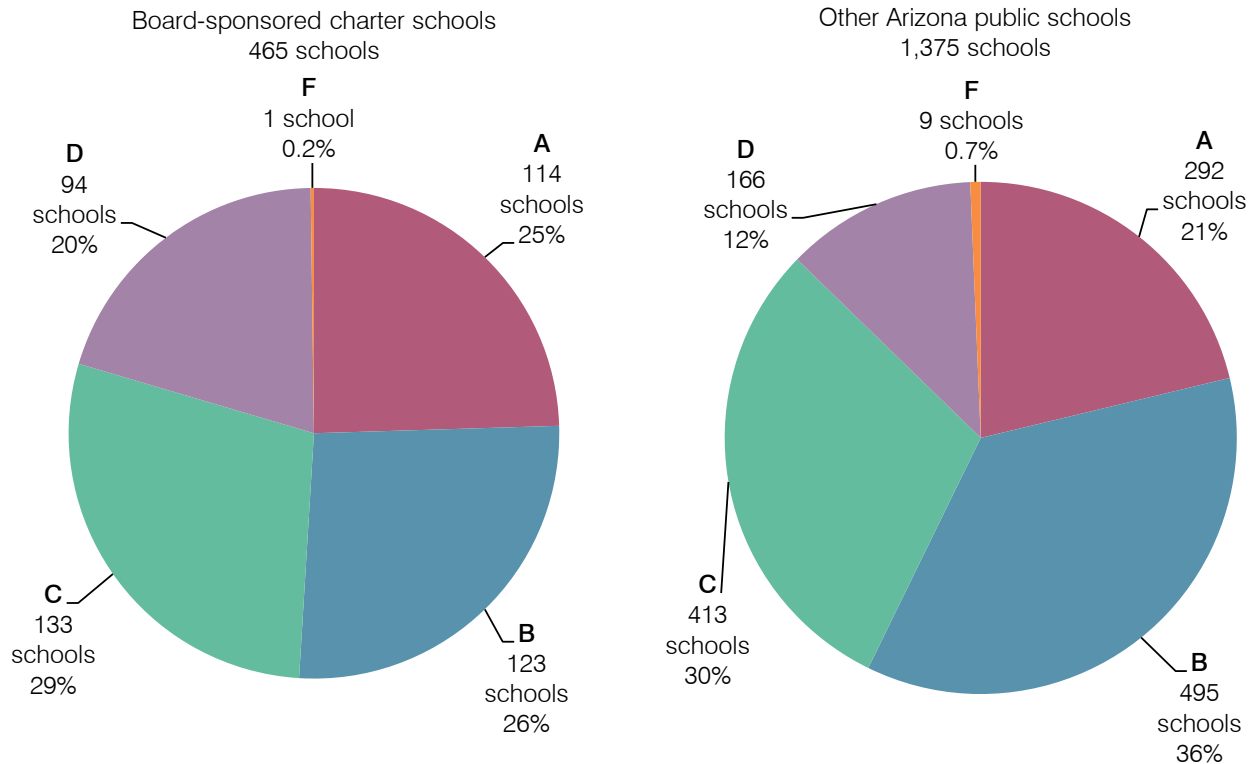
Although ADE's evaluation system provides a way to measure charter school performance, it is the Board's responsibility to ensure charter school accountability and, when necessary, to ensure that poor performance is improved. As shown in Figure 2 (see page 12), for the 2011-2012 school year, compared to other public schools, a higher percentage of board-sponsored charter schools received a rating of D based on ADE's A-F Letter Grade Accountability System. Specifically, out of the 465 board-sponsored charter schools that received a letter grade, 94 (20 percent) received a D, which means these charter schools' academic performance was below average.^{1,2} By comparison, 12 percent of other public schools in Arizona received a D letter grade.³ About the same percentage of charter schools and other public schools received failing grades. Additionally, based on ADE's AZ Learns system, numerous board-sponsored charter schools underperformed—meaning the schools' academic performance did not meet state performance or progress goals. Specifically, for the 2009-2010 and 2010-2011 school years, 7 percent and 4 percent of board-sponsored charter schools, respectively, received an underperforming designation.

¹ According to ADE staff, some schools did not receive a letter grade in the A-F Letter Grade Accountability System because they are too small. Additionally, if ADE does not have all the data it needs by the reporting deadline, ADE releases the letter grade report and will calculate these schools' grades at another date.

² According to a 2013 study by the Center for Student Achievement, a greater percentage of Arizona charter schools are alternative schools compared to school district schools, with 18 percent of charter school students enrolling in an alternative school compared to less than 1 percent of school district school students. However, the A-F Letter Grade Accountability System improved upon the AZ Learns system by using different weights and measures for the evaluation of alternative, K-2, and small school profile calculations. ADE developed these alternate models to account for the unique characteristics of these schools as required by A.R.S. §15-241.

³ Other public schools include Arizona school district schools and charter schools not sponsored by the Board.

**Figure 2: ADE academic letter grade system of school performance
School year 2011-2012**



Source: Auditor General staff analysis of A-F Letter Grade Accountability System profiles for all board-sponsored charter schools and other Arizona public schools, including traditional, small, alternative, and K-2 classroom settings, published by ADE in its 2012 state-wide accountability report.

Board has improved its oversight of charter schools, but can do more

The Board has taken steps to enhance its oversight of charter school accountability by implementing academic and financial performance standards that are consistent with best practices. In 2011, the Board worked with the National Association to conduct an evaluation of the Board's oversight practices. Consistent with several of the recommendations provided by the National Association, the Board has taken steps to improve charter school accountability, including enhancing its oversight of charter school academic performance and financial stability. However, opportunities for improvement remain. Specifically, the Board should continue its efforts to implement its academic intervention policy, further enhance its oversight of charter school financial stability, implement an operational review protocol, and further develop its database to help with its oversight efforts.

Enhanced oversight includes framework for evaluating academic performance—
The Board's efforts to enhance academic performance accountability reflected legislative direction and recommendations stemming from an external evaluation. Specifically, Laws 2012, Ch.

155, required the Board and other charter school authorizers in the State to develop a charter school performance framework that includes academic performance expectations, measurement of sufficient progress toward those expectations, operational expectations, and intervention and improvement policies, and to base charter school renewal and revocation decisions on the school's performance relative to the framework. In response to this legislative requirement and to one of three recommendations provided by a 2011 National Association evaluation of the Board's oversight practices, in October 2012, the Board adopted a charter school academic performance framework that it uses to help hold charter schools accountable for their academic performance.

The Board's academic performance framework incorporates additional academic standards for charter schools beyond those the State requires. These more rigorous academic performance standards are consistent with higher academic standards advocated by the California Charter School Association.¹ The Board designed its academic performance framework to communicate performance expectations to the charter schools it sponsors, to guide its review and assessment of charter schools' academic performance, and to assist in making decisions about renewing charter contracts. The Board has also included the academic performance framework in the new charter contracts it has approved for the 2013-2014 school year and the charter contracts it has renewed since October 2012.

The academic performance framework evaluates charter school academic performance based on the applicable framework measures (see textbox) using academic performance data that ADE already collects. For example, the subgroup proficiency measure compares state standardized test scores of a school's student subgroup, such as students with disabilities or students whose first language is not English, with similar students across the State. The Board also modifies the measures based on the type of charter school, such as small, alternative, elementary, middle, or high school. For example, the Board uses retention from one year to the next in place of graduation rate for alternative charter schools, which serve students who previously dropped out of school, are pregnant or parenting, or are in the criminal justice system.

The framework ties the academic performance measures into an overall performance rating. Once board staff have obtained the data for these measures, they calculate an overall performance rating for each charter school using a rating of exceeds, meets, does not meet, or falls far below standards for each charter school. A charter holder meets the Board's academic performance expectations if all of its schools receive an overall rating of meets or exceeds standards in the current and prior year's calculations.²

Academic framework measures

The academic framework uses nine measures to evaluate academic performance:

- Overall student growth
- Growth of lowest-performing students
- Proficiency
- Similar school comparison
- Subgroup proficiency
- State accountability system
- High school graduation rate
- Academic persistence
- College readiness

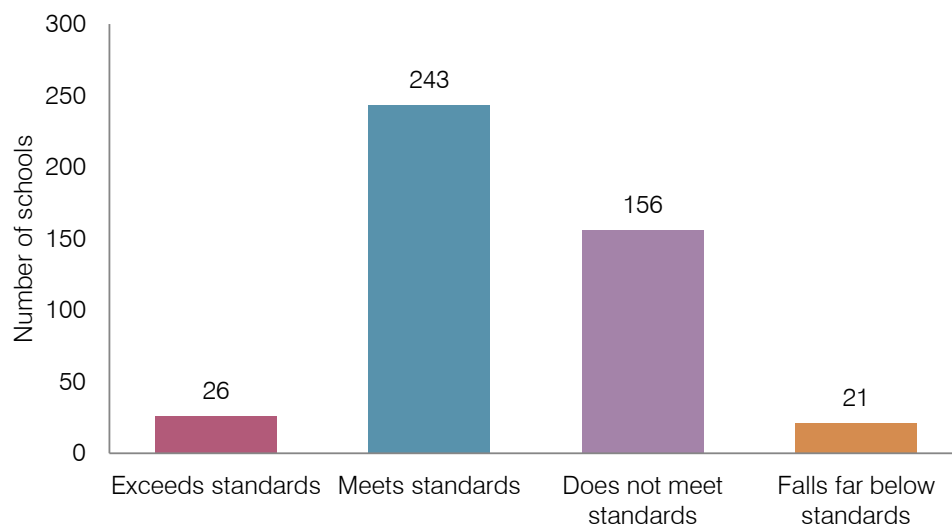
Source: Arizona State Board for Charter Schools. (2012). *Academic Performance Framework and Guidance*. Phoenix, AZ: Author.

¹ A 2011 California Charter Schools Association report indicates that in exchange for greater autonomy, charter schools should maintain higher educational and operational standards than school districts.

² The Board will not have 2 years of data available until after the 2012-2013 school year. Until that time, the Board will use the 2011-2012 school year's data to determine the overall ratings for a charter holder's schools and determine if a charter holder has met the Board's academic performance expectations. The Board's academic performance framework and guidance also requires charter schools that did not receive a rating in the prior year to provide information demonstrating progress toward board standards.

The Board has already used the new academic performance framework, which it implemented in November 2012, to conduct an initial analysis of its charter schools. This analysis was based on academic performance data collected by ADE from the 2011-2012 school year. Based on this analysis, and as shown in Figure 3, the Board determined that 269 charter schools, or 60 percent of all charter schools receiving a rating, would have exceeded or met the academic performance standards required by the framework.¹ In contrast, 156 charter schools (35 percent) would not have met the new standards, while an additional 21 charter schools' academic performance (4.7 percent) would have fallen far below the standards.

Figure 3: Board analysis of academic framework standards for board-sponsored charter schools School year 2011-2012 (Unaudited)



Source: Courtesy of the Board. Table was slightly modified from its original formatting to improve readability.

The Board also has plans in place for deciding how to use the ratings to determine what, if any, actions it should take to address academic performance that does not meet standards. Specifically, if a charter holder does not meet or exceed standards, the Board will require the charter holder to submit documentation showing whether it is making progress toward meeting standards.² For example, a charter holder could submit information about student test results that show improvement based on the charter holder's improvement plan. If a charter holder is unable to demonstrate sufficient progress, the Board will consider whether to take action, which, according to board staff, can result in nonrenewal or the Board revoking the charter.

¹ This calculation does not include unrated schools. Out of 479 charter schools board staff analyzed, 33 did not receive an academic performance rating. According to its academic performance framework guidance, the Board does not assign a rating to a school if it does not have enough data to make the calculations.

² The Board conducts site visits to determine a school's academic progress during the first year of operation. Additionally, if a school is too small for the Board to calculate a rating, the Board will require documentation that shows academic progress.

Continue efforts to implement academic intervention policy—During the audit, in August 2013, the Board adopted an academic intervention policy that outlines its process for reviewing academic performance annually and the possible intervention that the Board may take as a result of charter schools not meeting standards. Specifically, board staff will continue to conduct a site visit during the charter school’s first year of operation and will review academic performance data in the second and third operational years. If a charter holder’s schools meet the Board’s academic performance standards for two consecutive years by their third operational year, the schools will be waived from further review until the 5-year interval review. However, if a charter holder’s schools do not meet the Board’s academic performance standards, its schools will receive an additional review in their fourth year. Additionally, the charter holder will be required to submit additional documentation showing sufficient progress toward meeting the Board’s academic performance standards. The Board’s academic intervention policy statement also indicates that the Board will consider disciplinary action for charter holders that receive an overall rating of does not meet or falls far below standards for two consecutive years during the third and fourth operational years and after the 5-year interval reviews. The Board continues to require improvement plans for charter holders that do not meet or fall far below standards during the 5-year interval review. If a charter holder meets expectations during the 5-year interval review, meaning all its charter schools met or exceeded standards in the current and prior year’s academic performance calculations, the Board will waive the charter holder from annual reviews until the next interval review, which occurs in year 10.

This approach is consistent with literature suggesting that intervention is critical during the early operational years of charter schools. Specifically, according to a 2013 Center for Research on Education Outcomes report, annual reviews of a charter school’s academic performance are particularly important during a school’s first years of operation because any needed intervention can be most effective during those years.¹ Therefore, the Board should continue its efforts to implement its academic intervention policy by conducting annual reviews of charter schools’ academic performance, requiring schools to address academic performance that does not meet its standards, and taking disciplinary action as necessary.

Board also has taken steps to improve oversight of charter school financial stability, but should address gaps in its approach—In addition to adopting an academic performance framework, in August 2012, the Board adopted a financial framework modeled after the National Association’s best practices. Oversight of charter holders’ financial stability is important to ensure that charter schools can continue to operate and provide needed educational services to their students. Charter school closures often occur because of financial difficulties, creating upheaval for students and parents.² As it is doing for the academic performance framework, board staff annually collect financial data to calculate the financial framework’s measures beginning with the charter holder’s fiscal year 2012 audits. According to the Board’s financial performance framework and guidance, the Board reviews this information during its 5-year interval reviews and when charter holders submit renewal, contract amendment, and other change

¹ Center for Research on Education Outcomes. (2013). *Charter school growth and replication: Volume I*. Stanford, CA: Stanford University.

² Center for Research on Education Outcomes. (2009). *Multiple choice: Charter school performance in 16 states*. Stanford, CA: Stanford University and Office of the Auditor General Report No. 03-07.

requests.¹ The Board also plans to review a charter holder's financial performance data if the charter holder's academic review identifies poor academic performance.

The financial framework assesses immediate financial risk and long-term financial sustainability based on a review and calculation of seven measures (see textbox). For example, the unrestricted days cash ratio measures the number of days the charter holder could pay its expenses using cash on hand. The Board's calculation of this ratio will show whether the charter holder will have

difficulty in meeting its obligations, such as payroll and rent. Each charter holder's annual financial audit conducted by CPA firms provides the financial information board staff need to calculate and review these measures. For each measure, board staff annually determine whether the charter holder meets, does not meet, or falls far below standards. For example, if a charter holder does not have at least 30 days of available cash on hand, the charter holder would not meet standards in the unrestricted days cash measure (see textbox). According to board staff, the Board plans to review its financial measures and standards to assess whether they are effective in measuring financial stability in fiscal year 2014.

Financial framework measures

Measure	Definition	Standard
Going concern	Risk that the entity will go out of business within a year	No going concern issue identified in audit report
Unrestricted days cash	Number of days the entity can pay its expenses using cash on hand	At least 30 days
Default	Whether the charter holder has defaulted on a material loan obligation	No default on any material loans
Total liabilities to equity ratio	Total liabilities divided by net assets	At least 4.0
Net income	Total revenues minus total expenses	Greater than \$1
Cash flow	Change in cash balance from one year to another	For three years, cumulative cash flow is positive and in at least two of the years, including the most recent, cash flow is positive
Fixed charge coverage ratio	Net assets available for fixed financial commitments divided by those commitments	At least 1.1

Source: Auditor General staff analysis of the Board's *Financial Performance Framework and Guidance*.

As previously mentioned, the Board's new financial framework procedures call for annually collecting the financial data to calculate the financial framework measures. The Board will then review a charter holder's ratings of meets, does not meet, or falls far below standards in all measures during its 5-year interval reviews, contract renewal, and when applying for certain changes to its contract. If a charter holder does not meet standards in at least two measures or fall far below standards in one financial performance measure, board policy requires the charter holder to submit additional information that will explain the charter holder's situation or efforts to address the deficiencies.

¹ Changes that would trigger a financial review include new school site notifications, requests to amend a school's online instruction program, applications to replicate a charter (see Introduction, page 5, for information on replication), and applications to transfer a charter from another sponsor to the Board.

Despite these review practices, the Board does not plan to take action against or require corrective action of charter holders that show financial distress or poor financial stability based on the financial performance framework alone. Instead, it will consider this information as an additional factor in its decision-making regarding charter school academic performance. According to the Board, it does not have the authority to require action based on financial information. However, Arizona statute requires charter school authorizers to develop a performance framework and includes language regarding academic performance and operational expectations. Although operational expectations are not defined by statute, generally, operational expectations would include any information regarding the management of charter schools, which encompasses compliance with statutes, rules, contractual requirements, and financial management.

Assessing financial performance accountability on a more frequent basis to determine the need for action or enhanced oversight is consistent with practices used in other states. For example, authorizers in at least three states and Washington, DC, require at least some charter holders to submit monthly or quarterly financial reports, such as a balance sheet or income statement, to monitor the charter holders' financial situations. Specifically, two authorizers, the Denver Public Schools and the Indianapolis Office of Education Innovation, require quarterly financial reports from all charter holders regardless of financial performance. An authorizer in Washington, DC, the District of Columbia Public Charter School Board, requires monthly financial statements from charter holders with poor financial performance, untimely submission of annual audits, or other factors. Similarly, Florida statute requires all authorizers to obtain monthly financial statements from charter holders with poor financial performance, such as failure to submit taxes or failure to pay loans. Finally, the National Association best practices recommend that charter school authorizers frequently review and calculate the financial framework measures to identify immediate financial distress and provide increased oversight or require corrective action if necessary.

Therefore, the Board should adopt rules to define operational expectations, including financial framework expectations, and define any actions the Board may take resulting from charter holders not meeting those expectations to support its use of the financial framework. In addition, the Board should develop and implement policies and procedures regarding financial performance measures, including determining when action is needed, formalizing its criteria for taking action, and defining the types of action the Board should take, including requiring more frequent financial reporting from charter holders with continued poor financial performance. Given the Board's limited staff resources, a policy such as quarterly reporting for these charter holders may be more appropriate than requiring monthly reports as recommended by best practices.

Board's oversight of compliance with financial, legal, and contractual requirements can be improved—Since 1999, the Board has assessed charter holders' compliance with financial, legal, and contractual requirements. These requirements differ from financial stability oversight, which focuses on charter holders' ability to continue operating, and instead focus on compliance with requirements such as timely submission of their budgets to ADE. Such reviews are consistent with accepted best practices. For example, the National Association states that although charter schools have the autonomy to manage their finances consistent with state and federal law, authorizers should ensure that the charter schools it sponsors are implementing an educational program that is consistent with the charter, practicing sound governance and adhering to laws and charter requirements, including appropriately using public monies. In addition, the Arizona Constitution establishes that state monies received by public bodies—which

includes charter holders—must be used for a public purpose. As a result, charter holders must spend state aid for educational purposes.

Compliance reviews are part of annual CPA audits required of each charter holder. The Board relies on the CPAs who conduct the annual financial audits of charter holders to examine compliance with requirements regarding classroom spending and taxes and to determine whether there are significant weaknesses in the charter holder's accounting practices. The CPAs complete board-approved legal compliance checklists to assess charter holders' compliance with these and other requirements, such as attendance records that can affect school funding, instructional hours, and fingerprinting requirements.

Based on a review of the annual financial statement and legal compliance checklist results, board staff determine whether or not it will require the charter holder to submit a corrective action plan to address any noncompliance issues in accordance with board policy. Specifically, according to the *State of Arizona Five-Year Strategic Plans of State Agencies and The Master List of State Government Programs Fiscal Years 2012-2015* report, in fiscal year 2012, the Board reviewed 364 annual financial statement audits and accompanying legal compliance checklists for fiscal year 2011 and as shown in Table 4 (see page 6), assigned 59 charter holders to submit corrective action plans to address noncompliance issues identified in annual audits.¹ Examples of these noncompliance issues included the following:

- 22 charter holders were required to submit corrective action plans because their schools did not comply with fingerprinting requirements. All charter school instructional staff must have current fingerprint clearance cards.
- 9 charter holders were assigned corrective action plans because of noncompliance with classroom spending requirements such as the percent of Classroom Site Fund monies that must be spent on classroom teacher salaries.
- 15 charter holders were required to submit corrective action plans because of noncompliance with internal controls over cash disbursements or segregation of duties.

By policy, the Board uses the subsequent year's financial statement audit and legal compliance checklist to determine if the charter holder has addressed the noncompliance, but it may follow up sooner if appropriate. For example, if the noncompliance could affect students' health and safety, the Board does not wait until the following year to determine whether the charter holder has corrected the problem. If the charter holder is required to submit a corrective action plan a third time for the same issue, the Board may take disciplinary action such as withholding state monies or issuing a letter of intent to revoke (see Introduction, page 6, for information on the Board's disciplinary options).

However, auditors' review of the Board's procedures for overseeing compliance with financial, legal, and contractual requirements identified two ways in which this oversight can be improved:

¹ As of March 2013, the latest information available for auditors' analysis was fiscal year 2011 information. However, board staff completed its review of fiscal year 2012 audits in May 2013. According to the Board's audit finding report, the Board identified 67 charter holders whose fiscal year 2012 audits included findings that would require a corrective action plan.

- **Board should require charter holders to address additional internal control concerns**—As part of their audits of a charter holder’s financial statements, CPAs will review the charter holder’s internal control structure and determine if the charter holder has sufficient internal controls to achieve its objectives (see textbox). These internal controls include ensuring that monies are safeguarded and appropriately handled or student attendance is accurately reported. Based on its review of the audited financial statements, the Board may require charter holders to submit corrective action plans addressing internal control issues related to segregation of duties and cash disbursement supporting documentation, such as comparing and retaining invoices. For example, if an audit identifies material weaknesses or significant deficiencies in a charter holder’s schools’ cash disbursement documentation, the Board will require the charter holder to submit a corrective action plan indicating how it intends to correct them. In fiscal years 2007 through 2011, the Board required the submission of 106 corrective action plans from 73 charter holders to address identified internal control weaknesses or deficiencies. In addition, the Board tracks internal control findings that do not result in corrective action and will notify the charter holder if these findings are repeated.

Internal controls—Processes that provide reasonable assurance regarding achieving objectives for effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. Internal controls can include reconciliation of bank statements, policies and procedures for obtaining appropriate approval prior to issuing payment, and periodic reviews of financial records to ensure completeness and accuracy.

Source: Committee of Sponsoring Organizations. (n.d.) Internal control—integrated framework: Executive summary. Retrieved June 11, 2013, from www.coso.org

However, the annual audited financial statements also identify other internal control material weaknesses and significant deficiencies, such as failure to perform bank reconciliations, inadequately safeguarding cash, and poor payroll records, for which the Board does not require corrective action plans. Although the Board focuses on segregation of duties and cash disbursement internal control weaknesses because it views these as high-risk areas for fraud, these other internal control weaknesses can also create fraud risks. According to a 2004 Deloitte and Touche publication, strong internal controls can significantly reduce fraud opportunities within an organization, which can significantly prevent and deter fraud.¹ Additionally, Utah’s charter school board relies on an internal audit department to review annual audits every year and requires a charter holder to address any material weaknesses or repeat significant deficiencies in internal controls. Therefore, the Board should assess the risk that other internal control weaknesses or deficiencies pose to charter holders’ financial operations and based on its available resources, determine for what additional internal control weaknesses or deficiencies, such as failure to perform bank reconciliations and inadequately safeguarding cash, it should require in corrective action plans. The Board should then revise its policies and procedures to require charter holders to submit corrective action plans for the additional internal control findings it identifies.

- **Board should establish an operational framework for reviewing compliance and operational performance**—In its 2011 evaluation of the Board, the National Association recommended that the Board develop an operational framework to not only continue compliance oversight, but also to hold charter schools accountable to additional operational

¹ Deloitte Development, LLC. (2004). *Antifraud programs & controls*. New York, NY: Author.

indicators and standards (see textbox). Although the Board provides oversight for many of the compliance and operational areas suggested by best practices and holds charter holders accountable for compliance with state and federal law, the National Association found that the Board had not established sufficient operational measures and standards to evaluate charter holders' operational performance. For example, the National Association recommended the Board review student discipline policies, such as suspension and expulsion policies. The Board does not review these policies because charter schools' governing boards have authority to develop and implement policies for their charter schools. According to board staff, the Board has used its resources for other oversight efforts, such as developing and implementing the academic performance and financial frameworks, and will work to establish an operational framework when resources become available. Although the Board plans to develop an operational framework modeled after best practices, as of July 2013, it had not established a time line for developing the framework. Therefore, the Board should develop and implement an operational framework consistent with best practices.

An operational framework is an outline of expectations for charter schools' compliance with state and federal law or the charter contract.

Source: National Association for Charter School Authorizers. (2012). *NACSA performance framework and guidance (draft)*. Chicago, IL. Author.

Board should further develop its database to help it ensure charter school accountability—The Board should make greater use of its database to track charter school complaints and disciplinary actions and use this information, along with charter school performance information, to assist in strategically targeting its oversight efforts (see Sunset Factor 6, pages 33 through 34, for information on complaints the Board receives). The Board's database has the ability to track complaints and disciplinary action but as of July 2013, the Board was using a spreadsheet and a word processing document to track this information. If the Board used the database for this purpose, it could analyze complaint and disciplinary action information in conjunction with charter school performance information to identify charter holders who need enhanced or additional oversight. It could also use the results of this analysis to determine whether to intervene with a site visit or technical assistance or to consider disciplinary action. The National Association suggests that authorizers use complaint information to investigate potential grievances and determine if a school complies with state and federal law and the charter contract. The Board should make greater use of its database to monitor all charter holders' complaint and disciplinary actions and performance data and use this information to assist in strategically targeting its oversight efforts.

Board should develop rules to address contract weaknesses

Finally, **the Board needs to develop administrative rules** to ensure it can enforce its new academic and financial performance framework requirements for charter holders who have existing contracts that do not reflect these new requirements. **Although Laws 2012, Ch. 155, authorized the Board to develop performance frameworks** for charter holders and base charter renewal and revocation decisions on the charter holder's school's performance relative to the frameworks, most charter

holders are operating under contracts implemented before the frameworks were developed. Because neither board rules nor most contracts outline the Board's academic performance standards, **the Board may have difficulty taking action** to address academic performance that does not meet its expectations. To ensure that it can exercise appropriate oversight of charter schools based on its performance standards, **the Board should adopt rules** to define board standards for **academic, financial, and operational performance**, sufficient progress toward standards, and consequences for not meeting standards or making progress toward meeting the standards. Such rules would help the Board enforce the performance frameworks' standards and reduce the risk of costly appeals and overturned board decisions.

Recommendations:

- 1.1 To ensure it holds charter schools accountable for academic performance, the Board should continue its efforts to implement its academic intervention policy by conducting annual reviews of charter schools' academic performance, requiring schools to address academic performance that does not meet its standards, and taking disciplinary action as necessary.
- 1.2 To ensure it holds charter holders accountable for financial performance, the Board should:
 - a. **Adopt rules to define operational expectations, including financial framework expectations**, and define any actions the Board may take resulting from charter holders not meeting those expectations to support its use of the financial framework; and
 - b. Develop and implement policies and procedures regarding financial performance measures, including determining when action is needed, formalizing its criteria for taking action, and defining the types of action the Board should take, including requiring more frequent financial reporting from charter holders with continued poor financial performance.
- 1.3 The Board should assess the risk that other internal control weaknesses or deficiencies pose to charter holders' financial operations and, based on its available resources, determine which additional internal control weaknesses or deficiencies should require corrective action plans.
- 1.4 The Board should revise its policies and procedures to require charter holders to submit corrective action plans for the additional internal control findings it identifies.
- 1.5 The Board should develop and implement an operational framework consistent with best practices.
- 1.6 To assist in ensuring charter school accountability, the Board should make greater use of its database to monitor all charter holders' complaint and disciplinary actions and performance data and use this information to assist in strategically targeting its oversight efforts.
- 1.7 To ensure that it can exercise appropriate oversight of charter schools based on its performance standards, **the Board should adopt rules to define board standards for academic, financial,**

and operational performance; sufficient progress toward these standards; and consequences for not meeting standards or making progress toward the standards.

FINDING 2

The Arizona State Board for Charter Schools (Board) should improve how it provides information about charter schools to the public as well as the types of information that it provides. Although the information the Board already provides about charter schools is important, the Board does not make all of it available in one location—some information is available only on the Board’s Web site, while other information is available only in hard copy at the board office. In addition to making the information more readily available in one location, the Board can do more to improve the information’s usefulness to the public by compiling and providing comparative information about different charter schools on its Web site. Finally, the Board should develop and post guidance on its Web site to help parents understand the new academic performance standards the Board uses to evaluate charter schools’ performance.

Board should improve public information about charter schools

Board provides information to public, but information is in multiple locations or difficult to find

Although the Board provides important information to the public, this information is not provided in one location, which can make it difficult for the public to find and use the information to make informed choices. Specifically, the Board provides a variety of important information to the public, such as a charter school’s mission, academic performance, and compliance with financial requirements. However, the Board does not make some charter school information available on its Web site, thus making it more difficult for the public to obtain and review all charter school information. Therefore, the Board should follow through with its plans to place additional charter school information on its Web site.

Board provides important information about charter schools—

The Board makes information available to the public regarding the charter schools it sponsors and the charter holders who operate the charter schools, which is important to parents’ ability to make informed choices about their children’s education. Arizona statutes established charter schools to provide parents with academic choices for their children. According to the U.S. Department of Education, some of the most important decisions parents will make are about their children’s education, and parents want to choose a school that is a good fit for their child.¹ To make good decisions about the best school for their children, parents need information about charter schools’ missions and performance.

As a result of the Board’s responsibilities to sponsor and oversee charter schools, it has a wealth of information about these charter schools. For example, it has information about grades served, mission, academic performance, compliance with financial requirements, and information about complaints and disciplinary action. In addition, the Board’s Web site provides some general information and guidance for parents, such as a brochure that explains what charter schools are and a list of questions parents should consider when making decisions about a charter school.

Public information is in multiple locations, and some information is difficult to find—Although the Board provides several types of information to the public regarding the charter schools it sponsors, the infor-

¹ U.S. Department of Education, Office of Innovation and Improvement (2007). *Choosing a school for your child*. Washington, DC: Author.

mation is scattered in multiple places and difficult to find. Specifically, as shown in Table 6, some information is available only in hard copy at the Board’s office, while other information is on the Board’s Web site. For example:

**Table 6: Location of charter holder/school information available to the public
As of May 2013**

Type of charter information	File located at the Board’s office	File located on the Board’s Web site/database
Charter holder application	Yes	Limited ¹
Charter holder contract	Yes	No
Notifications, contract amendments, and general information	Limited ²	Limited ²
Annual academic performance information	No	Yes
Financial performance information	Before 2009	2009 and later
Complaints	Yes	Limited ³
Disciplinary actions	Limited ⁴	Limited ⁴

1 Only charter holder applications submitted beginning with the 2011-2012 application cycle and approved by the Board are available on its Web site.

2 Some contract amendments, other notifications, and general information such as the address, mission, and grades served are maintained in hard copy files at the Board’s office, but the hard copy files are not always updated when new information is submitted online. The Board began accepting online submissions in October 2011.

3 The Board’s Web site provides a count of complaints submitted through the Web site. However, the count does not include complaints submitted through other means, and the Web site does not provide other information about the complaints such as the nature and disposition of the complaint.

4 The Board maintains legal documentation of some disciplinary actions, such as a notice of intent to revoke, in hard copy files at its office. However, other disciplinary action information that does not require legal documentation, such as withholding a charter holder’s state aid, can be found only in the Board’s meeting minutes and is not available in either hard copy or online.

Source: Auditor General staff review of board information from its hard copy files, Web site, and database.

- **Board office file**—Some information can be found only in hard copy files at the Board’s office. This includes charter holders’ applications submitted prior to the 2011-2012 application cycle, which contain information on the schools’ education plans, curriculum, and business plans; and contracts, which specify the legal, regulatory, and academic and financial requirements that charter holders must follow. In addition, information about charter schools’ complaints and some disciplinary action is available only in the hard copy file at the Board’s office.
- **Web site information**—The Board’s Web site provides the public with information that cannot be found at the Board’s office. This includes information about charter schools’ academic and financial performance. Specifically, as of April 2013, the Board had published charter school academic performance information based on the new academic performance framework it adopted in 2012. In addition, the Board has begun publishing information about charter holders’ financial stability based on a new financial framework adopted in 2012. For

example, it includes information on the Board's evaluation of a charter school's financial stability and its ability to continue operating (see Finding 1, pages 9 through 22, for more information on the academic performance and financial frameworks).

Additionally, some information about charter schools may be difficult to find on the Board's Web site. For example, charter school disciplinary actions are recorded in board meeting minutes, which are filed by date, not by charter school or holder; therefore, it could be more difficult for members of the public to locate this important information. Board staff also reported that they often receive phone calls from members of the public asking how to find charter school academic performance information on the Web site, suggesting that this information may also be difficult to find.

As a result, members of the public may not find the information they need to make informed choices about charter schools, and parents could choose charters schools that are not performing well. According to a 2013 Center for Student Achievement study, 40 percent of Arizona charter school students attend charter schools that are assigned a C, D, or F grade by ADE's A-F Letter Grade Accountability System, raising the question of whether parents may be underinformed regarding charter school performance.¹

Board should continue placing additional charter school information on its Web site and take other steps to enhance public access to this information—The Board has taken steps to enhance the charter school information it provides to the public through its Web site, but can do more to assist the public in making informed choices about the schools their children attend. The Board has a goal of improving public awareness of quality choices and enhancing the accessibility of information on charter schools. According to board staff, the Board has a goal to publish financial stability information for all charter holders by December 2013, and has also set a goal to transfer historical charter school information that is located at the Board's office in hard copies onto the Board's Web site by December 31, 2014, such as charter holders' applications and contracts. To ensure the public has access to charter school information, the Board should follow through with its plans to place charter holders' framework dashboards, contracts, and legal documents on its Web site.

Additionally, the Board should take other steps to provide the public with access to charter school information. Specifically, the Board should provide easier access to information about disciplinary actions by making the information available by charter holder on its Web site. The Board should also provide more complete information about complaints on its Web site. As previously mentioned, this information is not currently available on its Web site. Finally, the Board should explore additional opportunities to provide guidance to the public, such as a guidance document explaining the type of charter school and charter holder information available and how to access the information. Doing so would help the public locate information on the Web site without having to call the Board's office for instructions about how and where to find it.

¹ Center for Student Achievement (2013). *Oh, the places they'll go: Arizona public school choice and its impact on students*. Phoenix, AZ: Author.

Board can do more to provide comparative charter school information to public

The Board's Web site has two shortcomings that prevent the public from easily comparing information about charter schools. First, although the Web site allows the public to perform a search of charter schools by grades served, location, and school characteristics (such as schools that focus on math and science, fine arts, or college preparatory), this search capability can return incomplete results because the Board does not have this information for all charter schools. According to board staff, the Board has not required charter schools to report the school characteristics that reflect their mission. Additionally, board staff would need to verify that this information is consistent with the charter contract and follow up with identified inconsistencies before it provides this information on its Web site. Second, charter school information is maintained in the database by charter school and some information, such as academic performance results, must be individually downloaded. The Board does not have a report or other mechanism that would allow a side-by-side comparison of important charter school information for multiple charter schools.

Auditors identified examples of other charter school authorizers that provide easily comparable information. For example, the District of Columbia Public Charter School Board (DC Board) publishes an annual comparison report about all the schools it oversees, such as the percent of points each school earned according to the DC Board's academic framework. The DC Board provides this information to help the public make informed decisions. Additionally, the DC Board publishes an annual authorizer report, which includes all oversight activities conducted and resulting disciplinary actions taken during the year. Similarly, the Denver Public Schools publishes an annual comparative report of all the charter schools it authorizes as well as the public schools in the district. This report includes each school's results on individual measures, such as student growth and parent satisfaction, and the percent of points each school earned according to the district's performance framework.

The Board should consult with its database contractor to determine the feasibility of developing and providing a low-cost report to the public on its Web site that compares charter school performance, based on the existing charter school academic and financial information in its database. Such a report could allow parents to compare charter school performance and could help the Board with its oversight activities by giving it the ability to review charter school academic and financial comparative information on an annual basis, as discussed in Finding 1 (see pages 9 through 22). Additionally, the Board should ensure the Web site accurately captures the charter schools' characteristics, such as schools that focus on math and science, fine arts, or college preparatory by revising its processes for collecting and verifying charter school characteristic information. For example, the Board could require new charter schools to identify their school characteristics in the initial application and could update these characteristics for existing charter schools during amendment requests, 5-year interval reviews, and at renewal.

Board should provide the public with guidance to understand academic accountability

The Board should also develop guidance for the public to help them interpret all of the academic performance information on the Board's Web site. The Board provides information about charter schools' academic performance in two ways. Specifically, the Board's Web site provides a link to the Arizona Department of Education (ADE) Web site's charter school report cards, which are based on ADE's A-F Letter Grade Accountability System. In addition, the Board's Web site includes information about charter schools' performance according to the Board's academic performance framework, which it adopted in 2012. However, these systems use different information and different benchmarks to assess individual charter school academic performance, which can lead to different results that could be confusing to the public. For example, some schools can meet state standards in ADE's A-F Letter Grade Accountability System, but not meet the academic performance standards the Board has established according to its academic performance framework. In fiscal year 2012, 125 charter schools received a B grade and 127 charter schools received a C grade, which are passing grades according to ADE's A-F Letter Grade Accountability System. However, of these 252 charter schools, 99 did not meet the Board's academic performance standards. This can occur because the Board's academic framework includes comparisons of proficiency scores for special education, English Language Learners, and free/reduced lunch students. There are also differences in how the Board and ADE weigh the measures that are used in both models.

It can be important for parents to review both state accountability profiles and board standards for charter schools. For example, parents can compare district and charter school performance using only ADE's A-F Letter Grade Accountability System. However, the Board's assessment of charter schools' academic performance using its academic performance framework can also provide important information to parents. Therefore, to help inform the public about charter school academic accountability, the Board should develop and post guidance on its Web site about both ADE and board academic standards and the Board's role in overseeing charter schools' academic accountability.

Recommendations:

- 2.1 To better inform the public about charter schools, the Board should:
 - a. Follow through with its plans to place additional charter school information on its Web site;
 - b. Make information about disciplinary actions available by school or charter holder on its Web site;
 - c. Provide more complete information about complaints on its Web site;
 - d. Explore opportunities to provide additional guidance to the public on how to locate charter school and charter holder information on its Web site; and

- e. The Board should consult with its database contractor to determine the feasibility of developing and providing a low-cost report on its Web site that the public can review with important charter school comparative information.
- 2.2 The Board should revise its processes for collecting and verifying charter school characteristic information to ensure that its Web site accurately captures this information for the charter schools it sponsors.
- 2.3 The Board should develop and post guidance on its Web site to help inform the public about both ADE and board academic standards and the Board's role in overseeing charter schools' academic accountability.

SUNSET FACTORS

Sunset factor analysis

In accordance with Arizona Revised Statutes (A.R.S.) §41-2954, the Legislature should consider the following 12 factors in determining whether the Arizona State Board for Charter Schools (Board) should be continued or terminated. This analysis includes three recommendations not covered elsewhere in this report. Specifically:

- To comply with statutory conflict-of-interest requirements, board members and board staff should have conflict-of-interest forms available for public review (see Sunset Factor 2, pages 31 through 32);
- Review and revise its policies and procedures for collecting new application fees to ensure it follows appropriate internal controls regarding cash transactions (see Sunset Factor 2, page 32); and
- The Board should develop and implement policies and procedures for when and how to conduct further investigation into a complaint (see Sunset Factor 6, pages 33 through 34).

1. The objective and purpose in establishing the Board and the extent to which the objective and purpose are met by private enterprises in other states.

The Legislature established the Board in 1994 to sponsor and regulate charter schools. Consistent with its statutory purpose, the Board's mission is to improve public education in Arizona by sponsoring charter schools that provide quality educational choices. The Board accomplishes this mission by:

- Reviewing and approving charter school initial, renewal, and replication applications;
- Providing oversight to ensure accountability for charter school academic, financial, and operational performance;
- Disciplining charter holders that violate statutory or contractual requirements; and
- Providing information to the public.

The Board is one of five government entities in the State allowed to authorize charter schools. In addition to the Board, statute allows the Arizona State Board of Education, school districts, some community colleges, and the State's universities to authorize charter schools. However, as of April 2013, the Board provided oversight for 511 of the charter schools in the State, including all the schools authorized by the Arizona State Board of Education. In 2004, the Arizona State Board of Education entered into an agreement with the Board to oversee its charter schools. In 2010, the Arizona State Board of Education decided not to renew charter school contracts, resulting in many of its schools transferring their contracts to the Board. According to the Arizona Department of Education's (ADE) Web site, Arizona school districts and Arizona State University authorized 76 charter schools as of September 2013. No community colleges and neither of the State's other universities authorize charter schools.

Most states have charter school laws and charter school authorizers. Specifically, in the 2011-2012 school year, 41 states and Washington, DC, had charter school laws. In November 2012, the State of Washington passed a charter school law allowing the establishment of charter schools. The states with charter school laws have several types of authorizing entities, including school districts—the most common type of

authorizer—and state education agencies, independent charter school boards, municipal government offices, higher education institutions, and nonprofit organizations. According to the National Association of Charter School Authorizers (National Association) staff, as of September 2013, only two states, Minnesota and Ohio, have nonprofit organizations as authorizers, and 12 states, including Arizona, have an independent charter school board.

2. The effectiveness with which the Board has met its objective and purpose and the efficiency with which it has operated.

The Board has generally met its statutory objectives and purpose, but could improve in some areas. Specifically, the Board has met its objectives and improved its processes in the following areas:

- **Initial Applications**—The Board has taken steps to make its application process more rigorous, and according to the National Association, the Board’s application process approaches a well-developed application review process. For example, in 2011, the Board changed its initial application process to include a performance management plan that explains the charter holder’s goals and how they will be met. In 2012, the Board further strengthened its process by adding an applicant interview to enhance the Board’s ability to evaluate the applicant’s capacity to operate a charter school. In addition to these changes, the Board continues to use an expert panel to evaluate applications (see Introduction, pages 4 through 5).

The Board also ensures only qualified applicants are approved. For example, in its 2012-2013 new application cycle, the Board reviewed 49 applications for administrative completeness. Of these, the Board deemed 21 applications administratively complete. However, the Board’s volunteer expert panel found all 21 applications substantively incomplete because the applicants did not provide all required information.¹ Fourteen of the 21 applicants submitted revised applications to the Board, and the Board determined 9 of these as qualified to operate a charter school. The Board’s rigorous application process has helped to decrease the risk of opening charter schools that are unable to remain open. Specifically, in fiscal years 2001 through 2011, 15 charter schools closed within the first 2 years of operation, and all but one of these closed prior to February 2007.

- **Replication Applications**—The Board has also taken steps to increase the number of quality schools in Arizona by authorizing well-performing charter holders to replicate their charter contracts (see Introduction, page 5, for additional information). According to the National Alliance for Public Charter Schools (National Alliance), one way to increase the number of quality schools is to replicate charters with effective governance models.² The Board’s strategic plan includes a goal to reduce the application requirements for charters that perform at or above the Board’s academic standards to encourage replication. From January 2009 through November 2012, 11 charter holders submitted replication

¹ According to board staff, the Board has taken steps to improve the quality of applications by providing online support for applicants. Additionally, the Arizona Charter School Association provides training and support to new charter school applicants, which according to board staff has improved the quality of applications.

² National Alliance for Public Charter Schools. (2012). *Measuring up to the model: A ranking of charter school laws* (3rd ed.). Washington, DC: Author.

applications, and the Board approved 30 replicated charter contracts. Eligible charter holders may submit multiple replication applications during any given year. Specifically, one charter holder submitted 9 replication applications during this time period. Additionally, in the same time period, the originally established charter holders met the State's performance academic standards in every fiscal year prior to replication. To be eligible for replication, a charter holder must receive an overall rating of meets or exceeds standards for each of the prior three school years based on the Board's academic performance framework.

However, the audit found that the Board can better meet its statutory objectives in the following areas:

- **Charter holder and school oversight**—The Board can improve charter holder and school accountability and its oversight of charter schools by continuing and strengthening its efforts to monitor academic performance, financial sustainability, and compliance with legal, financial, and contractual requirements. Board oversight is important to ensure that charter schools are held accountable for meeting board-established performance standards and that charter holders—entities that operate charter schools—are financially stable and comply with state and federal laws. Historically, the Board's oversight has focused on compliance, but in 2010, it implemented additional oversight practices for charter schools' academic performance. Additionally, in the 2012-2013 school year, it implemented additional academic and financial performance requirements and measures as recommended by the National Association.¹ The Board should strengthen its oversight by continuing its efforts to implement its academic intervention policy, developing and implementing policies and procedures for determining when action is needed to hold charter holders accountable for financial performance, and by following through with its plans to develop and implement an operational framework (see Finding 1, pages 9 through 22).
- **Public information**—The Board can improve how it provides information about charter schools to the public by making it easier for the public to access the information and providing additional important information. Some information is available only at the Board's office, such as the charter schools' education plans, curriculums, and business plans, while other information, such as academic and financial performance information, is available only on the Board's Web site. Although the Board makes information available to the public, it could better inform the public by following through with its plans to make additional charter school information available on its Web site. In addition, it should provide comparison information about charter schools on its Web site and include charter schools' disciplinary action and financial stability information on its Web site. Further, the Board should develop and post guidance on its Web site to help the public understand the academic performance standards used by the Board and ADE (see Finding 2, pages 23 through 28).
- **Managing conflicts of interest**—The Board has not kept up to date in its compliance with statutory requirements for reporting conflicts of interest. Statutes require that public officers

¹ The National Association of Charter School Authorizers is a national organization committed to advancing excellence and accountability in the charter school sector.

and employees disclose any interests they have in any charter or other contract with the Board and refrain from making decisions about those contracts.¹ The Board's responsibilities create the potential for conflicts of interest because its members include representatives of the charter school community and the Board is statutorily responsible for approving, renewing, and revoking charter contracts, as well as overseeing the charter schools it sponsors. Board staff can also have conflicts of interest because they provide the day-to-day oversight of board-sponsored charter schools. Although the audit did not find instances where board members with an interest in a charter school participated in decision-making about the school, the Board did not maintain up-to-date conflict-of-interest forms for members and staff. To comply with statutory conflict-of-interest requirements, board members and board staff should have conflict-of-interest forms available for public review.

- **Review its process for collecting fees**—Laws 2013, Ch. 68, authorized the Board to collect a new application fee without adopting rules. As a result, the Board established a \$6,500 initial application fee and began collecting this fee during its new charter application cycle for the 2014-2015 school year. Specifically, according to board staff, the Board received 21 new charter applications and collected \$136,500 in fees between May 2013 and July 2013. As of August 2013, the Board's process for collecting these fees includes obtaining the fee when the applicant submits an application and holding the check until the administrative review of the application is complete. Board staff then deposit the check for any applications that move on to the substantive review process and return checks for any applications that are determined to be incomplete. However, the Board has not established adequate controls for handling cash receipts consistent with the *State of Arizona Accounting Manual*. These controls include, but are not limited to, depositing cash on a timely basis, requiring cash to be properly safeguarded, and ensuring appropriate segregation of duties related to the handling of cash. As a result, the Board should review and revise its policies and procedures for collecting fees to ensure it follows appropriate internal controls regarding cash receipts.

3. The extent to which the Board serves the entire State rather than specific interests.

The Board sponsors charter schools across the entire State (see Figure 1, page 3, for a map of charter schools state-wide). Although most board-sponsored charter schools are located in Maricopa and Pima Counties, the Board sponsors 140 schools in other counties, including 30 schools in Yavapai County and 10 in Navajo County. The only counties without board-sponsored charter schools are La Paz and Greenlee Counties. According to the *Fiscal Years 2011 through 2013 Master List of State Government Programs*, the charter schools the Board sponsored accounted for 25 percent of Arizona public schools. Additionally, the Board serves the public state-wide by making information on the charter schools it sponsors available on its Web site, including resources for parents, applicants, and schools in addition to information about specific charter schools. However, the Board should follow through with its plans to provide charter holders' framework dashboards, contracts, and legal documents on its Web site, and it

¹ According to statute, any officer or employee of a public agency who has, or whose relative has, a substantial interest in any contract, sale, purchase, or service to such public agency shall make known that interest in the official records of such public agency and shall refrain from voting upon or otherwise participating in any manner as an officer or employee in such contract, sale, or purchase.

should also assess the feasibility of providing comparative information on its Web site (see Finding 2, pages 23 through 28, for additional information).

4. The extent to which rules adopted by the Board are consistent with the legislative mandate.

General Counsel for the Auditor General has analyzed the Board's rulemaking statutes and believes that the Board has established rules required by statute, with one exception. Specifically, the Board should adopt rules to define board standards for academic, financial, and operational performance, sufficient progress toward standards, and consequences for not meeting or making progress toward standards (see Finding 1, pages 9 through 22).

5. The extent to which the Board has encouraged input from the public before adopting its rules and the extent to which it has informed the public as to its actions and their expected impact on the public.

Although the Board has not amended or proposed new rules since 2006, the Board has encouraged input from stakeholders before adopting or amending rules and has informed the public about its actions and their expected impact. For example, in 2005, the Board submitted its proposed rules for publication in the Arizona Administrative Register and encouraged public input before implementing rule amendments establishing disciplinary actions available to the Board, including the use of corrective action plans, and defining board processes, such as approving charter holders' audit contracts with Certified Public Accounting firms. The Board posted a notice of proposed rulemaking docket opening on August 12, 2005, and notice of proposed rulemaking on November 4, 2005. The Board did not receive any public comments, and the proposed changes became effective on February 7, 2006.

Additionally, the Board has complied with the State's open meeting law. For example, the Board posted meeting notices and agendas for its September and October 2012 board meetings on the Board's Web site and at a physical location as specified on its Web site at least 24 hours in advance. The Board also complied with statutory requirements regarding its meeting minutes, including making recordings of its meetings available on its Web site within 3 business days. In addition, board staff post summaries of its meetings on its Web site within 3 business days. Finally, the Board provides a call to the public during its board meetings, inviting members of the public and stakeholders to address board members regarding items on the agenda or other concerns.

6. The extent to which the Board has been able to investigate and resolve complaints that are within its jurisdiction.

Statute authorizes the Board to exercise general supervision over the charter schools it sponsors. As a result, board staff receive complaints regarding charter schools and conduct limited investigations of complaints that are within the Board's jurisdiction. The Board has jurisdiction to investigate complaints that allege possible violations of a charter contract or state or federal laws. For example, complaints about open meeting law compliance, charter schools charging fees, such as requiring a deposit for locker use, and kindergarten programs that do

not provide core curriculum instruction during the hours when students can attend without paying a fee would fall under the Board's jurisdiction. According to information provided by the Board, it received 140 complaints against charter schools in fiscal year 2012, including complaints that were outside the Board's jurisdiction. The most common complaints pertained to school policies, such as dress code or tardiness policies, bullying or discipline policies, and enrollment policies. When a complaint is outside the Board's jurisdiction or better addressed by a different state agency, such as a school's compliance with special education requirements, the Board refers the complaint to the appropriate agency—in this case, the Arizona Department of Education's exceptional student services unit for investigation and resolution.

Although board staff conduct limited complaint investigations, the Board does not have policies and procedures for when to further investigate complaints that are within its jurisdiction and the steps staff should perform to properly investigate a complaint. Specifically, board staff forward such complaints to the school and request a response, but do not take additional steps to verify information the school provides. For example, one complainant asserted a school was using preregistration requirements, such as requiring an academic transcript and disciplinary history, to screen students, which would be a violation of Arizona law. Charter schools must enroll all eligible students and are statutorily required to use a lottery system to select students if they cannot accommodate all applicants. Board staff requested and received a response from the school, but did not investigate further, such as placing an anonymous telephone call to the charter school to request enrollment information to verify compliance with state law. Additionally, the Board received three complaints spanning 3 years, 2007 through 2009, asserting that a school's building conditions were a safety and health hazard. Although board staff requested a response from the charter holder for the first two complaints, they did not follow up to ensure that the school resolved the issue. Board staff referred the matter to the Department of Health Services when it received the third complaint in 2009. According to the *Arizona Agency Handbook*, an initial response to a complaint may resolve the matter without further investigation, but if the response does not fully resolve the matter, the agency should initiate an investigation of the complaint. Therefore, the Board should develop and implement policies and procedures for when and how to conduct further investigation into a complaint, including steps such as contacting the complainant, school, or any other witnesses, obtaining relevant documentation, and conducting site visits.

In addition, as discussed in Finding 1 (see pages 9 through 22), the Board should make greater use of its database to document the complaints it both receives and investigates to assist in its charter school oversight efforts.

7. The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation.

A.R.S. §41-192 authorizes the Arizona Attorney General's Office to prosecute actions and represent the Board. The Board refers complaints alleging school involvement in fraudulent behavior directly to the Arizona Attorney General's Office for investigation and possible prosecution.

8. The extent to which the Board has addressed deficiencies in its enabling statutes, which prevent it from fulfilling its statutory mandate.

The Board has sought statutory changes to address deficiencies in its statutes. The Legislature has amended several board statutes since calendar year 2008, some of which have enhanced the Board's ability to fulfill its statutory mandate. The Board has supported many of these changes, including:

- Laws 2008, Ch. 56, which amended A.R.S. §15-183, requires a charter school authorizer to notify the charter school that it may apply for renewal 18 months before the charter contract expiration date. In addition, the law requires a charter school applying for renewal to file a renewal application at least 15 months before the expiration of the charter contract. Prior to this amendment, statute required the charter school to apply for renewal at the conclusion of the first 14 years of operation.
- Laws 2010, Ch. 160, which amended A.R.S. §15-183, allows the Board to charge a processing fee to any charter school that amends its contract to allow the school to participate in the Arizona Online Instruction Program. As authorized by A.R.S. §15-808, the Arizona State Board of Education can select traditional public schools, and the Board can sponsor charter schools only to participate in the Arizona Online Instruction Program by providing online courses or online schools, following standards jointly developed by the Board and the Arizona State Board of Education.
- Laws 2012, Ch. 155, which amended A.R.S. §15-183, requires charter school authorizers to establish a performance framework that includes academic performance expectations, measurement of sufficient progress toward those expectations, operational expectations, and intervention and improvement policies to use when considering renewals and when conducting 5-year interval reviews. The law also allows the Board to collect fees for new charter school applications. Prior to the amendment, the Board did not have the authority to collect fees for initial applications.
- Laws 2013, Ch. 68, which amended A.R.S. §15-183, allows the Board to use the performance framework to revoke a charter at any time if the authorizer determines that the charter holder fails to meet or make sufficient progress toward performance expectations outlined in the performance framework. Additionally, the law reduces the time frame, from 90 to 60 days, for an authorizer to give the charter school operator written notice of its intent to revoke the charter. Finally, the law includes a provision exempting the Board from rulemaking to establish fees for new applications. The Board began to collect these fees in fiscal year 2013 for new charter school applications for the 2014-2015 school year.

9. The extent to which changes are necessary in the laws of the Board to adequately comply with the factors in the sunset law.

This audit did not identify any needed changes to the Board's statutes.

10. The extent to which the termination of the Board would significantly impact the public's health, safety, or welfare.

Terminating the Board could affect the public welfare if its responsibilities were not transferred to another agency because the Board sponsored charter schools attended by approximately 134,000 students in the 2011-2012 school year. The Board oversees most charter schools in the State. Without the Board to monitor and enforce charter schools' legal compliance and academic performance, students may not receive the education to which they are entitled. If the Board were terminated, other authorizers in the State, such as the Arizona State Board of Education, school districts, or state universities and community colleges, would need to assume responsibility for regulating charter schools in Arizona. However, according to an Arizona State Board of Education official, the Arizona State Board of Education no longer accepts new or renewal applications to sponsor charter schools (see Introduction, page 2, for more information). Further, the State could identify other entities not currently approved by statute as authorizers, and those entities would need to agree to sponsor and assume the regulation of charter schools if the Board were terminated.

11. The extent to which the level of regulation exercised by the Board compares to other states and is appropriate and whether less or more stringent levels of regulation would be appropriate.

This audit found that the level of regulation of charter schools in Arizona is generally similar to that of other states and appears appropriate. For example, Arizona does not limit the number or type of charter schools an authorizer sponsors, similar to other states. Additionally, Arizona law requires authorizers to make application and revocation decisions at a public hearing, similar to over half of the other states that have charter school laws and Washington, DC.

In addition, Arizona law requires authorizers to use performance frameworks as a basis for decisions during charter holder interval reviews, renewals, and revocations. Similar to Arizona, most other states require their authorizers to base renewal decisions on charter schools' performance. Although other states have found that some charter schools do not meet their states' academic or financial performance standards or compliance requirements, some state charter school authorizers have not held charter schools accountable for the underperformance or noncompliance. For example, a study and recent audits of the charter school systems in California, Hawaii, and Texas found that charter school authorizers rarely held charter schools accountable for underperformance or noncompliance, which limited the authorizers' ability to meet their obligation of providing quality educational choices.^{1,2,3}

The Board's practices vary somewhat from procedures used in other states, but not to the degree that Arizona's regulation is considerably more or less stringent. For example, the National Association recommends charter contract lengths of 5 years or, if contracts are longer,

¹ California Charter Schools Association. (2012). *Portrait of the movement: How charters are transforming California education*. Los Angeles, CA: Author.

² Office of the Auditor, State of Hawai'i. (2011). *Performance audit of the Hawai'i Public Charter School System: A report to the governor and legislature of the State of Hawai'i* (Report No. 11-03). Honolulu, HI: Author.

³ Sunset Advisory Commission, State of Texas. (2012). *Texas Education Agency staff report*. Austin, TX: Author.

to conduct periodic high-stakes reviews.¹ As of January 2012, Arizona was one of nine states that did not meet this standard. According to A.R.S. §15-183, Arizona's initial charter contract term is for 15 years. By comparison, Michigan law requires an initial charter contract term of 10 years, while Iowa law allows for contract terms of 4 years. Additionally, Arizona has less stringent regulation for charter school teachers. Two states, including Arizona and Washington, DC, exempt all charter school teachers from state certification requirements, whereas 38 states require all or some charter school teachers to be certified.

12. The extent to which the Board has used private contractors in the performance of its duties as compared to other states and how more effective use of private contractors could be accomplished.

The Board uses a private contractor for hosting its online database. Additionally, board staff reported that beginning with its 2014-2015 new charter school application cycle implemented in fiscal year 2014, it plans to contract with the National Association to substantively review new charter school applications, using both local and national reviewers. Board staff plan to continue to review new charter applications for completeness. Board staff also reported that contracting for application review will allow them to focus on other oversight responsibilities. The Board has previously used contractors for site visits and reviewing financial audits, but reported that a cost-benefit analysis indicated it would be more efficient to use board staff for these functions.

Two other charter school authorizers identified by the National Association as best practice authorizers and contacted by auditors indicated that they use private contracts to review new applications, conduct site visits, review financial reports, and conduct parent surveys. Specifically, the Denver Public Schools contracts with an external vendor to assist with renewal site visits for the lowest-performing schools. According to the Denver Public Schools, this provides two benefits. First, the consultants allow for an unbiased third party review of data, which makes appealing nonrenewal decisions difficult. Second, the third-party consultant can provide feedback to the school that the authorizer would not typically be able to provide to the school because of the protection of charter autonomy. Additionally, the Indianapolis Office of Education Innovation uses contractors to review annual financial audits, coordinate parent surveys, and conduct site visits for schools in their second, fourth, and sixth years of operation.

This audit did not identify any other areas where the Board should consider using private contractors.

¹ National Association of Charter School Authorizers. (2011). *The National Association of Charter School Authorizers' index of essential practices*. Chicago, IL: Author.

APPENDIX A

Methodology

This appendix provides information on the methods auditors used to meet the audit objectives.

This performance audit was conducted 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.

The Auditor General and staff express appreciation to the Arizona State Board for Charter Schools (Board), its Executive Director, and staff members for their cooperation and assistance throughout the audit.

Auditors used various methods to study the issues addressed in this report, which included attending board meetings; interviewing board members and staff; and reviewing federal laws and regulations, state statutes, administrative rules, and board documents, including policies and procedures. In addition, auditors reviewed the Board's 2011 strategic plan, and a 2011 evaluation conducted by the National Association of Charter School Authorizers (National Association).¹ Auditors also surveyed seven other states that either the National Association or the National Alliance for Public Charter Schools (National Alliance) identified as having strong oversight practices for authorizing charter schools and whose charter authorizers had similar responsibilities.² Further, auditors reviewed literature regarding charter school authorizing and performance and interviewed experts from the National Association, the National Alliance, and ADE staff who were involved in state-wide school improvement, research and evaluation, and finance.³

Auditors also used the following specific methods to address the audit's objectives:

- To determine the effectiveness of the Board's oversight of charter holder and school academic performance, auditors reviewed both state and board academic standards, including the Board's new academic measures and framework. Auditors also analyzed charter and public school district academic performance for the 2011-2012 school year as determined by the Arizona Department of Education's (ADE) A-F Letter Grade Accountability System. Further, auditors reviewed charter school academic performance for the 2011-2012 school year as determined by the Board's academic framework standards and analyzed charter schools' academic performance according to board standards in school years 2007 through 2011 for all charter schools that received a performance management plan assignment during a 5th-year interval review in fiscal years 2010 through 2012.
- To determine the Board's compliance with financial, legal, and contractual requirements, auditors reviewed the Board's financial measures and framework. Additionally, auditors reviewed and analyzed data from charter

¹ The Board received its 2011 evaluation in a letter report, which is held by the Board.

² Auditors interviewed staff and conducted reviews of authorizer Web sites and state statutes and administrative rules to determine authorizers' specific oversight practices for authorizers identified by either the National Association or National Alliance as best practice authorizers or oversight entities and for other states' charter authorizers with similar responsibilities. These authorizers and oversight entities included the Denver Public Schools, District of Columbia Public Charter School Board, Florida Department of Education, Indianapolis Office of Education Innovation, Texas Education Agency, and Utah State Charter School Board.

³ Auditors reviewed literature on academic performance of charter schools published by the Center for Research on Education Outcomes, the Arizona Charter School Association, the California Charter School Association, the National Association of Charter School Authorizers, and the National Alliance for Public Charter Schools.

school annual audits, legal compliance questionnaire, and corrective action plan assignments for fiscal years 2007 through 2011; ADE records for board requests for a withholding of state funds between fiscal years 2009 through 2012; and board action for letters of intent to revoke and consent/settlement agreements between February 2004 and August 2012.

- To assess and determine the effectiveness of information available to the public, auditors reviewed charter holder and school information in hard copy files located at the board office and on the Board's Web site, including the Board's online database. Auditors also reviewed public information provided by other state authorizers through an annual comparative report.¹ Finally, auditors reviewed literature on parental school choice from the U.S. Department of Education and the Center for Student Achievement.
- Auditors also used some additional methods to obtain information used throughout the report, including the Introduction and Sunset Factors. Specifically, auditors reviewed the National Alliance's 50-state database of charter school law and general data. Auditors also attended a board subcommittee meeting in September 2012 and listened to the subcommittee's minutes for the October 2012 meeting; attended the February 2013 board meeting; and reviewed the October 2012 and February 2013 board meeting materials; board meeting notices, agendas, and meeting minutes for the September 2012 and October 2012 board meetings; the *Arizona Agency Handbook*; and the Board's private contracting practices. In addition, auditors analyzed all new charter school applications submitted in fiscal years 2010 through 2012; a sample of 38 contract amendments submitted between October 1, 2011 and September 30, 2012; seven charter school renewal applications submitted between fiscal years 2010 and 2012; and five Notice of Intent to Revoke letters issued between calendar years 2010 and 2012. Auditors also compiled and analyzed unaudited information from the Arizona Financial Information System (AFIS) *Accounting Event Transaction File* and the AFIS *Management Information System Status of General Ledger-Trial Balance* screen for fiscal years 2011 through 2013. Further, auditors reviewed fiscal year 2012 complaint information provided by the Board and interviewed an expert regarding the authorizing and regulation of charter schools and other states regarding private contracting practices.
- Auditors' work on internal controls included reviewing the Board's policies and procedures for ensuring charter holder and school compliance with state statutes, administrative rules, and financial and contractual requirements. For example, auditors reviewed board policies and procedures for reviewing and analyzing charter holder and school academic and financial performance, taking disciplinary and corrective action, processing complaints, and disclosing conflicts of interest. In addition, auditors conducted data validation work to assess the reliability of the Board's database information used in its oversight responsibilities. Specifically, auditors interviewed board staff, reviewed data policies and procedures, and compared information in the database against hard copy files. Although auditors found that, in many instances, board data was inaccurate or incomplete, auditors determined that the Board's database was sufficiently reliable for the purposes of the audit. Auditors' conclusions on these internal controls are reported in Finding 1, Finding 2, and the Sunset Factors.

¹ Auditors reviewed published annual reports from the District of Columbia Public Charter School Board, Denver Public Schools, Indianapolis Office of Education Innovation, and Utah State Charter School Board.

AGENCY RESPONSE

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September 18, 2013

Ms. Debra Davenport, Auditor General
State of Arizona, Office of the Auditor General
2910 N 44th Street, Suite 410
Phoenix, AZ 85018

Dear Ms. Davenport:

The Arizona State Board for Charter Schools (Board) appreciates the opportunity to respond to the findings and recommendations included in the performance audit and sunset review of the Board. The Board and staff appreciate the efforts of the audit team to understand the Board's work and the professionalism with which they conducted the audit.

As requested, a response to each of the recommendations included in the report has been provided. Responses to the sunset factors were included as necessary.

Sincerely,

DeAnna Rowe
Executive Director

"To improve public education in Arizona by sponsoring charter schools that provide quality educational choices."

APP117

Response to Recommendations and Sunset Factors

Recommendations

1.1 To ensure it holds charter schools accountable for academic performance, the Board should continue its efforts to implement its academic intervention policy by conducting annual reviews of charter schools' academic performance, requiring schools to address academic performance that does not meet its standards, and taking disciplinary action as necessary.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

1.2 To ensure it holds charter holders accountable for financial performance, the Board should:

- a. Adopt rules to define operational expectations, including financial framework expectations, and define any actions the Board may take resulting from charter holders not meeting those expectations to support its use of the financial framework; and

The finding of the Auditor General is agreed to and the audit recommendation regarding the adoption of rules to define operational expectations to include the financial framework expectations will be explored and included to the extent possible.

- b. Develop and implement policies and procedures regarding financial performance measures, including determining when action is needed, formalizing its criteria for taking action, and defining the types of action the Board should take, including requiring more frequent financial reporting from charter holders with continued poor financial performance.

The finding of the Auditor General is agreed to and the recommendation to develop and implement policies and procedures regarding financial performance measures, including determining when action is needed, formalizing its criteria for taking action and defining the types of action the Board would take will be implemented to the extent practicable with the Board's current resources. The report finding and recommendation suggest that more frequent financial reporting be required of charter holders with continued poor financial performance and cites the practices of other authorizers including the Denver Public Schools, the Indianapolis Office of Education Innovation, and the District of Columbia Public Charter School Board. A review of the number of schools authorized by these entities, along with their respective budgets and staffing as compared to that of the Board suggests that such additional review of financial reports could be possible with funds to support additional FTE:

Authorizer	Number of Schools	Authorizer FTE	Authorizer Annual Budget
Denver Public Schools	36	9	\$750,000 plus additional funds to other departments that provide program-based support
Indianapolis Office of Education Innovation	27	4	\$375,000
District of Columbia Public Charter School Board	101	26	\$3,100,000
Arizona State Board for Charter Schools	515	8	\$748,100

Source: Information provided to the Board by the National Association of Charter School Authorizers on July 25, 2013 and August 21, 2013.

1.3 The Board should assess the risk that other internal control weaknesses or deficiencies pose to charter holders' financial operations and based on its available resources, determine for what additional internal control weaknesses or deficiencies it should require corrective action plans.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

1.4 The Board should revise its policies and procedures to require charter holders to submit corrective action plans for the additional internal control findings it identifies.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

1.5 The Board should develop and implement an operational framework consistent with best practices.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented to the extent practicable. As indicated in the Board's response to the Auditor General's recommendation in 1.2b, there is a significant funding difference between the Board's appropriation and the number of charter schools for which it provides oversight compared to the funding of other authorizers identified as having implemented best practices. The Board will evaluate the recommended best practices for incorporation in its operational framework and will consider their inclusion based on feasibility of implementation with its current capacity and funding.

1.6 To assist in ensuring charter school accountability, the Board should make greater use of its database to monitor all charter holders' complaint and disciplinary actions and performance data and use this information to assist in strategically targeting its oversight efforts.

The finding of the Auditor General is agreed to and the audit recommendation regarding the use of the database to monitor all charter holders' performance data incorporated in the Board's operational framework will be implemented. To the extent that complaint and disciplinary actions align with measures incorporated in the operational framework and funding exists for the further development of the database to track such information, the Board will implement the recommendation for the inclusion of complaint and disciplinary actions.

1.7 To ensure that it can exercise appropriate oversight of charter schools based on its performance standards, the Board should adopt rules to define board standards for academic, financial, and operational performance; sufficient progress toward these standards; and consequences for not meeting standards or making progress toward the standards.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

2.1 To better inform the public about charter schools, the Board should:

- a. Follow through with its plans to place additional charter school information on its Web site;

The finding of the Auditor General is agreed to and the audit recommendation will be implemented following the Board's plan to include charter holders' framework dashboards, contracts and other legal documents on the Web site. As the Board has moved to an electronic submission system, contracts, including the approved application, and other legal documents collected and generated moving forward will be made publicly available through ASBCS Online. Framework dashboards are also stored in ASBCS Online. Historical paper

versions of documents collected and created since 1995 will need to be scanned and uploaded to ASBCS Online. The conversion of these documents will occur over time, when existing staff have time to dedicate to the project. A more expeditious conversion could occur if additional resources were provided.

- b. Make information about disciplinary actions available by school or charter holder on its Web site;

The finding of the Auditor General is agreed to and the audit recommendation will be implemented when the resources for merging the historical paper files and the current electronic documents into the operational framework are made available. Until that time, the Board will transition to report current disciplinary actions in accordance with the operational framework, when adopted.

- c. Provide more complete information about complaints on its Web site;

The finding of the Auditor General is agreed to and the audit recommendation will be implemented when the resources for merging the historical paper files and the current electronic documents into the operational framework are made available. Until that time, the Board will transition to report current complaints in accordance with the operational framework, when adopted.

- d. Explore opportunities to provide additional guidance to the public on how to locate charter school and charter holder information on its Web site; and

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

- e. The Board should consult with its database contractor to determine the feasibility of developing and providing a low-cost report on its Web site that the public can review with important charter school comparative information.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

2.2 The Board should revise its processes for collecting and verifying charter school characteristic information to ensure that its Web site accurately captures this information for the charter schools it sponsors.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

2.3 The Board should develop and post guidance on its Web site to help inform the public about both ADE and board academic standards and the Board's role in overseeing charter schools' academic accountability.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Sunset Factors

2. The effectiveness with which the board has met its objective and purpose and the efficiency with which it has operated:

- –To comply with statutory conflict-of-interest requirements, board members and board staff should have conflict-of-interest forms available for public review.

The finding of the Auditor General is agreed to and the audit recommendation has been implemented. Conflict of Interest forms are sent annually in September to Board members and staff for submission. Completed forms are available for public review upon request.

- –Review and revise its policies and procedures for collecting new application fees to ensure it follows appropriate internal controls regarding cash transactions.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

6. The Board should develop and implement policies and procedures for when and how to conduct further investigation into a complaint.

The finding of the Auditor General is agreed to and the audit recommendation will be implemented when the resources for investigating complaints are available.

Performance Audit Division reports issued within the last 24 months

11-07	Department of Corrections— Oversight of Security Operations	12-06	Arizona Health Care Cost Containment System—Medicaid Fraud and Abuse Prevention, Detection, Investigation, and Recovery Processes
11-08	Department of Corrections— Sunset Factors	12-07	Arizona Health Care Cost Containment System—Sunset Factors
11-09	Arizona Department of Veterans' Services—Veterans' Donations and Military Family Relief Funds	13-01	Department of Environmental Quality—Compliance Management
11-10	Arizona Department of Veterans' Services and Arizona Veterans' Service Advisory Commission— Sunset Factors	13-02	Arizona Board of Appraisal
11-11	Arizona Board of Regents— Tuition Setting for Arizona Universities	13-03	Arizona State Board of Physical Therapy
11-12	Arizona Board of Regents— Sunset Factors	13-04	Registrar of Contractors
11-13	Department of Fire, Building and Life Safety	13-05	Arizona Department of Financial Institutions
11-14	Arizona Game and Fish Commission Heritage Fund	13-06	Department of Environmental Quality—Underground Storage Tanks Financial Responsibility
12-01	Arizona Health Care Cost Containment System— Coordination of Benefits	13-07	Arizona State Board of Pharmacy
12-02	Arizona Health Care Cost Containment System—Medicaid Eligibility Determination	13-08	Water Infrastructure Finance Authority
12-03	Arizona Board of Behavioral Health Examiners	13-09	Arizona State Board of Cosmetology
12-04	Arizona State Parks Board	13-10	Department of Environmental Quality—Sunset Factors
12-05	Arizona State Schools for the Deaf and the Blind	13-11	Arizona State Board of Funeral Directors and Embalmers

Future Performance Audit Division reports

Arizona Historical Society

**Electronic Index of Record
MAR Case # CV2016-051845**

No.	Document Name	Filed Date
1.	COMPLAINT (DECLARATORY JUDGMENT)	Mar. 22, 2016
2.	CERTIFICATE OF COMPULSORY ARBITRATION	Mar. 22, 2016
3.	CIVIL COVERSHEET	Mar. 22, 2016
4.	ACCEPTANCE OF SERVICE	Mar. 29, 2016
5.	MOTION TO DISMISS THE COMPLAINT, OR IN THE ALTERNATIVE, MOTION TO STAY PROCEEDINGS	Apr. 28, 2016
6.	PLAINTIFFS' RESPONSE TO DEFENDANT'S MOTION TO DISMISS THE COMPLAINT, OR IN THE ALTERNATIVE, MOTION TO STAY PROCEEDINGS --AND-- PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
7.	(PART 1 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
8.	(PART 2 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
9.	(PART 3 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
10.	(PART 4 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
11.	(PART 5 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
12.	(PART 6 OF 6) PLAINTIFFS' SEPARATE STATEMENT OF FACTS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT	May. 25, 2016
13.	NOTICE OF FIRST EXTENSION TO FILE REPLY IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS THE COMPLAINT, OR IN THE ALTERNATIVE, MOTION TO STAY PROCEEDINGS	May. 31, 2016
14.	NOTICE OF SECOND EXTENSION TO FILE REPLY IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE COMPLAINT, OR IN THE ALTERNATIVE, MOTION TO STAY PROCEEDINGS AND NOTICE OF FIRST EXTENSION TO FILE DEFENDANT'S RESPONSE TO PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT	Jun. 15, 2016
15.	DEFENDANT'S COMBINED REPLY TO ITS MOTION TO DISMISS -AND- RESPONSE TO PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT -AND- CROSS-MOTION FOR SUMMARY JUDGMENT	Jul. 8, 2016
16.	DEFENDANT'S STATEMENT OF FACTS	Jul. 8, 2016

**Electronic Index of Record
MAR Case # CV2016-051845**

No.	Document Name	Filed Date
17.	STIPULATION REGARDING DEADLINE FOR FILING PLAINTIFFS' COMBINED REPLY IN SUPPORT OF PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT AND RESPONSE TO DEFENDANT'S CROSS-MOTION FOR SUMMARY JUDGMENT	Jul. 14, 2016
18.	SECOND STIPULATION REGARDING DEADLINE FOR FILING PLAINTIFFS' COMBINED REPLY IN SUPPORT OF PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT AND RESPONSE TO DEFENDANT'S CROSS-MOTION FOR SUMMARY JUDGMENT	Aug. 15, 2016
19.	PLAINTIFFS' REPLY IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT -AND- RESPONSE TO DEFENDANT'S CROSS-MOTION FOR SUMMARY JUDGMENT	Aug. 22, 2016
20.	PLAINTIFFS' SUPPLEMENTAL SEPARATE STATEMENT OF FACTS AND PLAINTIFFS' RESPONSE TO DEFENDANT'S STATEMENT OF FACTS	Aug. 22, 2016
21.	ME: 150 DAY MINUTE ENTRY [08/20/2016]	Aug. 24, 2016
22.	REQUEST FOR ORAL ARGUMENT	Sep. 12, 2016
23.	ME: ORAL ARGUMENT SET [09/15/2016]	Sep. 19, 2016
24.	DEFENDANT'S REQUEST TO TAKE JUDICIAL NOTICE AND MOTION FOR LEAVE TO RAISE ADDITIONAL ARGUMENT	Oct. 7, 2016
25.	(PART 1 OF 2) PLAINTIFFS' RESPONSE TO DEFENDANT'S REQUEST TO TAKE JUDICIAL NOTICE AND MOTION FOR LEAVE TO RAISE ADDITIONAL ARGUMENT	Oct. 12, 2016
26.	(PART 2 OF 2) PLAINTIFFS' RESPONSE TO DEFENDANT'S REQUEST TO TAKE JUDICIAL NOTICE AND MOTION FOR LEAVE TO RAISE ADDITIONAL ARGUMENT	Oct. 12, 2016
27.	ME: RULING [10/14/2016]	Oct. 18, 2016
28.	NOTICE OF LODGING PROPOSED FORM OF JUDGMENT	Oct. 19, 2016
29.	JUDGMENT	Nov. 14, 2016
30.	NOTICE OF APPEAL	Dec. 13, 2016
31.	PLAINTIFFS' NOTICE OF TRANSCRIPT ORDERING	Jan. 4, 2017
32.	(PART 1 OF 2) PLAINTIFFS' NOTICE OF FILING TRANSCRIPT	Jan. 4, 2017
33.	(PART 2 OF 2) PLAINTIFFS' NOTICE OF FILING TRANSCRIPT	Jan. 4, 2017



**Electronic Index of Record
MAR Case # CV2016-051845**

APPEAL COUNT: 1

RE: CASE: UNKNOWN

DUE DATE: 01/11/2017

CAPTION: LEGACY EDUC, ET AL VS AZ BOARD CHARTER SCHOOLS

EXHIBIT(S): NONE

LOCATION ONLY: NONE

SEALED DOCUMENT: NONE

DEPOSITION(S): NONE

TRANSCRIPT(S): NONE

COMPILED BY: TERRYR001 on January 11, 2017; [2.4-12334.47]
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CERTIFICATION: I, MICHAEL K. JEANES, Clerk of the Superior Court of Maricopa County, State of Arizona, do hereby certify that the above listed Index of Record, corresponding electronic documents, and items denoted to be transmitted manually constitute the record on appeal in the above-entitled action.

The bracketed [date] following the minute entry title is the date of the minute entry.

CONTACT INFO: Clerk of the Superior Court, Maricopa County, Appeals Unit, 175 W Madison Ave, Phoenix, AZ 85003; 602-372-5375

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2016-051845

10/14/2016

HONORABLE JOHN R. HANNAH JR

CLERK OF THE COURT
W. Tenoever
Deputy

LEGACY EDUCATION GROUP, et al.

LYNNE C ADAMS

v.

ARIZONA STATE BOARD FOR CHARTER
SCHOOLS

KIM S ANDERSON

ROGER W HALL

RULING

Courtroom 102 - NE

1:31 p.m. This is the time set for Oral Argument on Defendant's Motion to Dismiss, Plaintiffs' Motion for Summary Judgment and Defendant's Cross-Motion for Summary Judgment. Plaintiffs Legacy Education Group and Tucson Preparatory School are represented by counsel, Lynne C. Adams and Roger W. Hall. Defendant Arizona State Board for Charter Schools is represented by counsel, Kim S. Anderson and Leslie K. Cooper.

A record of the proceedings is made digitally in lieu of a court reporter.

Arguments are heard.

IT IS ORDERED the Defendant's Motion to Dismiss is granted for the reasons stated on the record. This ruling is a legal interpretation of A.R.S. § 15-183(R) that does not depend on the facts.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2016-051845

10/14/2016

IT IS FURTHER ORDERED the Plaintiffs' Motion for Summary Judgment and Defendant's Cross-Motion for Summary Judgment are moot.

IT IS FURTHER ORDERED that the Defendant will have ten days to submit a form of judgment along with any application for fees or costs that may be appropriate. The plaintiffs will have five days to object if only a form of judgment is submitted and ten days to respond if an application for fees and costs is submitted.

3:05 p.m. Hearing concludes.

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9 Attorneys for Plaintiffs

10 ARIZONA SUPERIOR COURT
11 MARICOPA COUNTY

MICHAEL K. JEANES
Clerk of the Superior Court
By Leslie Groeneveld, Deputy
Date 03/22/2016 Time 15:35:38
Description Amount
----- CASE# CV2016-051845 -----
CIVIL NEW COMPLAINT 319.00

TOTAL AMOUNT 319.00
Receipt# 25130607

12 CV2016-051845

13 Case No. _____

13 Legacy Education Group dba East Valley
14 High School, an Arizona non-profit
15 corporation; and Tucson Preparatory
School, an Arizona non-profit
16 corporation,

14 **COMPLAINT**
15 **(Declaratory Judgment)**

16 Plaintiffs,

17 vs.

18 Arizona State Board for Charter Schools,

19 Defendant.

20 For their Complaint against Defendant, Plaintiffs allege as follows:

21 **PARTIES AND JURISDICTION**

22 1. Plaintiff Legacy Education Group is an Arizona non-profit corporation
23 that operates East Valley High School, an Arizona public charter school.

24 2. Plaintiff Tucson Preparatory School is an Arizona non-profit
25 corporation that operates Tucson Preparatory School, an Arizona public charter
26 school.

27 3. The schools operated by Legacy Education Group and Tucson
28 Preparatory School (collectively "Schools") are sponsored by and have valid and

1 current charter contracts with the Arizona State Board for Charter Schools (“Board”).

2 4. Many other charter schools that are sponsored by and have valid and
3 current charter contracts with the Board have chosen not to be named as plaintiffs in
4 this lawsuit. Given the Board’s discretion to make regulatory decisions that control
5 the ability of charter schools to operate at all and under what conditions, those
6 unnamed charter schools are concerned about the potential consequences of being
7 publicly associated with this lawsuit including potential retaliation by the Board.

8 5. Defendant Arizona State Board for Charter Schools is an agency of the
9 State of Arizona that was created by legislation in 1994.

10 6. This Court has jurisdiction to hear and adjudicate this Complaint and to
11 issue a declaratory judgment under A.R.S. §§ 41-1034(B) and 12-1831.

12 7. Venue is proper in this Court pursuant to A.R.S. § 41-1034(B).

13 **FACTUAL BACKGROUND**

14 8. The Schools’ charter contracts with the Board allow them to operate a
15 charter school or schools in Arizona, consistent with the terms of their charter
16 contracts and in compliance with any statutory requirements.

17 9. Pursuant to statute and the terms of the charter contracts, the Board
18 exercises general supervision over each of the Schools and over other charter schools
19 that it sponsors. *See* A.R.S. §§ 15-182 to -183.

20 10. The Board has adopted an Academic Performance Framework and a
21 Financial Performance Framework (the “Frameworks”), which include academic and
22 financial “dashboards.”

23 11. The Academic Performance Framework and the Financial Performance
24 Framework have been identified as a “policies” by the Board. *See* Board Policies,
25 “Performance Framework,” *available at* [https://asbcs.az.gov/board-staff-](https://asbcs.az.gov/board-staff-information/statutes-rules-policies/policies)
26 [information/statutes-rules-policies/policies](https://asbcs.az.gov/board-staff-information/statutes-rules-policies/policies).

1 12. The Frameworks have not been adopted by the Board as rules pursuant
2 to the Arizona’s Administrative Procedure Act (the “APA”). *See* A.R.S. §§ 41-1021
3 to -1038.

4 13. The Frameworks are generally applicable to all charter schools
5 sponsored by the Board, including the Schools, and the Board uses the Frameworks
6 to implement its statutory mandate to measure and evaluate charter schools’
7 performance. A.R.S. §§ 15-183(I)(1), (2), (3) & (4); A.R.S. § 15-183(R).

8 14. The Academic Performance Framework specifically indicates that it is
9 applicable to all charter schools sponsored by the Board, stating, among other things,
10 that the academic performance targets included in the document “are applied
11 consistently to all schools.” Academic Performance Framework, on-line PDF at
12 page 6.

13 15. The Frameworks implement the Board’s statutory directive as a charter
14 school sponsor. The Academic Performance Framework states that it was created to
15 implement a law:

16 As the authorizer or sponsor of charter schools, the State Board for
17 Charter Schools must adopt a performance framework that includes the
18 academic performance expectations of the charter school and the
19 measurement of sufficient progress toward the academic performance
20 expectations (A.R.S. § 15-183.R).

19 Academic Performance Framework, on-line PDF at page 3.

20 16. The Frameworks are the Board’s interpretation of its statutory
21 monitoring requirements, and they provide substance to the general authority
22 provided in statute. A.R.S. § 15-183(R).

23 17. A.R.S. § 15-183(R) leaves the details regarding the Board’s
24 implementation of its “oversight and administrative responsibilities,” including its
25 “performance framework,” to the Board’s discretion.

26 18. The Frameworks are also the Board’s interpretation of its
27 responsibilities, and they set forth the level of performance required by charter
28 schools and how the performance will be calculated—what factors will be included

1 in the calculations and how those factors will be weighted. Academic Performance
2 Framework, on-line PDF at pages 3-19. In fact, much of the Academic Performance
3 Framework is dedicated to setting forth the “indicators, measures, metrics, and
4 targets” that will be used by the Board to calculate a school’s dashboard numbers. *Id.*

5 19. The interpretive purpose of the Frameworks is further confirmed by
6 their prefatory language, which states that they are intended “to communicate the
7 [Board’s] academic expectations” to all charter schools. Academic Performance
8 Framework, on-line PDF at page 3.

9 20. The Frameworks are not advisory only, but have been and are used by
10 the Board to make substantive decisions regarding charter schools’ operations.

11 21. For example, the Board has based its determinations regarding whether
12 charter school contracts will be renewed or revoked in large part on the Frameworks
13 and the dashboards generated by the Frameworks. A.R.S. §§ 15-183(I)(1), (2), (3) &
14 (4).

15 22. In the past two years, the Board has relied on the Frameworks to require
16 charter schools to enter into conditional renewal agreements that impose onerous,
17 additional requirements on the schools in order to obtain renewal of their charters.

18 23. The Board has also based other decisions regarding charter schools and
19 their charter terms on the Frameworks, and has imposed additional requirements of
20 charter schools based at least in part on the Frameworks.

21 24. In the past, the Board has relied on the Frameworks to require charter
22 schools that are not meeting the standards established by the Frameworks to agree to
23 “performance management plans” and enter into onerous consent agreements on
24 penalty of losing funding or having their charters revoked; to deny requests by
25 charter schools to increase the grade levels they serve, even when demand for those
26 grades exists; to deny requests by charter schools to expand their enrollment, even
27 when demand exists; and to force non-traditional charter schools to comply with
28 standards and metrics designed for more traditional schools.

1 25. The Board has known for at least three years that the Frameworks were
2 rules that needed to be adopted in accordance with the APA. Specifically, in
3 September 2013, the Auditor General advised the Board that it needed to adopt rules.
4 ARIZONA STATE BOARD FOR CHARTER SCHOOLS, A REPORT TO THE LEGISLATURE,
5 Arizona Auditor General, PDF at page 27 (final paragraph), *available at*
6 http://www.azauditor.gov/sites/default/files/13-12_Report_0.pdf.

7 26. Although the Board told the Auditor General that it “agree[d] with all of
8 the findings and plan[ned] to implement all of the recommendations” (which the
9 Auditor General in turn told the Arizona State Legislature), *id.*, the Board did not
10 “adopt rules to define board standards,” but instead continued to rely solely on
11 policies.

12 27. The Board recently opened a rulemaking docket in accordance with the
13 APA to enact rules that would take the place of the Frameworks. But any rules
14 adopted by the Board in accordance with that rulemaking action are not enforceable
15 until they are finally adopted in compliance with the APA.

16
17 **COUNT ONE**
 (Declaratory Judgment)

18 28. The Schools incorporate by reference the preceding paragraphs of this
19 Complaint as if fully set forth herein.

20 29. Pursuant to A.R.S. § 41-1034(B), any person “who is or may be affected
21 by an existing agency practice of substantive policy statement that the person alleges
22 to constitute a rule” may file an action for a declaratory judgment in this Court in
23 accordance with Arizona’s Uniform Declaratory Judgments Act, A.R.S. §§ 12-1831
24 through 12-1846.

25 30. The Schools are or may be affected by the Board’s Frameworks.

26 31. A rule is “an agency statement of general applicability that implements,
27 interprets or prescribes law or policy, or describes the procedure or practice
28 requirements of an agency.” A.R.S. § 41-1001(19).

1 32. The rulemaking procedure of the APA applies “to all agencies and all
2 proceedings not expressly exempted.” A.R.S. § 41-1002(A).

3 33. The Board is subject to the APA, and there is no express exemption for
4 the Frameworks.

5 34. Because the Frameworks are generally applicable to all charter schools
6 that are sponsored by the Board, including the Schools, and because the Frameworks
7 implement or interpret a law that governs the Board’s regulation of charter schools,
8 they are “rules” that are subject to the APA.

9 35. The Frameworks are not “subjective policy statements,” as that term is
10 defined by A.R.S. § 41-1001(22), because, among other things, they are not
11 “advisory only” and because they impose “additional requirements or penalties” on
12 the charter schools regulated by the Board.

13 36. The Board must comply with the APA’s rulemaking requirements
14 before the Frameworks can be enforced or given effect. A.R.S. § 41-1030(A). “A
15 rule is invalid unless it is made and approved in substantial compliance with [the
16 APA], unless otherwise provided by law.” *Id.*

17 37. The Board’s failure to enact the Frameworks as rules in accordance with
18 the APA renders the Frameworks invalid, void and unenforceable.

19 38. The Board has taken action against the Schools and other charter
20 schools in the past based on the Frameworks, and because those actions were based
21 on invalid rules, they are also invalid, void and without any legal effect or
22 consequence.

23 WHEREFORE, the plaintiff Schools request:

24 A. A judicial determination and declaratory judgment pursuant to A.R.S. §
25 41-1034(B) that:

26 a. the Frameworks are actually rules under the APA;

27 b. the Board’s failure to adopt the Frameworks in compliance with the
28 APA renders the Frameworks void and unenforceable; and

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c. any and all past or future actions taken by the Board in reliance on the Frameworks are also void and without any legal effect or consequence.

B. A permanent injunction that prohibits the Board from enforcing or threatening to enforce the Frameworks or using them as the basis for any action against any of the charter schools that the Board sponsors and authorizes.

C. The Schools' attorneys' fees, costs, and litigation expenses for the prosecution of this action pursuant to A.R.S. §§ 12-348(A) and § 12-1840.

D. Such other and further relief as the Court may deem just and equitable.

DATED this 22nd day of March, 2016.

Roger W. Hall
BUCHALTER NEMER
16435 North Scottsdale Road, Suite 440
Scottsdale, AZ 85254

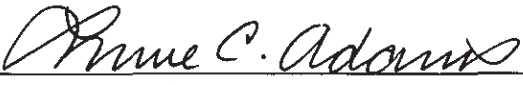
By 
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Attorneys for Plaintiffs

EXHIBIT B

Arizona State Board for Charter Schools

Academic Performance Framework and Guidance

As Revised on June 13, 2016

Historical Note:

Effective: October 9, 2012
Revision effective June 13, 2016

Board Approval Date: October 9, 2012; September 9, 2013; January 13, 2014; October 14, 2014, August 17, 2015,
June 13, 2016

Revised: November 26, 2012; September 9, 2013, January 13, 2014; October 14, 2014,
August 17, 2015, June 13, 2016

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Support and funding for the development of the Arizona State Board for Charter Schools Performance Framework, which includes the Academic Framework, Operational Framework and Financial Framework, were provided by NACSA and through its Fund for Authorizing Quality.

Additional funding to support the implementation of the Performance Framework was provided by:

- Governor Brewer’s Office of Education Innovation
- Arizona Community Foundation
- Stand for Children
- Rodel Charitable Foundation of Arizona
- Arizona Virtual Academy



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Academic Performance Framework Guidance

Charter schools may be established to provide a learning environment that will improve pupil achievement (A.R.S. § 15-181). As the authorizer or sponsor of charter schools, the State Board for Charter Schools must adopt a performance framework that includes the academic performance expectations of the charter school and the measurement of sufficient progress toward the academic performance expectations (A.R.S. § 15-183(R)).

Charter Holders have the autonomy to select and implement programs of instruction that align with their philosophical and methodological ideology and operational structure consistent with state and federal law and the charter contract. The purpose of the Academic Performance Framework (“academic framework”) is to communicate the State Board for Charter Schools’ (“Board”) academic expectations for ensuring that all Charter Holders in its portfolio are providing a learning environment where measurable improvement in pupil achievement can be demonstrated.

In developing the academic framework, the Board remained conscious of its limited resources to implement the academic framework. The Board was also mindful of its commitment to maintaining current levels of data collection so as not to unnecessarily burden the Charter Holders with requirements to submit additional information for the purpose of evaluating the academic performance of the Charter Holder. The successful implementation of the academic framework relies on having access to data collected through the administration and evaluation of state assessments.

The academic framework is organized by indicators, measures, metrics and targets.

The academic framework focuses purposefully on quantitative academic outcomes as a basis for analysis to be used in high-stakes decisions. If educational processes are required by law, such elements are included in the Operational Performance Framework and further guidance on the reasoning for this indicator can be found in the Operational Performance Framework and Guidance.

Minimum Academic Performance Expectations

The Academic Performance Framework is organized by indicators, measures, metrics, and targets.

Indicators

The Academic Performance Framework includes two indicators, or general categories, to evaluate a Charter Holder's academic performance.

1. **State Accountability:** State Accountability is the default indicator used to evaluate the academic performance of all charter schools sponsored by the Board. This indicator includes the letter grade of each school operated by the Charter Holder as assigned through Arizona's A–F Letter Grade Accountability System. In addition, this indicator considers state designations for school improvement.
2. **School-Specific Academic Goals:** A Charter Holder that operates a school that serves a special population that does not have an achievement profile established by the State Board of Education for state accountability pursuant to A.R.S. § 15-241(H) may petition the Board to adopt unique, school-specific academic performance standards. Only charter schools that have been approved by the Board to use the substitute indicator of school-specific academic goals will be evaluated under this indicator.

Measures

For each of the indicators, the academic framework utilizes measures to evaluate schools. The combination of measures, taken on the whole, provides the Board with a balanced scorecard of each school's performance over time. Multiple measures are used in the standards: A-F State Accountability Letter Grades, State designations for school improvement, and school-specific academic goals for Charter Holders approved to use the separate indicator for academic performance.

Metrics

Metrics are the methods of evaluating a measure. In the development of the academic framework, the Board reviewed the available data to determine which metrics are appropriate for evaluating its charter schools.

Targets and Rating Categories

For each of the measures, targets are set to rate the schools against the academic framework. The targets establish the levels of performance needed to place each school into the rating categories. There are five possible rating categories but due to the nature of the individual measures, not every measure will include all five ratings.

Exceeds Standard: The school's performance on this measure exceeds the performance targets and shows exemplary performance.

Above Standard: The school’s performance on this measure is above the performance targets required to meet the Board’s standard.

Meets Standard: The school’s performance on this measure meets the Board’s minimum performance targets.

Does Not Meet Standard: The school’s performance on this measure does not meet the Board’s minimum performance targets.

Falls Far Below Standard: The school’s performance on this measure signals a significant academic risk. Performance for any measure receiving this rating means the charter school is performing far below the Board’s performance targets and on par with the lowest-performing schools in the state. If a Charter Holder operates a charter school that falls far below the standard, and the Charter Holder may be brought before the Board for disciplinary action.

Indicators and Measures in Detail

Each of the indicators and measures is presented below. Included is an overview of each measure, methodological approaches, and factors considered in the development of specific targets.

Indicator: State Accountability

A-F Letter Grade Accountability System

	1a. Is the school meeting acceptable standards according to the state accountability system?
	<i>Exceeds Standard:</i> <input type="checkbox"/> School received a letter grade of A from the state accountability system.
	<i>Above Standard:</i> <input type="checkbox"/> School received a letter grade of B from the state accountability system.
	<i>Meets Standard:</i> <input type="checkbox"/> School received a letter grade of C from the state accountability system.
	<i>Does Not Meet Standard:</i> <input type="checkbox"/> School received a letter grade of D from the state accountability system.
	<i>Falls Far Below Standard:</i> <input type="checkbox"/> School received a letter grade of F from the state accountability system.

Targets for A–F Letter Grade Accountability System

Targets for this measure were set taking into consideration alignment with the state grading system and the Board’s mission to improve public education in Arizona. Schools receiving an “A” grade are assessed in the academic framework as “exceeds standard,” while schools receiving an “F” grade are considered “falls far below standard.”

Modifications for Alternative and Extremely Small Schools

Subject to final adoption by the State Board of Education, the Department of Education is required to use appropriate achievement profiles to assess alternative schools and extremely

small schools and may develop achievement profiles for Arizona Online Instruction schools and others pursuant to A.R.S. § 15-241(H).¹

State Designations for School Improvement

	1b. Is the school meeting performance expectations as set forth by state and federal accountability requirements?
	<i>Meets Standard:</i> <input type="checkbox"/> Not identified for improvement.
	<i>Does Not Meet Standard:</i> <input type="checkbox"/> Identified for improvement and/or targeted support.
	<i>Falls Far Below Standard:</i> <input type="checkbox"/> Identified for improvement and/or comprehensive support.

Targets for State Designations

Targets for this measure were set taking into consideration Arizona’s plan for school performance under the provisions outlined in the Every Student Succeeds Act and A.R.S. § 15-241.02. The Department of Education must annually measure proficiency rates, subgroup performance, graduation rates, and other academic indicators to identify all Arizona public schools required to implement targeted, comprehensive, and other supports necessary to improve school performance.

Indicator: School-Specific Academic Goals

A Charter Holder that operates a school that serves a special population that does not have an achievement profile established by the Department of Education and adopted by the State Board of Education for state accountability pursuant to A.R.S. § 15-241(H) may petition the Board to adopt unique, school-specific academic performance standards. If approved by the Board, four to six school-specific academic goals along with specific metric(s) and target(s) must be developed and agreed to by the Charter Holder and the Board. School-specific academic goals will be incorporated into the charter contract for the Charter Holder. (See Appendix A for guidance on School-Specific Academic Goals).

	2. Is the school meeting its school-specific academic goals?
	<i>Exceeds Standard:</i> <input type="checkbox"/> School exceeded its school-specific academic goals.
	<i>Meets Standard:</i> <input type="checkbox"/> School met its school-specific academic goals.
	<i>Does Not Meet Standard:</i> <input type="checkbox"/> School did not meet its school-specific academic goals.
	<i>Falls Far Below Standard:</i> <input type="checkbox"/> School fell far below its school-specific academic goals.

¹ A letter grade or its equivalent achievement profile will be used for schools that fall under this provision.

Overall Ratings

An Overall Rating is determined for each charter school operated by the Charter Holder in accordance with the following matrix.

Overall Rating			
1b. State Designation for School Improvement			
1a. A-F Letter Grade State Accountability	Not Identified for Improvement	Identified for Improvement and/or Targeted Support	Identified for Improvement and/or Comprehensive Support
A	Exceeds Standard	Does Not Meet Standard	Falls Far Below Standard
B	Above Standard	Does Not Meet Standard	Falls Far Below Standard
C	Meets Standard	Does Not Meet Standard	Falls Far Below Standard
D	Does Not Meet Standard	Does Not Meet Standard	Falls Far Below Standard
F	Falls Far Below Standard	Falls Far Below Standard	Falls Far Below Standard

For each charter school operated by a Charter Holder that has been approved by the Board to use School-Specific Academic Goals in place of the State Accountability indicator, the Overall Rating shall be determined as follows:

2. School-Specific Academic Goals	Overall Rating
School Exceeded its Goals	Exceeds Standard
School Met its Goals	Meets Standard
School Did Not Meet its Goals	Does Not Meet Standard
School Fell Far Below its Goals	Falls Far Below Standard

Dashboard

The Overall Rating is represented in the form of a color-coded graphic which will be referred to as the Dashboard. Examples for the Charter Holder and a charter school are included below.

Example Charter Holder

	State Accountability		School-Specific	Overall Rating
	1a. A-F Letter Grade State Accountability	1b. State Designation for School Improvement	2. School-Specific Academic Goals	
School 1	Exceeds Standard	Meets Standard	-	Exceeds Standard
School 2	Above Standard	Meets Standard		Above Standard
School 3	Meets Standard	Does Not Meet Standard	-	Does Not Meet Standard
School 4	Does Not Meet Standard	Falls Far Below Standard	-	Falls Far Below Standard
School 5	-	-	Meets Standard	Meets Standard

Example Charter School

FY	State Accountability		School-Specific	Overall Rating
	1a. A-F Letter Grade State Accountability	1b. State Designation for School Improvement	2. School-Specific Academic Goals	
2017	Does Not Meet Standard	Falls Far Below Standard	-	Falls Far Below Standard
2018	Meets Standard	Does Not Meet Standard	-	Does Not Meet Standard
2019	Above Standard	Meets Standard	-	Above Standard

Use of the Academic Framework

Evaluation

An evaluation is conducted annually to determine if the Charter Holder meets or is making sufficient progress toward the academic performance expectations set forth in the Board's academic performance framework. Overall Ratings for the most recent fiscal year that State achievement profiles are available are used to determine whether the Charter Holder meets the academic performance expectations set forth in the academic framework.

Meets the Board's Academic Performance Expectations

A Charter Holder meets the Board's academic performance expectations if all schools operated by the Charter Holder receive an Overall Rating of "Meets Standard," "Above Standard" or "Exceeds Standard" in the most recent fiscal year that State achievement profiles are available.

Demonstrating Sufficient Progress Toward the Board's Academic Performance Expectations

A Charter Holder that has one or more schools that receive an Overall Rating of "Does Not Meet Standard" or "Falls Far Below Standard" for three consecutive years has failed to demonstrate sufficient progress. In its determination of whether a Charter Holder demonstrates sufficient progress toward the Board's academic performance expectations, the Board will consider the Overall Rating for each of the schools it operates for the three most recent years that Overall Ratings are available and whether or not there has been improvement in the measures used to determine the Overall Rating.

The findings of the Demonstration of Sufficient Progress will be provided to the Board for consideration at the following times:

- If a charter school operated by the Charter Holder has failed to meet the Board's performance standard for three consecutive years
- During five year interval reviews
- When considering a charter contract renewal request submitted by the charter holder
- Upon receipt of information that a charter school operated by the charter holder has been assigned a letter grade of "F" by the Department of Education
- When considering disciplinary action against a charter holder that has breached one or more provisions of its charter contract or is in violation of state or federal law

Reviews

A Charter Holder's academic performance will be considered by the Board during periodic reviews, including five-year interval reviews.

Five-Year Interval Reviews²

The most recent Overall Rating of each school operated by a Charter Holder will be used to determine whether the Charter Holder is meeting or making sufficient progress toward meeting the Board's academic performance expectations. Charter Holders will be required to undergo an Academic Systems Review, as defined in Appendix B, at five-year intervals.

Other Reviews

Because academic performance can affect a Charter Holder's ability to meet the obligations of its charter contract or provisions of law, a Charter Holder's academic performance may also be reviewed at other times, including when the Board makes decisions related to a Charter Holder's financial and/or operational performance. The Board may also use academic performance data for public reporting to various stakeholders, such as schools, policymakers, students and families, and the public.

Expansion and Other Charter Holder Amendment and Notification Requests

A Charter Holder's academic performance will be evaluated by the Board when considering expansion requests. A Charter Holder's academic performance will also be evaluated by the Board when considering other requests identified in this section.

The expansion process is open to any Charter Holder if 75% or more of its schools eligible to receive an Overall Rating have an Overall Rating of "Meets Standard" or "Exceeds Standard" in the most recent year.

A Charter Holder's academic performance will be evaluated when considering the following expansion requests as identified in each of the specific requests:

- Add grade levels
- Add Arizona Online Instruction Program of Instruction
- Increase enrollment cap
- New charter applications submitted by officers, directors, partners or members, or charter representatives of existing Charter Holders
- Add a new charter school site
- Charter replication application

A Charter Holder's academic performance will be provided to the Board when considering the following amendment and notification requests as identified in each of the specific requests:

- Charter Holder Status Amendment Requests
- Transfer applications involving the transfer of the charter contract from another sponsor to the Board
- Transfer applications involving the transfer of a school site from an existing charter contract to its own charter contract

² Five year interval reviews are counted using the first year in which the charter holder may operate a charter school under its charter contract.

- Transfer applications involving the transfer of a school site from an existing charter contract to another existing charter contract

Associated Schools

The Board will consider the academic performance of associated schools in its consideration of replication applications and new charter applications submitted by officers, directors, partners or members, or charter representatives of existing Charter Holders and may consider associated schools at other times. An associated school is:

- A school operated by a Charter Holder that operates one or more other schools that contract with the same Education Service Provider.
- A school operated by the same Charter Holder but under different charter contracts.
- A school operated by a Charter Holder with at least fifty (50) percent of corporate board officers, directors, members or partners in common, as reflected in the charter contract.

Conclusion

A strong academic framework is critical for setting clear expectations for schools and for making high-stakes decisions more clear-cut and transparent. The creation and implementation of the academic framework required that the Board consider many factors, including which data elements are available, the quality of the data, and what information will support the Board in making high-stakes decisions.

Summarizing data into an Overall Rating that leads to certain predictable decisions and consequences supports the Board making objective, data-driven decisions. The academic framework provides an effective means to use ratings to “flag” a school for further evaluation, and then make a judgment about how to apply the consequences with relevant information being considered. This two-step process provides a transparent, data-driven method of placing schools in different categories of reward, review, or consequence.

APPENDIX A:
School-Specific Academic Goals

School-Specific Academic Goals

The Board recognizes that there are charter schools serving preponderant populations of at-risk students that are not included in the State’s criteria to obtain Alternative School status and has provided an opportunity for those schools to request use of school-specific academic goals in place of State Accountability.

Identifying Eligible Schools

The School-Specific Academic Goals indicator is not intended to replace State Accountability measures for schools that are identified as Alternative, or for any schools that have an achievement profile established by the Department of Education and adopted by the State Board of Education for state accountability pursuant to A.R.S. § 15-241(H).

Subject to adoption by the State Board of Education, the Department of Education is required to use appropriate achievement profiles to assess accommodation schools, alternative schools, and extremely small schools and may develop achievement profiles for Arizona Online Instruction schools and others. Under the current criteria to obtain Alternative School Status, the school must be approved by the Arizona Department of Education to serve students in one or more of the following categories:

- Students who have a documented history of disruptive behavior issues.
- Students who have dropped out of school and are now returning.
- Students in poor academic standing as demonstrated by being at least one year behind on grade level performance or academic credits.
- Students who are primary caregivers or are financially responsible for dependents and, therefore, may require a flexible school schedule.
- Students who are adjudicated.
- Students who are wards of the state and are in need of an alternative school setting

Schools receiving an achievement profile pursuant to A.R.S. § 15-241(H) are not eligible to apply for School-Specific Academic Goals.

Schools Eligible to Apply for School-Specific Academic Goals

A Charter Holder that operates a school that serves a special population that does not have an achievement profile established by the Department of Education and adopted by the State Board of Education for state accountability pursuant to A.R.S. § 15-241(H) may petition the Board to adopt unique performance standards. The Board shall consider a petition for use of the School-Specific Academic Goals if at least 70% of the students served by the school are identified as having at least one of the following risk factors:

- Identified as needing special education services
- Homeless

Schools that meet the criteria shall be approved by the Board to use school-specific academic goals. The Charter Holder shall provide verification that it meets the eligibility criteria at the time of initial application for use of school-specific academic goals and at subsequent five-year interval reviews.

Indicators and Measures

If approved by the Board, four to six school-specific academic goals along with specific metric(s) and target(s) must be developed and agreed to by the Charter Holder and the Board. School-specific academic goals will be incorporated into the charter contract for the Charter Holder. Schools shall select one or more measures from each of the indicators listed below:

Student Growth – Academic improvement over time on valid and reliable assessments of Arizona academic standards.

Student Achievement – Academic proficiency on valid and reliable assessments of Arizona academic standards.

Post-secondary Readiness – Outcomes in key subjects that indicate future success or that are aligned to college and career readiness such as graduation rates, SAT/ACT performance, workforce readiness, credit/course completion, or other metrics.

Student Engagement – Predictors of student achievement such as suspension rates, in-seat attendance rates, and positive socio-emotional or psychological adjustment rates.

Appendix B:

Academic Systems Review

Academic Systems Review

As part of the Five Year Intervals Review Process, the Board will conduct a comprehensive on-site Academic Systems Review to gain an understanding of how the school develops and implements the following:

- A curriculum that improves student achievement.
- A system for monitoring the integration of the State academic standards.
- A system for monitoring and documenting student proficiency.
- A professional development plan that supports effective implementation of the curriculum.

Purpose: This visit is designed to gather evidence regarding the school's implementation in providing a comprehensive program of instruction and designing a method to measure pupil progress toward pupil outcomes, as required in the charter contract. A set of criteria is used to determine the school's implementation.

Length: 0.5 – 1 day (typically scheduled 8:30 am to 12:30 pm)

Team: Board staff

Product: A Five-Year Intervals Review Report will summarize the Board staff's findings based on observations at the school site, discussion with school leadership team, and a review of documents. In addition, each report will include a summary of the charter holder's academic, financial and operational performance and any areas requiring further attention. The findings will consist of a summary of the school's implementation in specific areas and identification of any areas requiring attention.

Eligible Schools: All charter schools operated by a Charter Holder at the time of their five and ten year interval review.

Criteria: The school delivers a comprehensive program of instruction and has designed a method to measure pupil progress toward pupil outcomes that provides improved academic outcomes and educational success for all students.

Below are *the main questions that will guide the Board staff's inquiry during the site visit*

Does the school have an explicit, written curriculum for core content areas that is aligned with the state academic standards that drills down to the skill level?

Is there a systematic process in place for annually monitoring, evaluating, and reviewing the curriculum?

How is the integration of the state academic standards into the teachers' instructional practices assessed?

What does the school's teacher evaluation system comprise of? (Type, Frequency, Formative & Summative)

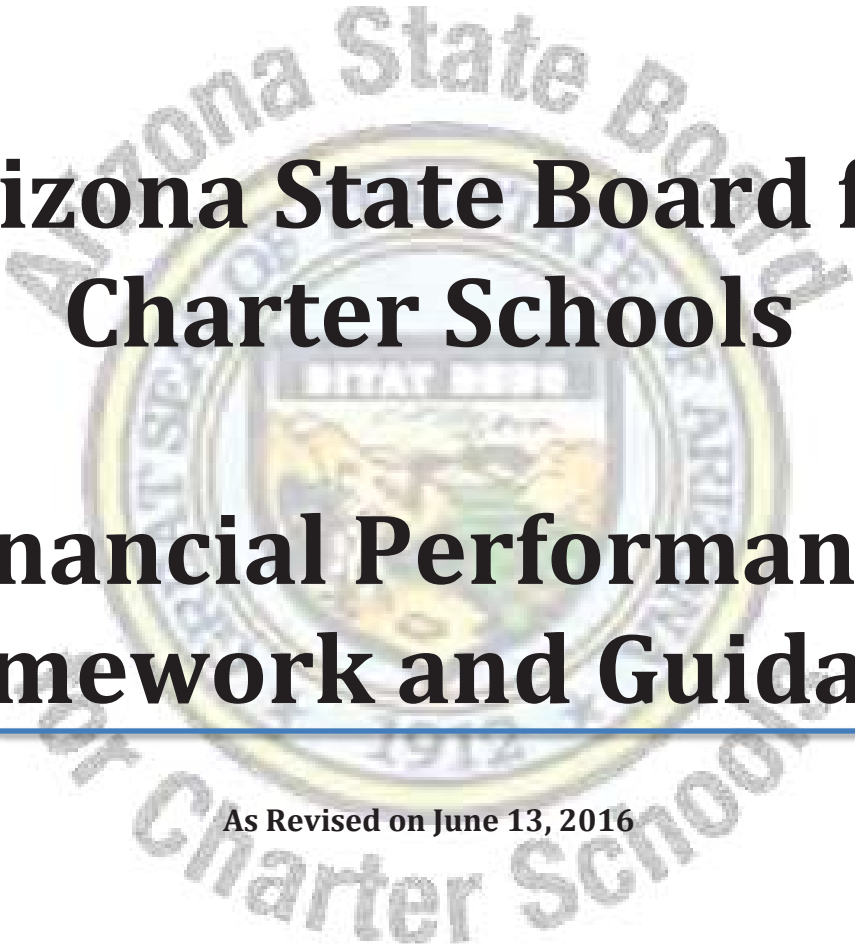
Is there a comprehensive assessment plan that utilizes data in a variety of ways to measure student performance and plan for teaching and learning?

How does the school staff track, analyze, and monitor its students' academic performance?

What evidence demonstrates that the professional development the teachers are engaged in is increasing student achievement?

How are the professional development activities aligned with the program of instruction (curriculum, methods of instruction, best practices)?
What types of follow-up activities occur?

EXHIBIT C



Arizona State Board for Charter Schools

Financial Performance Framework and Guidance

As Revised on June 13, 2016

Historical Note:

Effective: August 13, 2012
Revision effective June 13, 2016
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Financial Performance Framework Guidance

Charter holders have the autonomy to manage their finances consistent with state and federal law and the charter contract. The purpose of the Financial Performance Framework (“financial framework”) is to communicate the State Board for Charter Schools’ (“Board”) expectations for ensuring that **all charter holders in its portfolio** are viable organizations with strong fiscal management practices. To this end, the financial framework focuses on outcomes or performance goals not necessarily established in law.

The Board, in its oversight of charter holders and the schools that they operate, strives not to be over-reaching, but also recognizes the need to protect the public’s interests. Because charter schools are public schools they must maintain the public’s trust that they are implementing their education program as set out in the charter, spending public funds responsibly, and adhering to laws and charter requirements regarding their operations. However, the Board is aware of the delicate balance between appropriate oversight and infringement on autonomy.

In developing the financial framework, the Board remained conscious of its limited resources to implement the financial framework. The Board was also mindful of its commitment to maintaining current levels of data collection so as not to unnecessarily burden the charter holders with requirements to submit additional information for financial performance rating determinations.

FINANCIAL PERFORMANCE FRAMEWORK STRUCTURE

The financial framework, which has been included as Appendix A, gauges both near-term financial health and longer term financial sustainability. The portion of the financial framework that tests a charter holder’s near-term financial health is designed to depict the charter holder’s financial position and viability for the upcoming year. The portion of the financial framework that tests a charter holder’s longer term financial sustainability is designed to depict the charter holder’s financial position and viability over time. Charter holders meeting the desired standards demonstrate a low risk of financial distress. Charter holders not meeting the desired standards may currently be experiencing financial difficulties and/or may be at a higher risk for financial hardship in the future.

The financial framework includes five main levels of information: **Indicators, Measures, Metrics, Targets, and Ratings**. In addition to the information found below, the financial framework’s measures, metrics, targets, and ratings are further described in the “Measures in Detail” section of this guidance.

Indicators

Indicators are general categories of financial performance used to identify the financial information that best reflects the current financial status of a charter holder versus the information that better depicts the future financial viability of the charter holder. Near-Term Indicators and Sustainability Indicators are used in the financial framework.

Measures

Measures are the general means to evaluate an aspect of an indicator. Six measures are used in the financial framework: Going Concern, Unrestricted Days Liquidity, Default, Net Income, Cash Flow, and Fixed Charge Coverage Ratio.

Metrics

Metrics are a means for evaluating measures. As an example, the formula for evaluating Net Income is total revenues less total expenses.

Targets

Targets are the thresholds set to determine whether performance for a specific measure has been met or not. Using the Net Income measure again, the Board has set the target for the “Meets Standard” rating as Net Income is greater than or equal to \$1.

Ratings

For each measure a charter holder receives one of three ratings based on whether the charter holder met the target.

Meets Standard

The charter holder’s performance on this measure does not signal a financial risk to the charter holder and meets the Board’s expectation. Meeting the standard requires no follow up action by the charter holder.

Does Not Meet Standard

The charter holder’s performance on this measure signals a moderate financial risk to the charter holder and does not meet the Board’s expectation. This measure may require follow up depending on the interplay with other measures. Charter holders not meeting the standard in more than one measure are required to submit a financial performance response as addressed in the “Evaluation and Intervention” section of this document and Appendix B. Not meeting the standard may have an adverse impact on the consideration of the renewal application package and other requests made by the charter holder or at times when disciplinary action is considered. Charter holders may also be limited in their ability to expand their operations.

Falls Far Below Standard

The charter holder’s performance on this measure signals a potentially significant financial risk to the charter holder and is far below the Board’s expectation. Charter holders are required to submit a financial performance response as addressed in the “Evaluation and Intervention” section of this document and Appendix B. Falling far below the standard may have an adverse impact on the consideration of the renewal application package and other requests made by the charter holder or at times when disciplinary action is considered. Charter holders may be limited in their ability to expand their operations.

USING THE FINANCIAL PERFORMANCE FRAMEWORK

Collecting Evidence

The annual statutorily required audits conducted by independent certified public accountants provide the information necessary to determine a charter holder’s financial performance. In accordance with the parameters established in the [Board’s Strategic Plan](#), the financial framework uses information already collected by the Board to assess charter holders’ financial performance and does not require charter holders to provide additional information for rating determinations.

The following information from the annual audit reporting packages will be used:

- Independent Auditor’s Report on the financial statements
- Audited statement of financial position
- Audited statement of activities and changes in net assets
- Audited statement of cash flows
- Notes to the audited financial statements
- Applicable compliance questionnaire

Since a large percentage of the Board’s charter contracts are with non-profit entities, throughout this document the financial statements will be referred to using non-profit terminology. Statements reported in for-profit or governmental audits use the following corresponding names:

Non-profit	For-profit	Governmental
Statement of Financial Position	Balance Sheet	Statement of Net Assets
Statement of Activities and Changes in Net Assets ¹	Income Statement	Statement of Activities
Statement of Cash Flows	Statement of Cash Flows	Statement of Cash Flows (Note: This statement is required only under certain circumstances.)

Through ASBCS Online, the Board has provided online public access to the audit reporting packages of Board-sponsored charter holders. Information about how to access the annual audit reporting packages through ASBCS Online is available on the [Board’s website](#).

Evaluation and Intervention

The established targets are used to determine whether the charter holder is meeting each measure based on the available existing data. The evaluation is completed annually using the charter holder’s most recent audit reporting package and a determination is made as to whether the charter holder met the Board’s financial performance standard for the audited fiscal year. A charter holder that receives two or more “Does Not Meet Standard”, one or more “Falls Far Below Standard”, or both based on the charter holder’s most recent audit reporting package does not meet the Board’s financial performance standard.²

¹ This statement may also be referred to as the “statement of activities”.

² In those instances where the Board receives financial statements that cover multiple and different charter holder entities, the charter holder’s performance will be evaluated under the financial framework using the charter holder specific financial information and the financial information for the consolidated/combined entity. Failure of the individual charter holder or the consolidated/combined entity to meet the Board’s financial performance expectations will result in the charter holder being required to submit a financial performance response.

A charter holder’s financial performance will be used by the Board during the term of the charter:

- To stipulate the conditions which **waive** the charter holder from any submission requirements related to its financial operations.
- To stipulate the conditions which **require the charter holder to submit additional information** or clarification that will be used to inform the Board’s decision-making.

A charter holder’s financial performance will be considered by the Board as follows:³

- **Renewal**
- **Five-year interval reviews**
- **New School Site Notification Requests**
- **Arizona Online Instruction Program of Instruction Amendment Requests**
- **Replication**
- **Transfer of the charter contract from another sponsor to the Board**
- **Failing School designations**
- **If a charter school operated by a charter holder has failed to meet the Board’s academic performance standard for three consecutive years**
- **When the Board makes decisions related to a charter holder’s academic performance and/or compliance with its charter and state and federal laws⁴**

As shown in the table below, a charter holder’s financial performance for the most recent audited fiscal year and the prior audited fiscal year are used to determine whether the charter holder meets the Board’s financial performance expectations.

Previous Audit	Most Recent Audit	Meets Board’s Financial Performance Expectations?
MEETS financial performance standard	MEETS financial performance standard	Yes
DOES NOT MEET financial performance standard	MEETS financial performance standard	Yes
MEETS financial performance standard	DOES NOT MEET financial performance standard; no measure receives “Falls Far Below Standard”	Yes

³ At the time of consideration by the Board, the most current audited financial information will be provided.

⁴ In these situations, a charter holder will be able to address its financial performance at the Board meeting, but an opportunity will not be built in to the process for the charter holder to provide a written response in advance of the meeting.

MEETS financial performance standard	DOES NOT MEET financial performance standard; 1 or more measures receive “Falls Far Below Standard”	No
DOES NOT MEET financial performance standard	DOES NOT MEET financial performance standard	No

A charter holder’s financial performance is represented in a dashboard format, which summarizes the charter holder’s performance on each measure. The financial performance dashboard (“dashboard”) reflects financial performance for the two most recent audited years, identifies whether the performance meets the Board’s expectations, and becomes publicly available through ASBCS Online after the audit is reviewed and the financial data entered by Board staff.⁵ Information about how to access and interpret the dashboards is available on the [Board’s website](#).

A charter holder that meets the Board’s financial performance expectations will be waived from submitting a financial performance response at the times identified on page 5 and in Appendix B. A charter holder that does not meet the Board’s financial performance expectations at the times identified on page 5 and in Appendix B will be **required to submit a financial performance response**. For more information regarding the financial performance response, please see Appendix C. If only one audit is available, a charter holder seeking to expand its operations must meet the Board’s financial performance standard in order to be waived from submitting a financial performance response.

MEASURES IN DETAIL

This section describes each of the measures included in the financial framework. A charter holder’s financial performance is evaluated annually using the charter holder’s most recent audit reporting package. It is important to note that the financial framework excludes measures of how a charter holder manages and expends its funds as the financial framework is not designed to evaluate a charter holder’s spending decisions. For example, there are no measures that address what portion of the costs are for direct instruction; rather the measures focus on the overall expenses versus the offsetting revenues. The financial framework analyzes the financial performance of a charter holder, not its processes for managing that performance.

1a. Going Concern – Near-Term Indicator

Definition: Going concern is the idea that the charter holder will continue to engage in its activities for the foreseeable future.

⁵ In those instances where the Board receives financial statements that cover multiple and different charter holder entities, the charter holder’s dashboard will include both the charter holder’s financial performance and the financial performance of the consolidated/combined entity. (See also footnote 2.)

Overview: Auditing standards require an auditor to evaluate an organization’s ability to continue operating for the next year. If the auditor has substantial doubt about whether the organization will operate for at least the next year, then the independent auditor’s report would include a paragraph explaining this concern and information, including management’s plans, would be disclosed in the notes to the audited financial statements. The auditor’s consideration of management’s plans may alleviate the “substantial doubt” about the organization’s ability to continue operating. In those instances, the auditor may disclose in the notes to the audited financial statements the conditions and events that initially caused the auditor to believe there was substantial doubt, but wouldn’t include a paragraph in the independent auditor’s report.

Source of Data: Independent Auditor’s Report on the financial statements and the notes to the audited financial statements.

1a. Going Concern
<p>Meets Standard:</p> <p><input type="checkbox"/> The most recent audit reporting package does not include explanatory paragraph in Independent Auditor’s Report or disclosure in the notes to the financial statements</p>
<p>Does Not Meet Standard:</p> <p>No “Does Not Meet Standard” target established for this measure</p>
<p>Falls Far Below Standard (in one of two ways):</p> <p><input type="checkbox"/> Independent Auditor’s Report for the most recent audit reporting package includes an explanatory paragraph and disclosure is included in notes to the financial statements</p> <p>or</p> <p><input type="checkbox"/> Disclosure included in notes to the financial statements for the most recent audit reporting package, but no modification to Independent Auditor’s Report</p>

Basis for Target Level: If the audit reporting package includes a going concern disclosure in the independent auditor’s report or the notes to the audited financial statements, then the independent auditor has concerns about the charter holder’s viability. A charter holder in this situation may have difficulty meeting operational and academic obligations required under law and its charter contract.

1b. Unrestricted Days Liquidity – Near-Term Indicator

Definition: The unrestricted days liquidity measure indicates how many days a charter holder can pay its expenses without an influx of cash.

Overview: Unexpected costs arise when operating a charter school. Additionally, circumstances outside of the charter holder’s control may impact the amount and timing of funding received from the State and other sources. Therefore, maintaining a reserve is a common best practice. The unrestricted days liquidity measure translates into a more readily understandable number a charter holder’s unrestricted cash balance and available balances from other sources of liquidity disclosed in the annual audit reporting package, including lines of credit. Please note that the Board will not round numbers when determining a charter holder’s financial performance on this measure.

A.R.S. §15-977 limits how Classroom Site Fund (CSF) monies may be spent. Therefore, if a charter holder does not spend all of the CSF monies it received during the fiscal year, then at the end of the year, the charter holder needs to have enough cash in the bank to cover the unspent portion from current and prior years (“carryover”). Since the CSF carryover monies may only be used for the purposes specified in statute, any year-end CSF cash carryover balance will be removed when determining the charter holder’s unrestricted cash.

Source of Data: Audited statement of financial position, audited statement of activities and changes in net assets, notes to the audited financial statements, and compliance questionnaire⁶.

<p>1b. Unrestricted Days Liquidity: (Unrestricted Cash + Other Sources of Liquidity*) divided by (Total Expenses/365)</p> <p>* “Other Sources of Liquidity” is defined as available balances from any sources of liquidity other than cash that are disclosed in the annual audit reporting package and may include, but not be limited to, lines of credit.</p> <p>[Note: The Classroom Site Fund cash carryover balance at June 30th would be considered restricted cash and, therefore, would be removed as part of identifying a charter holder’s unrestricted cash as of June 30th.]</p>
<p>Meets Standard:</p> <p><input type="checkbox"/> 30 or more days liquidity</p>
<p>Does Not Meet Standard:</p> <p><input type="checkbox"/> At least 15 days liquidity but fewer than 30 days liquidity</p>
<p>Falls Far Below Standard:</p> <p><input type="checkbox"/> Fewer than 15 days liquidity</p>

Basis for Target Level: Having access to cash or other sources of liquidity equaling at least 30 days of operating expenses is a standard minimum for any organization. In the event of unforeseen circumstances (e.g., unexpected costs, changes to State funding), 30 days of cash or other liquidity would help the charter holder make payroll, pay the rent, and keep the charter school’s doors open until the charter holder receives its next State equalization payment or until other funding is secured. If a charter holder has fewer than 15 days of cash or other liquidity, should unforeseen circumstances arise, the charter holder may have difficulty making its next payroll and meeting other obligations before receiving its next influx of cash.

1c. Default – Near-Term Indicator

Definition: Default indicates that a lender has issued a formal notice of loan default to the charter holder.

Overview: In addition to making timely payments, financial institutions may include other terms and requirements (sometimes referred to as “covenants”) in their agreements with charter holders. Individuals who make loans to charter holders may establish agreements with similar requirements. Failure to make timely payments or comply with debt covenants does not automatically result in a formal notice of default being issued by the lender and therefore would not be considered a “material” default. However, in those cases where formal notice of default has been issued by the lender, this measure will be rated “Falls Far Below Standard”.

⁶ For fiscal years prior to and including 2011, the year-end Classroom Site Fund cash carryover was not required to be disclosed in the audit reporting package. Beginning with fiscal year 2012, the year-end CSF cash carryover must, at a minimum, be disclosed in the Classroom Site Fund section of the applicable compliance questionnaire.

Source of Data: Notes to the audited financial statements.

1c. Default: Defined as in True Default on Obligations
Meets Standard: <input type="checkbox"/> Charter holder is not in default on material loans
Does Not Meet Standard: No "Does Not Meet Standard" target established for this measure
Falls Far Below Standard: <input type="checkbox"/> Charter holder is in default on material loans

Basis for Target Level: A charter holder that has received formal notice of default from a lender may be at higher risk of financial distress and may have difficulty meeting its operational and academic obligations required under law and the charter contract.

2a. Net Income – Sustainability Indicator

Definition: Net income, which equals total revenues less total expenses, looks at whether or not a charter holder is operating within its available resources.

Overview: The net income measure identifies whether a charter holder operates at a surplus (total revenues exceed total expenses) or a deficit (total expenses exceed total revenues). It should be noted that a charter holder may make a strategic choice to operate at a deficit for a year. Continued deficits for a sustained period of time could adversely affect the charter holder's ability to meet its obligations.

Source of Data: Audited statement of activities and changes in net assets.

2a. Net Income: Total Revenues less Total Expenses
Meets Standard: <input type="checkbox"/> Net income is greater than or equal to \$1
Does Not Meet Standard: <input type="checkbox"/> Net income is zero or negative
Falls Far Below Standard: No "Falls Far Below Standard" target established for this measure

Basis for Target Level: Positive net income contributes to the charter holder's reserve. Having a reserve gives the charter holder more flexibility in responding as situations arise that are outside of the charter holder's control. The targets established for this measure focus on whether the charter holder operated during the fiscal year with a surplus or deficit rather than the magnitude of the surplus or deficit.

2b. Cash Flow – Sustainability Indicator

Definition: The cash flow measure shows the change in a charter holder’s cash balance from one fiscal year to another.

Overview: This measure is similar to the unrestricted days liquidity measure, but looks at longer term financial stability versus near-term financial health. Since cash flow fluctuations from year-to-year can have a long-term impact on the charter holder’s financial health, this measure assesses three-year cumulative cash flow. For information regarding the underlying factors that have contributed to the annual cash flow fluctuations experienced by the charter holder, please review the audited statement of cash flows. If the Board has received only one or two audit reporting packages at the time of review, the charter holder’s financial performance under this measure will be evaluated using the information available.

<p>Cash Flow Calculation Example</p> <p>Calculate the annual cash flow: FY2012 Cash Flow = FY2012 Total Cash – FY2011 Total Cash FY2011 Cash Flow = FY2011 Total Cash – FY2010 Total Cash FY2010 Cash Flow = FY2010 Total Cash – FY2009 Total Cash</p> <p>Add together the FY2012 Cash Flow, FY2011 Cash Flow, and FY2010 Cash Flow to determine the three-year cumulative cash flow.</p>

For each fiscal year, the cash flow equals the current year’s total cash minus the prior year’s total cash. Adding the cash flow for each of the three fiscal years together will provide the three-year aggregate cash flow. The “Cash Flow Calculation Example” textbox found on this page shows how to calculate the cash flow measure using fiscal year 2012 as the most recent audited fiscal year available.

Source of Data: Audited statement of financial position.

<p>2b. Cash Flow: One-Year Cash Flow = Current Year Total Cash less Prior Year Total Cash</p>
<p>Meets Standard:</p> <p><input type="checkbox"/> Three-year cumulative cash flow is positive</p>
<p>Does Not Meet Standard:</p> <p><input type="checkbox"/> Three-year cumulative cash flow is negative</p>
<p>Falls Far Below Standard:</p> <p>No “Falls Far Below Standard” target established for this measure</p>

Basis for Target Level: Cash flow should be greater than zero as a positive cash flow over time generally indicates increasing financial health and sustainability of the charter holder.

2c. Fixed Charge Coverage Ratio – Sustainability Indicator

Definition: The fixed charge coverage ratio looks at the amount of cushion in the charter holder’s cash flow to cover fixed obligations or charges.

Overview: Fixed charges represent the charter holder’s fixed financial commitments. These charges occur regardless of changes in revenue or other circumstances that may affect the charter holder’s financial situation, which is why the term “fixed” is used. For this ratio, fixed charges would include lease payments, loan payments, and interest.

The ratio includes interest and lease expense in both the numerator and denominator even though it appears that in the end they would cancel each other out. This has been done for two

reasons. First, because the ratio components are more encompassing, it helps in determining the true cushion in cash flow to cover fixed obligations. Second, if the ratio's numerator included only change in net assets, depreciation and amortization and the denominator was unchanged, the ratio would solve for a charter holder's ability to meet lease and interest expense payments after it has already paid lease and interest expense, because lease and interest expense have already been deducted to arrive at the change in net assets.

The individual ratio components are described in more detail below:

- *Change in Net Assets* – The change in net assets results from revenues, expenses and the release of assets from restrictions. For for-profit charter holders, the ratio would use net income after tax instead of change in net assets.
- *Depreciation* – Depreciation is the allocation of a fixed asset's costs over the useful life of the asset and involves the movement of costs from the statement of financial position to the statement of activities and changes in net assets. Fixed assets include items such as buildings, furnishings and vehicles. Depreciation is known as a noncash expense. Although charter holders are required to record this expense in their accounting records, depreciation does not use cash. Therefore, depreciation is added back into the ratio's numerator.
- *Amortization* – Amortization is similar to depreciation but it involves the allocation of an intangible asset's costs over a period of time. Intangible assets include items such as bond issuance costs. Although charter holders are required to record this expense, as applicable, in their accounting records, amortization does not use cash. Therefore, amortization is added back into the ratio's numerator.
- *Interest Expense* – Interest expense reflects the charter holder's cost of borrowing for the fiscal year. As a result of the accounting method charter holders are required to use, interest expense may not equal the amount of interest paid to lenders. Interest paid reflects the cash paid to lenders for interest and may be higher or lower than the interest expense for the fiscal year. In calculating the ratio, the dollar amount used for "interest expense" would also be used for "interest".
- *Lease Expense* – Lease expense includes facility leases and operating leases where at the end of the lease ownership of the item does not transfer to the charter holder.
- *Current Portion of Long-Term Debt and Capital Leases (CPLTDCL)* – The CPLTDCL includes the portion of debt that must be paid by the charter holder within the next fiscal year. The "current portion of long-term debt" would include bond/loan payments for charter holders that own their facilities, as well as payments related to other long-term loans obtained by the charter holder and capital leases.

Please note that the Board will not round numbers when determining a charter holder's financial performance on this measure.

Source of Data:

- Changes in Net Assets – Audited statement of activities and changes in net assets.
- Depreciation and Amortization – Audited statement of cash flows and/or notes to the audited financial statements.
- Interest Expense – Notes to the audited financial statements. Interest expense may also be available on the audited statement of activities and changes in net assets, if the statement includes sufficient detail, or the statement of functional expense, if available.

If interest expense cannot be determined, interest paid may be used and is found on the statement of cash flows.

- Lease Expense – Notes to the audited financial statements.
- Current Portion of Long-Term Debt and Capital Leases – Audited statement of financial position.

2c. Fixed Charge Coverage Ratio: $(\text{Change in Net Assets}^* + \text{Depreciation} + \text{Amortization} + \text{Interest Expense} + \text{Lease Expense}) / (\text{Current Portion of Long-Term Debt and Capital Leases} + \text{Interest} + \text{Lease Expense})$

** Net Income After Tax would be used when calculating the ratio for for-profit charter holders.*

Meets Standard:

Fixed Charge Coverage Ratio is equal to or exceeds 1.10

Does Not Meet Standard:

Fixed Charge Coverage Ratio is less than 1.10

Falls Far Below Standard:

No "Falls Far Below Standard" target established for this measure

Basis for Target Level: Financially healthy entities have a cushion in cash flow coverage. The 1.1 used in the "meets" target is typical for non-profit organizations. Since capitalized expenses, such as buses and equipment, are not included in the statement of activities and changes in net assets, they need to be covered by the cushion in cash flow or through outside financing. Another benefit of excess cash flow is that a charter holder can build up cash and equity to purchase larger assets, such as a building. Since banks will only finance up to a certain amount of the building, the difference needs to be funded by the charter holder. The only way to build up cash/equity is through retention of the earnings cushion or from an injection of equity from an outside source. Charter holders that operate where fixed charges are only covered at 1:1 will not have the same flexibility as those that generate cash flow in excess of that level.

Appendix A

Financial Performance Framework

Board Strategic Plan Objective: All charter holders in the portfolio are viable organizations with strong fiscal management practices.

1. NEAR-TERM INDICATORS

1a. Going Concern

Meets Standard:

The most recent audit reporting package does not include explanatory paragraph in Independent Auditor’s Report or disclosure in the notes to the financial statements

Does Not Meet Standard:

No “Does Not Meet Standard” target established for this measure

Falls Far Below Standard (in one of two ways):

Independent Auditor’s Report for the most recent audit reporting package includes an explanatory paragraph and disclosure is included in notes to the financial statements

or

Disclosure included in notes to the financial statements for the most recent audit reporting package, but no modification to Independent Auditor’s Report

1b. Unrestricted Days Liquidity: $(\text{Unrestricted Cash} + \text{Other Sources of Liquidity}^*) \text{ divided by } (\text{Total Expenses}/365)$

* “Other Sources of Liquidity” is defined as available balances from any sources of liquidity other than cash that are disclosed in the annual audit reporting package and may include, but not be limited to, lines of credit.

[Note: The Classroom Site Fund cash carryover balance at June 30th would be considered restricted cash and, therefore, would be removed as part of identifying a charter holder’s unrestricted cash as of June 30th.]

Meets Standard:

30 or more days liquidity

Does Not Meet Standard:

At least 15 days liquidity but fewer than 30 days liquidity

Falls Far Below Standard:

Fewer than 15 days liquidity

1c. Default: Defined as in True Default on Obligations

Meets Standard:

Charter holder is not in default on material loans

Does Not Meet Standard:

No “Does Not Meet Standard” target established for this measure

Falls Far Below Standard:

Charter holder is in default on material loans

2. SUSTAINABILITY INDICATORS

2a. Net Income: Total Revenues less Total Expenses

Meets Standard:

Net income is greater than or equal to \$1

Does Not Meet Standard:

Net income is zero or negative

Falls Far Below Standard:

No "Falls Far Below Standard" target established for this measure

2b. Cash Flow: One-Year Cash Flow = Current Year Total Cash less Prior Year Total Cash

Meets Standard:

Three-year cumulative cash flow is positive

Does Not Meet Standard:

Three-year cumulative cash flow is negative

Falls Far Below Standard:

No "Falls Far Below Standard" target established for this measure

2c. Fixed Charge Coverage Ratio: $(\text{Change in Net Assets}^* + \text{Depreciation} + \text{Amortization} + \text{Interest Expense} + \text{Lease Expense}) / (\text{Current Portion of Long-Term Debt and Capital Leases} + \text{Interest} + \text{Lease Expense})$

* Net Income After Tax would be used when calculating the ratio for for-profit charter holders.

Meets Standard:

Fixed Charge Coverage Ratio is equal to or exceeds 1.10

Does Not Meet Standard:

Fixed Charge Coverage Ratio is less than 1.10

Falls Far Below Standard:

No "Falls Far Below Standard" target established for this measure

Appendix B

Financial Expectations Not Met: Charter Holder Action & Board Consideration

For charter holders that do not meet the Board’s financial performance expectations, the table below specifies by monitoring, expansion or transfer area what the charter holder must do and how that information will be used by the Board in its decision-making. This table in no way precludes the Board from considering a charter holder’s financial performance or from assigning a financial performance response at other times when the Board makes decisions related to a charter holder’s academic performance and/or compliance with its charter and state and federal laws.

	Charter Holder Action	Board Consideration
Academic Performance Framework (Monitoring)	<p>If a charter school operated by the charter holder has failed to meet the Board’s academic performance standard for three consecutive years <u>and</u> the charter holder does not meet the Board’s financial performance expectations, the charter holder must submit a financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C.</p>	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. The charter holder’s financial performance response and the evaluation instrument completed by staff will be provided to the Board when the Board considers the charter holder’s academic performance. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years (if three years are available) will be included in the staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents.</p> <p>The charter holder’s financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>
Arizona Online Instruction (AOI) Program of Instruction Amendment Request (Expansion)	<p>The charter holder must submit:</p> <ul style="list-style-type: none"> • A financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C. • A start-up budget to cover expenses projected to occur during the start-up period (until August 1 of the year the school opens). • An operational budget to cover the first-year of operations. • For each budget, a separate document describing assumptions for each line item, to include disaggregated costs, and basis for determining those costs. 	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. Additionally, Board staff will review the start-up and operational budgets and assumptions. The charter holder’s financial performance response, including the start-up budget, operational budget and assumptions, as well as the evaluation instrument completed by staff will be provided to the Board when the Board considers the amendment request. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in the staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents.</p>

	<p>Demonstrate through the assumptions that the amounts listed are viable and adequate for the start-up period and first year of operation.</p> <p>If the charter holder submits the amendment request prior to the Board receiving the charter holder’s first audit reporting package, then the charter holder must submit:</p> <ul style="list-style-type: none"> • Internal, unaudited financial statements for the fiscal year(s) to date. • A start-up budget to cover expenses projected to occur during the start-up period (until August 1 of the year the school opens). • An operational budget to cover the first-year of operations. • For each budget, a separate document describing assumptions for each line item, to include disaggregated costs, and basis for determining those costs. Demonstrate through the assumptions that the amounts listed are viable and adequate for the start-up period and first year of operation. 	<p>The charter holder’s financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>
<p>Failing School Designation (Monitoring)</p>	<p>The charter holder must submit a financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C.</p>	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. The charter holder’s financial performance response and the evaluation instrument completed by staff will be provided to the Board when the Board considers whether to revoke or restore the charter of the failing school. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in the staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents.</p> <p>The charter holder’s financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>
<p>Five-Year Interval Review (Monitoring)</p>	<p>The charter holder must submit a financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the</p>	<p>Board staff will review the charter holder’s financial performance response and evaluate it in accordance with Appendix C. A copy of the completed evaluation instrument will be placed in the charter holder’s DMS in ASBCS Online.</p> <p>The Board may consider the charter holder’s</p>

	<p>financial performance response, please see Appendix C.</p>	<p>financial performance at the time of the interval review. In these instances, Board staff will review the financial performance response and evaluate it in accordance with Appendix C. The charter holder’s financial performance response and the evaluation instrument completed by staff will be provided to the Board when the Board considers the charter holder’s performance at the time of the interval review. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in the staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents. The charter holder’s financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>
<p>New School Site Notification Request (Expansion)</p>	<p>The charter holder must submit:</p> <ul style="list-style-type: none"> • A financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C. • A start-up budget to cover expenses projected to occur during the start-up period (until August 1 of the year the school opens). • An operational budget to cover the first-year of operations. • For each budget, a separate document describing assumptions for each line item, to include disaggregated costs, and basis for determining those costs. Demonstrate through the assumptions that the amounts listed are viable and adequate for the start-up period and first year of operation. <p>If the charter holder submits the notification request prior to the Board receiving the charter holder’s first audit reporting package, then the charter holder must submit:</p> <ul style="list-style-type: none"> • Internal, unaudited financial statements for the fiscal year(s) to date. • A start-up budget to cover expenses projected to occur during the start-up 	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. Additionally, Board staff will review the start-up and operational budgets and assumptions. The charter holder’s financial performance response, including the start-up budget, operational budget and assumptions, as well as the evaluation instrument completed by staff will be provided to the Board if the Board considers the notification request. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in any staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents.</p> <p>The charter holder’s financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>

	<p>period (until August 1 of the year the school opens).</p> <ul style="list-style-type: none"> • An operational budget to cover the first-year of operations. • For each budget, a separate document describing assumptions for each line item, to include disaggregated costs, and basis for determining those costs. Demonstrate through the assumptions that the amounts listed are viable and adequate for the start-up period and first year of operation. 	
<p>Renewal Application Package (Monitoring)</p>	<p>The charter holder must submit a financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C.</p>	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. The charter holder’s financial performance response and the evaluation instrument completed by staff will be provided to the Board when the Board considers the charter holder’s renewal application package. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in the staff report provided to the Board, as well as an analysis prepared by staff of the charter holder’s financial performance, focusing on those measures where the charter holder failed to meet the Board’s target and using information from the charter holder’s response and related documents.</p> <p>If the charter holder is not meeting the Board’s academic performance expectations and/or is not complying with statutory and contractual requirements, the charter holder’s financial performance may be considered as an aggravating factor by the Board in its decision about whether or not to renew the charter contract.</p>
<p>Replication Application Package (Expansion)</p>	<p>The charter holder must submit:</p> <ul style="list-style-type: none"> • A financial performance response that addresses each measure for the most recent audited fiscal year presented in the dashboard where the charter holder received a “Does Not Meet Standard” or a “Falls Far Below Standard”. For additional information regarding the financial performance response, please see Appendix C. • A start-up budget to cover expenses projected to occur during the start-up period (until August 1 of the year the school opens). • A three-year operational budget to 	<p>Board staff will review the financial performance response and evaluate it in accordance with Appendix C. Additionally, Board staff will review the start-up and operational budgets and assumptions. The charter holder’s financial performance response, including the start-up budget, operational budget and assumptions, as well as the evaluation instrument completed by staff will be provided to the Board when the Board considers the replication application package. Additionally, a table showing the charter holder’s financial data and financial performance for the last three audited fiscal years will be included in the staff report</p>

	<p>cover expenses projected to occur during the first three years of operation.</p> <ul style="list-style-type: none"> • For each budget, a separate document describing assumptions for each line item, to include disaggregated costs, and basis for determining those costs. Demonstrate through the assumptions that the amounts listed are viable and adequate for the start-up period and first three years of operation. <p>The templates for the replication start-up budget and three-year operational budget are available on the Board's website.</p>	<p>provided to the Board, as well as an analysis prepared by staff of the charter holder's financial performance, focusing on those measures where the charter holder failed to meet the Board's target and using information from the charter holder's response and related documents.</p> <p>The charter holder's financial performance may be considered by the Board as an aggravating factor in its decision-making.</p>
<p>Transfer Application Package Involving the Transfer of the Charter Contract from Another Sponsor to the Board (Transfer)</p>	<p><i>Charter holders that want to transfer their charter contracts to the Board should contact the Board at (602) 364-3080 for the requirements.</i></p>	<p>If the charter holder is not meeting the Board's academic performance expectations and/or is not complying with statutory and contractual requirements, the charter holder's financial performance may be considered as an aggravating factor by the Board in its decision about whether or not to transfer the charter contract.</p>

Appendix C

Financial Performance Response & Evaluation

Financial Performance Response

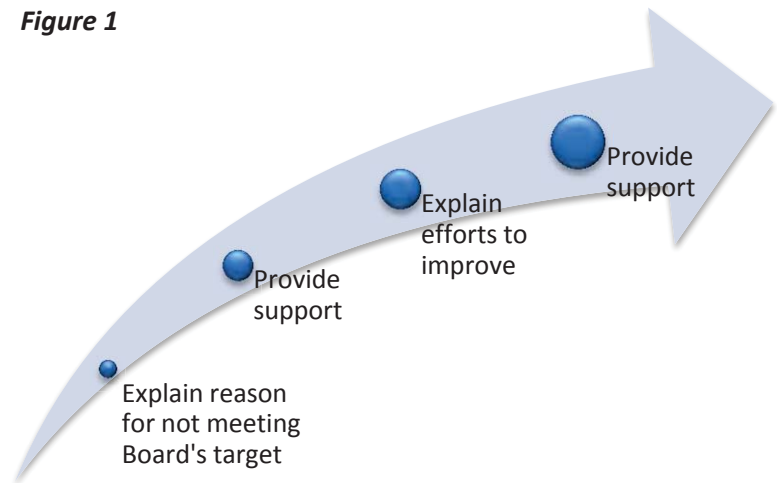
A charter holder that does not meet the Board’s financial performance expectations will be required to submit a financial performance response (“Response”) at specified times (see Appendix B). The Response provides the charter holder with the opportunity to explain its financial performance and efforts to improve.

What Must Be Covered

Through the Response, the charter holder must answer three questions for each measure where the charter holder received a “Does Not Meet Standard” or “Falls Far Below Standard” for the **most recent audited fiscal year presented in the dashboard:**

1. Why did we not meet the measure’s target in the audited fiscal year?
2. What specifically have we done to improve our performance so that it’s possible to meet the measure’s target in the next fiscal year or a subsequent fiscal year?
3. What can we provide to support our explanations and analysis?

Figure 1



Where to Begin

As counterintuitive as it may seem, the first step in preparing the Response shouldn’t be to pore over the financial records, but rather to step back and identify what changed or happened with the charter holder from the prior year to the most recent audited fiscal year presented in the dashboard. The accounting records and the resulting financial statements are not the cause of the financial performance. Instead, they show the effect of decisions made by or for the charter holder during the fiscal year. Once you know what happened, then you can go to the financial statements and records to see how what happened affected the charter holder’s financial performance in the most recent audited fiscal year presented in the dashboard and to identify improvement in the next or subsequent fiscal year.

Show and Tell

Adopt a “show us, don’t just tell us” approach to your Response. While Figure 1 illustrates the Response’s necessary components, it should not be interpreted as requiring the Response to include equal parts explanation (“tell us”) and support (“show us”). Generally, the easiest and best way to explain why the measure’s target was not met and the efforts to improve is to show us through accounting system or management reports, interim financial statements, projections, forecasts, or supplemental worksheets.¹ The narrative is then used to briefly provide the context and to point us to the relevant portions of the supporting documentation. Please see the [Board’s website](#) for additional guidance and technical assistance on preparing a Response.

Financial Performance Response Evaluation

Board staff evaluates each submitted Response. For a Response to be evaluated as “Acceptable”, the Response must include the four components identified in Figure 1 for each applicable measure.

¹ Board staff has access to the annual audit reporting packages, publicly available Arizona Department of Education (ADE) attendance and state funding reports, and the charter holders’ budgets submitted to ADE. Therefore, these documents may be referenced in, but do not need to be provided with, the Response.

Appendix D

Definition of Terms

AUDIT – A systematic collection of the sufficient, competent evidential matter needed to attest to the fairness of management's assertions in the financial statements or to evaluate whether management has efficiently and effectively carried out its responsibilities. The auditor obtains this evidential matter through inspection, observation, inquiries, and confirmations with third parties.

AUDIT REPORTING PACKAGE – The annual audit required by A.R.S. §15-914 includes several components, including the financial statements, a report on internal control and compliance required under auditing standards, the applicable compliance questionnaire(s), and the management letter, if one is issued by the audit firm. For a charter holder that expends more than \$500,000 in federal awards (e.g., federal grants), the audit reporting package submitted would include additional information and documents.

COMPLIANCE QUESTIONNAIRE – As part of the annual audit required by A.R.S. §15-914, the auditor must complete the appropriate compliance questionnaire(s). The compliance questionnaires assist the Board in determining whether a charter holder is complying with certain legal and contractual requirements. The Board currently issues three compliance questionnaires – the Legal Compliance Questionnaire, the USFRCS Compliance Questionnaire¹, and the Procurement Compliance Questionnaire. For most charter holders, the Legal Compliance Questionnaire is the only compliance questionnaire that must be completed.

FINANCIAL AUDIT – An audit made by an independent external auditor for the purpose of issuing an audit opinion on the fair presentation of the financial statements in conformity with GAAP. Refer to AUDIT.

FISCAL YEAR – The twelve-month period that begins on July 1st and ends on June 30th.

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP) – These are the uniform minimum standards for financial accounting and reporting. They govern the form and content of the financial statements of an entity. GAAP encompass the conventions, rules, and procedures necessary to define accepted accounting practice at a particular time. They include not only broad guidelines of general application, but also detailed practices and procedures. The primary authoritative body on the application of GAAP for most charter holders is the Financial Accounting Standards Board.

NOTES TO THE AUDITED FINANCIAL STATEMENTS – Sometimes referred to as disclosure notes, the notes follow immediately after the financial statements. In addition to summarizing certain accounting policies used by the charter holder, the financial statements may include information regarding leases the charter holder has entered into, loans the charter holder has received (sometimes referred to as “notes”) and its compliance with loan terms, and restrictions on the charter holder’s cash.

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS – This financial statement shows what made up the charter holder’s revenue and expenses for the fiscal year. Generally, revenue is shown by type and expenses are shown by program type (i.e., program services, management and general). This statement also shows whether a charter holder operated at a surplus (total revenues exceed total expenses) or a deficit (total expenses exceed total revenues), as well as the change in net assets. This statement is also referred to as the income statement (for-profit) or the statement of activities (governmental).

STATEMENT OF CASH FLOWS – This financial statement shows where the charter holder’s cash came from and how the cash was used during the fiscal year. It categorizes cash activity as resulting from operating, investing, and capital and related financing activities.

¹ USFRCS stands for Uniform System of Financial Records for Charter Schools.

STATEMENT OF FINANCIAL POSITION – This financial statement shows the charter holder’s assets, liabilities, and net assets as of June 30th. Assets are what the charter holder owns, liabilities are what the charter holder owes, and net assets are the difference between the two. Net assets represent any surpluses (total assets exceed total liabilities) or deficits (total liabilities exceed total assets) that have accumulated since the charter holder was formed. This statement is also referred to as the balance sheet (for-profit) or the statement of net assets (governmental).

STATEMENT OF FUNCTIONAL EXPENSE – This financial statement shows a detailed breakdown of expenses by expense type and by program and supporting services. While not required for charter holder audits, some audit reporting packages received by the Board include this additional statement.

IN THE SUPERIOR COURT OF THE STATE OF ARIZONA
IN AND FOR THE COUNTY OF MARICOPA

LEGACY EDUCATION GROUP, et al.,

Plaintiffs,

v.

ARIZONA STATE BOARD FOR CHARTER
SCHOOLS,

Defendant.

No. CV 2016-051845

Phoenix, Arizona
October 14, 2016
1:31 p.m.

BEFORE THE HONORABLE JOHN R. HANNAH, JR.

TRANSCRIPT OF PROCEEDINGS

Oral Argument

Proceedings recorded by electronic sound recording; transcript
produced by AVTranz.

LUCI CLARK
Transcriptionist

I N D E X

October 14, 2016

<u>PLAINTIFFS' WITNESSES</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VD</u>
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None

<u>DEFENDANT'S WITNESSES</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VD</u>
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None

M I S C E L L A N E O U S

PAGE

Court's Ruling

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APPEARANCES

October 14, 2016

Judge: John R. Hannah, Jr.

For the Plaintiffs:

Lynne C. Adams

Roger W. Hall

Witnesses:

None

For the Defendant:

Kim S. Anderson

Leslie K. Cooper

Witnesses:

None

1 Phoenix, Arizona

2 October 14, 2016

3 (The Honorable John R. Hannah, Jr. Presiding)

4 ORAL ARGUMENT:

5 THE COURT: This is Legacy Education Group versus
6 Arizona State Board for Charter Schools CV 2016-051845.
7 Counsel, please introduce yourselves.

8 MR. HALL: Good afternoon, Your Honor. Roger Hall on
9 behalf of the Plaintiffs, Legacy Education Group dba East
10 Valley High School and Tucson Preparatory School. With me is
11 Plaintiffs' co-counsel, Lynne Adams.

12 MS. ANDERSON: Kim Anderson representing the Arizona
13 State Board for Charter Schools. And with me as co-counsel is
14 Leslie Cooper.

15 THE COURT: All right. This is the time set for
16 argument on the motions that have been filed. I just now
17 printed and read the Plaintiffs' response to the Defendant's
18 request to take judicial notice.

19 I'm inclined just to let counsel -- rather than say
20 anything about what I'm going to consider or what the scope of
21 this is going to be given that this is a bit of a moving
22 target, I think I'm just going to let counsel argue and then
23 figure it out as we go along.

24 The original motion was a motion to dismiss the
25 complaint because the State has since moved -- cross moved for

1 summary judgment. I'm sort of inclined to let the Plaintiffs
2 go first under those circumstances as the proponents of action
3 on my part. I think that makes more sense from my point of
4 view. Then I'll hear from the other side. I'll hear from you
5 all again. If there's a reason to keep going after that I'm
6 open to that, but with that I'll give the Plaintiffs the floor
7 and --

8 MR. HALL: Thank you, Your Honor.

9 THE COURT: -- let you make your argument.

10 MR. HALL: Your Honor, your file is thick with
11 motions and responses, replies, cross motions, exhibits, but
12 this really isn't a complicated case. Under Arizona's
13 Administrative Procedure Act, the APA, nearly all state
14 agencies, including the Arizona State Board for Charter
15 Schools, are required to enact rules to regulate their
16 constituent entities.

17 In this case, those entities are the charter schools
18 throughout the state. The APA and case law interpreting the
19 APA which the charter schools, we cite in our briefing, make
20 clear that agencies like the Board are to govern by properly
21 noticed adopted and published rules, not simply via policies.

22 The Board, though, has done exactly what the APA
23 forbids. It regulates the charter schools under its
24 supervision through policy instead of through properly enacted
25 rules. And since the Board oversees nearly all of the charter

1 schools in the state, more than 96 percent, that affects all
2 the charter schools.

3 Now regarding the APA, to help agencies figure out
4 when they're supposed to enact rules, the APA provides a
5 definition of what a rule is. Bless you. A rule is "an agency
6 statement of general applicability that implements, interprets,
7 or prescribes law or policy or describes the procedure or
8 practice requirements of an agency."

9 Now that's a pretty long definition, but when you
10 boil it down what it means is if an agency issues a statement
11 that applies to all of its constituent entities and it tells
12 those entities you either have to do something or you have to
13 not do something, then that should be enacted as a rule.

14 And the public policy reasons behind this are fairly
15 straightforward when you think about it. They exist to allow
16 public participation in the regulatory process and to protect
17 the public. For instance, other provisions in the APA require
18 that there be public notice of an agency's rule-making. It has
19 to be done at an open meeting. There's a mandatory 30-day
20 public comment period. There's a provision for a hearing if
21 one is requested. The agency has to provide an economic
22 analysis of the effect the proposed rule will have on the
23 regulated entities. And the public can comment on that
24 economic analysis as well.

25 Both the opening of the rule-making process and the

1 final adoption of the rules must be done in a properly noticed
2 open meeting.

3 THE COURT: I've been struggling with this idea that
4 this is rule-making in the traditional sense. And you
5 mentioned economic analysis.

6 MR. HALL: Yes.

7 THE COURT: These are all state entities, right? A
8 charter school is -- what is a charter school exactly?

9 MR. HALL: A charter school --

10 THE COURT: What kind of entity is it?

11 MR. HALL: Certainly, Your Honor. A charter school
12 is defined by statute as a public school.

13 THE COURT: All right.

14 MR. HALL: It receives the bulk -- they receive the
15 bulk of their money from the state treasurer based on student
16 population. The same as a traditional district school.

17 THE COURT: All right.

18 MR. HALL: Now, they're created by entering into
19 what's called a charter contract with a sponsoring agency. A
20 sponsoring agency, as we've said, for 96 percent of the charter
21 schools in the state is the Arizona state ward for charter
22 schools. ASU sponsors some, you know, Board of Regents
23 universities can be sponsors.

24 THE COURT: So when a charter school is created, it's
25 created by a charter contract.

1 MR. HALL: Yes.

2 THE COURT: Is that the term you used? And the
3 charter contract is between the Board, the charter, the ones
4 that are sponsored by the charter court. The contract is
5 between the charter board and the folks who are going to
6 operate the school?

7 MR. HALL: Yes.

8 THE COURT: Is that correct?

9 MR. HALL: Yes.

10 THE COURT: Okay. Go ahead.

11 MR. HALL: Okay. So when adopting rules, the agency
12 has to do an economic impact analysis. The final -- or the
13 opening of the rule-making docket and the final adoption have
14 to be done in open meeting and before the rules become final,
15 the Governor's Regulatory Review Council, GRRC for short, has
16 to approve the rules.

17 THE COURT: I'm trying to get my head around the idea
18 that these are rules when the rules presumably are made by --
19 in the charter agreement in the first place and it's a public
20 entity. Why do we have rule-making? Why do we need to have
21 rules that are created by an agency that is overseeing public
22 schools? I'm having a bit of a hard time with that.

23 MR. HALL: Well, the Administrative Procedure Act
24 requires the enactment of the rules. Now certain broad
25 requirements exists in the charter contract but those are only

1 specific as to each school. Rules would affect all charter
2 schools --

3 THE COURT: But it's the State dealing with itself?

4 MR. HALL: I'm sorry, what?

5 THE COURT: It's the State dealing with itself. All
6 the rules that I know of are how the State deals with employees
7 or how the State deals with harbors or whoever. This is the
8 State dealing with itself.

9 MR. HALL: But it's not, Your Honor.

10 THE COURT: Why not?

11 MR. HALL: Because the charter --

12 THE COURT: If they're public schools.

13 MR. HALL: The charter contract is with a state
14 entity of the one hand, the State Board for Charter Schools.
15 And generally with a 501(c)(3) or --

16 THE COURT: Okay.

17 MR. HALL: -- some type of private entity on the
18 other side, the charter operators throughout the state even
19 though they run public schools they themselves are usually
20 private entities.

21 THE COURT: Yeah.

22 MR. HALL: So it's not --

23 THE COURT: Who are being given permission to do a
24 function for the State.

25 MR. HALL: They are given permission through the

1 contract to run public schools. Yes.

2 THE COURT: Let me ask you this.

3 MR. HALL: Yes.

4 THE COURT: This law that you're -- that's the
5 genesis of this lawsuit was passed when? 2012 or 2013?

6 MR. HALL: The frameworks, the policies that the
7 Charter Board is using to regulate charter schools were enacted
8 in 2012.

9 THE COURT: Okay. But the --

10 MR. HALL: The charter schools laws themselves were
11 enacted by the legislature back in the mid-90s.

12 THE COURT: All right. And the charter school board
13 has always had oversight responsibility.

14 MR. HALL: Yes.

15 THE COURT: If I were to say they should have gone
16 through the rule-making process. These rules are invalid.
17 What happens then? How do they then regulate or oversee the
18 charter schools?

19 MR. HALL: Okay. As I just alluded to, from the
20 mid-90s until 2012 there were none of these frameworks policies
21 in place.

22 THE COURT: Okay.

23 MR. HALL: And for the decade and a half the charter
24 school board still was able to deal with new site requests from
25 charter schools. They were able to deal with enrollment cap

1 increase requests. They were able to deal with grade level
2 increases. They were able to evaluate charter schools
3 performance. They did this.

4 THE COURT: And on what basis did they evaluate
5 charter school performance before that? I'm getting kind of
6 far afield, but you can see where I'm going here.

7 MR. HALL: No, I do understand. Presumably, they
8 have operational metrics in place to do that. And they --

9 THE COURT: And what's the --

10 MR. HALL: -- could go back to those.

11 THE COURT: So what's the difference? If we call
12 these -- if I were to say that these were guidelines and the
13 charter board has discretion to follow them, does that solve
14 the problem?

15 MR. HALL: No, it doesn't.

16 THE COURT: Why not?

17 MR. HALL: Because as I've been stepping through
18 these requirements, there was no opportunity for public input
19 in enacting these guidelines. You go through rule-making.
20 There's a mandatory 30-day public comment period. The charter
21 board did not have to do any type of economic analysis to
22 figure out what impact its frameworks were going to have on the
23 regulated entities. And in this case, that is significant.
24 The charter board would force charter schools to enter into
25 performance management agreements, demonstrations of sufficient

1 progress --

2 THE COURT: Sure, but they're public schools.

3 MR. HALL: -- conditional renewals.

4 THE COURT: Why can't the State just do that? Why
5 does the State need to go through -- why was that rule-making
6 when these are public schools in the first place?

7 MR. HALL: All state agencies have to go -- almost
8 all state agencies have to go through rule-making. State
9 Retirement System has to do it. AHCCCS has to do it. The
10 Board of Education has to do it. They don't just get to go
11 into their opening meeting and on 24 hours' notice issue
12 decrees. The public under the Administrative Procedure Act has
13 a right to be involved in how the agencies that serve that
14 public enact its rules.

15 THE COURT: Okay.

16 MR. HALL: And the rule-making process, the
17 Administrative Procedure Act, provides protections for the
18 public that don't exist when agencies simply govern by fiat.

19 THE COURT: Okay.

20 MR. HALL: Okay. And that leads me to my next point.
21 That none of these protections that I enumerated exist when an
22 agency just adopts policies. The public doesn't get a say.
23 The Governor's Regulatory Review Council doesn't get to oversee
24 the rules and approve them. There's no economic impact
25 analysis.

1 And as I was saying, the economic analysis is very
2 important here because the policies the Board was using when
3 schools got put on these performance plans they had to report
4 data quarterly. It was extremely expensive. Literally,
5 literally hundreds of man hours and tens of thousands of
6 dollars to submit all this data to the State Board for Charter
7 School staff.

8 And charter schools, for the most part, aren't rich.
9 They don't have staff to be doing all of this. You know, they
10 all have a principal that's also a teacher. An administrator
11 that's also maybe the CFO. And so when people are taken away
12 from their duties to have to do this, it hurts the students.
13 They're not big bureaucracies like school districts. And so
14 the economic effect is tremendous.

15 In enacting policies in any agency whatever comment
16 the public has, they don't get the 30 days' notice as under the
17 rule-making. They get whatever notice is provided in public
18 meeting. You know, they call the public. The charter board
19 gets three minutes per person per item. That's not enough time
20 to comment on an extensive frameworks package that applied to
21 all charter schools throughout the state. And so --

22 THE COURT: Oh, okay. Well, one of their other
23 arguments is that the -- it comes from the other sponsoring --
24 the other entities that have the authority to sponsor a charter
25 school don't have to go through all this. The -- including

1 school districts. If a school district creates a policy,
2 that's what you get. You get -- they have a meeting.
3 Everybody gets three minutes a shot to talk about it and then
4 they enact the policy. And that's perfectly good enough for a
5 school district. Did the legislature intend to create two
6 different regimes here?

7 MR. HALL: A couple of points on that. First, Your
8 Honor, school districts don't get the charter schools any more
9 effective, you know, within the next two years. They're not
10 going to have that authority. It was taken away from them in
11 statute.

12 But the second part is, you know, legislative intent,
13 I think that's beyond the scope of this oral argument. The
14 fact remains that the Administrative Procedure Act does apply
15 to the State Board for Charter Schools and the State Board for
16 Charter Schools is required to follow the Administrative
17 Procedure Act and enact rules to govern its regulated entities.

18 THE COURT: So every time that State Charter School
19 Board makes any kind of a policy that affects these hundreds of
20 schools, it has to go through formal rule-making?

21 MR. HALL: You know, it would depend on the policy,
22 but these policies are so broad and give the State Board for
23 Charter Schools so much power over the charter schools that
24 they regulate that yes, they should have gone through the
25 rule-making process.

1 THE COURT: Okay. Go ahead. Don't get thrown by the
2 fact that I'm behind the computer. It just means I'm --

3 MR. HALL: Okay.

4 THE COURT: -- looking something up. I'm listening,
5 too.

6 MR. HALL: Okay. So the first part of the APA's
7 definition of a rule is satisfied. These frameworks apply to
8 all the charter schools in the state. In other words, there's
9 statements of general applicability to the regulated entities.
10 And the Board even admits in its motion to dismiss that the
11 frameworks are the implementation of its statutory oversight
12 authority. You can see that on pages 3 and 4 of the motion to
13 dismiss.

14 So the second part of the definition of a rule is
15 also satisfied because the frameworks implement or interpret a
16 prescribed law or policy or describe the procedure or practice
17 requirements of the Board. So since both elements of the
18 definition of a rule are met, the frameworks are rules.

19 But this isn't news to the Board. And this is
20 important. More than three years ago back in September of
21 2013, the Auditor General advised the Board in writing that its
22 frameworks needed to be adopted as rules. The Auditor General
23 told the Board. The Board responded in writing. Said, you
24 know, Auditor General, we agree. We should adopt the
25 frameworks as rules. The Board didn't adopt the rules, though.

1 THE COURT: But that's not a judicial admission that
2 binds them here, is it?

3 MR. HALL: I don't think that's a judicial admission.

4 THE COURT: Okay.

5 MR. HALL: But I raise it to show that the Board -- I
6 mean, not in a judicial sense, but has acknowledged --

7 THE COURT: Okay.

8 MR. HALL: -- that it was told it needed to enact
9 rules. The Board did open a rule-making docket back in
10 February of 2014, but just let it die on the vine. The Board
11 didn't pursue that. Then in January of this year, Ms. Adams
12 and I sent a letter -- or a petition, actually, to the
13 Governor's Regulatory Review Council and said GRRC, these
14 frameworks are really rules in disguise. Exercise your
15 statutory authority and hold them to be void because they are
16 rules in disguise.

17 In response to that, Charter Board contacted
18 individual members of GRRC, persuaded them not to hold the
19 hearing but said if you don't hold this hearing we're going to
20 go ahead and open a new rule-making docket. So they opened
21 their docket in April. And then in October, October 4th
22 actually, the Board submitted their five year review to GRRC
23 for approval as part of the rule-making process.

24 THE COURT: Is that what they notified me of a couple
25 of weeks ago? No, that was notice of proposed --

1 MR. HALL: It was included in their -- the five year
2 report is Exhibit 1 to the Plaintiff's response that you read a
3 few minutes ago.

4 THE COURT: Oh, okay. Was that the context of the
5 notice of proposed rule-making that they -- their request to
6 take judicial notice --

7 MR. HALL: Right. No, it's actually two different
8 things. The --

9 THE COURT: Okay. That's what I'm trying to --

10 MR. HALL: The notice of proposed rule-making
11 includes a reference to that.

12 THE COURT: Okay.

13 MR. HALL: But it's not the notice of proposed
14 rule-making itself.

15 THE COURT: Okay.

16 MR. HALL: Okay. The five year report was submitted
17 to the Governor's Regulatory Review Council to support the
18 notice of proposed rule-making.

19 THE COURT: Okay.

20 MR. HALL: Five-year report was prepared by the
21 Charter Board, approved by GRRRC.

22 THE COURT: Okay.

23 MR. HALL: In the five-year report, the Board said it
24 intends to amend all the rules and make new rules to address
25 the issues raised in the petition. The petition being the

1 petition that Ms. Adams and I submitted to GRRC saying the
2 frameworks are rules in disguise.

3 So now they've told GRRC our rules are going to fix
4 what Mr. Hall and Ms. Adams complained about in their petition.
5 And again, I say all this not to try to bind them to any type
6 of judicial admission, but to show the Court that this isn't
7 news to the Board. They've known for a long time and
8 acknowledged either tacitly or directly that they should have
9 enacted rules. And the fact that they are now enacting rules
10 kind of goes right along with that.

11 The Board's also argued, probably because it has to,
12 that the frameworks aren't really rules. Those arguments seem
13 a bit half-hearted because if they weren't really rules why
14 would the five-year plan say they're going to amend its rules
15 to enact the frameworks as rules.

16 THE COURT: Well, I thought they said that even the
17 new -- under the notice of proposed rule-making, they wouldn't
18 be enacting the frameworks themselves as rules. Maybe I
19 misread that, but that's what I understand that they were
20 saying.

21 MR. HALL: In the notice of proposed rule-making,
22 they said that they were going to amend all the rules and make
23 new rules to address the issues raised in the petition.

24 THE COURT: Okay.

25 MR. HALL: And the petition said these frameworks are

1 rules in disguise. The main thrust of the argument --

2 THE COURT: You mean the petition -- the petition
3 that your folks -- the petition meaning what your folks filed a
4 few months ago.

5 MR. HALL: With GRRC, not with this Court.

6 THE COURT: Right.

7 MR. HALL: Yes. Okay.

8 THE COURT: Okay.

9 MR. HALL: The Board's main argument now is look,
10 Your Honor, we've opened our rule-making docket. We've done a
11 notice of proposed rule-making, what's the big deal? Well, it
12 is a big deal. The frameworks have been used and continue to
13 be used by the Board in taking negative action against charter
14 schools.

15 The statutes on which the Board relies or relied to
16 create the frameworks do authorize their use in revocation
17 decisions and in renewal decisions and to conduct five-year
18 reviews of charter schools. But that's it. That's as far as
19 the statutory authority for use of the frameworks extends.

20 Frameworks don't extend to deny charter schools grade
21 expansion requests. They don't extend to deny enrollment cap
22 increases by charter schools even when there's a waiting list
23 of students to get in. They don't exist to deny requests by
24 charter schools to add sites even when sites are bursting at
25 the seams. They don't exist to allow these onerous performance

1 management plans, demonstrations of sufficient progress,
2 conditional renewals, and heightened monitoring that costs the
3 schools so much in time and dollars.

4 And they definitely don't exist --

5 THE COURT: What are the -- I'm sorry. You got on a
6 little roll there and I stopped you.

7 MR. HALL: That's okay.

8 THE COURT: Are there rules or criteria that are
9 written down in the regulations that say under what
10 circumstances somebody can start a charter school?

11 MR. HALL: Very broadly, yes.

12 THE COURT: Okay. Broadly --

13 MR. HALL: And it says you have to submit an
14 application. It has to describe the -- broadly describe the
15 curriculum you're going to use. You have to submit fingerprint
16 requests, this type of thing.

17 THE COURT: Okay. It doesn't sound like there's
18 much, if anything, about the quality of education that you can
19 provide.

20 MR. HALL: The schools are required to meet the
21 Board's performance expectations. So it's pretty nebulous.

22 THE COURT: Which is what these frameworks are
23 intended to give substance to.

24 MR. HALL: That's what the Board argues, yes.

25 THE COURT: Okay.

1 MR. HALL: But again, they should have enacted as
2 rules.

3 THE COURT: The implication of your position is they
4 have to give everybody a charter and then revoke them one at a
5 time.

6 MR. HALL: Well, I don't think they have to give
7 everybody a charter. I mean, there's --

8 THE COURT: Then what's the basis for not giving them
9 a charter?

10 MR. HALL: If the application doesn't show that the
11 applicant is sufficiently qualified to open and operate a
12 charter school.

13 THE COURT: What do the rules say about
14 qualifications?

15 MR. HALL: Again, it's very, very broad. If you were
16 to --

17 THE COURT: It means you can get a fingerprint
18 clearance card.

19 MR. HALL: No, it's much more than that. The
20 application has to describe the curriculum, the program of
21 instruction. It's going to describe the grade -- excuse me --
22 the grade levels served, the methods by which student education
23 is going to be measured. They have to lay out a plan as to how
24 they're going to operate their charter. You know, it's not
25 just scribble a few lines on a piece of paper and get a

1 charter. It's an extensive process.

2 It gets submitted to Board staff. Board staff
3 reviews it. They offer assistance, technical assistance, in
4 getting the application cleaned up. The applicant goes back,
5 tries to fix any problems. It comes back to staff. It's quite
6 an involved process.

7 THE COURT: Okay.

8 MR. HALL: Okay. One last important thing the
9 frameworks have been used for that's not in statute. There's a
10 lot of schools that are Montessori schools, schools that have
11 other specialized learning models, schools that exist on
12 reservations that don't lend themselves to measurement by the
13 traditional metrics that the Board uses to evaluate schools.
14 But nevertheless, these other types of schools are forced to
15 comply with those metrics upon penalty of, you know,
16 potentially losing funding or worse even, being closed. Twenty
17 of twenty-five Native American charter schools that came up for
18 renewal got shut down by the Board.

19 And so none of this is in statute. The statute only
20 says you can use frameworks to renew, revoke, and do your
21 five-year reviews. So the Board has gone far, far beyond its
22 statutory mandate and using these frameworks for all sorts of
23 regulatory purposes. And these frameworks were adopted with
24 really -- no, really -- not at all following the rule-making
25 process.

1 And the Board functioned well, as we touched on
2 before, before it enacted these frameworks. It was still
3 evaluating schools. It was still evaluating these requests
4 from schools. It's not too much of a burden to ask the Board
5 to comply with the law that is written to apply with it.

6 And it's important that this Court step in and say
7 Board, you can't continue to enforce these frameworks because
8 they are rules in disguise. Because otherwise, the Board is
9 going to continue to enforce these frameworks until their
10 rule-making is finally, finally adopted. And we don't know
11 when that'll be.

12 THE COURT: So --

13 MR. HALL: They're projecting June of 2017. But
14 that's highly aspirational, Your Honor. Assuming the rules are
15 done by June of 2017, GRRC still gets 90 days to review them.
16 And if GRRC has zero changes they want made -- that's basically
17 a year from now that they'll be regulating by fiat instead of
18 through rules.

19 THE COURT: So --

20 MR. HALL: If GRRC has changes, it's going to be
21 longer.

22 THE COURT: Okay. One last question. I'm going to
23 -- I need to hear from the other side. What about the issue
24 that's been debated between the parties about the scope of
25 relief.

1 MR. HALL: Right.

2 THE COURT: Could you address that?

3 MR. HALL: Certainly. The first part that I just did
4 address that the frameworks shouldn't be allowed to be enforced
5 against charter schools anymore. The second part is that to
6 the extent possible, this should order the Board or order that
7 actions against charter schools that were improperly taken in
8 reliance on these frameworks that are rules in disguise should
9 be undone.

10 THE COURT: Defend that against the argument that
11 that's an end run around the administrative process and the
12 administrative appeal requirement.

13 MR. HALL: It's not an end run because if a policy
14 was void ab initio because it didn't go through the rule-making
15 process, it is not a defense to say oh well, we violated the
16 law in revoking your charter or not allowing you to expand in
17 violation of these laws that the Court has not said were
18 violations, too bad, too sad.

19 THE COURT: So is everything the Charter School Board
20 has done since 2012 or 1995 void then?

21 MR. HALL: I would not take that position, Your
22 Honor.

23 THE COURT: Okay. Then, tell me --

24 MR. HALL: Some actions --

25 THE COURT: Then tell me where the water line is.

1 MR. HALL: Right. And I don't think you can place a
2 particular date on that. Some actions are just too far in the
3 past to be undone. Some schools may have been closed. Many of
4 these reservation schools have closed. The charter operators
5 and the Board members and whoever have moved on to other
6 endeavors. Some, however, still exist.

7 THE COURT: So it's just a question of who's still
8 within the statute of limitations and who wants to bring --

9 MR. HALL: Yeah. It's --

10 THE COURT: -- lawsuit?

11 MR. HALL: It's not really a statute of limitations
12 issue, per say. I mean, if there's no community support for
13 the people who were originally involved, saying, you know, we
14 don't want to go through that again. We don't want to open up
15 another charter school. You can't make them do that, but there
16 are schools --

17 THE COURT: No, but wouldn't they have a cause of
18 action to say, you know, we were shut down illegally. We were
19 going to make X dollars. You know, we're owed damages.

20 MR. HALL: You know, that's kind of a law school
21 question, Your Honor, because as a practical --

22 THE COURT: No, except it's not --

23 MR. HALL: -- matter --

24 THE COURT: Except it's not academic at all. If I
25 were to issue an order like you're talking about, those kind of

1 suits would be filed.

2 MR. HALL: Some would.

3 THE COURT: Yeah.

4 MR. HALL: I don't think it would be in the hundreds
5 because people have moved on. Schools have moved on.
6 Corporations have dissolved. There might be some where action
7 was taken against schools in 2016, this year, maybe late 2015
8 that might try to seek some relief. And before that, there may
9 conceivably be causes of action. But as a practical matter, I
10 don't see those being pursued. There's nobody that's going to
11 be able to pay counsel on an hourly basis to pursue it. And,
12 you know, I represent charter schools all the time and I don't
13 see the potential recovery there for any type of contingent fee
14 litigation on that basis. So as a practical matter, I don't
15 think the floodgates would open.

16 But before we move on, before you turn things over to
17 the Charter Board, I don't want this Court to be distracted by
18 the potential difficulty in fashioning a perfect remedy.
19 Perfection should not be the enemy of the good. The difficulty
20 in fashioning that perfect remedy shouldn't prevent this Court
21 from following the law from finding that the Board has been
22 regulated by policy and not rule since 2012 and for halting
23 that in its tracks. And as much as it can, undoing the damage
24 that has been done by the regulation by fiat. Thank you, Your
25 Honor.

1 THE COURT: Thank you.

2 MS. ANDERSON: Good afternoon, Your Honor. Kim
3 Anderson for the State Board for Charter Schools. This case is
4 about whether the Charter Board's performance frameworks must
5 be promulgated as rules under the APA and the relief available
6 to the Plaintiffs if the Court decides that they must.

7 When we look at 15-183(R), the legislature acted to
8 tell charter schools how they were to implement their oversight
9 responsibilities for the charter schools they sponsor which is
10 sponsors use proponent's frameworks. So when the Court
11 considers the Charter Board's frameworks and what the
12 Plaintiffs are saying about those frameworks, the Court should
13 also consider the contents of the frameworks themselves which
14 describe how the Charter Board collects, analyzes information
15 about its charter schools. And the substance of the Charter
16 Board's rule-making efforts which are not to enshrine the
17 frameworks themselves into rule, but to describe the Charter
18 Board's processes around those frameworks.

19 It's Plaintiffs' argument that the frameworks must be
20 promulgated as rules under the APA. That ignores the mandates
21 of the Arizona legislature and the contents and the scope of
22 the frameworks. When the legislature established schools in
23 1994, the legislature assigned duties and responsibilities to
24 the Charter Board in its creation as a state agency and it
25 assigned duties and responsibilities to the Charter Board as a

1 charter school sponsor of which it is one of several.

2 The legislature has assigned responsibility to the
3 performance framework to charter school sponsors. When it
4 first established a charter school, the legislature gave three
5 entities the authority to establish charter schools, the State
6 Board for Charter Schools, the State Board of Education and
7 school district governing bodies. And these entities were
8 given "oversight and administrative responsibilities for the
9 charter schools they sponsor."

10 Move forward to 2010, the legislature has now added
11 to the list of entities that can sponsor schools. They've
12 added the universities under the Board of Regents. They've
13 added community college districts. They added groups of
14 community college districts. And with that, in 2012 and in
15 2013, the legislature amended ARS 15-183(R) to tell charter
16 school sponsors how they were to implement that oversight and
17 administrative responsibilities for the charter schools they
18 sponsor.

19 And the legislature did this by requiring charter
20 school sponsors to adopt and use publicly available frameworks
21 and it directed the frameworks how they were to be used by the
22 sponsors in certain decision-making.

23 THE COURT: And that applies to all the sponsoring --

24 MS. ANDERSON: Yes.

25 THE COURT: -- groups?

1 MS. ANDERSON: Yes, 15-183 applies to all charter
2 school sponsors -- 183(R). Specifically, beginning in 2012,
3 ARS 15-183 was amended to state in implementing its oversight
4 and administrative responsibilities for the charter schools it
5 sponsors, the sponsor shall ground its actions in evidence that
6 the charter holders performance in accordance with the
7 performance framework adopted by the sponsor. The performance
8 framework shall be publicly available and it shall be placed on
9 the sponsor's website and it shall include the academic
10 performance expectations of the charter school and the measure
11 of sufficient progress toward those academic performance
12 expectations.

13 THE COURT: Does that include -- how am I going to
14 put this? I want to use the word cut off. That's not a very
15 accurate word, but are there performance -- do the frameworks
16 set performance levels and say, school, if you fall below this
17 measure in this aspect, then you are subject to having your
18 charter revoked?

19 MS. ANDERSON: The frameworks provide for levels of
20 performance.

21 THE COURT: Okay.

22 MS. ANDERSON: Exceeds academic performance
23 expectations, meets academic performance expectations, does not
24 meet, falls far below.

25 THE COURT: Right.

1 MS. ANDERSON: However, because a charter school does
2 not meet or falls far below academic performance expectations
3 is not an automatic renewal -- or revocation or non-renewal of
4 its charter. The Board then exercises its discretion and can
5 use that as a basis for consideration of non-renewal or
6 revocation.

7 THE COURT: But that's up to the Board.

8 MS. ANDERSON: Yes.

9 THE COURT: If the, let's say, I was a charter
10 operator. My school fell far below standards, the Board -- I
11 assume there's some kind of a process. You know, they get a
12 hearing and so on. They could go in front of the Board and
13 say, you know, here are all the extenuating circumstances. Let
14 my school continue to operate. The Board would have the
15 authority to do that?

16 MS. ANDERSON: The process for a charter revocation
17 under 15-183 is that the Board would have to issue a notice of
18 intent to revoke the charter.

19 THE COURT: Okay.

20 MS. ANDERSON: The school is then given 60 days to
21 correct the problems associated with the reasons for the
22 proposed revocation and the notice must state the reasons for
23 the proposed revocation.

24 THE COURT: Okay.

25 MS. ANDERSON: A hearing is set at the Office of

1 Administrative Hearings. The parties call witnesses, exhibits,
2 evidence. That recommended decision and findings of fact and
3 conclusions of law go back before the Board for the Board to
4 make a final decision.

5 THE COURT: Is the Board -- are there any
6 circumstances associated with the failure to meet the criteria
7 in the frameworks that require the Board to revoke the charter?

8 MS. ANDERSON: No.

9 THE COURT: Okay.

10 MS. ANDERSON: No, there is no requirement that
11 because a school did not meet academic performance expectations
12 that it must be revoked or it can't be renewed.

13 THE COURT: So the Board -- just to make sure I
14 understand. Does the Board have the same discretion now that
15 it had before 2012 when the legislature passed this 15-83(R)
16 (sic)?

17 MS. ANDERSON: It has the same discretion, however,
18 the difference is that with the legislature's amendment of
19 15-183(R) to provide for the sponsors to ground their actions
20 and evidence of its performance framework, that performance
21 framework now provides an additional basis on which the Board
22 may revoke the charter.

23 THE COURT: Is there a list somewhere in the statute
24 of reasons that a charter can be revoked?

25 MS. ANDERSON: Yes, in 15-183(I)(3).

1 THE COURT: Okay.

2 MS. ANDERSON: The performance frameworks were also
3 to include intervention and improvement policies. So the
4 frameworks were designed to achieve a goal. That goal being
5 the implementation of charter school sponsors, oversight and
6 administrative responsibilities through the adoption of a
7 performance framework whose contents and availability were
8 dictated by the legislature. And the legislature told the
9 charter school sponsors the ways in which the frameworks were
10 to be or could be used.

11 The legislature added to ARS 15-183(I) (3) the
12 requirement that charter school sponsors must use the
13 performance framework that they adopted in conducting their
14 five-year interval reviews. The legislature provided for
15 charter school sponsors and were discretionary to use the
16 performance frameworks in charter renewal decisions. And then
17 in 2013, the legislature expanded on this to add that charter
18 school sponsors may use their frameworks in considering early
19 charter renewal decisions and in charter revocation decisions.

20 And just last year, under 15-183(I) (4), the
21 legislature requires that in making -- in determining whether
22 to renew or revoke a charter, the charter school sponsor must
23 consider making sufficient progress toward the academic
24 performance expectations set for in the performance framework
25 as one of the most important factors.

1 So the legislature has set the statutory structure
2 governing adoption, the contents, the publication, and the use
3 of performance frameworks by charter school sponsors in
4 implementing their oversight and administrative
5 responsibilities for the charter schools they sponsor. And the
6 Charter Board, as a charter school sponsor, followed the
7 legislature's direction in adopting and publishing on its
8 website its performance frameworks.

9 Not all charter school sponsors are state entities
10 with rule-making authority. And I believe you asked that
11 question. But the legislature did give all charter school
12 sponsors the same obligations with respect to the performance
13 frameworks. So that the legislature gave the responsibilities
14 -- the same responsibilities to all charter school sponsors in
15 the manner that it did with the performance frameworks, but
16 that not all sponsors have the ability to promulgate rules. It
17 counsels against imputing a requirement that the Board must
18 create its performance frameworks under the APA.

19 THE COURT: Well, what -- okay. Well, what about
20 their argument that the APA applies unless the legislature says
21 otherwise and there is no exemption for the Charter School
22 Board?

23 MS. ANDERSON: Well, again, I would go back to the
24 Board's argument under 15-183(R) that the legislature, in
25 essence, created a system for all charter school sponsors for

1 the performance framework that is outside of the rule-making.

2 THE COURT: Yeah, but on what basis do I find that
3 it's outside the rule-making?

4 MS. ANDERSON: Because it's under 15-183(R) that
5 provides the process for adopting the frameworks, the
6 performance frameworks. And that is the process that was
7 followed.

8 THE COURT: Okay. So I suppose the argument would be
9 that the legislature implicitly -- it's implicit in this that
10 the APA doesn't apply. I mean, I've got another case where the
11 statute says that the State -- that the agency doesn't have to
12 comply with the APA, but they still have to go out for notice
13 and public comment. So that's what they've said. You're
14 saying that I should read something like that into this statute
15 even though it doesn't say that.

16 MS. ANDERSON: I'm asking you to read into the
17 statute that the Board's frameworks were created through that
18 statutory structure.

19 THE COURT: Okay.

20 MS. ANDERSON: And not all sponsors are subject to
21 the APA, such as the State Board of Education, but has some
22 kind of, you know, provides public notification process.

23 THE COURT: Okay. Does the State -- is it the
24 State's position that of these some aspects of how the Charter
25 Board regulates the charter schools are subject to the APA even

1 though they call themselves public schools? Even though the
2 charter schools call themselves public schools?

3 MS. ANDERSON: The Board -- well, in terms -- there
4 are processes through which the Board has implemented through
5 the rule; however, whether the Board must do it pursuant to
6 rule in other circumstances is a different question from what
7 the Plaintiffs have specifically asked which is does the
8 performance framework have to be implemented by rule.

9 In terms of the relief that's been requested, even if
10 the Court finds that the framework should be promulgated as
11 rules under the APA, the only relief available is a declaratory
12 judgment. They are seeking relief far beyond a judicial
13 declaration on whether the practice or substantive policy
14 statement as it states in 41-1034(B) constitutes the rule.

15 Specifically, the Court should dismiss the
16 Plaintiff's request that the performance frameworks be rendered
17 void and unenforceable. The Court should dismiss the
18 Plaintiff's request that the Court award Plaintiffs and all
19 charter schools sponsored by the Charter Board relief from any
20 and all past or future actions taken by the Board in reliance
21 on the frameworks.

22 These requests for relief would require the Court or
23 the Charter Board to speculate which past actions were
24 allegedly taken in reliance on the Charter Board's framework,
25 which charter schools were allegedly affected, how is the

1 requested relief to be affected. How are past or future
2 actions to be declared void? What does that even mean? To say
3 that this Court does not need to know what that means at this
4 time to make a decision is -- that just does not make sense.

5 What is the effect of the requested relief on Board
6 actions as to charter schools that went through the
7 administrative appeals processes already? What is the effect
8 of the requested relief on Board actions and decisions that
9 were not appealed?

10 The Plaintiffs themselves have alleged no injury.
11 They don't assert the frameworks were used to make decisions
12 with regard to them. They don't allege that they anticipate
13 such decisions in a foreseeable future. Instead, Plaintiffs
14 secretly on behalf of unnamed parties that have suffered
15 undefined wrongs at some unspecified time in the past as a
16 result of the Charter Board's use of the frameworks.

17 So in requesting injunctive and retroactive relief,
18 the Plaintiffs are asking the Court to speculate. How have the
19 Plaintiffs been affected by the frameworks? How will the
20 Plaintiffs in the future be affected by the frameworks? How
21 are the unnamed charter schools and non-parties -- how were
22 they or will be in the future affected by the frameworks?

23 THE COURT: Okay. Well, if I was to -- I'll tell you
24 they have not yet convinced me that this should apply to
25 anything in the past. But if I were to say -- if I were to

1 issue declaratory relief, there would be an interim between now
2 and when the rules that are in the pipeline are promulgated.
3 Could be a year. Could be more than that.

4 What would be -- if I issued declaratory relief, I'm
5 in effect saying you all can't enforce these policies, then
6 what? What happens?

7 MS. ANDERSON: Well, again, I think it depends on how
8 that -- how the parties propose that that relief be fashioned.
9 The Charter Board that the -- the Charter Board would use its
10 -- in its decision-making can't be arbitrary and capricious.
11 So the question then becomes what is -- first of all, what does
12 it mean to not use the frameworks for decision-making because
13 as I will discuss in a moment, we need to look at what those
14 frameworks are. Does that mean no data gathering because
15 that's what the frameworks say? That's what the frameworks
16 are. What does that mean would be the question in terms of how
17 that would be applied to decision-making in the future?

18 THE COURT: Right. And that's what I'm wrestling
19 with. And I'm trying to envision what the process looks like
20 without any standards. And what happens -- Mr. Hall talked a
21 little bit about what happened before 2012. What were the --
22 the Court is too cheap to get me a Westlaw subscription that
23 gives me the versions of the statute as they existed in some
24 specific prior year.

25 Do you know what the grounds for revocation were

1 before this statute was enacted?

2 MS. ANDERSON: Yes. The grounds for revocation were
3 that the charter holder failed -- breached one or more
4 provisions of its charter contract.

5 THE COURT: Okay. And what is typically in a charter
6 contract?

7 MS. ANDERSON: There are certain things that are
8 required to be in a contract under 15-183(E) states what's to
9 be in the contract, but that provides a framework -- you know,
10 a minimum of this is what has to be in there, but it doesn't
11 preclude adding provisions. And in fact, what's interesting in
12 this case is that Tucson Preparatory in fact their charter
13 contract states that they must -- that they are subject to the
14 frameworks.

15 THE COURT: Really?

16 MS. ANDERSON: Yes. And that they must meet or
17 demonstrate sufficient progress toward the academic performance
18 expectations as demonstrated in the frameworks.

19 THE COURT: Well, that makes this completely moot as
20 to them, doesn't it?

21 MS. ANDERSON: Yes, Your Honor.

22 THE COURT: What about the other one? There are two
23 Plaintiffs, right?

24 MS. ANDERSON: Right.

25 THE COURT: What about the other one?

1 MS. ANDERSON: The other one does not have that
2 provision in their charter contract.

3 THE COURT: Okay.

4 MS. ANDERSON: And that's part of where this
5 discussions about the Auditor General's recommendations come
6 from. Their statement is that the Auditor General formally
7 advised the Board it needed to adopt the frameworks as rules
8 under the APA. But when we look at the Auditor General's
9 report, it notes that the Charter Board had adopted the
10 frameworks as authorized by the legislature under 15-183(R).
11 It also noted that the Charter Board was including a
12 requirement of compliance with its frameworks in their new
13 charter contracts. And in noting that there were charter
14 holders operating under charter contracts implemented before
15 the frameworks were required, the Auditor General recommended
16 that rules be developed to address that gap.

17 The Auditor General did not, as the Plaintiffs state,
18 advise the Charter Board that it needed to adopt the frameworks
19 as rules. And nor do they cite any authority as to whether the
20 Auditor General can indeed require agencies to promulgate
21 rules.

22 THE COURT: Go back to my question. Was there any
23 other basis for statutory ground for revoking a charter other
24 than violation of the contract?

25 MS. ANDERSON: No, Your Honor. I believe that the --

1 that was the basis for each of one or more provisions of the
2 charter contract until the performance framework was added by
3 the legislature and corresponding language was added into the
4 revocation statute.

5 THE COURT: Okay.

6 MS. ANDERSON: In their complaint, the Plaintiffs
7 acknowledge that the Board recently opened a rule-making docket
8 to enact rules. We know now that the Board has in fact filed
9 notice of proposed rule-making and its proposed rules. It has
10 taken action. It does not enshrine the frameworks in the
11 rules.

12 The Court should also consider lack of time that
13 since the Charter Board complied with the legislature's
14 directions that they adopt and publicize frameworks. And this
15 action was filed after the Board opened to its rule-making.

16 Those are the arguments in support of the Plaintiffs'
17 motion to dismiss. In terms of, excuse me, Defense motion to
18 dismiss. In terms of the Plaintiffs' motion for summary
19 judgment, the Charter Board disputes facts that the Plaintiffs
20 used to support their conclusions that the frameworks must be
21 adopted as rules and these defeat their motion for summary
22 judgment. The first is the one I discussed just recently with
23 regard to what the Auditor General said or did not say or did
24 or did not recommend.

25 The Charter Board also disputes the Plaintiffs'

1 statement of fact 17 that on February 14, 2014 the Charter
2 Board initiated a rule-making docket to do what it described as
3 adopt the frameworks as rules. The Board opened rule-making in
4 2013 and again in 2016 and in each case the proposed rules
5 demonstrate how the frameworks are used. They don't convert
6 the contents of the frameworks into rule. And they provide
7 that revisions to the frameworks will be made as needed and
8 that the public will be provided with notice and an opportunity
9 to comment on those revisions.

10 Their motion for summary judgment is premised on
11 their assertion that frameworks themselves fall squarely with
12 the APA's definition of a rule. They provide no analysis of
13 the frameworks or examination of the contents of the frameworks
14 themselves. The frameworks offer information about the Board's
15 evaluation of its charter schools, how it corrects and how it
16 analyzes that information that the charter sponsor uses in
17 decision-making.

18 The Charter Board's academic framework and financial
19 frameworks are attached in Exhibit 1 to their -- to the
20 Plaintiffs' motion for summary judgment. They are
21 respectively, 112 pages for the academic performance framework,
22 26 pages for the financial performance framework. The
23 revisions, the revised or the new frameworks, the academic
24 performance framework is 16 pages. Financial performance is 22
25 pages. This is what Plaintiffs propose must be promulgated by

1 rule.

2 Much of what the frameworks describe is how the Board
3 gathers and analyzes information. This does not belong in the
4 rule. There's a distinction between procedure requirements and
5 ones that are part of the information gathering process that's
6 necessary to enable the Board to make its decisions. And this
7 distinction was recognized in the Shelby (phonetic) case.

8 If we look at some of the specifics of the old and
9 new frameworks, we look at page 2 of each of the frameworks,
10 the second paragraph. It states, "Charter holders have the
11 autonomy to select and implement programs of instruction that
12 align with their philosophical and methodological ideology and
13 operations structure consistent with state and federal law and
14 the charter contract." This is the Charter Board's perspective
15 as a sponsor. This is not appropriate for a rule.

16 There's also concluding statements in the frameworks.
17 A strong academic framework is critical for setting clear
18 expectations for schools and for making high stakes decisions
19 more clear cut and transparent. The creation and
20 implementation of the academic framework require the Board to
21 consider many factors including data element areas available,
22 quality of data.

23 So that's why I asked you to look at the frameworks
24 themselves. They also state perspectives of the Charter Board.
25 These also are not rules. The frameworks state the academic

1 framework utilizes a number of measures to evaluate schools.
2 The combination of measures taken on the whole provides the
3 Board with a balanced scorecard of each schools performance
4 over time.

5 The frameworks provide descriptions. In both the old
6 and the new financial performance framework they provide the
7 definition of the term unrestricted days and quitting
8 (phonetic). The processes contained within the framework
9 provide for gathering of information. That does not belong in
10 rule. The frameworks provide transparency in terms of how the
11 Charter Board evaluates academic and financial performance.

12 THE COURT: Is there a different -- would it be fair
13 to say that there's a difference between the oversight and
14 administrative responsibility for a charter school that the
15 Board has as a sponsor and the administrative responsibilities
16 of the Charter Board as a state agency?

17 MS. ANDERSON: I'm sorry, Your Honor. I didn't
18 understand the question.

19 THE COURT: You've got the Board at this point, the
20 school boards, the community colleges. They all have the
21 ability to sponsor a school.

22 MS. ANDERSON: Yes.

23 THE COURT: This statute says the sponsoring entity
24 has oversight and administrative responsibilities which is what
25 you're talking about. Making sure the schools are functioning

1 properly. Isn't that a different -- fundamentally different
2 responsibility from the kind of responsibility that gets put
3 into a rule by a state agency? Maybe I'm not articulating it
4 very well.

5 MS. ANDERSON: No, I think that --

6 THE COURT: I think maybe that's a statutory basis
7 for the argument you're making.

8 MS. ANDERSON: There is --

9 THE COURT: You're talking about the sponsorship
10 responsibilities.

11 MS. ANDERSON: Yes. I'm talking about the
12 distinction that's made between the responsibilities to the
13 Charter Board under 15-182 when it was established versus the
14 responsibilities assigned to charter school sponsors under
15 15-183(R).

16 THE COURT: Say that again. Now you lost me.

17 MS. ANDERSON: Okay.

18 THE COURT: I thought I had something and then you
19 lost me. Say that again.

20 MS. ANDERSON: There are responsibilities assigned to
21 the Charter Board --

22 THE COURT: Right.

23 MS. ANDERSON: -- when it's in its creation under
24 15-182.

25 THE COURT: Okay.

1 MS. ANDERSON: There are duties and responsibilities
2 assigned under 15-183 to charter school sponsors of which the
3 Board is one of several.

4 THE COURT: Right. Okay. Yes. All right.

5 MS. ANDERSON: In the event that the Court concludes
6 that the frameworks or portions of them should have been
7 promulgated as rules it should conclude that there were made in
8 approved and substantial compliance with the APA. A concept of
9 the court and the Arizona State Retirement System case. It is
10 undisputed that in every stage of the development, adoption and
11 revision to the frameworks the Charter Board provided multiple
12 opportunities for public participation and comment.

13 The affidavit by Whitney Chappa (phonetic) attached
14 to the Defendant's statement of facts, Exhibit A, provides a
15 comprehensive list of the number of opportunities that were
16 provided. These opportunities are not disputed by the
17 Plaintiffs. It's undisputed that the Charter Board published
18 its frameworks widely, solicited input from numerous sources.
19 It's undisputed the Charter Board held six public meetings
20 before adopting the old frameworks. It's undisputed the
21 Charter Board conducted 19 additional public meetings as it
22 considered adopted revisions and then created and adopted the
23 new frameworks.

24 The Charter Board provided substantially more
25 opportunities for notice and comment upon its frameworks than

1 the APA requires. The Charter Board also solicited -- as
2 indicated in Ms. Chappa's affidavit -- the Charter Board
3 solicited oral and written comments for their frameworks. And
4 by contrast, the APA does not require a provision to afford
5 oral comment unless it's requested.

6 The Board's actions here are in sharp contrast to the
7 actions in the Arizona State Retirement case. In that case,
8 the staff developed and implemented a policy with no notice to
9 the public, no opportunity for comment. The case described the
10 underlying purpose of the APA which is that agencies give
11 public notice of the proposed rules and an opportunity to
12 provide comments. And in that case because the Retirement
13 System had not developed its policy -- or had developed its
14 policy without substantial compliance, the court invalidated
15 that.

16 Here the Charter Board involved the public and
17 related community at every step, provided multiple
18 opportunities for oral and written comment complying with this
19 underlying purpose which is that agencies get public notice and
20 an opportunity to provide comments.

21 The Charter Board has also requested leave to raise
22 an additional argument which is that their current rule,
23 R75-301, permits the Charter Board to collect and review
24 reports about its data records documents from any source
25 relating to any activity or program conducted by or for a

1 charter school. And this would certainly give the Charter
2 Board the authority to correct the data and the information and
3 to review that from charter schools through means such as the
4 frameworks to carry out the responsibilities.

5 It is the request of the Board that the Court grant
6 the motion to dismiss. And if the Court does not do so, to
7 deny Plaintiffs' motion for summary judgment and to grant the
8 Defendant's cross motion for summary judgment. Thank you.

9 MR. HALL: Thank you, Your Honor. I'd like to touch
10 on several points that Ms. Anderson raised and that the Court
11 discussed with her. I think the first one that the Court needs
12 to be aware of is the issue of Tucson Preparatory schools
13 contract.

14 Tucson Preparatory school serves pregnant teenagers,
15 nursing teenagers, homeless students. A very -- in fact,
16 almost its whole population is a highly at risk population.
17 That's what it was chartered to serve. Its original contract
18 with the State Board for Charter Schools did not have a
19 requirement that it complied with the frameworks because the
20 frameworks didn't exist then.

21 When Tucson Preparatory school came up for renewal
22 and explained the population it serves to the Board and
23 explained the transient nature of these students, how they are
24 sometimes living in washes and can't make it to school and
25 don't have clothing, the Board said okay, we understand that,

1 but going forward -- we're going to renew, but going forward we
2 still want you to comply with our frameworks.

3 And so Tucson Preparatory schools was given a choice.
4 Either have this provision of compliance with the frameworks in
5 their renewal contract or not get renewed at all. So it's not
6 necessarily the case that this issue is moot as to Tucson
7 Preparatory school because had they not agreed to that
8 provision in that renewal contract, they wouldn't exist.

9 THE COURT: Well, I think we're outside the record.
10 So I think you're -- at least for today, you're safe on that
11 ground. I'm not going to say the matter is moot as to them
12 because there's nothing, I don't think, in the materials that
13 are in front of me in the record that confirms what -- anything
14 said about what their contract says, so.

15 MR. HALL: Okay. I just wanted to make that clear
16 though.

17 THE COURT: Okay. That's fine.

18 MR. HALL: The other thing is I want to hopefully
19 have the Court understand this whole public school, private
20 operating entity issue. 15-183(B) addresses this and it talks
21 about the sponsoring entity. And again, for 96 percent of the
22 schools, that's the State Board for Charter Schools. Private
23 entities serving a public purpose. In this case, it's running
24 a charter school.

25 So it is not the case that a charter school is

1 somehow the same as a district school. School districts are
2 political subdivisions. Charter schools are not. Charter
3 schools are contracted to perform an educational function. And
4 so I think that's hopefully helps to explain the difference.
5 If you were to look at Title 15, Arizona's Education Code,
6 you'd see about two and a half, three inches worth of statutes
7 that apply to schools and school districts and you'd see 30
8 pages that apply to charter schools.

9 15-183(E) (5) exempts -- specifically exempts charter
10 schools from all statutes relating to school districts unless
11 their charter says they have to apply to them or unless those
12 30 pages of the charter schools statute says they apply to
13 them. Otherwise charter schools don't operate like district
14 schools.

15 **THE COURT: Doesn't this go to the distinction**
16 **between the Charter Board as a state agency and the Charter**
17 **Board as a sponsor?**

18 MR. HALL: You know, that was an interesting
19 discussion you had with Ms. Anderson because all the Charter
20 Board does is charter schools and regulate them. That's what
21 they exist to do.

22 THE COURT: Well, but that -- sort of -- then maybe
23 they have regulations about certain generally what their
24 procedures are, but that's not the same as saying they need
25 regulations that determine the criteria -- how they implement

1 their criteria that they've created as a sponsor. It's like
2 saying that the Department of Corrections in relationship with
3 a private prison has to promulgate rules for how the private
4 prison runs. You can't operate like that. We can't operate
5 like that.

6 MR. HALL: That analogy kind of works because the
7 Department of Corrections does enter into a contract with the
8 private prisons.

9 THE COURT: Right.

10 MR. HALL: The Charter School Board enters into a
11 contract with the charter school operators, but both of those
12 agencies are still required to enact overall rules in how they
13 conduct their business. And so the private contract with a
14 private prison or the private contract with a charter operator
15 is in fact a subset but it's still governed by the requirement
16 that both agencies promulgate rules.

17 THE COURT: Well, and actually -- look DOC is
18 actually exempt from rule-making.

19 MR. HALL: Right.

20 THE COURT: So, you know.

21 MR. HALL: So perhaps that analogy --

22 THE COURT: About which the Court has no comment.

23 MR. HALL: -- isn't quite as good as it could be.
24 One other thing, though, along those same lines that you and
25 Ms. Anderson were discussing and she was pointing out how all

1 sponsors are required to adopt frameworks. And that the
2 Charter Board was following its statutory mandate in doing so.
3 Well, that's true. All the sponsors are required to adopt
4 frameworks, but as the Court mentioned, if the legislature
5 wanted to exempt the Charter Board from enacting rules to adopt
6 those frameworks, it knows how to do that. And it didn't do
7 that. And there's a whole line of cases that say public
8 agencies only have those powers the legislature granted to
9 them. And the legislature never granted the Charter Board
10 exemption from the APA in adopting its frameworks. It knows
11 how to do it. Didn't do it. So they're subject to the APA.

12 Now the fact that maybe the Board of Regents or the
13 community college districts aren't subject to the APA that
14 issue isn't before this Court. The Board didn't exempt them so
15 they have to follow the law.

16 Regarding the remedy, 12-1838 allows this Court to
17 grant supplemental relief with that judgment statute. Allows
18 this Court to grant supplemental relief. And that relief can
19 be whatever this Court deems appropriate. And under that same
20 statute, you don't have to show damages. You just have to show
21 that you're affected. These schools are affected, the
22 Plaintiffs, as well as all the other charter schools, are
23 affected by the Board's regulation by policy instead of rules.

24 And consistent with supplemental relief, if this
25 Court only grants prospective relief to the Plaintiffs, that is

1 a green light to the Charter Board and other agencies that, you
2 know, it doesn't matter if you're not following the APA. The
3 court's not going to do anything about it for past actions.
4 You're just going to have to straighten up and fly right in the
5 future. We think that's a terrible message to send. I mean,
6 you have to do what you're supposed to do under the law and if
7 you did something wrong under the law, that needs to be
8 corrected.

9 If the State gets sued because it didn't follow the
10 law and this Court says it didn't follow the law, that's what
11 the whole judicial system is for. It's to give Plaintiffs a
12 remedy when there's wrongdoing by an entity. So if the State
13 was wrong in regulating through policy and they get sued
14 because of that because a school is damaged because they
15 regulated through policy, you know, that's the consequence a
16 State agency must bear for not following the law in the first
17 place. I don't think this Court should say well, we don't want
18 to let causes of action arise by only giving -- and only give
19 prospective relief because that leaves prior bad acts
20 unresolved.

21 And, you know, Ms. Anderson said that if the
22 frameworks were struck down, the Board could open itself up to
23 charges of being arbitrary and capricious. That's not a
24 particularly difficult thing. Don't be arbitrary and
25 capricious. Don't play favorites among charter schools. Look

1 at your own meeting minutes. Those are written down. See what
2 you did in the past and act consistently. There's ways that
3 this Board and any board can avoid acting arbitrarily and
4 capriciously without having to rely on frameworks that are
5 rules in disguise.

6 We'd reiterate that this Court should take the step
7 of invalidating the frameworks, not allowing the Board to enforce
8 them, and undoing or at least allow the undoing of any damage
9 that was done in the past because the Board took action against
10 charter schools in reliance on those improperly adopted
11 frameworks.

12 THE COURT: Thank you.

13 MS. ANDERSON: Your Honor, if I could briefly address
14 the question that you raised with regard to the charter
15 contract with Tucson Preparatory's contract that is contained
16 within the record, that information.

17 THE COURT: Is it in the record?

18 MS. ANDERSON: Yes. It's contained at --

19 THE COURT: Where?

20 MS. ANDERSON: The affidavit of Whitney Chappa at
21 paragraph 13.

22 THE COURT: This is in your response -- the --

23 MS. ANDERSON: Yes, in the Board's --

24 THE COURT: -- statement of facts.

25 MS. ANDERSON: -- combined reply to the motion to

1 dismiss in response to the motion for summary judgment of the
2 Plaintiffs.

3 THE COURT: Okay. I've got Whitney Chappa's
4 affidavit. Where is it now?

5 MS. ANDERSON: Paragraph 13. The bottom of page 2.

6 THE COURT: Okay. All right. I'm going to rule from
7 the bench. The State's motion to dismiss is granted. The
8 reasons are as follows. The Court finds that the
9 Administrative Procedures Act does not apply to the frameworks
10 -- the performance framework that is described in ARS Section
11 15-183(R). The 15-183(R) states that the sponsoring entity of
12 a charter school shall have oversight and administrative
13 responsibility for the charter schools it sponsors.

14 I didn't manage to figure out or work around to find
15 what the statute said before it was amended and before the
16 amendment in 2012; that's where it stopped. The sponsoring
17 entity of a charter school shall have oversight and
18 administrative responsibility. Then in 2012 the legislature
19 promulgated these more specific requirements. Those
20 requirements apply to all the charter school sponsors some of
21 which are not state agencies that are subject to the
22 Administrative Procedures Act.

23 The administrative requirements that the Charter
24 School Board as a school sponsor has to follow are in 15-83(R)
25 (sic). The performance framework shall be publicly available

1 and placed on the sponsoring entities website. That's what
2 they're required to do as process in implementing the
3 framework.

4 That is distinct from the responsibilities of the
5 Charter School Board as a state agency. Under 15-182(E), the
6 State Board for Charter Schools shall do the following. Adopt,
7 grant charter status, adopt and use an official seal, keep a
8 record of its proceedings, adopt rules for its own government.
9 It's empowered to sponsor schools and the Court doesn't
10 disagree that it has some responsibility for promulgating
11 rules. It, meaning the Charter Board, has some responsibility
12 to promulgate rules to govern its operations. But to say that
13 it has to promulgate rules to -- that embody or implement its
14 oversight and responsibility for charter schools it sponsors as
15 a sponsor is a bridge too far.

16 That as a -- and the Court finds that was the
17 legislative intent behind 15-183(R). This would not -- what
18 I'm about to say would not be dispositive if the statute
19 clearly told me that this is a process to which Administrative
20 Procedures Act should apply, but **it's impracticable. You can't**
21 -- they can't create a rule for every aspect of overseeing a
22 charter school any more than a school board can create a rule
23 for overseeing every aspect of a school.

24 By definition, they are an oversight body and the --
25 and to require them to amend the framework every time they

1 decided to rely on a different standard or implement a
2 different test or anything like that to require them to go
3 through the rule-making process would make it impossible for
4 them to do any kind of effective oversight which supports my
5 conclusion that that's not what the legislature intended of
6 them.

7 It's also the implication of this distinction that
8 the usual rule that says the legislature has to exempt an
9 agency from rule-making that doesn't apply because this isn't a
10 rule-making situation in the first place.

11 The implication of the Plaintiffs' position is that
12 there should have been rules governing the -- there should have
13 been rules that laid out the oversight and administrative
14 responsibility of the charter schools. That those should have
15 existed since 1994. The fact that there's no evidence before
16 the Court that anyone ever thought that this sponsorship
17 responsibility should be administered by rule suggests to the
18 Court that that's not what was intended as does the implication
19 of what the Plaintiffs are asking for which is that the Court
20 would void the frameworks and therefore it would be -- the
21 charter schools would essentially go without oversight or with
22 oversight that's only -- that's completely standardless and
23 undefined until these rules are promulgated.

24 And if that's what the world is going to look like,
25 then it would make as much sense to say that all the charter

1 schools should be shut down until we have these rules because
2 we can't regulate them.

3 So those are the reasons for the Court's decision.
4 It is a grant that the motion to dismiss -- this is a legal
5 interpretation of 15-183(R) that does not depend on the facts.
6 So the summary judgment motions are moot. The Court will enter
7 a final order. If the State would like to submit a form of
8 judgment for the Court's signature, then it may. Ten days to
9 do that?

10 MS. ANDERSON: Yes, Your Honor.

11 THE COURT: All right. Ten days to submit a form of
12 judgement and any application for fees or costs that may be
13 appropriate. The Plaintiffs will have five days to object if
14 it's just a form of judgment. Ten days to respond if it's an
15 application. And then the Court will enter a final judgment.

16 Excuse me. Anything else? All right. We'll recess,
17 then. Thank you, folks.

18 (Proceedings concluded at 3:05 p.m.)
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October 30, 2016