



Albany Community Charter School

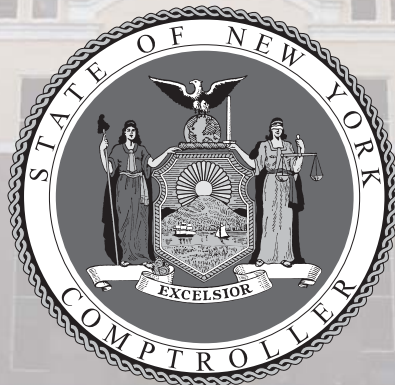
Financial Operations

Report of Examination

Period Covered:

July 1, 2011 — February 28, 2013

2013M-185



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

October 2013

Dear School Officials:

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

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

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

Respectfully submitted,

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



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

A charter school is a public school, financed by local, State, and Federal resources that is not under the control of the local school board. Charter schools have fewer legal operational requirements than traditional public schools. Charter schools are required to set both financial and academic goals, and a school's renewal of its charter is dependent on meeting these goals. The Albany Community Charter School's (School) current charter was renewed in January 2010.

The School is located in the City of Albany and is governed by the Board of Trustees (Board), which currently comprises 10 members. The Board is responsible for the general management and control of the School's financial and educational affairs. The Principal of the School is the School's chief executive officer and is responsible, along with other administrative staff, for the School's day-to-day management under the Board's direction.

During the 2012-13 school year, the School had 478 students and has 69 employees. The School's budgeted expenses for the 2012-13 fiscal year were approximately \$7 million, funded primarily with tuition payments from area school districts for resident pupils, and State and Federal aid.

The School entered into leases for the current elementary school building in August 2008 and for the middle school building in July 2012. The School contracts with a not-for-profit foundation (Foundation) for various services. The Foundation provides start-up grants, school facilities, a revolving loan fund, and technical assistance to charter schools.

Scope and Objectives

The objectives of our audit were to evaluate the process for selecting and negotiating the related financial terms for the building space needed for school operations and the effectiveness of the School's compact contract with the Foundation for the period July 1, 2011, to February 28, 2013. Our audit addressed the following related questions:

- Did the Board use an adequate process to identify suitable building space for School operations and negotiate related financial terms that best meet School needs?
- Did the School receive all the services from the Foundation as outlined in a compact agreement, and is the fee structure of the compact agreement reasonable?

Audit Results

We found no evidence that the Board had fulfilled its fiduciary responsibility to the School by ensuring that it fully evaluated the choice of its site selection for the elementary school or middle school. In addition, School officials could have saved money if they purchased the elementary school by issuing a bond instead of continuing to lease the building. Depending on the year purchased and using interest rates from 5 to 7 percent for the debt, we calculated that the School could have saved from about \$207,000 to \$2.3 million by issuing debt and purchasing the elementary school rather than leasing it. If the interest rate on the debt exceeded approximately 7.31 percent, it would not be profitable for the School to purchase the building. However, considering interest rates for the past 5 years, it is likely that the School would have been able to issue a bond with a lower interest rate.

On May 26, 2011, the Board approved a compact contract between the School and the Foundation that states that the Foundation will provide the School with access to legal and financial assistance, technical support, and advocacy at State and local levels. The fee for these services was 1 percent of pupil revenue from the prior academic year. On April 18, 2013, the Board approved a revised compact contract with the Foundation that supersedes the prior compact contract. The revised contract increases the fee from 1 percent for the 2012-13 school year to 1.5 percent for the following year, and 2 percent for the final year of the contract. With the increase in the fee percentage and the expected growth of the number of students over the next two years as the School expands to include middle school grade levels, the fee that the School pays the Foundation is expected to increase three times the 2011-12 school year payment. The fee structure of a percentage of pupil revenue does not appear to be reasonable as the services being provided do not have any bearing on the number of students at the School, nor the State Education Department Charter School Tuition rate.¹

Comments of School Officials

The results of our audit and recommendations have been discussed with School officials and their comments, which appear in Appendix A, have been considered in preparing this report. School officials generally agreed with the findings and indicated that they would consider the recommendations to improve operations. Appendix B includes our comments on issues raised in the School's response.

¹ The tuition rate to be used by public school districts with resident students attending charter schools

Introduction

Background

A charter school is a public school, financed by local, State, and Federal resources, that is not under the control of the local school board. Charter schools have fewer legal operational requirements than traditional public schools. Most of the regulations for a charter schools are contained in the entity's by-laws, charter agreement, and fiscal/financial management plans. Charter schools are required to set both financial and academic goals, and a school's renewal of its charter is dependent on meeting these goals. The Albany Community Charter School's (School) current charter was renewed in January 2010.

The School is located in the City of Albany and is governed by the Board of Trustees (Board), which currently comprises 10 members. The Board is responsible for the general management and control of the School's financial and educational affairs. The Principal of the School is the School's chief executive officer and is responsible, along with other administrative staff, for the School's day-to-day management under the Board's direction. The Business Manager is the chief accounting officer and is responsible for maintaining custody of, depositing, and disbursing School funds; maintaining the financial records; and preparing the monthly and annual financial reports.

During the 2012-13 school year, the School had 478 students and has 69 employees. The School's budgeted expenses for the 2012-13 fiscal year were approximately \$7 million, funded primarily with resident pupil tuition billings, and State and Federal aid.

The School began to lease its current elementary school building in August 2008 and the middle school building in July 2012. The School contracts with a not-for-profit foundation (Foundation) for various services. The Foundation provides start-up grants, school facilities, a revolving loan fund, and technical assistance to a number of charter schools.

Objectives

The objectives of our audit were to evaluate the process for selecting and negotiating the related financial terms for building space needed for school operations and the effectiveness of the School's compact contract with the Foundation. Our audit addressed the following related questions:

- Did the Board use an adequate process to identify suitable building space for School operations and negotiate related financial terms that best meet School needs?

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

**Scope and
Methodology**

We reviewed the third-party relationship and contracts with the Foundation and examined the School's lease agreements and compact contract for the period July 1, 2011, to February 28, 2013.

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

**Comments of School
Officials and Corrective
Action**

The results of our audit and recommendations have been discussed with School officials and their comments, which appear in Appendix A, have been considered in preparing this report. School officials generally agreed with the findings and indicated that they would consider the recommendations to improve operations. Appendix B includes our comments on issues raised in the School's response.

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

Building Selection and Lease Agreements

The Board is entrusted with the responsibility of safeguarding School resources. The Board fulfills this responsibility, in part, by fully evaluating existing options before committing these resources. When selecting a suitable site on which to construct a school building, or locating an existing building for acquisition or lease, the Board should establish a process to properly identify the needs of the School in terms of the location, size of the building and suitability for intended use and future expansion, and should confirm that related costs are appropriate to ensure the School's long-term financial viability.

The Board should analyze all cost aspects and compare them to comparable properties and current market conditions. This would provide assurance that the agreed-upon terms are reasonable and align with market conditions. When comparing leases for different properties, it is important to analyze the total cost for each, including any leasehold improvements necessary to make the property suitable for its intended use. This process should also entail exploring the option of buying and rehabilitating existing buildings and/or buying land and constructing a new building suitable for school needs.

We found no evidence that the Board had fulfilled its fiduciary responsibility to the School by ensuring that it fully evaluated the choice of its school building for the site selection of the elementary school or middle school. In addition, the School could have saved from about \$207,000 to \$2.3 million if it purchased the elementary school by issuing debt instead of continuing to lease the building.

Site Selection

The New York State Office of General Services (OGS) annually publishes a list of vacant and unused buildings, or portions thereof, that are owned by the State and may be suitable for the operation of a charter school. Education Law requires that this list shall be provided to applicants for charter schools and to existing charter schools. Further, at the request of a charter school or a prospective applicant, a school district is required to make available a list of vacant and unused school buildings, or portions thereof, including private school buildings, within the school district that may be suitable for the operation of a charter school.

The Board did not use an adequate process for site selection and lease cost analysis. The Board could not demonstrate that it identified and fully evaluated site options other than the current locations, including receiving a list of vacant and unused properties from OGS or requesting a similar list from the Albany City School District.

Instead the Board allowed the Foundation to select the site for the elementary school location, secure the financing for the construction, and construct the building. A Board member stated that the Board accepted the Foundation's site location prior to construction beginning, though this was not included in the Board minutes or other documentation.

The Foundation also selected the middle school location. The Foundation owned the building and the School took over the location from another charter school when that school moved to a different location. While the Board minutes did indicate that the Board President discussed site options with the Foundation, the Board was unable to demonstrate that it identified and fully evaluated other site options for a middle school. When the Board does not perform a thorough site selection analysis, the School is susceptible to incurring a greater expense than necessary for building-related expenses.

Lease Agreement and Cost Analysis

The School leases both its elementary school and middle school from the Foundation. The School makes monthly lease payments that are based on the lease agreements between the two parties.

The current lease agreement for the elementary school began on June 1, 2010, and ends on June 30, 2040. During the first eight years of the lease agreement, the rent increases from \$717,384 in the 2010-11 school year to \$800,000 in 2017-18 school year, at which time rent will be renegotiated. At the completion of the 2017-18 school year, the agreement includes a clause for the School to purchase the building, rather than continuing to lease. We were informed by the the Business Manager that the School intends to purchase the building at that time, as provided in the lease agreement. The approximate size of the elementary school is 42,500 square feet.

The current lease agreement for the middle school began on July 1, 2012. The lease is for one year with the option to renew the lease for an additional one year for five consecutive years until June 30, 2018. The annual rent is \$365,000 until December 2013, at which time the rent will be renegotiated based upon the interest rate the Foundation obtains. The approximate size of the middle school is 32,000 square feet.

Both buildings are located in the City of Albany's South End. When the 2012-13 school year annual rent payment and purchase price are compared to the square footage and purchase price for each building, the elementary school is a more costly building as compared to the middle school. Table 1 shows the comparison.

Table 1: Square Foot Comparison		
	Elementary School	Middle School
Rent/Square Footage	\$17.16	\$11.41
Purchase Price/Square Footage	\$223.53	\$162.50
Rent/Purchase Price	7.68%	7.02%

Due to the significant difference between the rent amounts for each school, the escalation of rent payments for the elementary school, the lack of an adequate site selection process, and the current option to purchase the elementary school, we performed an analysis of financing options and determined the amount of money the School could have saved through the 2017-18 school year by purchasing the elementary school by issuing debt instead of continuing to lease the building. The School could have saved money by issuing debt and purchasing, rather than leasing, the elementary school. In order to calculate the potential savings, we performed the following steps:

1. We calculated the monthly payment that would be required for a 30-year amortizing loan (payment of principal and interest each month) using the interest rates that were used in conjunction with the loan amount required to purchase the elementary school building. Using the monthly payment, we calculated the total annual payment for each school year from the 2008-09 school year until the 2011-12 school year.
2. We then totaled the difference between the calculated annual loan payment and the actual and estimated lease payments for the duration of the lease agreement² for each year to determine the savings the School could have achieved had the School chosen to purchase the elementary school building at the beginning of the particular school year.
3. We determined the savings on principal by calculating the amount of principal that would have been paid back by the end of the 2017-18 school year.
4. We calculated the total savings by adding together the results from steps 2 and 3 for each school year.

We performed these steps for multiple interest rates.³ We also calculated the interest rate that would make the cash and principal

² The actual and estimated rent payments were determined by reviewing the lease agreement and any amendments to the lease and the accounting records.

³ These rates were determined to be realistically obtainable because, for example, a charter school in New York City was able to issue bonds with interest rates between 5 percent and 6 percent in March 2013.

savings equal to the lease payments and the purchase price of the elementary school, which is referred to as the breakeven interest rate. The School would have to secure an average interest rate less than 7.31 percent to make the purchase of the elementary school profitable.

Table 2: Potential Savings through the 2017-18 School Year				
Debt Issued At:				
Year of Purchase	5% Interest Rate	6% Interest Rate	7% Interest Rate	Breakeven Interest Rate
2008-09	\$2,280,780	\$1,255,664	\$215,409	7.21%
2009-10	\$2,149,525	\$1,224,102	\$286,624	7.30%
2010-11	\$1,961,705	\$1,136,987	\$302,917	7.36%
2011-12	\$1,696,041	\$972,871	\$242,682	7.33%
2012-13	\$1,453,968	\$833,036	\$207,055	7.33%

When the Board does not consider and evaluate all possible financing options for obtaining buildings and space for School operations, and continue to monitor these options, the Board has no assurance that the option chosen is the most economical and that agreed-upon terms are reasonable and in line with prevailing market conditions.

Recommendations

1. The Board should properly fulfill its fiduciary responsibility by conducting and documenting thorough analyses of alternatives before making major financial commitments.
2. At a minimum, for future building acquisitions, the Board should request a list of buildings available from OGS and the local school district to ensure all available buildings are evaluated for suitability and cost.

Compact Contract

Schools require a number of services to adequately conduct business. A school can choose to obtain these services by using employees to perform the services or hiring an independent service provider. Ultimately, it is a board's responsibility to choose a method that provides the services required by a school in the most cost efficient manner possible.

On May 26, 2011 the Board approved a compact agreement between the School and the Foundation. All Board members present at the Board meeting voted in favor of the compact agreement, except for the Board President who recused himself from voting because he is also the Foundation's Chairman. The compact contract states that the Foundation will provide legal and financial assistance, technical support, and advocacy at State and local levels to the School. When asked to describe the specific services being provided to the School, the Foundation did not provide any further detail. The fee for these services is 1 percent of total pupil revenue from the prior academic year. The total fee paid to the Foundation for the 2011-12 school year was \$55,114.

As a result of the insufficient detail about what exact services were being provided, we reviewed expenses from select account codes to determine if there were any duplicate services being provided by the Foundation or another entity. No duplicate services were discovered.

On April 18, 2013, the Board approved a revised compact contract with the Foundation that supersedes the prior compact contract. The revised compact provides further detail about the specific services that the Foundation could provide the School and increases the fee from 1 percent for the 2012-13 school year to 1.5 percent for the following year, and 2 percent for the contract's final year. With the increase in the fee percentage and the expected growth of the number of students over the next two years as the School expands to include middle school grades, the fee that the School pays the Foundation is expected to increase to three times the amount of the 2011-12 school year payment.

The fee structure of a percentage of pupil revenue does not appear to be reasonable as the services being provided do not have any bearing on the number of students at the School, nor the State Education Department Charter School Tuition rate.⁴ When the School enters

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

contracts that do not provide sufficient detail about the services being provided and do not have a reasonable fee structure, the School is susceptible to incurring costs that are greater than necessary for the services it receives.

Recommendations

3. The School should ensure that contracts include a sufficient description of the benefits, rights, and responsibilities of all parties to the contract, and the School should use this information to monitor compliance with the contract.
4. The School should determine if there is a more cost effective means to receive the desired services currently being provided by the Foundation.

APPENDIX A

RESPONSE FROM SCHOOL OFFICIALS

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

The School's response letter refers to an attachment that supports the response letter. Because the School's response letter provides sufficient detail of its actions, we did not include the attachment in Appendix A.



65 Krank Street Albany, New York 12202

September 30, 2013

State of New York
Office of the State Comptroller
Andrew A. SanFilippo, Executive Deputy Comptroller
Division of Local Government and School Accountability
110 State Street
Albany, New York 12236

RE: Albany Community Charter School
Financial Operations
Report of Examination
July 1, 2011 to February 28, 2013
2013M-185

Dear Mr. SanFilippo:

Thank you for the opportunity to respond to the recommendations contained in the Report of Examination with respect to the Financial Operations of the Albany Community Charter School (ACCS). Provided below are the School's responses to OSC's findings and recommendations regarding the ACCS Board's site selection process for the elementary and middle schools, as well as the compact contract between ACCS and the [REDACTED] ("Foundation") approved in 2011.

Compact Agreement with Foundation

As pointed out in the Draft Report, schools do require a number of services to adequately conduct business. As a charter school, the Board has an obligation, one which it takes very seriously, to not only see to it that the services provided to the Schools are adequate but that they meet or exceed the School's commitments under its charter granted by the Board of Regents, fulfill its obligations under the charter contract with its authorizer (the State University of New York) and ultimately and most crucially serve the needs of its students. Satisfying these

obligations requires the Board, which is vested with the ultimate oversight authority, to identify those individuals and organizations that possess the requisite skill and expertise to deliver the required services.

It is common place for school districts, private schools and charter schools alike to utilize a variety of services from educational service providers in the areas of curriculum design and consulting, student benchmarking and performance, staff professional development, legal services and board governance training, financial management, accounting, human resources, strategic planning and regulatory affairs. Such persons and organizations providing such required services have a variety of methodologies for charging fees for service. For example, it is quite common for providers of professional development services or student information system service providers to charge a per student fee. Additionally, charter management organizations and other educational service providers providing a suite of services typically charge a school as a percentage of revenue would mirror a per student charge.

With respect to charter management organizations and others providing a suite of services to a charter school, fees can range from 1% to 12% depending on the level of service and degree of management provided. Such arrangements are generally, and in the case of the School's relationship with the Foundation, is reduced to writing in the Compact (as amended) which was carefully thought through and considered, with Trustees of the Board exercising their best business judgment, fiduciary duty, duty of care, duty of loyalty and duty and commitment to serving the needs of the stakeholders of- and most importantly students and family at the School.

See
Note 1
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The Foundation is in a unique position to provide the services through the network of charter schools in Albany since it is able to leverage each of the school's resources so that the schools can act and react together in regard to various external factors which affect each school, but for which each school cannot always respond individually. These services are identified in the compact, and include legal, advocacy, communications, and assistance with board education, and each of the schools face challenges in this regard that can best be met collectively.

With respect to the Compact specifically, care was taken to define roles and responsibilities with sufficient detail while recognizing the need to retain flexibility whereby any action that may not fit squarely into a chapter and verse section of the Compact does not require an amendment to the Compact. While the day-to-day interaction between the Foundation and the School is at the School management level, the Board retains the ultimate decision making authority with respect to the Foundation/School relationship and as stewards of public funds, works to ensure that the Compact with the Foundation and every contract or relationship with every service provider is one that make fiscal and operational sense alike an in all respects is in the best interest of the students and School community.

As the School's relationship with the Foundation continues to grow, the Board will continue to exercise all of its duties and best judgment as it does with all vendors by negotiating terms and holding vendors accountable for the services they provide.

The School appreciates OSC's suggestions that additional detail be included in the Compact and shall take such suggestions into account in future revisions to the Compact and other service agreements where clear and robust terms are needed along with strict accountability for performance.

Site Selection

As referenced above, as a charter school, the Board has an obligation, and the board is vested with the ultimate oversight authority, to make various business decisions regarding the facilities to be used by the school. These decisions were carefully thought through and considered, with Trustees of the Board exercising their best business judgment, fiduciary duty, duty of care, duty of loyalty and duty and commitment to serving the needs of the stakeholders of, and most importantly students and family at the School.

Lease / Bond Issuance

The draft report makes more than one statement that *"the School could have saved money if they (sic) purchased the elementary school by issuing a bond instead of continuing to lease the building."* OSC estimates the range of such savings to be \$207,000 to \$2.3 million.

We are not sure of all of the detailed assumptions OSC made when making the cost comparison, however, it appears that a number of items may have been overlooked in the calculations including:

See
Note 2
Page 21

- The need to borrow additional funds for a Debt Service Reserve Fund; all charter schools borrowing in the tax-exempt bond market (along with other revenue backed bonds with similar credit profiles) must set aside an amount that is roughly equivalent to one year of debt service. Given interest rates today, earnings on this reserve does not come close to the cost of the additional debt.
- Borrowers also need to include funds in the par amount of the bonds for significant transaction costs. See example in Exhibit 1 for the issuance costs associated with a recent tax-exempt bond transaction the School was considering.

See
Note 3
Page 21

As the [REDACTED] runs in Exhibit 1 show, the dollar amount for the Debt Service Reserve and the costs of issuance for the single project size is \$1,020,000 on a \$5.2 million project cost (or 19.6% higher). On the second example with the larger project size, the delta is \$2,135,000 on \$14,700,000 (or 14.5% higher). These differences are significant and must be included in what the School is borrowing in order to make the comparative analysis meaningful. (See link for publication with data on average costs of issuance as well as Debt Service Reserve Funds: http://www.lisc.org/docs/resources/effc/bond/2012/2012_Charter_School_Bond_Issuance_v2.pdf)

In the case of the elementary school, we found only one scenario where borrowing the full amount necessary to execute a tax-exempt bond transaction would have “appeared” to be less expensive, i.e. if the school was able to close a deal with a weighted average interest rate of 5%. While the difference in debt service resulting from a 5% interest rate and the actual lease payment for SY 2013-2014 is \$39,293—making the bond transaction appear cheaper—it does not take into account the credit the landlord (the ██████████ Foundation) grants the School at the time of purchase. This credit represents the portion of the rent paid that has amortized the principal on the mortgage loan the landlord, ██████████, has on the facility. If that credit (totaling roughly \$500,000 for both school facilities) is taken into account, there is no scenario suggested by OSC where bonding would have resulted in lower annual facility costs.

See
Note 4
Page 21

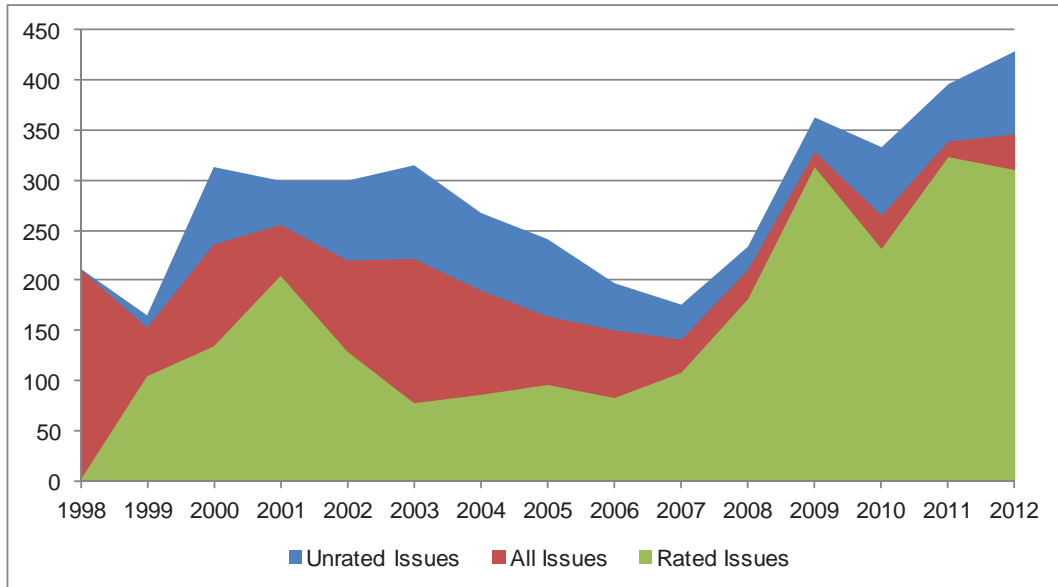
Description	Actual or Assumed Date of Execution	Approx. Purchase Price	Assumed Interest Rate	Transaction Fees	Amount of DSRF	Amort. Term	Loan/Bond Amount \$	Monthly Rent/Debt Service	Monthly Rent/Debt Service vs. SY 2008-2009	SY 2008-2009 Annual Rent/Debt Service	Annual Rent/Debt Service vs. SY 2008-2009	SY 2013-2014 Annual Rent/Debt Service	Annual Rent/Debt Service vs. SY 2013-2014
Krank Street Lease	September 2008	NA	NA	\$0	\$0	NA	NA	\$52,500.00	NA	\$630,000.00	NA	\$735,300.00	NA
Tax-Exempt Bond Transaction	September 2008	\$9,500,000	5.00%	\$625,000	\$696,007	30 years	\$10,821,007	\$58,000.60	\$27,583.94	\$696,007.17	\$66,007.17	\$696,007.17	(\$39,292.83)
Tax-Exempt Bond Transaction	September 2008	\$9,500,000	6.00%	\$625,000	\$785,918	30 years	\$10,915,526	\$65,493.16	\$35,076.50	\$785,917.87	\$155,917.87	\$785,917.87	\$89,910.70
Tax-Exempt Bond Transaction	September 2008	\$9,500,000	7.00%	\$625,000	\$878,442	30 years	\$11,008,050	\$73,203.53	\$42,786.87	\$878,442.39	\$248,442.39	\$878,442.39	\$92,524.52

Moreover, for ACCS to have opted to access the bond market at the time of lease execution (September 2008), it would have been virtually impossible to have achieved anything close to a 5% rate for the following reasons:

1. ACCS was still a new school (only starting its third year) and had no charter renewals to offer to investors as evidence of a stable charter school credit.
2. September 2008 was one of the worst periods in history for a charter school (or similar types of credits) to borrow in the tax-exempt bond market. The worldwide credit crisis pushed spreads between high quality municipal bonds and lower quality sectors to near historic highs with spreads averaging over 250 basis points for all sectors. Spreads for charter school bonds were regularly over 300 basis points higher than sectors with AAA credits. (See chart below).
3. While rates have certainly come down since then—particularly in the second quarter of 2013, the School’s lease is through 2018 and due to the federal program that financed the mortgage loan, prepayments are not permitted until 2017.

See
Note 5
Page 21

**Average Annual Spread to MMD for Charter School Revenue Bonds, 1998-2012
(basis points)**



Comparison with New York City Charter School

The report also refers to “a charter school in New York City which was able to issue bonds with interest rates between 5 percent and 6 percent in March 2013”. It is important to compare ACCS to the school that may be the one which the report references - the [REDACTED]

See
Note 6
Page 22

While both schools are high quality charter schools, the NYC school benefitted a number of factors including credit enhancement from the Charter School Financing Partnership, a full term charter renewal, and a waiting list of almost 2,700 children. Moreover, the School had the ability to borrow through a New York State issuer. New York State charter schools are not authorized to issue tax-exempt bonds, rather they must access the market through a conduit issuer. The NYC school issued via the Build New York Resource Corporation. Charter schools in the City of Albany have only one New York issuer option, i.e. the Albany Capital Resource Corporation. Its Board, however, made it clear in 2011 that it will not approve the issuance of tax-exempt bonds on behalf of charter schools. To date, it has voted down three [REDACTED] network schools ([REDACTED], [REDACTED], and the [REDACTED]), despite its own bond counsel attesting to the fact that all were qualified projects.

As a result, the only way ACCS would be able to get financed is through an out-of-state issuer such as the Phoenix Industrial Development Authority or the Wisconsin Public Finance

Authority. Because bonds issued by these organizations are not legally “New York State paper”, investors do not get the benefit of triple tax-exemption and therefore rates are materially higher than if the borrower was able to access a New York issuer.

Recently, ACCS considered a tax-exempt bond issuance for the purchase of its middle school. The best rate that was offered by a bond investor using an out-of-state issuer was 7.33% - significantly higher than 5%. See Exhibit 2 for [REDACTED] commitment letter.

See
Note 7
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These higher tax-exempt bond rates caused the School to make the decision recently to forego the bond market in to finance the purchase of its middle school building. Instead, it made the decision to opt with a 6% loan with a Community Development Financial Institution (CDFI). Below is the comparative analysis. And while the School did not have the 5% and 6% tax-exempt bond options, we included the debt service payments that would have resulted had they been offered to the School. As you will see, the CDFI loan has materially lower annual payments—and is almost identical to current rent payments. This choice also gives the School the flexibility to opt into the CDFI Loan Guarantee Fund Program for both schools. This Program is a billion dollar program where the U.S. Treasury guarantees bonds issued by CDFIs on behalf of not-for-profits—thereby lowering overall interest rates.

(See link for further information on program:

<http://www.cdfifund.gov/docs/2013/bond/Guarantee%20Program%20-%20Outreach%20Session%20PowerPoint.pdf>

Option	Description	Actual or Assumed Date of Execution	Approx. Purchase Price	Assumed Interest Rate	Transaction Fees	Amount of DSRF	Amort. Term	Loan/Bond Amount \$	New Monthly Rent/Debt Service	New Monthly Rent/Debt Service vs. Current \$	New Annual Rent/Debt Service	New Annual Rent/Debt Service vs. Current \$
MS Baseline	Dove Street - Lease	June 2012	NA	NA	\$0	\$0	NA	NA	\$30,416.67	NA	\$365,000.00	NA
#1	Tax-Exempt Bond Transaction	June 2012	\$5,036,625	5.00%	\$476,798	\$379,001	30 years	\$5,892,424	\$31,583.39	\$1,166.73	\$379,000.71	\$14,000.71
#2	Tax-Exempt Bond Transaction	June 2012	\$5,036,625	6.00%	\$476,798	\$428,123	30 years	\$5,946,154	\$35,676.92	\$5,260.26	\$428,123.09	\$63,123.09
#3	Tax-Exempt Bond Transaction	June 2012	\$5,036,625	7.00%	\$476,798	\$478,525	30 years	\$5,996,556	\$39,877.10	\$9,460.44	\$478,525.17	\$113,525.17
#4	Tax-Exempt Bond Transaction	November 2013	\$4,781,887	7.33%	\$476,798	\$513,594	30 years	\$5,776,887	\$43,992.33	\$13,575.67	\$527,908.00	\$162,908.00
Option Chosen	LISC Loan	November 2013	\$4,781,887	6.00%	\$57,819	\$0	25 years	\$4,839,706	\$31,167.71	\$751.05	\$374,012.47	\$9,012.47

Other comments regarding lease

The report states that *“significant differences between the rent amounts for each school, the escalation or rent payments for the elementary school...”* The two facilities are very different in terms building construction and design. In addition, the Krank Street facility had significant site development costs due to the fact the building is located on a very steep incline. All of these items added to the cost of the facility. It is important to note, however, that the rent payments are a direct pass through of the debt service due on the collateral loan. The escalation in rents on Krank Street are due to increases in debt service. These increases are actually required by the lender in order for the School to get used to paying more for facility costs as it gets closer to the point where it purchases the building. Again, all increases associated with principal amortization are credited to the School at the time of purchase. The School effectively gets some of the benefits of ownership while renting, without the risks of ownership.

See
Note 8
Page 22

As referenced above, as a charter school, the Board has an obligation, and the Board is vested with the ultimate oversight authority, to make business decisions regarding facilities to be used by the school and the most appropriate manner to finance those decisions. These decisions were carefully thought through and considered, with Trustees of the Board exercising their best business judgment, fiduciary duty, duty of care, duty of loyalty and duty and commitment to serving the needs of the stakeholders of, and most importantly students and family at the School.

We appreciate the opportunity to respond to the draft audit report. If you have any further comments or concerns, please do not hesitate to let us know.

Sincerely,

Bramble Buran
Chair – Board of Trustees
Albany Community Charter Schools

Enclosures

APPENDIX B

OSC COMMENTS ON THE SCHOOL'S RESPONSE

Note 1

The relationship between the School and the Foundation is different from a charter school's relationship with a management company. Management company agreements typically cover the specific roles and responsibilities the management company staff performs at the School. The Foundation's invoice did not provide sufficient details to support the fees charged. Without detailed standards, contracts, and invoices, the Board is not properly exercising its fiduciary duty and is unable to adequately measure the performance of the Foundation.

Note 2

Our audit methodology and detailed assumptions for the cost comparison were discussed with School officials during the audit process and at the exit conference. School officials did not question the methodology or assumptions during the course of the audit or at the exit conference. We considered the impact of both interest rate savings and principal savings in our calculations. The total savings is the combination of annual savings that could be achieved by having a lower debt service payment and the principal savings for purchasing the building prior to the end of the lease term. We did not overlook any factors that would have a material impact on the calculation. The School's response does not consider this principal savings.

Note 3

The amortized loan amount used in our report to determine the potential cost includes both a debt service reserve fund and an amount for transaction fees. The amortized loan amount was provided to us by School officials.

Note 4

This analysis was not provided to OSC examiners during fieldwork, nor was the analysis documented in any Board minutes. In addition, the analysis fails to include the principal reduction that was incorporated into OSC's cost savings analysis. While the 5 percent interest rate scenario is the only interest rate presented by OSC where the annual mortgage payment would be less than the School's 2012-13 annual rent, the savings through principal reduction in OSC's analysis is greater than any payment difference in the 6 and 7 percent interest rate scenarios. The principal reduction savings results in a potential cost savings in all interest rate scenarios presented in Table 2.

Note 5

While prepayment of the mortgage loan may not be permitted, the Foundation presented the School with the option to purchase the elementary school building during fieldwork.

Note 6

The New York City charter school named in the response letter was not the charter school described in the report.

Note 7

The cost savings analysis conducted by OSC was for the School's elementary building and not the middle school building. The breakeven interest rate for the middle school could be materially different from the approximate 7.31 percent breakeven interest rate for the elementary school.

Note 8

School officials informed us that the Foundation had chosen the construction site for the elementary school. The Board did not exercise its best judgment and obligation of fiscal responsibility to seek alternative site locations to help reduce the construction cost of the elementary school. The Board could not demonstrate that it identified and fully evaluated other site options.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

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

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

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

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

Site Selection and Lease Agreements:

- We reviewed lease agreements and building documentation and interviewed School officials to gain an understanding of the terms of the lease agreements and the School's ability to purchase each building.
- We reviewed Board minutes and conducted interviews with School officials to determine if the Board had a process for choosing its school locations and documenting the process.
- We compared the lease agreements between two tenants at the same location to determine if School rent was excessive for the middle school location based on price per square foot. We also compared the rent per square foot, purchase price per square foot, and rent as a percentage of the purchase price for each of the School's locations to determine if the elementary school location rent is excessive.
- We reviewed Board minutes to determine when the Board approved the lease agreements, and we determined which Board members were present at the Board meeting when the lease agreements were approved.
- We reviewed the Board members' conflict of interest forms submitted to the Charter School Institute for the particular school year to determine if any Board member had a conflict of interest with the Foundation and, if a Board member did, whether that Board member voted.

Compact Contract:

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

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX D

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