



Financial Performance Framework

MEASURES AND SUMMATIVE PERFORMANCE RATINGS GUIDE

Developed based on framework approved on December 10, 2018 and October 17, 2022, administrative rules approved on July 8, 2019, August 9, 2021, November 22, 2021 and October 17, 2022, and policy and procedures adopted October 16, 2023

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Introduction

Arizona Revised Statutes (“A.R.S.”) requires the Arizona State Board for Charter Schools (“Board”), as a sponsoring entity of a charter school, to ground its actions in evidence of the charter holder’s performance in accordance with the Board’s performance framework and requires the Board’s performance framework to include the financial expectations of the charter school. In December 2018, the Board approved its Financial Performance Framework (“financial framework”) and adopted the administrative rules to implement the financial framework on July 8, 2019. On August 9, 2021, the Board adopted revisions to its financial framework administrative rules.

The financial framework communicates the Board’s expectations for ensuring that all charter holders in its portfolio are viable organizations with strong fiscal management practices. The term “charter holder” refers to the entity that has entered into a charter contract with the Board to operate one or more charter schools. It is important to note that the financial framework analyzes the financial performance of the charter holder, not the charter holder’s process for managing that performance.

Measures

General Overview

This section describes each of the financial framework’s six measures and identifies the applicable calculations, measure ratings and data sources. Defined terms are italicized and identified in all capital letters. Each measure’s subsection includes the definitions applicable to that measure.

The annual statutorily required audits conducted by independent certified public accountants and the average daily membership (“ADM”) calculations completed by the Arizona Department of Education (“Department”) using student attendance data submitted to the Department by the charter holder provide the information necessary to determine a charter holder’s performance under the financial framework.

A charter holder’s performance as evaluated using the financial framework is represented in a dashboard. Through ASBCS Online, the Board has provided online public access to each charter holder’s financial dashboard and the audits of Board-sponsored charter holders. Information about how to access a charter holder’s financial dashboard and annual audits through ASBCS Online is available on the [Board’s website](#).

Going Concern

Description	Accounting principles require charter holder management to evaluate their entity's ability to continue operating. Under auditing standards, the charter holder's independent CPA then audits the conclusion reached by management.
Dashboard Displays	Going Concern
Calculation	Considers absence or presence of certain disclosure in the audit
Measure Ratings	<p>Meets Standard: The most recent audit does not include explanatory paragraph in Independent Auditor's Report or disclosure in the notes to the financial statements <i>(No substantial doubt about the charter holder's ability to continue is raised in the audit)</i></p> <p>Below Standard (in one of two ways):</p> <ol style="list-style-type: none"> 1. Disclosure in Independent Auditor's Report and financial statement notes <i>(Substantial doubt about the charter holder's ability to continue operating is raised in the audit and is not alleviated by management's plans)</i> <p>OR</p> <ol style="list-style-type: none"> 2. Disclosure in financial statement notes only <i>(Substantial doubt about the charter holder's ability to continue operating is raised in the audit, but is alleviated by management's plans)</i>
Data Source	<ul style="list-style-type: none"> ▪ Independent Auditor's Report on the financial statements ▪ Notes to the audited financial statements
Rating Adjustments	None
Definitions	None
Calculation Considerations	None

Default

Description	Failure to make timely payments or comply with other requirements may result in a lender or landlord issuing a notice of default.
Dashboard Displays	Default
Calculation	Considers absence or presence of certain disclosure in the audit
Measure Ratings	<p>Meets Standard: Charter holder is not in default on material loans or facility agreements or both</p> <p>Below Standard: Charter holder is in default on material loans or facility agreements or both</p>

Data Source	▪ Notes to the audited financial statements
Rating Adjustments	None
Definitions	None
Calculation Considerations	None

Unrestricted Days Liquidity

Description	Indicates a charter holder’s available reserve by identifying how many days’ expenses can be paid without another influx of cash.
Dashboard Displays	Available Reserve
Calculation	$(\text{Unrestricted Cash} + \text{OTHER SOURCES OF LIQUIDITY}) \text{ divided by } [(\text{Total Expenses} - \text{NONCASH EXPENSES})/365]$
Measure Ratings	<p>Meets Standard: 30 or more days liquidity</p> <p>Approaches Standard: At least 15 days liquidity but fewer than 30 days liquidity</p> <p>Below Standard: Fewer than 15 days liquidity</p>
Data Source	<ul style="list-style-type: none"> ▪ Audited statement of financial position (balance sheet) ▪ Audited statement of activities (income statement) ▪ Audited statement of cash flows (cash flow statement) ▪ Notes to the audited financial statements ▪ Compliance questionnaire
Rating Adjustments	None
Definitions	<p>OTHER SOURCES OF LIQUIDITY = Available balances from any sources of liquidity other than cash that are disclosed in the audit and may include, but not be limited to, lines of credit.</p> <p>NONCASH EXPENSES = May include depreciation, amortization and write-offs of loan issuance costs and prepayment penalties.</p>
Calculation Considerations	The unspent Classroom Site Fund (“CSF”) balance at June 30 is considered restricted and, therefore, is removed to arrive at the charter holder’s Unrestricted Cash.

Adjusted Net Income

Description	Considers whether a charter holder is operating within its available resources. If the charter holder's adjusted expenses exceed its revenues (negative adjusted net income), then performance on this measure also considers the percentage calculated by dividing the charter holder's adjusted net income by its total revenues.
Dashboard Displays	Revenues Exceed Expenses
Calculation	Total Revenues minus (Total Expenses – <i>NONCASH EXPENSES</i>) [NOTE: If Adjusted Net Income is zero or negative, the Adjusted Net Income is divided by Total Revenues.]
Measure Ratings	<p>Meets Standard: Adjusted net income is greater than or equal to \$1</p> <p>Approaches Standard: Adjusted net income is zero or negative <u>and</u> adjusted net Income divided by total revenues is between 0 and negative 4.99%</p> <p>Below Standard: Adjusted net income is negative <u>and</u> adjusted net income divided by total revenue is less than or equal to negative 5%</p>
Data Source	<ul style="list-style-type: none"> ▪ Audited statement of activities (income statement) ▪ Audited statement of cash flows (cash flow statement)
Rating Adjustments	None
Definitions	NONCASH EXPENSES = May include depreciation, amortization and write-offs of loan issuance costs and prepayment penalties.
Calculation Considerations	None

Lease Adjusted Debt Service Coverage Ratio

Description	Considers how easily debt principal, interest and facility costs can be paid as they become due. A ratio of less than 1.0 means the charter holder is unable to cover its facility and debt costs for the year without dipping into savings or borrowing additional funds.
Dashboard Displays	Facility & Debt Costs Covered
Calculation	(Adjusted Net Income + Interest Expense + Facility Lease Expense) divided by (<i>DEBT PRINCIPAL</i> + Interest + Facility Lease Expense)
Measure Ratings	<p>Meets Standard: Lease adjusted debt service coverage ratio exceeds 1.10</p> <p>Approaches Standard: Lease adjusted debt service coverage ratio is between 1.0 and 1.10</p>

Below Standard:

Lease adjusted debt service coverage ratio is less than 1.0

- Data Source**
- Audited statement of activities (income statement)
 - Audited statement of cash flows (cash flow statement)
 - Notes to the audited financial statements

Rating Adjustments None

Definitions DEBT PRINCIPAL = Includes principal payments associated with bonds or loans for a charter that purchases its facilities, as well as other long-term loans obtained by a charter holder, and capital leases.

Calculation Considerations None

Average Daily Membership

Description Averages the annual percent change in the charter holder’s student count used for state funding for the three most recent completed school years. The measure considers the most recent four fiscal years of average daily membership (“ADM”) data available.

Dashboard Displays Stable or Increasing # of Students

Calculation

1. Calculate the annual growth rates
[NOTE: Year 1 would be the most recent year and Year 4 would be the “oldest” year.]
 Year 1 Growth Rate = (Year 1 – Year 2)/Year 2
 Year 2 Growth Rate = (Year 2 – Year 3)/Year 3
 Year 3 Growth Rate = (Year 3 – Year 4)/Year 4
2. Calculate three-year average
 (Year 1 Growth Rate + Year 2 Growth Rate + Year 3 Growth Rate)/3

Measure Ratings **Meets Standard (in one of two ways):**

1. Charter holder has increase

OR

2. Charter holder has decrease of:

- SMALL: 4.99% or less
- MEDIUM: 4.99% or less
- LARGE: 2.99% or less

Approaches Standard:

Charter holder has decrease of:

- SMALL: 5% to 14.99%
- MEDIUM: 5% to 14.99%
- LARGE: 3% to 9.99%

Below Standard:

Charter holder has decrease of:

- SMALL: 15% or more

- MEDIUM: 15% or more
- LARGE: 10% or more

- Data Source**
- ADM calculations completed by the Department using student attendance data submitted to the Department by the charter holder
- Rating Adjustments**
- A charter holder’s “Approaches Standard” or “Below Standard” rating on this measure will be increased by one rating category if the charter holder received no “Below Standard” ratings and no more than one “Approaches Standard” rating on the financial framework’s other five measures. Under this scenario, an initial “Approaches Standard” on this measure would become a “Meets Standard” and an initial “Below Standard” would become an “Approaches Standard.”
 - A charter holder’s “Approaches Standard” or “Below Standard” rating on this measure will be unchanged if the charter holder received one or more “Below Standard” ratings, two or more “Approaches Standard” ratings or both on the financial framework’s other five measures.
- Definitions**
- SMALL = Charter holder with fewer than 200 ADM
- MEDIUM = Charter holder with 200 to 599 ADM
- LARGE = Charter holder with 600 or more ADM
- Calculation Considerations**
- *ADM Adjustment* – Board staff will adjust the annual ADM for the fiscal years used in the calculation when a) the charter holder reduces the grade levels served at its charter school, b) a school transfers from a multi-school charter contract to its own charter contract, or c) a school operating under a multi-school charter contract closes.
 - *Second/Third Year Charters* – For a charter holder with only two years of ADM available, the annual growth rate will be used. For a charter holder with three years of ADM available, the average of the two annual growth rates will be used.

OTHER CONSIDERATION

In instances where a charter holder entity has multiple charter contracts with the Board and the Board receives audited financial statements that aggregate the financial activities of all the charter contracts, Board staff will note on each charter contract’s financial performance dashboard the overall ADM performance of the charter holder entity using the ratings described below. The charter holder entity’s performance will not affect the individual charter contract’s performance on the Average Daily Membership measure.

- **Meets Standard:** At least two-thirds of the charter contracts individually received a “Meets Standard.”
- **Approaches Standard:** More than one-third of charter contracts individually received an “Approaches Standard,” less than one-third of charter contracts individually received a “Below Standard,” or both.
- **Below Standard:** More than one-third of charter contracts individually received a “Below Standard.”

FIRST-YEAR FINANCIAL REVIEWS

Since only one year of ADM data would be available, the ADM measure will not be applicable for first-year charter contracts. Board staff will conduct a desk review of all new schools approved through the new application, replication application or amendment processes in the fall of their first year of operation. The desk review will include Board staff reviewing information submitted by the charter

holder regarding its operations, financial situation, payroll processes and board financial responsibilities, as well as contract information on file with the Board and ADM, payment and budget information available through the Arizona Department of Education's website. For each new brick-and-mortar school, Board staff will conduct a visit to count students.

Summative Financial Performance Ratings

Good Standing

A charter holder receives a summative financial performance rating of "Good Standing" if the charter holder has no measures rated "Below Standard" and no more than one measure rated "Approaches Standard." A charter holder with a rating of "Good Standing" meets the Board's financial performance expectations.

Adequate Standing

A charter holder receives a summative financial performance rating of "Adequate Standing" if the charter holder has no measures rated "Below Standard" and two or more measures rated "Approaches Standard." A charter holder with a rating of "Adequate Standing" meets the Board's financial performance expectations.

Intervention

A charter holder receives a summative financial performance rating of "Intervention" if the charter holder either has a) one or more measures rated "Below Standard" or b) three consecutive years in "Adequate Standing." A charter holder assigned an "Intervention" rating for the first time must submit information to the Board regarding the charter holder's financial performance. A charter holder that receives an "Intervention" rating for two or more consecutive years shall be placed "On Probation," shall be determined to not meet the Board's financial performance expectations, and must submit information to the Board.

For additional information regarding the financial intervention process, review the *"First-Time" Financial Intervention Process Guide* and *"On Probation" Financial Intervention Process Guide* available on the [Board's website](#) in the "Financial Performance Framework" section.

Appendices

- A. Description, Calculation and Data Source for Six Framework Measures
- B. "Meets," "Approaches," and "Below" Standard Ratings for Six Framework Measures
- C. Policy and Procedures for Revising the Board's Performance Frameworks

A. Description, Calculation and Data Source for Six Framework Measures

	Going Concern	Default	Unrestricted Days Liquidity	Adjusted Net Income	Lease Adjusted Debt Service Coverage Ratio	Average Daily Membership
Dashboard Displays	Going Concern	Default	Available Reserve	Revenues Exceed Expenses	Facility & Debt Costs Covered	Stable or Increasing # of Students
Description	Accounting principles require charter holder management to evaluate their entity's ability to continue operating. Under auditing standards, the charter holder's independent CPA then audits the conclusion reached by management.	Failure to make timely payments or comply with other requirements may result in a lender or landlord issuing a notice of default.	Indicates a charter holder's available reserve by identifying how many days' expenses can be paid without another influx of cash.	Considers whether a charter holder is operating within its available resources. If the charter holder's adjusted expenses exceed its revenues (negative adjusted net income), then performance on this measure also considers the percentage calculated by dividing the charter holder's adjusted net income by its total revenues.	Considers how easily debt principal, interest and facility costs can be paid as they become due. A ratio of less than 1.0 means the charter holder is unable to cover its facility and debt costs for the year without dipping into savings or borrowing additional funds.	Averages the annual percent change in the charter holder's student count used for state funding for the three most recent completed school years. The measure considers the most recent four fiscal years of average daily membership ("ADM") data available. ¹
Calculation	Considers absence or presence of certain disclosure in the audit	Considers absence or presence of certain disclosure in the audit	(Unrestricted Cash + Other Sources of Liquidity) divided by [(Total Expenses – Noncash Expenses)/365] [NOTE: The unspent CSF balance at year-end (June 30) is considered restricted and is removed to arrive at the charter holder's Unrestricted Cash.]	Total Revenues minus (Total Expenses – Noncash Expenses) [NOTE: If Adjusted Net Income is zero or negative, then Adjusted Net Income is divided by Total Revenues.]	(Adjusted Net Income + Interest Expense + Facility Lease Expense) divided by (Debt Principal + Interest + Facility Lease Expense)	1. Calculate Annual Growth Rates ("GR") [NOTE: Year 1 would be the most recent year and Year 4 would be the "oldest" year.] Year 1 GR = (Year 1 – Year 2)/Year 2 Year 2 GR = (Year 2 – Year 3)/Year 3 Year 3 GR = (Year 3 – Year 4)/Year 4 2. Calculate Three-Year Average ² (Year 1 GR + Year 2 GR + Year 3 GR)/3
Data Source	<ul style="list-style-type: none"> Independent Auditor's Report on the financial statements Notes to the audited financial statements 	<ul style="list-style-type: none"> Notes to the audited financial statements 	<ul style="list-style-type: none"> Audited statement of financial position, audited statement of activities <u>and</u> audited statement of cash flows Notes to the audited financial statements Compliance questionnaire 	<ul style="list-style-type: none"> Audited statement of activities and audited statement of cash flows 	<ul style="list-style-type: none"> Audited statement of activities <u>and</u> audited statement of cash flows Notes to the audited financial statements 	<ul style="list-style-type: none"> ADM calculations completed by the Arizona Department of Education ("Department") using student attendance data submitted to the Department by the charter holder

¹ Board staff will adjust the annual ADM for the fiscal years used in the calculation when a) the charter holder reduces the grade levels served at its charter school, b) a school transfers from a multi-school charter contract to its own contract, or c) a school operating under a multi-school charter contract closes.

² For a charter holder with only two years of ADM available, the annual growth rate will be used. For a charter holder with three years of ADM available, the average of the two annual growth rates will be used.

B. “Meets,” “Approaches,” and “Below” Standard Ratings for Six Framework Measures

	Going Concern	Default	Unrestricted Days Liquidity	Adjusted Net Income	Lease Adjusted Debt Service Coverage Ratio	Average Daily Membership ^{3 4}
Meets Standard	No substantial doubt about the charter holder’s ability to continue is raised in the Independent Auditor’s Report or the notes to the audited financial statements	Charter holder is not in default on material loans or facility agreements or both	30 or more days liquidity	Adjusted net income is greater than or equal to \$1	Lease adjusted debt service coverage ratio exceeds 1.10	1. Charter holder has <u>increase</u> OR 2. Charter holder has <u>decrease</u> of: <ul style="list-style-type: none"> • <i>SMALL</i>: 4.99% or less • <i>MEDIUM</i>: 4.99% or less • <i>LARGE</i>: 2.99% or less
Approaches Standard	<i>No “Approaches Standard” criteria established for this measure</i>	<i>No “Approaches Standard” criteria established for this measure</i>	At least 15 days but fewer than 30 days liquidity	Adjusted net income is zero or negative <u>and</u> adjusted net income divided by total revenues is between 0% and negative 4.99%	Lease adjusted debt service coverage ratio is between 1.0 and 1.10	Charter holder has <u>decrease</u> of: <ul style="list-style-type: none"> • <i>SMALL</i>: 5% to 14.99% • <i>MEDIUM</i>: 5% to 14.99% • <i>LARGE</i>: 3% to 9.99%
Below Standard	1. Substantial doubt about the charter holder’s ability to continue operating is raised in the Independent Auditor’s Report and notes to the audited financial statements and is not alleviated by management’s plans OR 2. Substantial doubt about the charter holder’s ability to continue operating is raised in the notes to the audited financial statements, but is alleviated by management’s plans	Charter holder is in default on material loans or facility agreements or both	Fewer than 15 days liquidity	Adjusted net income is negative <u>and</u> adjusted net income divided by total revenues is less than or equal to negative 5%	Lease adjusted debt service coverage ratio is less than 1.0	Charter holder has <u>decrease</u> of: <ul style="list-style-type: none"> • <i>SMALL</i>: 15% or more • <i>MEDIUM</i>: 15% or more • <i>LARGE</i>: 10% or more

³ A charter holder’s “Approaches Standard” or “Below Standard” rating on the Average Daily Membership measure will be increased by one rating category if the charter holder received no “Below Standard” and no more than one “Approaches Standard” rating on the financial framework’s other five measures. Under this scenario, an initial “Approaches Standard” on the Average Daily Membership measure would become a “Meets Standard” and an initial “Below Standard” would become an “Approaches Standard.” A charter holder’s “Approaches Standard” or “Below Standard” rating on the ADM measure will be unchanged if the charter holder received one or more “Below Standard” ratings, two or more “Approaches Standard” ratings, or both on the financial framework’s other five measures.

⁴ The criteria identified will be applied to charter holders with only two years of ADM available (annual growth rate) or charter holders with three years of ADM available (average of two annual growth rates).

C. Policy and Procedures for Revising the Board's Performance Frameworks

In October 2023, the Board established the following policy and procedures for revising its Academic Performance Framework, Financial Performance Framework and Operational Performance Framework (collectively referred to as "Performance Frameworks" or individually as the "Academic Framework," "Financial Framework" and "Operational Framework").

1. Beginning with the conclusion of the fiscal year 2024 cycle¹, Board staff shall at least annually review the Performance Frameworks. The annual review shall include the analysis identified in Step 1a and will consider, as applicable, the data and information identified in Steps 1b through 1l.
 - a. The portfolio's overall performance under the Performance Frameworks, to include overall performance by measure and trends. A review of trends will include, but not be limited to considering the most recent and two prior years, reviewing to determine percentages of charters that met and did not meet the Board's standards and expectations.
 - b. Issues or items identified through the analysis completed under Step 1a of the Performance Frameworks' data, including any risks or pressure points.
 - c. Lessons learned by Board staff during the most recent year implementing the Performance Frameworks.
 - d. Performance of schools that closed during the fiscal year under review to identify any possible issues or risks with the current Performance Frameworks.
 - e. Board member feedback received on the Performance Frameworks.
 - f. Stakeholder feedback received on the Performance Frameworks.
 - g. Actions taken by other agencies (e.g., Arizona Department of Education, State Board of Education) that may affect the Performance Frameworks.
 - h. Statutory or regulatory changes that may affect the Performance Frameworks.
 - i. Data maintained by other agencies (e.g., academic performance data, average daily membership).
 - j. Results of reviews or audits of the Board conducted by outside organizations, including national, state or local entities.
 - k. Best practices for charter school authorizing.
 - l. Any other relevant information.
2. The review under Step 1 will take place for each individual framework no more than six months after the charter holder/school performance dashboards are finalized for a given fiscal year under a framework.
3. Upon completing the review required under Step 1, Board staff will select the applicable option below based on the review results.
 - a. Recommend to the Board that no changes be made to the Performance Frameworks.

¹ The fiscal year 2024 cycle would include charter holders' fiscal year 2024 performance results under the Academic Framework and Operational Framework and charter holders' fiscal year 2023 performance results under the Financial Framework determined using the audits and average daily membership received by the Board in fiscal year 2024.

- b. Recommend to the Board that no changes be made to the Performance Frameworks at this time, but that additional data be collected.
 - c. Release for public comment proposed changes to the Performance Frameworks. Public comment opportunities and Board consideration will occur in accordance with the Board’s [“Procedures for Rule and Policy Adoption”](#).
 - d. Request the Board establish a subcommittee to consider whether changes should be made to the Performance Frameworks and to make a recommendation to the full Board. Generally, the subcommittee option would apply when at least one of the following is true:
 - i. Board staff proposes significantly changing the Performance Frameworks’ measures or overall ratings in a way that is not generally accepted as an improvement/positive change by stakeholders.
 - ii. Board staff proposes adding new or significantly changing existing processes under the Performance Frameworks in a way that is not generally accepted as an improvement/positive change by stakeholders.
 - iii. Board staff proposes adding new or significantly changing existing processes such that a final decision on how to proceed would benefit from stakeholder discussions when a clear path for addressing a concern is not evident or when multiple valid options exist.
4. The annual review of the Academic Framework, Financial Framework and Operational Framework required under Step 1 may occur separately or simultaneously.
5. Board staff shall annually report the review results and next steps for the Academic Framework, Financial Framework and Operational Framework at a regularly scheduled public Board meeting as described below.
- a. Board staff may choose to report out all three frameworks’ results at the same Board meeting or report out individual framework’s results at separate Board meetings, so long as all three reports occur within the timeframes and under the conditions identified in Step 5b through Step 5d.
 - b. If Board staff’s review results in proposed changes under Step 3c, then Board staff shall provide the report to the Board prior to releasing the proposed changes for public comment.
 - c. If Board staff’s review results in a subcommittee being requested under Step 3d, then Board staff shall provide the report to the Board at the same meeting at which the Board considers Board staff’s request to establish a subcommittee.
 - d. The review results for the Academic Framework, Financial Framework and Operational Framework must be reported to the Board no later than the November Board meeting unless circumstances outside of Board staff’s control make that not possible (e.g., release of letter grades delayed, federal government extends deadline for submitting single audits). In situations where circumstances outside of Board staff’s control occur, then the report to the Board must occur no later than 2 months after the situation is resolved (e.g., letter grades are released, deadline extension passes) or the next regularly scheduled Board meeting after that date.

6. Board members or, if applicable, subcommittee members may direct Board staff on additional data and information that should be collected and analyzed.
7. Documentation demonstrating compliance with the policy and procedures, such as presentations given at or materials prepared for Board meetings, shall be maintained by Board staff.
8. The policy and procedures do not prevent the Board from responding quickly to address concerns with its Performance Frameworks as they are raised or making changes to its Performance Framework at other times, provided that the review required under Step 1 occurs annually within the timeframes specified in Step 5 and the actions taken outside of the annual review adhere to the Board's "[Procedures for Rule and Policy Adoption](#)".