Ha:san Educational Services 11/13/14

Arizona State Board for Charter Schools

Response to October 2014 letter*: Financial Performance Sustainability Indicators based upon 2013 Audit.*

Near-Term Indicators

Going Concern

This finding was based upon Note 10 to the f/y 13 Audit Financial Statements, to wit:

"For fiscal years 2013 and 2012, the School experienced decreases in net assets and in fiscal 2013 experienced negative cash flows from operations. Also at June 30, 2013 the School has a deficit in working capital of $650,897. These decreases have put a strain on the liquidity of the school. The financial statements do not include any adjustments due to the School's liquidity issues."

Management and the Board are aggressively pursuing additional students to reduce the liquidity strain and establish an adequate cash reserve. It has also developed plans to reduce expenses, extend note payable maturities and realize additional grant funding from Title VIII. Management projects that all cash needs will be met throughout fiscal 2014 with an ending cash surplus remaining."

During fiscal 2014, the School replaced its ASRS pension plan with a 401k plan saving the school over $100,000 in pension and related expenses. Also, during f/y 14 and into early f/y 15, actions were taken to reduce bus lease expenses for a future annual saving of over $60,000 and changed its copier lease situation to realize a further annual saving of about $5,000.Other cost-cutting measures were also taken. Student count went from 145 to 158 in f/y 14.

Despite some additional costs associated with lease payoffs etc, the school had positive net income of over $140,000 and has budgeted for net income of over $100,000 in the current fiscal year. This is despite continuing deferrals and shortfalls in Title VIII fundings (the past 3 years have seen a Title VIII accumulated shortfall versus calculated benefit of nearly $400,000 – management expects that it will be paid at least half of this amount in the future). Title VIII accounts for nearly 40% of the school's funding.

The school finished fiscal 2014 with a modest cash surplus.

Unrestricted Day's Liquidity

This measure is showing gradual improvement, but, at the current level of 17 days, is still under target levels. Realization of owed amounts from federal sources, continuation of positive net income trends and reductions in non-income cash costs should allow for further improvement in this measure in the second half of the current fiscal year.

Sustainability Indicators

Net Income

Due to severe cuts in both state and federal funding, deferrals in federal funding, and carry-over costs associated with the closing of its Middle School, Ha:san exhibited negative Net Income of ($179,578). Although major cost cutting measures were implemented, they could not be put into place quickly enough to offset the shortfalls.

As a result of these measures, however, the school showed a sharp turn-around, and fiscal 2014 the school had net operating income of $142, 395. For the first four months of the current fiscal year, operating income exceeded $200,000. Even assuming continued short-term revenue

volatility, the school budget for the full year anticipates net income in excess of $100,000 with commensurate improvement in financial ratios.

Fixed Charge Coverage Ratio

This ratio, .13 in f/y 13 was very low and continued weak into f/y 14 due to net losses and other factors leading to a decline in assets.

With a swing to positive net income and an expected moderate increase in assets coupled with a sharp reduction in lease expenses as described previously, current data suggests that a 1.1 coverage ratio is achievable in f/y 15.

Cash Flow

Cash flow in f/y 14 was negative, also reflecting the operating environment, however, as a consequence of aforementioned cost control and other measures not fully implemented during the year, the cash flow decline was more than cut in half. To date, cash flows are positive, and are expected to be so for the full f/y 15 and subsequent years.

As the Standard is for three consecutive years, the Meets Standard criteria cannot be met until f/y 16.

Frank Prezelski, CFA
Director of Finance & Operations
Ha:san Educational Services/Ha:san Preparatory & Leadership School