

---

**AGENDA ITEM:** Compliance Matters – Legacy Education Group

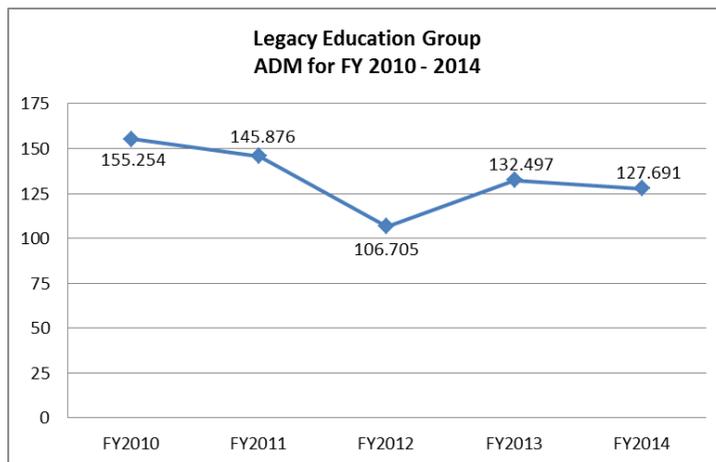
**Issue**

Based on its submitted fiscal year 2013 audit, Legacy Education Group has violated state record retention requirements during three of the last four fiscal years by not retaining supporting documentation for all of its non-payroll cash disbursements. Additionally, the fiscal year 2013 audit included a qualified auditors’ opinion on the financial statements because of the nature of the charter holder’s records.

Pursuant to the Board’s [Audit & Compliance Questionnaire Follow-up Matrix](#), the charter holder has been placed on the agenda for the Board’s consideration.

**Background**

Legacy Education Group operates one school, East Valley High School, serving grades 9-12 in Mesa. The graph below shows the charter holder’s 100<sup>th</sup> day average daily membership (ADM) for fiscal years 2010 through 2014.



The academic dashboard for the charter school operated by the charter holder has been included below. Legacy Education Group had its five-year interval review in fiscal year 2011 and the charter holder’s academic performance is being monitored under the Board’s Academic Intervention Schedule.

Academic Performance							
East Valley High School							
		2012 Traditional High School (9-12)			2013 Traditional High School (9 to 12)		
		Measure	Points Assigned	Weight	Measure	Points Assigned	Weight
<b>1. Growth</b>							
1a. SGP	Math	NR	0	0	44	50	15
	Reading	71	100	30	37	50	15
1b. SGP Bottom 25%	Math	NR	0	0	NR	0	0
	Reading	NR	0	0	NR	0	0
<b>2. Proficiency</b>							
2a. Percent Passing	Math	41 / 51.7	50	10	37.5 / 47.4	50	10
	Reading	63 / 74.4	50	10	61.3 / 72.8	25	10
2b. Composite School Comparison	Math	-8	50	7.5	-0.3	50	7.5
	Reading	-8.1	50	7.5	-2.1	50	7.5
2c. Subgroup ELL	Math	NR	0	0	NR	0	0
	Reading	NR	0	0	NR	0	0
2c. Subgroup FRL	Math	46 / 42.7	75	7.5	33.3 / 43.1	50	3.75
	Reading	70 / 66.8	75	7.5	61.9 / 70	50	3.75
2c. Subgroup SPED	Math	NR	0	0	12.5 / 11.4	75	3.75
	Reading	NR	0	0	27.3 / 37.9	50	3.75
<b>3. State Accountability</b>							
3a. State Accountability		C	50	5	D	25	5
<b>4. Graduation</b>							
4a. Graduation		54	25	15	54	25	15
<b>Overall Rating</b>		Overall Rating			Overall Rating		
Scoring for Overall Rating 89 or higher: Exceeds Standard <89, but > or = to 63: Meets Standard <63, but > or = to 39: Does Not Meet Standard Less than 39: Falls Far Below Standard		63.12		100	43.44		100

The charter holder's financial dashboard has been included below.

Financial Performance - Fiscal Year 2013 Audit			
Legacy Education Group			
Near-Term Indicators			
Going Concern	Yes	Falls Far Below	
Unrestricted Days Liquidity	11.53	Falls Far Below	
Default	No	Meets	
Sustainability Indicators			
Note: Negative numbers are indicated below by parentheses.			
Net Income	(\$541,004)	Does Not Meet	
Fixed Charge Coverage Ratio	0.29	Does Not Meet	
Cash Flow (3-Year Cumulative)	\$72,157	Meets	
Cash Flow Detail by Fiscal Year	FY 2013	FY 2012	FY 2011
	\$58,101	\$14,056	-
Does Not Meet Board's Financial Performance Expectations			

### **Financial Record Retention**

Based on its fiscal years 2010, 2011 and 2013, Legacy Schools has failed to comply with financial record retention requirements found in the *General Retention Schedules for Education – K-12* published by the Arizona State Library, Archives and Public Records for three of the past four fiscal years. According to the fiscal year 2013 audit, 5 of 30 non-payroll cash disbursements tested did not have supporting documentation on file, and 4 of 12 bank statements sampled from the fiscal year were not on file.

Between February 2014 and July 2014, Board staff and the charter holder communicated regarding this matter. The charter holder provided Board staff with the information and documentation requested. Based upon a review of the information provided, the charter holder has:

- Provided a printout from its accounting system of all non-payroll disbursements for July 1, 2013 through May 20, 2014.
- Provided supporting documentation for 20 non-payroll disbursements selected from the printout by Board staff.
- Addressed steps taken to ensure future compliance in this area. These steps include copies of supporting documentation and bank statements being maintained by the third party vendor with the charter holder maintaining the originals and revisions to the charter holder's Debit Card Use Policy addressing documentation requirements.

### **Qualified Auditors' Opinion**

The fiscal year 2013 audit included a qualified auditors' opinion on the financial statements because of the nature of the charter holder's records. The auditors' report indicated the audit firm was unable to obtain complete records supporting the charter holder's accounts payable balance stated at \$117,451 and the "receivable from other agencies" balance stated at \$490,291 as of June 30, 2013. In communications with the audit firm that occurred subsequent to the audit's submission, the audit firm identified for Board staff three findings that provide additional information regarding the qualified opinion. The findings addressed record retention (see "Financial Record Retention" section above), detail tie-in of accounts payable, and cost allocation with Legacy Schools.

Between February 2014 and July 2014, Board staff communicated with the charter holder regarding this matter. The charter holder provided Board staff with the information and documentation requested. Based upon a review of the information provided, in addition to the items addressed in the "Financial Record Retention" section above, the charter holder has:

- Provided a copy of its "Policy for Determination of Shared Costs" with Legacy Schools.
- Contracted with a third party vendor for accounting services.

### **Other Matters**

In addition to the matters identified above, the fiscal year 2013 audit identified weaknesses in internal controls related to segregation of duties. The charter holder submitted a satisfactory corrective action plan. Further, the fiscal year 2013 audit identified issues related to nonpayment of certain payroll taxes to the Internal Revenue Service and the Arizona Department of Revenue for the audited fiscal year and the late payment of state unemployment contributions to the Arizona Department of Economic Security subsequent to fiscal year end. The audit indicates that the charter holder leases employees from Legacy Schools, which is responsible for paying the costs of salaries, taxes and benefits of the employees provided to the charter holder. Since the audit indicates the charter holder paid the full amount due to Legacy Schools under this agreement and the payroll taxes are the responsibility of Legacy Schools, the charter holder was not required to submit a corrective action plan regarding these issues.

### **Board Options**

Option 1: The Board may choose to withhold 10% of the charter holder's monthly State aid apportionment and to issue a Notice of Intent to Revoke the charter holder's charter contract unless the charter holder agrees to

the terms of a consent agreement. Staff recommends the following language for consideration: I move to find Legacy Education Group is in noncompliance with state law for its failure to comply with financial record retention requirements and approve withholding 10% of the charter holder's monthly State aid apportionment until compliance is demonstrated through no material weaknesses, significant deficiencies or other instances of noncompliance being identified in the charter holder's fiscal year 2014 audit report package relating to noncompliance with financial record retention requirements.

Further, I move to issue a Notice of Intent to Revoke the charter contract of Legacy Education Group for failing to comply with state law and its charter contract when it failed to comply with state financial record retention requirements, which contributed to the charter holder's fiscal year 2013 audit including a qualified opinion on the financial statements.

- Within 48 hours of receipt of the Notice the charter operator shall notify staff and parents/guardians of registered students of the Notice of Hearing on Intent to Revoke Charter and provide a school location where the copy may be reviewed;
- Within 20 days of receipt of the Notice the charter operator shall provide copies of all correspondence and communications used to comply with the preceding provision; and
- Within 20 days of receipt of the Notice the charter operator shall provide the Board with the names and mailing addresses of parents/guardians of all students registered with the school.

All that taken into consideration, the Board will enter into a consent agreement that includes the same terms and provisions as the consent agreement included with the staff report provided for this agenda item.

If Legacy Education Group is unwilling to agree to the terms of the consent agreement and a signed consent agreement, along with governing board minutes approving the consent agreement, are not received within 20 business days of today's date, then it is the Board's decision that the 10% withholding will begin with the charter holder's October payment and the revocation process will proceed based on the reasons already specified.

Option 2: The Board may choose to withhold 10% of the charter holder's monthly State aid apportionment and to issue a Notice of Intent to Revoke the charter holder's charter contract. The following language is provided for consideration: I move to find Legacy Education Group is in noncompliance with state law for its failure to comply with financial record retention requirements and approve withholding 10% of the charter holder's monthly State aid apportionment until compliance is demonstrated through no material weaknesses, significant deficiencies or other instances of noncompliance being identified in the charter holder's fiscal year 2014 audit report package relating to noncompliance with financial record retention requirements.

Further, I move to issue a Notice of Intent to Revoke the charter contract of Legacy Education Group for failing to comply with state law and its charter contract when it failed to comply with state financial record retention requirements, which contributed to the charter holder's fiscal year 2013 audit including a qualified opinion on the financial statements.

- Within 48 hours of receipt of the Notice the charter operator shall notify staff and parents/guardians of registered students of the Notice of Hearing on Intent to Revoke Charter and provide a school location where the copy may be reviewed;
- Within 20 days of receipt of the Notice the charter operator shall provide copies of all correspondence and communications used to comply with the preceding provision; and
- Within 20 days of receipt of the Notice the charter operator shall provide the Board with the names and mailing addresses of parents/guardians of all students registered with the school.

Option 3: The Board may choose to withhold 10% of the charter holder's monthly State aid apportionment. The following language is provided for consideration: I move to find Legacy Education Group is in

noncompliance with state law for its failure to comply with financial record retention requirements and approve withholding 10% of the charter holder's monthly State aid apportionment until compliance is demonstrated through no material weaknesses, significant deficiencies or other instances of noncompliance being identified in the charter holder's fiscal year 2014 audit report package relating to noncompliance with financial record retention requirements.

## **CONSENT AGREEMENT**

This Consent Agreement (“Agreement”) is made by and between Legacy Education Group (“Charter Operator”), a nonprofit corporation organized under the laws of the state of Arizona and operating East Valley High School, a charter school, and the Arizona State Board for Charter Schools (“Board”) collectively referred to herein as the “Parties.”

### **JURISDICTION**

The Board is charged by Arizona Revised Statutes (“A.R.S.”) §§ 15-182(E)(1) and (2) and 15-183(R) with granting charter status to qualifying applicants for charter schools and exercising general supervision over the charter schools it sponsors. A charter is effective for fifteen years. A.R.S. § 15-183(I). The charter may be renewed for successive periods of twenty years. A.R.S. § 15-183(J). The Board may submit a request to the Arizona Department of Education to withhold up to ten percent of the monthly apportionment of state aid that would otherwise be due a charter school if the Board determines at a public meeting that the charter school is not in compliance with federal law, with the laws of this state or with its charter. A.R.S. § 15-185(H). The Board may revoke a charter of a school it sponsors at any time if the charter school breaches one or more provisions of its charter or if the Board determines that the charter holder has failed to comply with charter school statutes or any provision of law from which the charter school is not exempt. A.R.S. § 15-183(I)(3).

### **RECITALS**

1. The Charter Operator operates East Valley High School (“the School”) pursuant to a charter contract (“Charter”) executed on May 17, 2005 between the Charter Operator and the Board.
2. Pursuant to A.R.S. § 15-183 and the Charter, the Board sponsors the Charter

Operator to operate one school site to serve students in grades nine through twelve.

3. Kathy Tolman is the Charter Representative and person authorized to execute documents on behalf of the Charter Operator.

4. The Charter of the Charter Operator and the Board requires that the Charter Operator comply with all state, federal and local laws applicable to the operation of a charter school.

5. A.R.S. §§ 15-183(E)(6) and 15-914 and the Charter of the Charter Operator and the Board require that the Charter Operator undergo an annual financial and compliance audit, including the completion of a legal compliance questionnaire, by an independent certified public accountant (“Annual Audit”).

6. A.R.S. § 39-121.01 requires the Charter Operator to maintain and preserve all records reasonably necessary or appropriate to maintain an accurate knowledge of its official activities which are supported by state monies.

7. The Charter Operator is required to retain financial records in accordance with the General Retention Schedules for Education – K-12 published by the Arizona State Library, Archives and Public Records.

8. The Charter Operator’s Annual Audit for the fiscal years ending June 30, 2010, 2011 and 2013 found that the Charter Operator failed to retain financial records, including invoices and other supporting documentation.

9. The Charter Operator’s failure to retain financial records contributed to the Charter Operator’s Annual Audit for the fiscal year ending June 30, 2013 including a qualified auditors’ opinion on the financial statements.

10. The Charter Operator breached its Charter and state law when it failed to

maintain, preserve and retain financial records as identified in the Annual Audit for the fiscal years ending June 30, 2010, 2011 and 2013.

11. At its public meeting held on August 11, 2014, the Board determined that the Charter Operator was not in compliance with the laws of this state and with its Charter when it failed to retain financial records as demonstrated by three of the Charter Operator's last four Annual Audits. The Board passed a motion to withhold ten percent of the monthly apportionment of state aid that would otherwise be due the Charter Operator and to issue a notice of intent to revoke the Charter of the Charter Operator. The Board's motion provided for the Parties to enter into a consent agreement in lieu of a revocation proceeding and hearing, and the withholding of ten percent of the Charter Operator's monthly apportionment of state aid.

#### **AGREEMENT TERMS AND CONDITIONS**

The Parties agree as follows:

12. Because of the Board's determination that the Charter Operator is not in compliance with the laws of this state or with its Charter, the Charter Operator is subject to a withholding of ten percent of its monthly apportionment of state aid.

13. Because of the Board's decision to issue a notice of intent to revoke the Charter, the Charter Operator is subject to the revocation and termination of its Charter.

14. A.R.S. §§ 15-183(Q) and 41-1092.07(F)(5) provide that informal disposition of this matter may be made by stipulation, agreed settlement, consent order or default.

15. In consideration of the Parties foregoing their option to proceed with the charter revocation proceedings and hearing, it is in the best interests of the Board and the Charter Operator to mutually resolve this matter.

The Charter Operator agrees as follows:

16. The Charter Operator waives its right to a hearing and to provide its defense, except as set forth herein, on the Recitals set forth in this Agreement.

17. By entering into this Agreement, the Charter Operator agrees to the Recitals set forth in this Agreement and understands that it cannot contest any of the Recitals in the future.

18. This Agreement does not limit other actions the Board may take under the law if it determines that the Charter Operator is not in compliance with its Charter or with state or federal law.

19. The Charter Operator shall retain its financial records, including invoices, other supporting documentation, and bank statements, in accordance with the General Retention Schedules for Education – K-12 (financial records) published by the Arizona State Library, Archives and Public Records. Compliance with this provision shall be demonstrated by no material weaknesses, significant deficiencies or other instances of noncompliance being identified through the Charter Operator's Annual Audits for the fiscal years ending June 30, 2014 through 2019 related to noncompliance with financial record retention requirements and by the Annual Audit auditors' report including an unqualified opinion on the Charter Operator's financial statements for the fiscal years ending June 30, 2014 through 2019.

The Parties agree as follows:

20. If the Charter Operator fails to comply with the terms and conditions of this Agreement, the Board may, on no less than thirty (30) calendar days' notice, hold a hearing at which time the Board will receive information to determine whether evidence exists that the Charter Operator failed to comply with the terms and conditions of this Agreement. The Charter Operator shall be entitled to present all appropriate evidence at this hearing. If the Board determines that a breach of this Agreement has occurred, the Board may revoke the Charter Operator's Charter to

operate the School and terminate its Charter for breach of this Agreement and of its Charter and the state and federal laws identified in the Recitals.

21. The Board may also consider the Charter Operator's failure to comply with the terms and conditions of this Agreement in its determination of the Charter Operator's request for the renewal of its Charter.

22. This Agreement is not binding on either party until both the Board and the Charter Operator's governing board accept it by the number of votes necessary to pass a measure at a public meeting. This Agreement is effective immediately upon its approval and execution by the authorized representatives of the Charter Operator and the Board.

23. If either party rejects this Agreement or any part of it, then this Agreement is null and void, and not binding on the Parties and the Board may proceed with the charter revocation hearing and may direct the Arizona Department of Education to begin withholding ten percent of the Charter Operator's monthly state aid apportionment.

24. The Charter Operator has the legal right to consult with an attorney prior to entering into this Agreement.

25. The Parties shall be responsible for their own attorneys' fees and costs, if any, in this matter.

ARIZONA STATE BOARD FOR CHARTER SCHOOLS

\_\_\_\_\_  
By: Janna Day  
President, Arizona State Board for Charter Schools  
Date: \_\_\_\_\_

LEGACY EDUCATION GROUP AND EAST VALLEY HIGH SCHOOL

\_\_\_\_\_  
By: Kathy Tolman

Charter Representative, Legacy Education Group  
Date: \_\_\_\_\_

COPY mailed this  
\_\_\_\_\_ day of \_\_\_\_\_, 2014 to:

Legacy Education Group  
Attention: Kathy Tolman, Charter Representative  
7420 East Main Street  
Mesa, AZ 85207

By \_\_\_\_\_