

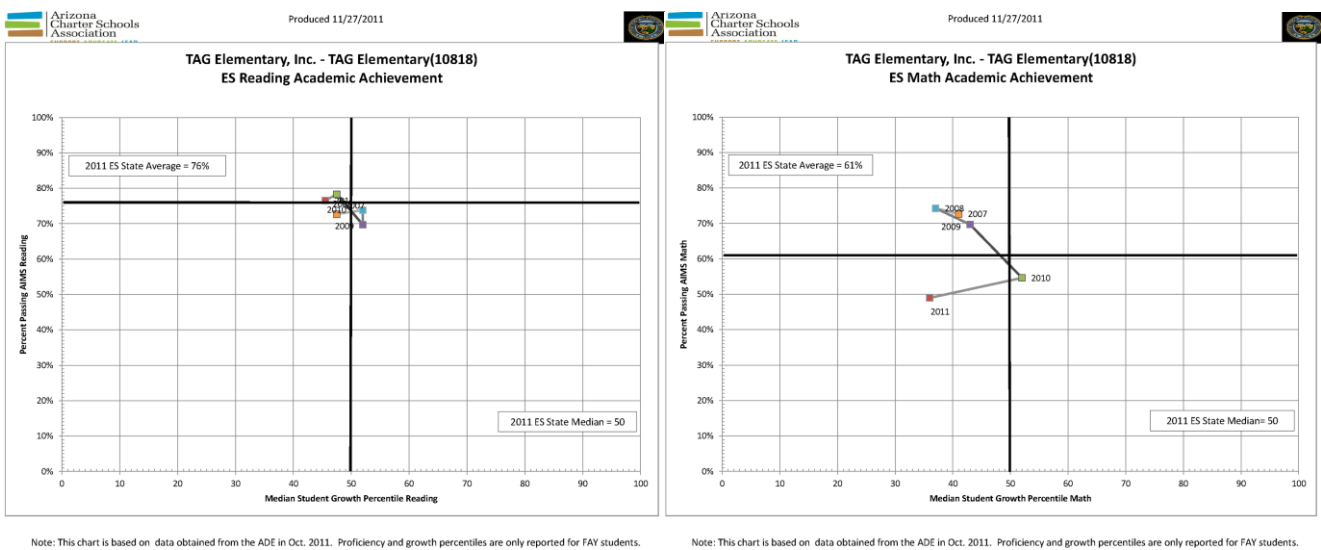
AGENDA ITEM: Compliance Matters – TAG Elementary, Inc.

Issue

Based on its submitted fiscal year 2011 audit, TAG Elementary, Inc. has violated federal payroll tax requirements during three of the last four fiscal years by not depositing taxes required to be deducted and withheld from wages of its employees and related taxes into the Treasury of the United States. 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

TAG Elementary, Inc. operates one school site serving grades K-8 in Tucson. As of February 8, 2012, the school’s 40th day ADM for fiscal year 2012 is 212.587. The graphs below are representations of the academic performance of TAG Elementary.



TAG Elementary, Inc. was notified of its eligibility to apply for renewal in December 2011. As part of the renewal application, TAG Elementary, Inc. is required to submit a performance management plan. If TAG Elementary, Inc. chooses to apply for renewal, it must submit its renewal application package by March 24, 2012 and the renewal application package must be considered by the Board prior to June 24, 2012.

Federal Payroll Taxes

Based on the annual audits, TAG Elementary, Inc. has failed to comply with federal payroll tax requirements in fiscal years 2008, 2009 and 2011. According to the fiscal year 2011 audit, the charter holder had outstanding federal payroll taxes payable from fiscal year 2011, as well as from the two previous fiscal years.¹ A letter dated February 28, 2012 from TAG Elementary, Inc. states that the total amount of back taxes owed to the Internal Revenue Service (IRS) is \$195,474.81.² The approximately \$195,475 owed in federal back taxes

¹ Board staff contacted the audit firm for clarification as to why the fiscal year 2010 audit indicated that the charter holder was in good standing with the IRS when the fiscal year 2011 audit indicates that the charter holder had outstanding federal payroll taxes payable from fiscal year 2010. The audit firm indicated that at the time of the fiscal year 2010 audit, the charter holder was current with federal payroll taxes up to June 16, 2010. Through the 2011 audit, it was determined that the charter holder didn’t make all of the final fiscal year 2010 payment.

² A letter dated September 30, 2010 provided as part of the fiscal year 2009 corrective action plan states that the total amount owed to the IRS at that time was \$130,968. The September 2010 letter also indicated that information had been submitted to the IRS requesting an installment agreement. In its request, the charter holder asked for monthly payments of \$3,638, which would result in the amount owed being paid back in 36 months.

represents 14.5% of the charter holder's projected state equalization payment for fiscal year 2012.

On February 1st, Board staff emailed a letter asking TAG Elementary, Inc. to provide certain information by March 2nd. By the deadline, Board staff received the charter holder's response. After submitting its initial response, the charter holder also provided updates, as requested, to Board staff. In the information submitted, the charter holder:

- Stated that it is gathering the financial information that the IRS requires in order to enter into a formal installment agreement. The charter holder also stated that it has engaged an "enrolled agent" to assist the charter holder. Additionally, the charter holder stated that it has made voluntary payments to the IRS to pay down the back taxes owed. In recent months, the voluntary payments have equaled approximately \$10,000 a month. Further, on February 6th, a request was submitted to the IRS for abatement of penalties on the back taxes.
- Provided evidence that during fiscal years 2011 and 2012, it made voluntary payments totaling \$9,500 and \$48,108.64, respectively, toward the back taxes owed to the IRS as follows:
 - \$6,000 as part of the fourth quarter of calendar year 2010
 - \$3,500 on April 25, 2011
 - \$4,000 on September 7, 2011
 - \$4,000 on October 5, 2011
 - \$5,000 on November 7, 2011
 - \$5,000 on December 6, 2011
 - \$10,000 on January 17, 2012
 - \$9,917.65 on February 1, 2012
 - \$10,190.99 on March 3, 2012
- Provided evidence that it has deposited the required federal payroll tax amounts for payrolls that occurred between July 1, 2011 and February 16, 2012.

In addition to third-year noncompliance with federal payroll tax requirements, the fiscal year 2011 audit identified other issues that required the submission of a corrective action plan.³ These included material weaknesses related to segregation of duties over cash disbursements, material weaknesses in the charter holder's accounting practices and material weaknesses in the charter holder's control environment. On February 1st, Board staff emailed a letter asking TAG Elementary, Inc. to provide certain information related to these items by March 2nd. On February 1st, the charter holder contacted Board staff and requested a two-week extension for submitting the requested information. Board staff granted the two-week extension, which made March 16th the new deadline for submitting the information related to these items. The February 1st letter also referenced issues identified in the fiscal year 2011 audit related to the possible misclassification of workers as independent contractors. The audit indicates that the charter holder needed to reduce expenses and therefore chose to classify as many workers as possible as independent contractors to save payroll taxes. Since this may involve interpretation of federal laws and regulations, including those pertaining to whether an individual is an independent contractor or employee, the letter indicated that this matter will be forwarded to the IRS for its review.

Board Options

Option 1: The Board may decide to take no action at this time.

Option 2: The Board may approve withholding 10% of the charter holder's monthly state aid apportionment. The following language is provided for consideration: I move to find TAG Elementary, Inc. is in noncompliance

³ The fiscal year 2011 financial statements for TAG Elementary, Inc. were prepared assuming the organization will continue as a going concern. "Going concern" is the idea that an organization will continue to engage in its activities for the foreseeable future. If the auditor doubts that the organization will exist for at least the next year, the auditor's report would include a paragraph explaining this concern, as was the case with TAG Elementary, Inc.

with federal law for its failure to comply with federal payroll tax requirements and approve withholding 10% of the charter holder's monthly State aid apportionment until compliance is demonstrated. Compliance will be demonstrated by the charter holder providing:

- Evidence that all required federal payroll taxes for payrolls during the period of February 17, 2012 through June 30, 2012 have been timely deposited by the charter holder into the Treasury of the United States; and
- Evidence that the charter holder has continued to make voluntary contributions of approximately \$10,000 a month to the IRS during the period of April 2012 through June 2012 for back federal payroll taxes owed.

Option 3: The Board may vote to issue a Notice of Intent to Revoke the charter holder's charter contract. The following language is provided for consideration: I move to issue a Notice of Intent to Revoke the charter contract of TAG Elementary, Inc. for its failure to comply with federal payroll tax requirements and its charter contract.

- Within 48 hours of receipt of the Notice the charter operator shall notify staff and parents/guardians of registered students of the Notice of Intent to Revoke and the Notice of Hearing 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 4: The Board may choose to withhold 10% of the charter holder's monthly State aid apportionment and delay consideration regarding the issuance of a Notice of Intent to Revoke the charter holder's charter contract until after a determination to renew the charter has been made. Staff recommends the following language for consideration: I move to find TAG Elementary, Inc. is in noncompliance with state law for its failure to comply with federal payroll tax requirements and approve withholding 10% of the charter holder's monthly State aid apportionment until compliance is demonstrated. Compliance will be demonstrated as follows:

- Evidence that all required federal payroll taxes for payrolls during the period of February 17, 2012 through June 30, 2012 have been timely deposited by the charter holder into the Treasury of the United States; and
- Evidence that the charter holder has continued to make voluntary contributions of approximately \$10,000 a month to the IRS during the period of April 2012 through June 2012 for back federal payroll taxes owed.

Further, the Board finds there is a basis on which to revoke the charter contract of TAG Elementary, Inc. Given the fact that the charter holder's renewal application package, if submitted, would be considered by the Board prior to June 24, 2012, the Board should proceed with the withholding, but not issue a Notice of Intent to Revoke the Charter until after a determination to renew the charter has been made. Should the charter holder not submit a renewal application package by the deadline, the Board directs staff to place the charter holder on the next Board agenda for further consideration.