ARIZONA CONNECTIONS ACADEMY

August 12, 2013

Arizona State Charter Board
1616 West Adams Street, Suite 170
Phoenix, AZ 85007

Dear President Logan and State Charter Board Members,

I am writing to support staff's recommended change to the Financial Performance Framework that would eliminate the Total Liabilities to Equities Ratio (TLER). We agree with staff's assessment and believe that there are better ways of assessing a charter holder's financial health.

In additional to supporting the TLER elimination, we respectfully request that the Board consider adding language to the Framework that addresses situations when a school partners with an Educational Management Organization (EMO). As currently written, the Framework appears to apply a one-size-fits-all approach that does not fit all charter models. In reality there is a distinction between those charter holders who are self-organized and self-sustaining versus those that have a relationship with an EMO.

There are three specific aspects of the Framework that are not applicable for schools that partner with a third party management provider. They are:

**1b. Unrestricted Days Cash – Near-Term Indicator**

*Definition: The unrestricted days cash ratio indicates how many days a charter holder can pay its expenses without another influx of cash.*

This measure requires the school to end the year with 30 days of operating cash. Based on Arizona Connections Academy's FY13 forecast, this would require the school to end the year with approximately $1 million in cash. For Arizona Connections Academy, the primary current obligation of the school is to Connections. Connections waits until funds are available, so having the school sit on this much cash is not necessary and is not in line with our current practice.

**2b. Net Income – Sustainability Indicator**

*Definition: Net income, which equals total revenues less total expenses, looks at whether or not a charter holder is operating within its available resources.*

This measure requires that the school finishes with net income every year. The intent is to ensure that a reserve is established for the school. Arizona Connections Academy has relied in the past on previous years' surplus to cover current year's operations. Once again, ACA building a surplus to respond to future cash needs is not applicable to an EMO model, as Connections meets these needs for the school as they arise. Furthermore, it is good practice for a school to dip into a reserve it may have built in previous years in order to sustain operations in a challenging year (as was experienced during the Great Recession). This is the concept behind "Rainy Day Funds" states establish.

**2c. Cash Flow – Sustainability Indicator**

*Definition: The cash flow measure shows the change in a charter holder's cash balance from one fiscal year to another.*

In short, this requires a school to have a three-year cumulative positive cash flow. We do not think that this is an applicable method of measurement for our model. Again, our relationship with an EMO provides the school with significant financial flexibility, thus allowing us to direct almost all resources to students. Arbitrarily requiring certain balances be maintained that do nothing to enhance the financial viability of the school, will harm students and compromise our mission.

We believe that these issues are covered in our EMO contract, which includes deficit protection language. For example, contracts between Connections Academy and many of the schools it supports include language along the lines of "In the event that, as of June 30 of any year during the Term, Total Revenues are less than the Charter School's expenditures, ..., Connections shall issue a credit to the extent required to maintain a positive Net Asset balance". This arrangement enables the charter school to maximize its ability to focus the school's resources on its educational program while running with a minimum level of reserve. The alternative would be to reduce services to students and redirect those savings into building an unnecessary reserve. This provides greater financial flexibility and protection than the ratios recommended in the Performance Framework.

We understand the intent of the Financial Framework and we substantially agree with its intent. There is a need to ensure that the Charter Board can effectively perform regulatory oversight with the greatest amount of effort directed toward those schools demonstrating risk. Our requested clarifications are intended to be consistent with that intent, by defining the standard in such a way that if a school can document the ability to utilize the resources of an EMO, that fact will

be incorporated as part of the standard of compliance. In making this clarification for schools that partner with an EMO, the Framework would provide for effective oversight, without consuming additional staff time and resources.

Thank you for consideration of our request.

Dr. Aaron Coe

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