

FINAL STATEMENT OF REASONS **Charter School Closure Procedures**

UPDATE OF INITIAL STATEMENT OF REASONS

SECTION 11962. DEFINITION OF PROCEDURES FOR SCHOOL CLOSURE SECTION 11962.1. DEFINITIONS RELATED TO THE DUTIES OF A CHARTERING AGENCY

The proposed regulations define the term “procedures” as used in *Education Code (EC)* Section 47605(b)(5)(P) and 47605.6(b)(5)(Q) and add definitions related to the duties of a chartering authority.

Specifically, a reasonably comprehensive description of closure procedures, under these regulations, would designate a responsible entity to conduct closure-related activities, specify the parties that need to be notified as well as the minimum information that should be included in such notification when a charter school closes, designate the transfer and maintenance of all pupil records to the responsible entity named above (or an alternate entity named in the procedures), specify that personnel records must be transferred and maintained in accordance with applicable law, clarify the terms of the required final audit (and that it may also serve as the annual audit required under *EC* sections 47605(b)(5)(I) and 47605.6(b)(5)(I)), and identify funding for the activities described in the school’s proposed closure procedures, which may include but is not limited to any reserve that the school would normally maintain for contingencies and emergencies. The proposed section 11962.1 defines the terms “notification” and “timely” as used in *EC* section 47604.32, and specifies that the term “pupil records” has the same meaning as that of *EC* section 49061(b), while the term “personnel records” has the same meaning as that of *Labor Code* section 1198.5.

The proposed regulations were developed by the California Department of Education and recommended to the State Board of Education based upon contributions received from a broadly based workgroup convened by the State Superintendent of Public Instruction. The workgroup included representatives of the Advisory Commission on Charter Schools, charter school organizations, county and district school administrators, school boards, certificated and classified employees, and parents. The workgroup was focused on addressing serious issues identified during the closure process involving a large charter school operator. The closure disrupted the lives of more than 6,000 students and several hundred teachers. Notification of affected parents and students was minimal. Few student and personnel records could be recovered. Identification and auditing of assets and liabilities proved difficult. Essentially no funding was available for necessary closure activities, and closure costs fell principally on the local educational agencies that had authorized the schools. The proposed regulations respond to these and other issues.

SUMMARY AND RESPONSE TO COMMENTS RECEIVED DURING THE INITIAL PUBLIC COMMENT PERIOD OF 45 DAYS, THROUGH JANUARY 4, 2007

Coleen Wagner, in an e-mail dated December 21, 2006:

Comment: Ms. Wagner expressed concern that the draft regulations require a level of detail at the petition stage that is overly burdensome and provides additional opportunity for districts to deny a charter petition.

Response: We do not agree that the proposed regulation requires a level of detail that is overly burdensome. Recent charter school closures have highlighted the need for clarification of those factors which will be relevant and timely in the event of closure. To protect students and staff, as well as to ensure the continued success of the charter school movement, it is important to provide guidance in those areas which have been problematic in the past to allow charter schools and their authorizing entities the opportunity to think about and discuss some of these issues early, prior to the phase where a closure—especially a closure resulting from revocation—takes place.

Comment: Ms. Wagner expressed concern that a requirement for the charter petitioners to identify a funding source to pay for closure activities will require a reserve, the amount of which is not identified, and which will give chartering agencies great latitude in requiring amounts unattainable by many startup schools. This requirement would provide hostile chartering agencies yet another avenue to deny or close a charter.

Response: Closure activities will have costs associated with them. The proposed regulation was intended to provide maximum flexibility to charter petitioners and charter authorizing entities in addressing the financial implications of closure by not specifically requiring any particular means of funding or any minimum amount. The reference to the use of a reserve, stated permissively, was intended exclusively to clarify that an otherwise existing reserve could be identified for funding of closure activities and that such a reserve was not by its nature excluded from consideration for that purpose. Many charter schools plan for contingencies currently by setting aside a reserve, and we wanted to be sure that identification of that reserve was an acceptable way of addressing the regulation. However, given the concerns about reserves potentially being required raised by Ms. Wagner and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As just noted, the reference was permissively stated and had been included merely to ensure that otherwise existing reserves would not be arbitrarily excluded as means of funding closure activities. The effect, if any, of the proposed regulation on chartering is irrelevant as existing law provides an appeals process to address denial of charter petitions, as well as denial of charters at the time of renewal, and recent

changes in law both narrowed and added an appeals process related to charter school revocations effective January 1, 2007.

Comment: The independent audit requirement is overly broad and will result in excessive costs. Many of the accounting items can be done by the closure entity, lessening the expenses that would be incurred by an independent auditor. The accounting seeks identification of all property, regardless of the dollar value, which is ridiculous.

Response: Annual, independent financial audits which employ generally accepted accounting principles are already a requirement of charter schools (reference *EC* Sections 47605(b)(5)(I) and 47605.6(b)(5)(I)). The final audit specified in *EC* Sections 47605(b)(5)(P) and 47605.6(b)(5)(Q) is the one element of closure procedures specifically enumerated in statute, thereby highlighting its importance in the legislative scheme. Thus, ensuring that the final audit is also an independent audit is entirely consistent with statute. A lesser standard than independence for the final audit would be inconsistent with statute. Moreover, the proposed regulations do not require an additional financial audit; to the contrary, the regulations clearly state that the closure audit may function as the annual audit in an attempt to provide assurance to charter schools that they will not be required to perform two audits for the same year. The reference to an accounting of all assets being included in the conduct of the audit is standard accounting practice and the requirement that the audits be conducted according to generally accepted accounting principles addresses the concern about dollar value of supplies and materials deemed assets by the auditors. However, in response to this concern, we are proposing to incorporate changes in the proposed regulations aimed at clarifying that only items of material value must be addressed. Materiality is defined in the 2005 Governmental Accounting, Auditing, and Financial Reporting manual as follows: "In the context of financial reporting, the notion that an omission or misstatement of accounting information is of such significance as to make it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement."

Comment: Identifying an entity to conduct closure procedures implies that the school is not an appropriate entity to perform the activities; the language should be clarified to allow the school to identify itself to perform the closure activities.

Response: The proposed regulations do not limit the charter school's ability to identify itself as the responsible entity to conduct closure-related activities. No change is needed.

Comment: Requiring charter schools to notify students of their district of residence will cause an additional workload burden, requiring the staff to determine what is the student's district of residence and limiting the ability to send a form letter with confidence that it will be error free. The students should

be well aware of their district of residence. If not, many websites carry that information, particularly websites that list information for people moving into an area and county office of education websites that provide links to the districts in their county. There are many ways for individuals to find out this information; it is not productive and is overly burdensome to require the school to do it for each and every student.

Response: The proposed regulations do not require the school to provide notice to families as to an individual student's district of residence. Rather, the proposed regulations would require that notice of the closure of a charter school be provided to parents so that they are aware of the closure and have time to find another school, and to other specified entities that have responsibilities to oversee the school and its operations. Oversight entities must be apprised of the names of the students in attendance at the school and their districts of residence so that records transfer can be accomplished and compulsory attendance laws will not be violated, and to assure that students will not be "lost" following a charter school closure. The proposed regulations address notification in the least burdensome manner consistent with statute.

Comment: Charter schools should never need to reaffirm that they will follow the law. Inclusion of the item relating to personnel records is unnecessary and vague. If there is some law that charters need to follow, it should be specified.

Response: We do not agree that the proposed requirement to address transfer and maintenance of personnel records in accordance with applicable law is unnecessary and merely a reaffirmation that the charter school will follow the law, nor do we agree that it is vague. *EC* Sections 47605(b)(5)(P) and 47605.6(b)(5)(Q) require a charter petition to contain a reasonably comprehensive description of the procedures to be used if the charter school closes. Recent closures of charter schools where inadequate planning and preparation had been given on how to handle school closure have resulted in the loss of personnel records and failure to pay teachers and/or make payments to staff retirement programs such as the State Teachers Retirement System and the Public Employees Retirement System. Once the school has closed, it is very difficult, if not impossible, to obtain these records and to get them to the appropriate entities or individuals. The proposal requires that due consideration be given to teachers and other employees working at the charter school by ensuring that their personnel records will not simply disappear.

Regarding the concern about vagueness, we opted to draft the regulation in such a way as to give maximum flexibility to charter schools. This is particularly important given the nature of charter school governance structures, which range from governance by the authorizing school district board of trustees to governance by non-profit or for-profit corporate boards of directors. In addition, the range of employment status given to charter school staff (e.g., contract employees, employees of the district or charter school, employees of a non-profit

public benefit corporation, etc.) also varies considerably from one school to the next, such that it would be difficult if not impossible to determine in a regulation that applies statewide all of the laws which might or might not be applicable to every charter school. We believe that the proposed regulation is sufficiently specific in that it establishes the subject as something that must be addressed within the required closure procedures developed by the charter school petitioners, while also recognizing the fact that a school's charter may determine employment standards and conditions including governance structures, which will apply. Decisions related to employment standards and conditions, as well as governance structures, will individually impact the charter school, which must comply with whatever body of law applies to employees as a result of such decisions. Moreover, the proposed regulation does not restrict how a charter school will address this issue; it merely requires that the charter school state how it will address the issue as part of the "reasonably comprehensive" description of closure procedures required by law. Finally, the proposed regulation addresses the fact that whatever means are identified for proper transfer and maintenance of personnel records in accordance with applicable law, a source of funding has been identified to pay for any associated costs.

Comment: Charter schools operated by a nonprofit corporation should retain their rights to dispose of property in accordance with the California Corporations Code. The discussion required for disposing of assets is unnecessarily restrictive and speculative. The school cannot possibly know what assets will remain at the time of closure, making their disposition uncertain.

Response: Nothing in the proposed regulations would prevent a charter school operated by a nonprofit corporation from disposing of property in accordance with the California Corporations Code. To the contrary, the regulations merely require that disposal of assets be among those issues to be addressed in a charter school's closure procedures.

Linda Ngarupe, University Preparation School at CSUCI and University Preparation Middle School at CSUCI, in an e-mail dated December 28, 2006:

Comment: Ms. Ngarupe expressed concern that the regulations will require charter schools to set aside funding that should be used to educate children, and that it would place an undue burden on charter schools.

Response: The proposed regulations do not require that funds be set aside to pay for closure activities. Rather, they provide maximum flexibility to charter petitioners and charter authorizing entities by not specifically requiring a particular means of funding possible closure activities. We recognize that it can be difficult for a startup school to hold back funds to pay for closure; however, our experience has been that the lack of pre-planning for closure activities and how they will be funded must be addressed. Charter schools and their authorizers need to plan for the possibility of closure early, not wait until closure is imminent,

to assure smooth transition of all student and personnel records, and to plan for disposition of existing debts and assets.

The reference to the use of a reserve was permissively stated and intended to ensure that otherwise existing reserves would not be arbitrarily excluded from consideration. As noted above, many charter schools plan for contingencies currently by setting aside a reserve. However, given the concerns about reserves potentially being required raised by Ms. Ngarupe and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As stated above in previous responses to comments, existing law already provides an appeals process to address denial of charter petitions and denial of charter renewals, and recent changes in law both narrowed and added an appeals process relating to charter school revocations effective January 1, 2007.

Sherry Skelly Griffith and Laura Walker Jeffries, Association of California School Administrators (ACSA), in a letter dated January 2, 2007, and in testimony at the public hearing of January 4, 2007:

Comment: ACSA recommends an amendment to subsection (d), the definition of “timely,” as found on page 3, commencing with line 9, as follows:

(d) “Timely” as used in Education Code section 47604.32(d) means receipt of the evidence transmitted pursuant to subdivision (a) within 10 calendar days of the official action taken by the charter authority. If the responsible entity conducting the closure-related activities fails to report to the chartering authority any of the closure reporting requirements this shall be reported in writing and transmitted to the California Department of Education within the 10 calendar day requirement.

Ms. Griffith and Ms. Jeffries stated that this amendment is important to assure that the state receives information when the party responsible for the closure process fails to report all required information.

Response: A requirement to notify the California Department of Education of a failure by a designated entity to perform any of the closure activities identified in a school’s closure plan would be unnecessary because CDE has no authority to take action in these circumstances.

Jennifer McQuarrie, Legislative Advocate, CharterVoice, in a letter dated January 3, 2007 (and in testimony at the public hearing of January 4, 2007):

Comment: Generally, CharterVoice believes that the level of detail required by the regulations is overly burdensome, enlarges the underlying statute, and is premature. Most charter schools do not have established operations at the time they submit a petition for approval. Thus, the detail required by the regulations will be very speculative in nature, providing chartering agencies with a long list of

new reasons to deny granting a charter petition. A less burdensome method would be to require a school closure plan to be adopted after the school opens and is operational.

Response: We do not agree that the proposed regulation requires a level of detail that is overly burdensome. Recent charter school closures have highlighted the need for clarification of those factors which will be relevant and timely in the event of closure. To protect students and staff, as well as to ensure the continued success of the charter school movement, it is important to provide guidance in those areas which have been problematic in the past to allow charter schools and their authorizing entities the opportunity to think about and discuss some of these issues early, prior to the phase where a closure—especially a closure resulting from revocation—takes place. The effect, if any, of the proposed regulation on chartering is irrelevant as existing law provides an appeals process to address denial of charter petitions, as well as denial of charters at the time of renewal, and recent changes in law both narrowed and added an appeals process related to charter school revocations effective January 1, 2007.

The proposed regulations are intended to clarify and implement *EC* Sections 47605(b)(5)(P) and 47605.6(b)(5)(Q), which require a charter petition to include reasonably comprehensive descriptions of closure procedures. Ms. McQuarrie's proposed alternative for adoption of closure procedures following a charter's approval would be in violation of the statute. Therefore, no statutory authority exists for the State Board to consider this alternative.

Comment: The requirement that a petition identify a funding source to pay for closure activities will likely result in a required reserve, the amount of which is not identified, giving chartering authorities great latitude in requiring high amounts unavailable to many schools. We believe this requirement enlarges and amends the underlying statute, rather than providing clarification. The underlying statute only refers to procedures relating to school closure, not payment identification.

Response: The proposed regulations are not inconsistent with statute within the meaning of *EC* section 33031. They elaborate appropriately on the definition of procedures to be used if a charter school closes. The statute does not enumerate a specific list of procedures, but rather states what the procedures minimally must ensure and include. The proposed regulations clarify what it means to be "reasonably comprehensive" in a charter petition's discussion of closure procedures.

Closure activities will have costs associated with them. The proposed regulation was intended to provide maximum flexibility to charter petitioners and charter authorizing entities in addressing the financial implications of closure by not specifically requiring any particular means of funding or any minimum amount. The reference to the use of a reserve, stated permissively, was intended exclusively to clarify that an otherwise existing reserve could be identified for

funding of closure activities and that such a reserve was not by its nature excluded from consideration for that purpose. Many charter schools plan for contingencies anyway by setting aside a reserve, and we wanted to be sure that identification of that reserve was an acceptable way of addressing the regulation. However, given the concerns about reserves potentially being required raised by Ms. McQuarrie and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As just noted, the reference was permissively stated and had been included merely to ensure that otherwise existing reserves would not be arbitrarily excluded as means of funding closure activities.

Comment: A reserve may jeopardize the funding determination calculations for non-classroom based charter schools. A reserve would likely be unenforceable if bankruptcy proceedings were initiated, thereby making it useless. A closure reserve would make for an absurd result if closure activities are paid before any outstanding staff payroll obligations.

Response: The reference to the use of a reserve was permissively stated and intended to ensure that otherwise existing reserves would not be arbitrarily excluded from consideration. As noted above, many charter schools plan for contingencies currently by setting aside a reserve. However, given the concerns about reserves potentially being required raised by Ms. McQuarrie and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As stated above in previous responses to comments, existing law already provides an appeals process to address denial of charter petitions and denial of charter renewals, and recent changes in law both narrowed and added an appeals process relating to charter school revocations effective January 1, 2007.

Comment: The independent audit is excessively burdensome and will result in undue costs. Many of the required accounting tasks can be done by the closure entity rather than an outside auditor, thereby lessening the incurred auditing expenses. In addition, the accounting itself is too expansive in that it seeks identification of all property, irrespective of dollar value. Arguably, it includes all school owned items including erasers, pencils, and paperclips. It should be narrowed to property over a particular dollar value.

Response: Annual, independent financial audits which employ generally accepted accounting principles are already a requirement of charter schools (reference *EC* Sections 47605(b)(5)(I) and 47605.6(b)(5)(I)). The final audit specified in *EC* Sections 47605(b)(5)(P) and 47605.6(b)(5)(Q) is the one element of closure procedures specifically enumerated in statute, thereby highlighting its importance in the legislative scheme. Thus, ensuring that the final audit is also an independent audit is entirely consistent with statute. A lesser standard than independence for the final audit would be inconsistent with statute. Moreover, the proposed regulations do not require an additional financial audit; to the contrary,

the regulations clearly state that the closure audit may function as the annual audit in an attempt to provide assurance to charter schools that they will not be required to perform two audits for the same year. The reference to an accounting of all assets being included in the conduct of the audit is standard accounting practice and the requirement that the audits be conducted according to generally accepted accounting principles addresses the concern about dollar value of supplies and materials deemed assets by the auditors. However, in response to this concern, we are proposing to incorporate changes in the proposed regulations aimed at clarifying that only items of material value must be addressed.

Materiality is defined in the 2005 Governmental Accounting, Auditing, and Financial Reporting manual as follows: "In the context of financial reporting, the notion that an omission or misstatement of accounting information is of such significance as to make it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement."

Caprice Young, President and CEO, California Charter Schools Association (CCSA), in a letter undated but hand-delivered at the public hearing of January 4, 2007, and presented verbally by Colin Miller, representing the CCSA, at the hearing:

Comment: We believe the proposed regulations go far beyond what is included in statute, would create unfunded mandates on charter schools that are not established under the law, and would create additional burdens on charter school approval.

Response: We do not agree that the proposed regulation requires a level of detail that is overly burdensome or goes beyond statute. Recent charter school closures have highlighted the need for clarification of those factors which will be relevant and timely in the event of closure. To protect students and staff, as well as to ensure the continued success of the charter school movement, it is important to provide guidance in those areas which have been problematic in the past to allow charter schools and their authorizing entities the opportunity to think about and discuss some of these issues early, prior to the phase where a closure—especially a closure resulting from revocation—takes place. The effect, if any, of the proposed regulation on chartering is irrelevant as existing law provides an appeals process to address denial of charter petitions, as well as denial of charters at the time of renewal, and recent changes in law both narrowed and added an appeals process related to charter school revocations effective January 1, 2007. We do not agree that the regulations create an unfunded mandate on charter schools that are not yet established under the law. *EC* Sections 47605(b)(5)(P) and 47605.6(b)(5)(Q) clearly place the burden on charter petitioners to provide reasonably comprehensive descriptions of closure procedures as part of their charter petition.

Comment: The existing law only addresses three elements of a school's closure: audit for the purpose of determining disposition of assets and liabilities, plan for disposing of net assets, and the maintenance and transfer of pupil records. Items included in the regulations that do not pertain to these three issues go beyond the scope of the rulemaking process. Subsections (b), (c), (e), (h), (j), and (i) do not pertain to the items specified in the law, and therefore should be deleted from these regulations. Further, Education Code Section 47604.32 explicitly addresses the notification requirements for school closures by school districts. The additional requirements imposed on charter schools in subsection (b) of these regulations would exceed that existing statutory requirement.

Response: The proposed regulations are not inconsistent with statute within the meaning of *Education Code* section 33031. They elaborate appropriately on the definition of procedures to be used if a charter school closes. The statute does not enumerate a specific list of procedures, but rather states what the procedures minimally must ensure and include. The proposed regulations clarify what it means to be "reasonably comprehensive" in a charter petition's discussion of closure procedures.

Comment: We are particularly concerned with subsection (i) of the proposed regulations, which would require a charter school to identify a funding source for closure activities. This subsection would allow a district to require that a charter school create a financial reserve to pay for closure activities. This reserve would be required before the charter has even been approved, and before the school opens. This requirement is excessive, and goes far beyond what the law requires. Current law does not require that charter schools establish a specific reserve level. In fact, requiring such a reserve in regulation would impose an unfunded mandate on charter schools that is not required in law. This newly mandated financial requirement would exceed the scope of the regulatory process.

Response: Closure activities will have costs associated with them. The proposed regulation was intended to provide maximum flexibility to charter petitioners and charter authorizing entities in addressing the financial implications of closure by not specifically requiring any particular means of funding or any minimum amount. The reference to the use of a reserve, stated permissively, was intended exclusively to clarify that an otherwise existing reserve could be identified for funding of closure activities and that such a reserve was not by its nature excluded from consideration for that purpose. Many charter schools plan for contingencies anyway by setting aside a reserve, and we wanted to be sure that identification of that reserve was an acceptable way of addressing the regulation. However, given the concerns about reserves potentially being required raised by Ms. Young and Mr. Miller and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As just noted, the reference was permissively stated and had been included merely to ensure that otherwise existing reserves would not be arbitrarily

excluded as means of funding closure activities. The effect, if any, of the proposed regulation on chartering is irrelevant as existing law provides an appeals process to address denial of charter petitions, as well as denial of charters at the time of renewal, and recent changes in law both narrowed and added an appeals process related to charter school revocations effective January 1, 2007.

As stated in previous responses to comments, we do not agree that requiring a charter petitioner to contemplate how closure activities will be funded exceeds the regulatory authority of the State Board.

Comment: The reserve requirement of subsection (i) is too broad, and would likely create a hardship on many start-up schools. Earmarking funds for closure at the early stage of charter development is not prudent. This requirement would also provide school districts with additional reasons to deny a charter. A district could simply state that a charter is not “financially sound” if it does not include a financial reserve large enough to cover the district’s estimate of closure costs. For many charter schools, establishing a funding reserve before the school opens is simply not feasible because start up costs are extremely high. Requiring a reserve to be set up to cover closure costs could result in more charters not having the resources for other more immediate start-up priorities. Adding yet one more financial constraint on charter approval would be a severe hardship for many charters, and could severely stifle charter approval statewide. We urge you to delete subsection (i) and consider further revisions as described above.

Response: As previously stated, the proposed regulations do not require a funding reserve. The reference to the use of a reserve, stated permissively, was intended exclusively to clarify that an otherwise existing reserve could be identified for funding of closure activities and that such a reserve was not by its nature excluded from consideration for that purpose. However, given the concerns about reserves potentially being required raised by Ms. Young and Mr. Miller and others, changes are being proposed to the draft regulations to delete the reference to the reserve account. As just noted, the reference was permissively stated and had been included merely to ensure that otherwise existing reserves would not be arbitrarily excluded as means of funding closure activities. The effect, if any, of the proposed regulation on chartering is irrelevant as existing law provides an appeals process to address denial of charter petitions, as well as denial of charters at the time of renewal, and recent changes in law both narrowed and added an appeals process related to charter school revocations effective January 1, 2007.

ALTERNATIVES DETERMINATION

The State Board has determined that no alternative would be more effective in carrying out the purpose for which the regulation is proposed or would be as

effective as and less burdensome to affected private persons than the proposed regulations.

LOCAL MANDATE DETERMINATION

The proposed regulations do not impose any mandate on local agencies or school districts.