State of Delaware

Financial Performance Framework
Guidance Document

This resource provides Delaware districts, charter schools, and the public with information on gauging both near term financial health and longer-term financial sustainability.

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Financial Performance Framework Guidance

Charter schools have the autonomy to manage their finances consistent with state and federal law; however, authorizers must ensure that the schools they approve are financially stable. Authorizers, through the charter school renewal process must determine whether that school is not only academically and operationally sound, but also financially viable. The Financial Performance Framework gauges both near term financial health and longer-term financial sustainability.

The portion of the framework that tests a school's near-term financial health is designed to depict the school's financial position and viability in the upcoming year. Schools meeting the desired standards demonstrate a low-risk of financial distress in the coming year. Schools that fail to meet the standards may currently be experiencing financial difficulties and/or are at enhanced risk for financial hardship in the near term. These schools may require additional review and immediate corrective action on the part of the Delaware Department of Education (DDOE).

The portion of the framework that tests a school's longer-term financial sustainability are designed to depict a school's financial position and viability over time. Schools meeting the desired standards demonstrate a lower risk of financial distress in the future. Schools that fail to meet the standards are at enhanced risk for financial hardship in the future.

The Financial Performance Framework is designed to be a stand-alone document that clearly identifies each school's financial standing in the context of the three indicators.

The purpose of the Financial Performance Framework is to provide key data to assess the financial health and viability of charter schools and to determine whether deeper analysis or monitoring is required. Through a set of nine interconnected metrics, the Financial Framework analyzes the current state of charter schools while taking into account the school's financial trends over a period of time. The measures are designed to be complementary and together, they provide a lens into a school's near-term financial situation, historic trends, and future viability.

For each measure, a school will receive one of the ratings described below:

Meets Standard: The school generally meets the stated expectations and/or minor concerns are noted.

Approaching Standard: The school meets some of the stated expectations but not others and/or moderate concerns are noted.

Far Below Standard: The school falls below the stated expectations and/or major concerns are noted. The failures are material and significant to the viability of the school.

USING THE FRAMEWORK

Collecting Evidence

Sources. All charter schools are required to submit an independent annual financial audit using accrual-based accounting that provides the following information:

- Audited balance sheet*
- Audited income statement*
- The notes to the audited financial statements
- Authorized enrollment information
- Actual enrollment information
- Annual debt schedule, indicating the total principal and interest due

*Throughout this document financial statements will be referred to in the governmental nomenclature. Statements reported in nonprofit or governmental audits use the following corresponding names:

Generic (For Profit)	**Non Profit**	**Governmental**
Balance Sheet	Statement of Financial Position	Statement of Net Assets
Income Statement	Statement of Activities and Changes in Net Assets	Statement of Activities

COMPREHENSIVE ANALYSIS

If a school receives two or more designations of "Approaching Standard" or one or more ratings of "Far Below Standard" the authorizer will conduct a comprehensive analysis of the identified areas. When a school qualifies for an additional review, it may be either in immediate distress, financially trending negatively, or both. The school could also have made a strategic financial decision that resulted in ratings that qualified them for additional review, but upon additional questioning has sufficient reasons for the financial results in the given year and is not in immediate distress or negative financial trending.

OVERALL RATING METHODOLOGY

Charter schools will receive an overall rating of “Meets Standard,” “Approaching Standard,” or “Far Below Standard” based on the following criteria.

- **MEETS STANDARD (Green)**
  - The school receives a rating of “Meets Standard” on every measure of the Financial Performance Framework
    OR
  - The authorizer, upon analyzing the factors contributing to ratings of other than “Meets Standard” among the measures of the Financial Performance Framework, determines that there is currently no concern or very little concern for the school’s financial viability.

- **APPROACHING STANDARD (Yellow)**
  - The authorizer, upon analyzing the factors contributing to ratings of other than “Meets Standard” among the measures of the Financial Performance Framework, determines that there is concern for the school’s financial viability. The school and authorizer must closely monitor risk factors and the school should take measures promptly to mitigate risk to financial viability.

- **FAR BELOW STANDARD (Red)**
  - The authorizer, upon analyzing the factors contributing to ratings of other than “Meets Standard” among the measures of the Financial Performance Framework, determines that there is immediate concern for the school’s financial viability. The school and authorizer must closely monitor risk factors and the school must immediately take measures to mitigate risk to financial viability. The authorizer should strongly consider submitting the school for formal review pursuant to 14 Del. C. § 515.

“Material” and “significant” mean that the authorizer deems the matter relevant to:

- The authorizer’s accountability decisions including but not limited to decisions about whether to renew, not renew, or revoke a charter; or
- Information that a family would consider relevant to make a decision to choose the school.

For any measure where a school is determined to have “Approaching Standard” or “Far Below Standard” the authorizer will provide an explanation of the rating. If a school receives two or more designations of “Approaching Standard” or one or more ratings of “Far Below Standard” the authorizer will conduct a comprehensive analysis of the identified areas. The result of the measures in the framework and additional analysis will be used to determine an overall rating for Financial Performance. For any measure where a school is determined to have “Approaching Standard” or “Far Below Standard” the school will have the opportunity to address the ratings.

1. *Current Ratio*

Definition: The current ratio depicts the relationship between a school's current assets and current liabilities.

Overview: The current ratio measures a school's ability to pay its obligations over the next twelve months. A current ratio of greater than 1.0 indicates that the school's current assets exceed its current liabilities, thus indicating ability to meet current obligations. A ratio of less than 1.0 indicates that the school does not have sufficient current assets to cover the current liabilities and may not be in a satisfactory position to meet its financial obligations over the next 12 months.

Source of Data: Statement of Net Position

Calculation: Current assets divided by current liabilities

Current Ratio
Meets Standard: o Current ratio is greater than or equal to 1.1 o Current ratio is greater than or equal to 1.0 but less than 1.1 and one-year trend is positive (current year ratio is higher than last year's)
Approaching Standard: o Current ratio is greater than or equal to 0.9 but less than 1.0 o Current ratio is greater than or equal to 1.0 but less than 1.1 and one year trend is negative
Far Below Standard: o Current ratio is less than 0.9

2. Debt to Asset Ratio

Definition: The debt to asset ratio measures the amount of liabilities a school owes versus the assets they own; in other words, it measures the extent to which the school relies on borrowed funds to finance its operations.

Overview: The debt to asset ratio compares the school's liabilities to its assets. Simply put, the ratio demonstrates what a school owes against what it owns. A lower debt to asset ratio generally indicates stronger financial health.

Source of Data: Audited Statement of Net Position

Calculation - Total liabilities divided by total assets

Debt to Asset Ratio
Meets Standard: o Debt to asset ratio is less than or equal to 0.90
Approaching Standard: o Debt to asset ratio is greater than 0.90 but less than 1.0
Far Below Standard: o Debt to asset ratio is greater than or equal to 1.0

3. Days Cash

Definition: The days cash on hand ratio indicates how many days a school can pay its expenses without another inflow of cash.

Overview: The days cash ratio tells authorizers whether or not the school has sufficient cash to meet its obligations. This critical measure takes on additional importance in states and localities where the timing of school payments is irregular and/or can be delayed.

Source of Data: Statement of Net Position and Statement of Activities

Calculation: Cash divided by (total expenses/365)

Days Cash
Meets Standard: o At least 75 days cash or; o Between 45 and 75 days cash and one year trend is positive *For schools in years 1-3, the days cash should be at least 30 days and the one year trend is positive.
Approaching Standard: o Days cash is greater than 30 days but less than or equal to 45 or; o Days cash is between 45 and 75 days and one year trend is negative
Far Below Standard: o Less than or equal to 30 days cash

4. Debt Service Payments / Loan Covenants

Definition: Debt service payments indicates if a school is not meeting debt obligations.

Overview: This metric addresses whether or not a school is meeting its loan covenants and/or is delinquent with its debt service payments. A school which cannot meet the terms of its loan may be in financial distress.

Source of Data: Notes to the audited financial statements

Debt Service Payments
Meets Standard: o School is not delinquent with debt service payments and complies with all loan covenants.
Approaching Standard: o School is not delinquent with debt service payments, but is out of compliance with loan covenants.
Far Below Standard: o School is delinquent with debt service payments.

5. Aggregated Three-Year Total Margin

Definition: Aggregated total margin measures the deficit or surplus a school yields out of its total revenues; in other words, whether or not the school is living within its available resources.

Overview: The total margin measures if a school operates at a surplus (more total revenues than expenses) or a deficit (more total expenses than revenues) in a given time period. The total margin is important to track as schools cannot operate at deficits for a sustained period of time without risk of closure. The aggregated three-year total margin is helpful for measuring the long-term financial stability of the school by smoothing the impact of single-year fluctuations on the single-year total margin indicator.

Source of Data: Three years of audited Statements of Activities.

Calculation - Total Margin: Net income divided by total revenue

Calculation - Aggregated Total Margin: Total three-year net income divided by total three-year revenues

Aggregated Three-Year Total Margin
Meets Standard: o Aggregated three-year total margin is positive
Approaching Standard: o Aggregated three-year total margin is greater than or equal to -1.5% but not positive
Far Below Standard: o Aggregated three-year total margin is less than -1.5%

6. Cash Flow

Definition: The cash flow measure indicates a school's change in cash balance from one period to another.

Overview: Cash flow indicates the trend in the school's cash balance over a period of time. This measure is similar to days cash on hand, but indicates long-term stability versus near-term. Since cash flow fluctuations from year-to-year can have a long-term impact on a school's financial health, this metric assesses both three-year cumulative cash flow and annual cash flow. The preferred result is greater than zero.

Source of Data: Three years of Statements of Net Position

Cash Flow
Meets Standard: o Three-year cumulative cash flow is positive and cash flow is positive each year or; o Three-year cumulative cash flow is positive, cash flow is positive in two of three years, and cash flow in the most recent year is positive *Schools in their first or second year of operation must have positive cash flow
Approaching Standard: o Three-year cumulative cash flow is positive and; o Cash flow is negative in the current year or; o Three-year cumulative cash flow is negative
Far Below Standard: o Cash flow is negative in the past two years.

7. Debt Service Coverage Ratio

Definition: The debt service coverage ratio indicates a school's ability to cover its debt obligations in the current year.

Overview: This ratio measures whether or not a school can pay the principal and interest due on its debt based on the current year's net income. Depreciation expense is added back to the net income because it is a non-cash transaction and does not actually cost the school money. The interest expense is added back to the net income because it is one of the expenses an entity is trying to pay, which is why it is included in the denominator.

Source of Data:

- Net income: Statement of Activities
- Depreciation expense: Notes to the financial statements
- Interest expense: Statement of Revenues, Expenditures and Changes in Fund Balances
- Principal and interest payments: Notes to the financial statements

Calculation: (Net income + Depreciation + Interest Expense) / (Principal and Interest Payments)

Debt Service Coverage Ratio
Meets Standard: o Debt service coverage ratio is equal to or exceeds 1.10
Approaching Standard: o Debt service coverage ratio is greater than .90 but less than 1.10
Far Below Standard: o Debt service ratio is less than or equal to .90

8. Enrollment Variance

Definition: Enrollment variance tells authorizers whether or not the school is meeting its authorized enrollment, thereby generating sufficient revenue to fund ongoing operations.

Overview: The enrollment variance depicts actual versus authorized enrollment. A school budgets based on projected enrollment but is funded based on actual enrollment; therefore, a school that fails to meet its enrollment targets may not be able to meet its budgeted expenses. It is critical to capture this information as early in the school year as possible to determine whether an authorizer may need to take action or intervene in some way. Schools less than five years into operating may have greater fluctuations in their enrollment because they have not yet established themselves in the community. However, mature schools with large, unexplained fluctuations in enrollment may be at risk financial distress if they are not able to adjust accordingly. Often, financially stable schools will purposefully underestimate enrollment so that they may budget more conservatively.

Source of Data:
- Authorized enrollment in approved charter
- Actual enrollment (September 30 count)

Calculation: Actual enrollment divided by authorized enrollment

Enrollment Variance
Meets Standard: o Enrollment variance equals or exceeds 95% in the most recent year
Approaching Standard: o Enrollment variance is greater than 80% but less than 95% in the most recent year
Far Below Standard: o Enrollment variance is less than or equal to 80% of authorized enrollment in the most recent year

Student Retention

Definition: The number of students that re-enroll at a school year after year. ***Student retention data is for information purposes only and is not utilized to provide a financial rating.*** Student retention data will be listed for a five-year period.

Overview : Student retention measures whether a school retains students from year to year, thus improving the sustainability of the school.

Sources of data: EschoolPLUS data, excluding those students leaving the highest school grade level and those enrolling at the lowest grade level.

9. Financial Management and Oversight

Definition: The school materially complies with applicable laws, rules, regulations and provisions of the charter relating to financial reporting requirements.

Overview: This measure assesses the timeliness of reporting, the implementation of the Citizen Budget Oversight Committee, and the adherence to the policies and procedures of the State's Official Financial Management System.

Source of Data:

- Review of CBOC minutes
- PCard Reports
- Reports from the Division of Accounting

Is the school meeting financial reporting and compliance requirements?
Meets Standard: The school materially complies with applicable laws, rules, regulations and provisions of the charter relating to financial reporting requirements, including but not limited to: o On-time submission and completion of financial reports, including annual budget, revised budgets (if applicable), periodic financial reports as required by the authorizer, and any reporting requirements if the board contracts with an education service provider, pursuant to 14 Del. C., §512 (14) o On-time submission and completion of the annual independent audit and corrective action plans, if applicable o All reporting requirements related to the use of public funds o Adherence to the policies and procedures of the State's Official Financial Management System, pursuant to Del. C., Title 14, Ch. 5, §512 (9) o A Citizen Budget Oversight Committee, pursuant to (14 Del. C. §1508 and 14 DE Admin. Code 736) o A clean audit opinion without material exceptions o An audit that does not include an on-going concern disclosure in the notes or an explanatory paragraph related thereto within the audit report
Approaching Standard: o The school partially complies with all aspects of the PCard program and has received two or more compliance infractions per quarter during the prior fiscal year o On more than one occasion during the prior fiscal year, the school completed and submitted the monthly reconciliation and certification to the Division of Accounting after the deadline o The school completed and submitted the payroll internal controls plan after the deadline, or the Division of Accounting's review of the plan resulted in a rating of "Major Improvement Needed" or "Unsatisfactory"

○ The annual audit identified material weaknesses and/or significant deficiencies in internal controls. ○ The annual audit expressed a modified and/or qualified opinion on the Governmental Activities and Major Fund.
Far Below Standard: ○ The school does not comply with the requirements of the PCard program and one or more employees have had their PCard privileges suspended or terminated ○ On one or more occasions during the prior fiscal year, the school failed to complete and submit the monthly reconciliation and certification to the Division of Accounting ○ The school failed to complete and submit the payroll internal controls plan ○ The annual audit included an on-going concern disclosure in the notes or an explanatory paragraph related thereto within the audit report.