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CONFLUENCE CHARTER SCHOOLS

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Financial Assessment and Planning Project Final Report

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WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING

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INTRODUCTION

ORGANIZATION INFORMATION

Confluence Charter Schools is a non-profit, public charter school system that was established in 2003 with the vision of providing a world-class public education to prepare students for success in college, career, and life. Confluence has grown from one school to a network of schools located in five sites across the city of St. Louis. The network's schools include Old North serving grades K-8, South City serving grades K-8, Aspire (formerly Walnut Park) serving grades PK-6, Confluence Preparatory Academy serving grades 9-12, Confluence Elite Academy (co-located inside Confluence Preparatory) serving grades 7-8, and Grand Center Arts Academy serving grades 6-12.

Confluence Charter Schools is governed by one board of directors and has two charter school sponsors—University of Missouri-Columbia and Saint Louis University. University of Missouri-Columbia sponsors Old North, South City, Aspire, and Confluence Preparatory Academy. Saint Louis University sponsors Grand Center Arts Academy. As a result of having two sponsors, the District is comprised of two local education agencies, or LEAs. The schools are self-managed and supported by the Resource Office staff. Since its establishment twelve years ago, Confluence has grown to become the largest network of public charter schools in Missouri, serving 3,158 students between the two LEAs[1].

PROJECT BACKGROUND AND OBJECTIVES

The Confluence Charter Schools Board of Directors hired CliftonLarsonAllen LLP (CLA) to assist Confluence in completing a financial assessment and creating a strategic financial plan for the network. More specifically, the Board of Directors and stakeholders asked CLA to answer the following key questions:

- Is the organization maximizing federal, state, local, and private funding streams, including potential earned revenue opportunities at Sun Theater?
- Are resources, including staff, being deployed in an efficient and effective manner when benchmarked against the appropriate financial metrics and industry standards?

[1] Missouri Department of Elementary and Secondary Education, http://dese.mo.gov/sites/default/files/qs-charter-MissouriCharterSchoolsataGlance_1.pdf accessed November 1, 2015

- Is the resource office staffed adequately to fulfill the needs of the schools? If so, Can the Resource Office be leveraged to create additional revenue by providing services to other charter schools?
- Is there an organizational structure or solution that would most benefit all the schools in the network and best resolves the existing loan balances between LEAs?
- How can the organization best address the current facilities decisions facing them and what alternatives could be considered to best support the organization's long-term facility needs?

This report is a summation of this work. CLA would like to thank Confluence board members, management, and staff for the effort put forth to work with our firm throughout the engagement.

CONSULTANT QUALIFICATIONS

CliftonLarsonAllen, LLP (CLA) is a professional services firm with three integrated businesses working together to advance our clients' success, create uncommon careers for people, and do what is right for the public, our clients, and each other. We are proud to be the only national Top-10 professional services firm with a strategic focus on servicing tax-exempt entities and the public sector. CLA's Public Sector Group has nearly 600 full-time equivalent professionals servicing 8,000 nonprofit, higher education, K-12, and governmental clients.

K-12 Education represents one of our Public Sector Group's core practice areas. Our firm has served governmental entities, K-12 districts, and charter schools for over 30 years, the latter since 1991 when the first charter school law passed in Minnesota. Roughly 80 percent of our work is audit and tax-related; the other 20 percent consists of consulting and outsourcing of various forms, including:

- Operational, organizational, and financial performance improvement
- Strategic, business, and capital planning
- Program, product, and service profitability analysis
- Enterprise risk management
- Mergers, acquisitions, restructuring, and other joint ventures
- Information technology and security

Beyond the services listed above, our firm and team members have been directly involved in designing, managing, and/or advising on charter school feasibility studies, financial and operational improvement plans, capacity-building plans, and charter network expansion plans. CLA works with charter school clients at all lifecycle stages—from start-up, through growth, maturity, decline, and turnaround. Additionally, we have a longstanding working relationship with the National Association of Charter School Authorizers (NACSA), most recently assisting in the development of their financial performance framework. The appendix of this report includes additional information related to CLA's thought leadership and individual team member qualifications.

PROJECT SCOPE AND APPROACH

CLA designed an approach that would provide Confluence with a set of findings, recommendations, and suggested financial plans of action that instill confidence in key stakeholders that the organization and its finances are structured and deployed in a manner that maximizes revenue and costs efficiencies. Given that approach and the key questions posed on the previous pages, we approached our work through five lines of inquiry.

- **Resource Office Assessment** to consider current resource office structure and capacity and ability to expand service provision outside of the Confluence network.
- **Organizational Structure and LEA Loan Balances** to model scenarios that would resolve LEA to LEA loans and understand potential implications.
- **Facilities Financing Analysis** to help Confluence better understand the short and long term impacts of facility and financing decisions.
- **Revenue Analysis** to understand existing and potential sources of revenue.
- **Cost Analysis** to understand efficiency and benchmark key financial metrics against like organizations.

While each line of inquiry required specific research activities to answer the key questions, major research activities across all lines included historical document analysis, interviews with key stakeholders and staff, scenario development and analysis, benchmarking, and financial modeling. The specific methodology and research activities for each line of inquiry are included in the corresponding sections of the report. Further, this research and the recommendations need to be considered as a whole because of interdependence and related impacts at the school and enterprise level. Our findings and recommendations are presented as follows:

- **Resource Office Assessment**
- **Organizational Structure and LEA Loan Balances**
- **Facilities Financing Analysis**
- **Revenue and Cost Analysis**

RESOURCE OFFICE ASSESSMENT

PURPOSE

The purpose of the Resource Office Assessment is to understand if the office is staffed with the adequate capacity to fulfill the needs of the schools and whether the office staff could be leveraged to create additional revenue by providing outsourced services to other area charter schools.

RESEARCH METHODOLOGY

CLA designed the research to test the capacity of the office and understand the market need and included the following major activities:

Gathered and analyzed relevant background information to understand the current organizational structure and inform remainder of staffing assessment and loan analysis work. Documentation included historical budgets and financial performance; organizational charts, relevant policies, workflows, and procedures; and historical staff assessments and reports produced internally and by the organization's sponsors.

Interviewed Resource Office and school staff to understand their roles, responsibilities, capacity and workload. The CLA team members interviewed key individuals representing primary support areas and each school in the network. Interviews followed a semi-structured approach that would allow CLA to understand how the Resource Office could better use its resources efficiently and effectively and whether or not it were positioned to provide services to other charter schools in order to generate revenue. This semi-structured approach simultaneously allowed interviewers to follow a common outline and permitted for additional probing in areas of interest or concern as they came up. The following is a list of the participating individuals, including title and location.

- Greg Allerdissen, Senior Accountant, Resource Office
- Angela Carpenter, Co-Principal, Aspire
- Dion Edwards, Athletic Director, Resource Office
- Rene Hughes, Business Manager, Grand Center Arts Academy
- Phil Kennedy, Director of Academics, Resource Office
- John Klein, Director of Operations, Enrollment, and Attendance, Resource Office
- Jeff Kuntze, CFO/COO, Resource Office

- Sikini Lee, Administrator, Grand Center Arts Academy
- Scott Mitchell, SOM, Old North
- Dr. Sonya Murray, Principal, Old North
- Terry Noble, Director of Human Resources, Resource Office
- Mike Powers, Principal, Confluence Preparatory Academy
- Brian Tharp, SOM, South City
- Jim Walters, Director of Teacher Training and PLC's, Resource Office

Analyzed cost structure of the Resource Office. Reviewed current and historical financial costs of the resource office and other shared services and personnel across the network and compared it to the structures and expenses of support offices and district offices of four local LEAs and more than twenty similarly sized school networks across the country.

OVERVIEW OF INTERVIEW FINDINGS

Our research honed in on six cross-cutting characteristics—purpose and interaction, communications and culture, customer service, systems and procedures, overall strengths and challenges, and expansion opportunities. The historical financial and supporting documents review allowed CLA to understand the costs, organizational structure, and historical levels of service. The interviews allowed CLA an opportunity to consider multiple perspectives and viewpoints regarding the services and capabilities of the Resource Office, with the stated goal of employees providing an opinion as to whether the Resource Office has a marketability that could create additional revenue to the Confluence Network of Schools.

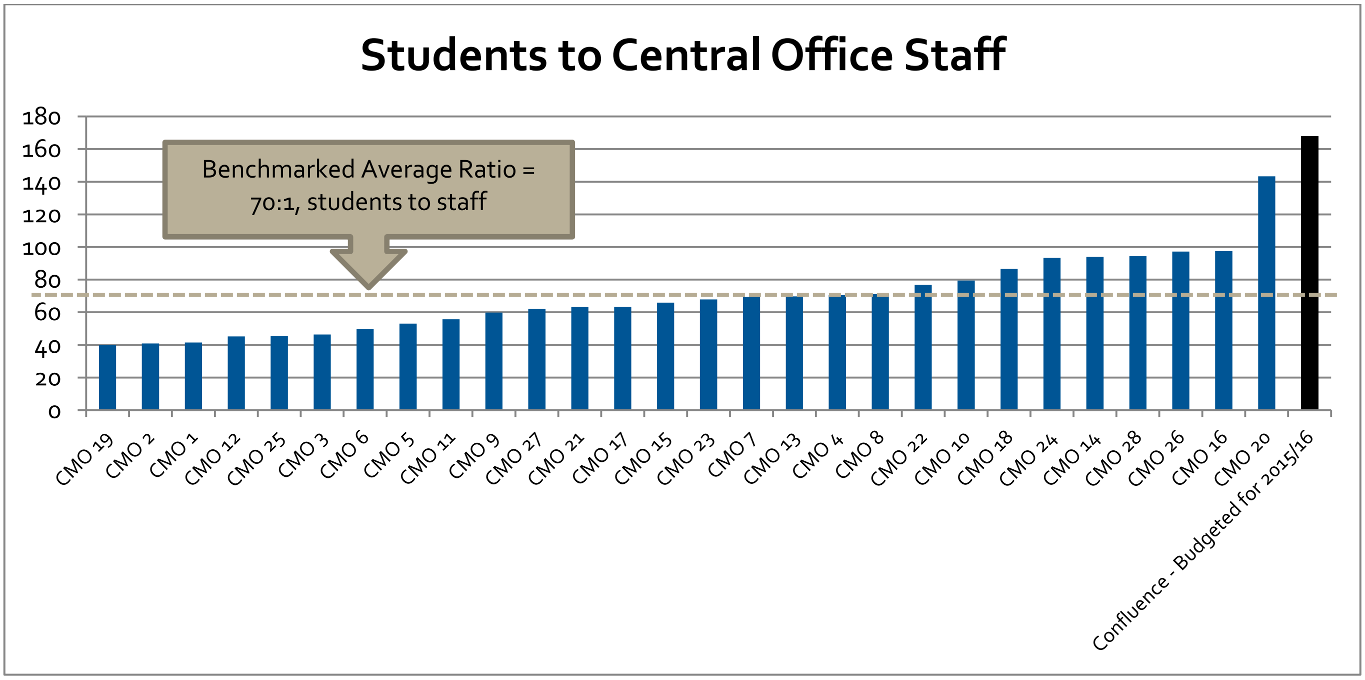
The following is a summary of the broad sentiment, as expressed by several key Resource Office and school staff, as it relates to outsourced services at the Resource Office level.

- The Resource Office is seen as a central office that takes on operational tasks and functions allowing school leadership to focus crucial time on teaching and learning as opposed to more business-like back office functions. It should be noted that while the Resource Office does provide academic functions such as professional development, curriculum research and development, and data analysis, school representatives did not mention these services as readily as the operational supports.
- The Resource Office is generally viewed as a pro-active entity that is attentive to the needs of the schools in the Confluence Network, though there is still some progress to be made in terms of achieving collective network-wide buy-in for a dedicated central office.

- The Resource Office communicates its role and disseminates information to schools both regularly and sufficiently.
- There is collective-buy in to the work and mission of the schools at the Resource Office level. Though there are some challenges between the schools and the Resource Office in terms of roles and responsibility, empathy and mutual respect exists across the system.
- The Resource Office provides quality services to the schools and the students. There is a sense that students and the schools come first.
- The Resource Office has seen marked improvements in the quality of their systems, policies and procedures both at the central office and school level.

OVERVIEW OF BENCHMARKING

We benchmarked Confluence's Resource Office (RO) against 28 networks ranging from 415 to 11,985 students. When benchmarking the staffing and costs of the resource office and network-wide administrative costs against like-sized districts and comparable charter networks nationwide, Confluence Charter Schools' staffing costs were low versus peer organizations. Confluence has 22 RO staff for its budgeted enrollment of 3,695 students; a ratio of 168 students per 1 RO staff versus the average ratio of the benchmarked organizations at 70 students per 1 RO staff. The range for all organizations was a low of 40 to a high of 143 students per staffer. Confluence was well outside of that range at 168 students per staffer.



CLA dove deeper to look at costs and revenues of a handful of academically high performing networks of comparable size to better understand expenses and revenues per student. The following chart is a side by side comparison of the most recent publically available financials for five comparable networks.

Financial Peer Comparison							
	Kipp Metro 2014	Collegium 2014	Florida Charter 2014	Perspectives 2014	Applied Tech. 2013	Peer Average	Confluence Network
Enrollment	2054	2216	4222	2159	1670	2348	3529
Total							
Revenue	$30,162,849	$28,030,559	$39,916,304	$27,992,242	$23,086,209	**$29,837,633**	**$44,430,280**
Expenses	$26,334,821	$27,228,030	$37,032,219	$26,495,623	$23,026,884	**$28,023,515**	**$42,678,994**
Expenses (Per Student)							
Personnel	$8,952	$8,895	$4,072	$8,734	$9,580	**$8,047**	**$7,767**
Occupancy	$936	$971	$798	$798	$275	**$756**	**$653**
Total Expenses	$12,821	$12,287	$8,771	$12,272	$13,756	**$11,981**	**$12,094**
Revenue (Per Student)							
Government Grants & Program Services	$2,584	$12,535	$9,095	$12,045	$13,377	**$9,927**	**$12,489**
Other Grants/Contributions	$11,660	$51	$312	$882	$28	**$2,587**	**$25.2**
Total Revenue	$14,685	$12,649	$9,454	$12,965	$13,791	**$12,709**	**$12,590**
Days Cash							
Days Cash	85	55	150	30	84	81	24

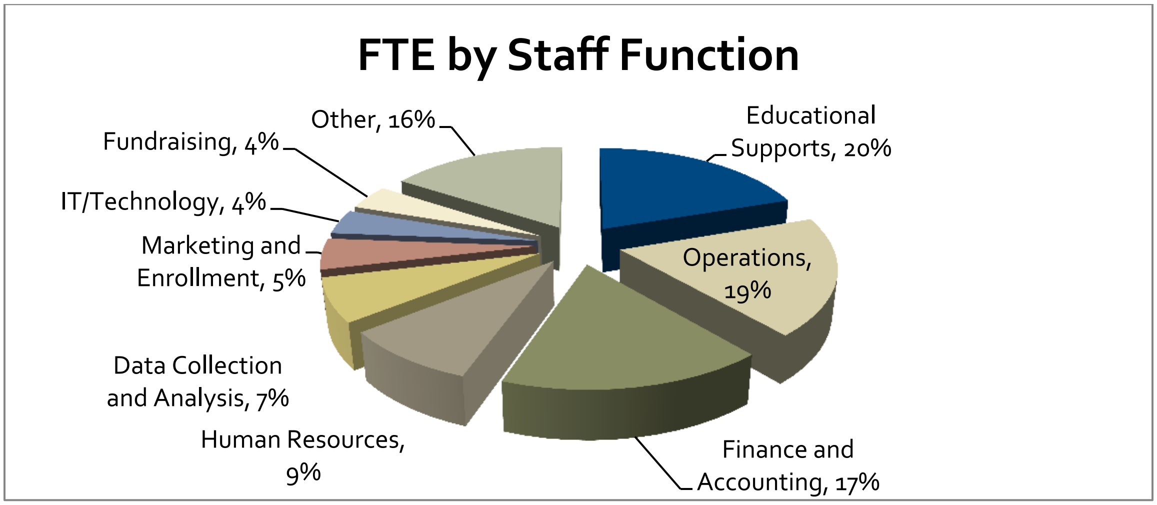
* Confluence academies enrollment in 2014 – 2981
* GCAA enrollment in 2014 - 548
* Confluence academies # of full time teachers in 2014 – 241.10
* GCAA # of full time teachers in 2014 – 45.70

ANALYSIS

While there was broad buy-in that the Resource Office provides quality services and has seen marked improvements in areas that may have historically been lacking, these improvements have tested staff capacity. Interviewees reported that staff is "maxed out" from a workforce perspective and it would be imperative to increase the human capital in order to provide the same level of services to external schools. Further, interviewees expressed a fear that growing services to include non-Confluence schools could result in Confluence schools not receive the attention they need. Further, when comparing the costs and services of the Resource Office to other like-sized districts and networks, it is likely that other networks are providing more extensive services to their networked schools. According to a national study on CMO effectiveness[2], the following is a summary of the typical roles of a central management office:

Establish Purpose	Mission/Vision
	Theory of action/change
	Network wide goals
Develop Growth Strategy	Size and pacing
	Grade level strategy and feeder school system
	Location choices and facilities management
	Takeovers and new starts
	Fundraising and partnerships
Provide Operational Structures	Finance and budgeting
	Human resources
	Operational practices and procedures
	Facilities management or support
Define, Refine, and Enforce Educational Model	Curriculum
	Instruction and instructional time
	Assessment of school and students
	Expectations for student behavior and performance
Assure Consistent Quality	Professional development
	Replicate schools with fidelity
	Accountability for schools and individuals
	Incentives for staff and students to work productively
	Interventions in performance problems
	Standardized school organizational structures

The chart below shows the typical organizational structure staffing by function according to the same report.



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[2] Sourced from The National Study of Charter Management Organization Effectiveness by Mathmatica Policy Research, Inc. Published June 2010.

RECOMMENDATIONS

1. Postpone Outsourcing Plans

The assumption that there is a market for outsourced "back-office" services is reasonable given the local charter landscape however, market pricing and demand for these services was not explored given the acknowledged existing capacity constraints. Pursuit would require thorough market research on product pricing, market need and opportunities. Further considerations related to mission fit, risks to nonprofit tax-exempt status, and infrastructure needs should to be examined in detail prior to pursuit of this business line.

2. True Cost Allocation

The Resource Office should fully allocate costs associated with Resource Office to each of the schools to better understand what the true school operating costs are. Further, this would test their business model by truly allocating costs across their system/network of schools in the interim before marketing their services/capabilities to other charter schools. This allows the Resource Office to:

- Better understand true operational costs at the school level.
- Develop a system that fairly charges the schools for the cost of services rendered.
- Better articulates Resource Office value to schools by demonstrating cost savings and efficiency.

3. Ongoing Assessment and Capacity Investment

The Resource Office should continue assessing its needs, role, and capabilities to determine optimal infrastructure and personnel needs to best serve Confluence students prior to pursuing outsourcing services. In particular:

- Establish clarity around delineation of roles and responsibilities between schools and Resource Office.
- Determine optimal number and mix of personnel needed to best serve students.
- Build up relevant technology and systems.
- Invest time and energy in continued improvement of their relationship with schools.

ORGANIZATIONAL STRUCTURE AND LEA LOAN BALANCE

PURPOSE

The purpose of the Organizational Structure and LEA Loan Balance Analysis was to consider a host of alternative LEA structures to seek out an organizational structure that allows for consistency and efficiency, costs savings, and resolution of the current and ongoing practice of loaning funds between LEAs.

RESEARCH METHODOLOGY

CLA designed the research to understand the current scenario, allow for creativity to develop a set of structure options to consider, develop a criteria to measure options, and ultimately chose the option that best meets the criteria. Research included the following major activities:

Gathered and analyzed relevant background information to understand the current organizational structure and inform remainder of staffing assessment and loan analysis work. Documentation included historical budgets and financial performance; organizational charts, LEA to LEA loan documents, bond documents, and reports produced internally and by the organization's sponsors.

Interviewed Resource Office and Board leadership to understand historical practices, authorizer relationships, and organizational politics. The CLA team members interviewed key individuals using a protocol developed by CLA. Interviews followed a semi-structured approach that would allow CLA to understand how the current dual LEA structure is working and the benefits and drawback of such a structure. Further, CLA interviewers solicited feedback on current needs at the network and school level that the structure may or may not be meeting and organizational politics, if any, which must be considered when evaluating options. This semi-structured approach simultaneously allowed interviewers to follow a common outline and permitted for additional probing in areas of interest or concern as they came up. The following is a list of the participating individuals, including title and location.

- Jeff Kuntze, CFO/COO, Resource Office
- Craig H Larson, Ed. D., Vice Chair and Treasurer, Board of Directors
- Lance LeComb, Secretary, Board of Directors

OVERVIEW OF FINDINGS

Our research focused on four possible options regarding the structure and resolution of the LEA to LEA loans:

- Status Quo – Two LEAs and two sponsoring organizations

- Consolidation – One LEA with one sponsoring organization
- More Evenly Split Schools – Restructure so that the schools are more evenly divided between the two LEAs and two sponsoring organizations
- Additional LEAs – Add additional LEAs and sponsors (i.e. 1 for GCAA, 1 for CPA, 1 for elementary schools)

The loans between the LEAs began in 2010. The loans are actually advancements of monies borrowed during the previous fiscal/school year. The loans carry an interest rate of 1.5% per annum. Interest only payments begin June 30 of the following FY and continue for four (4) years. Principal and interest payments are due over a period of five (5) years, commencing July 1, 2020, with the loan due in full June 30, 2025. As of the June 30, 2014 audited financials, the outstanding principal balance of the loans was $4,048,717. At its October 2015 board meeting, the board approved a loan amount of $1.6 million for the 2015 fiscal year bringing the total outstanding principal balance to approximately $5.6 million.

During the review of the bond documents and supporting materials, it was determined that the bond covenants do not allow for the Confluence Academies LEA to forgive or write-off the loan or any portion thereof. Further, the independent auditors report identified a going concern about GCAA's ability to continue in the Management's Discussion and Analysis portion of the 2014 audit. Specifically the note states "…Grand Center Arts Academy LEA has incurred continued operating deficits in the general fund and has a remaining total fund balance of $189,792 and an unassigned fund balance deficit of ($434,320). The operating deficits have been funded through advances from a related party and now total approximately, $4,000,000. All of this creates substantial doubt about the LEA's ability to continue as a going concern. Management's plan in regard to these matters is described in Note 9. Our opinion is not modified with respect to this matter." Management's Plan to Address Funding Uncertainties (Note 9) can be found on page 30 of the audit, which is publically available. Summarized, the plan states that GCAA has been building out facilities and ramping up enrollment over the last four years, causing the deficit fund balances. The deficits are planned to continue until 2015-16 when the school reaches full enrollment. The Board intends to continue funding loans until that time. The note further states management's intention to complete this work which examines the possibility of combining the two LEAs – thus resolving the loan balance as well as the going concern about GCAA's ability to continue operations.

The 2015 audit was not complete as of the writing of this report; however, it is our expectation that the going concern stated in the 2014 audit will continue to be expressed given the additional $1.6 million loaned during the most recently completed fiscal year. Further, it is our understanding that the independent auditor is also requiring the Confluence Academy LEA to recognize some portion of the loan as an allowance for doubtful accounts in this year audit.

Review of budgeted financials showed Confluence Charter Schools is budgeting to pay approximately $215,000 in sponsor fees for the 2015-16 school year. GCAA will pay approximately $90,000 and Confluence will pay $125,000 which is currently the cap according to current Missouri Charter statutes.

Interviews with management and board members, as well as review of prior internally produced reports, indicated that SLU, the sponsor of GCAA, was not interested in adding additional Confluence schools to its portfolio.

ANALYSIS

Upon review of the financials and historical documentation, the research team ruled out the idea of splitting the schools more evenly among sponsors as well as adding additional sponsors. These options were disregarded for the following reasons:

- SLU not being interested in sponsoring additional schools that might be added to the GCAA LEA.
- When looking at the most reasonable ways to allocate schools to LEAs—both high schools in one LEA, each high school in a separate LEA, elementary schools in a separate LEA—it was determined that all reasonable scenarios would only add to further LEA to LEA loans given both GCAA and CPAs annual operating deficits.
- It was further decided that there was no value in exploring additional multiple LEA structure given that all structures considered would increase sponsor fees and complexity.

When looking at the two remaining options—status quo and consolidation— financial analysis did not yield a realistic scenario where GCAA could continue to operate as it has historically, even fully enrolled, and generate enough annual operating surpluses to pay off the loans according to the current terms.

CLA examined the benefits and drawbacks of consolidation and drew the following conclusions.

- **Reserves will be significantly lower as a consolidated LEA.** As a consolidated LEA, the loans are not written-off but resolved by the consolidation. It should be noted that this drawback will likely be a moot point once the 2015 audit is finalized and requires the Confluence Academy LEA to recognize some portion of the loan as doubtful. The chart on the following page shows the overall effect on the fund balance if the LEAs were consolidated.

LEA	2014 Fund Balance ($)	2014 Fund Balance (%)
CA Fund Balance	$8,750,855	23.9%
GCAA Fund Balance	$189,792	3.4%
Consolidated LEA Fund Balance	**$6,802,214**	**15.0%**

- **As a consolidated LEA, GCAA would be more fully integrated into the portfolio of schools.** Internally this consolidation could have many benefits—more integrated culture, sharing of best practices. Externally, GCAA's scores would be included with the rest of the Confluence schools on state rand publicly facing reports. Thus, GCAA's results may not be as widely recognized because they will no longer be a separate LEA. However, including the GCAA scores with the entire portfolio of Confluence Schools will increase the overall score of the consolidated LEA. GCAA will still have school specific reports, as will all the schools, but GCAA's results may be blended in more than today.
- **As a consolidated LEA, the need to loan from LEA to LEA would be eliminated.** Again, this is a benefit and a potential drawback. From an external perspective, this eliminates one LEA covering the deficits of the other. Internally, all subsidies will be blended if the organization does not monitor and highlight financial performance by school.

RECOMMENDATIONS

Given the findings and the analysis, CLA recommend the following:

1. **Consolidate into one LEA.**

   Given expected allowance for doubtful notes receivable on the 2015 CA audit, the benefits of remaining two LEAs are significantly diminished. Further, the allowance should resolve the going concern noted on the 2014 and most likely 2015 GCAA audits.

2. **Reconfigure monthly financial management reports to better monitor organization-wide and school-level financial performance.**

   Note; as a separate LEA requiring a separate audit, the deficit at GCAA is significantly more noticeable than the deficit at Confluence Preparatory Academy, which has been equally as significant if not larger during the last several fiscal years (see the Revenue and Cost Analysis section for more detail.)

FACILITIES FINANCING ANALYSIS

PURPOSE

The purpose of the Facilities Financing Analysis was to address short-term facilities decisions facing Confluence and to analyze how those decisions may affect the organization long term.

RESEARCH METHODOLOGY

CLA designed the research to understand the immediate decisions, develop a set of purchase or lease options to consider, develop a criteria to measure options, and ultimately chose the option that best meets the criteria. Research included the following major activities:

Analyze current leases, bond documents, and planned facilities financing to understand the options and restrictions. Documentation included leases, bond documents, additional information from the primary bondholder(s), and financing options under consideration. Analysis identified areas of strength and opportunity in existing financing and leases.

Ongoing conversations with Resource Office financial leadership. The CLA team members were in ongoing conversations with the CFO to ensure understanding of financing options being pursued.

Development of a timeline of key events, purchase options and recommendations. CLA created a summary of key events and purchase windows and analyzed options to understand near-term and long-term impacts of decisions.

OVERVIEW OF FINDINGS

Our research focused on four possible options related to facilities financing:

1. Status Quo – purchase no buildings. Continue with leases as written,
2. Purchase CPA, Sun Theater, and Beaux Arts Building.
3. Purchase CPA and continue to lease the other buildings.
4. Purchase Sun Theater and Beaux Arts Building and continue to lease CPA.

A review of the terms of the leases and purchase options is as follows:

Confluence Preparatory Academy, located at 310 N 15th Street is in a 20 year lease, initially signed October 2009. The lease grants CPA the exclusive use of 126,364 square feet. The annual lease costs for the 2015-16 school year is $1.233 million. This includes the base rent as well as amortization of a portion of the Tenant

Improvement loan. The Tennant Improvement loan was a $5.0 million loan from the landlord. The loan is being amortized and paid down at the rate of approximately $400,000 per year. There is an option to purchase as early as October 2016 (FY2016-17). The purchase price is approximately $8.9 million as detailed below:

- $40 per sq. ft. X 126,364 sq. feet = $5.055million
- Approximate Balance of the TI Loan as of October 2016 = $3.817million
- Additional costs (Atrium glass costs) = $45,000-50,000
- Additionally Confluence financed a 42,444 sq. ft. gymnasium on the roof of the building in 2011. This would transfer to Confluence at no cost upon purchase.

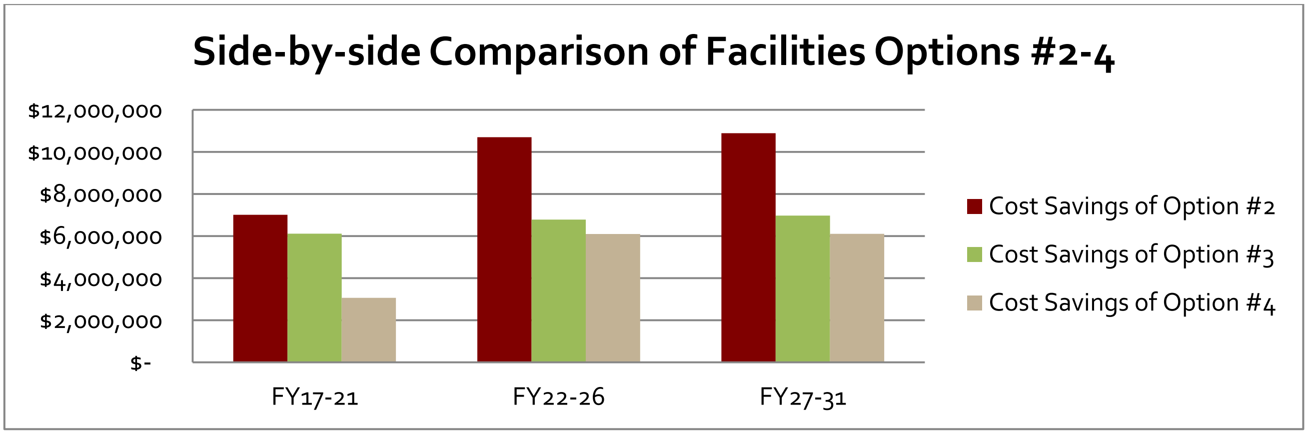
Grand Center Arts Academy, located in the Beaux Arts and Pythius Hall buildings at 711 N. Grand, is in a 15 year lease, effective July, 2011. Confluence Academy is the leasing entity. The lease grants Confluence Academy exclusive use of up to 111,463 sq. feet which is used to house Grand Center Arts Academy. The annual lease costs for the 2015-16 school year is $847,100 which includes the $763,900 for the Beaux Arts and Pythius Hall buildings and an additional $83,200 for lease amendments related to the 2nd floor build out allowance and transfer of Sun Theater debt. The annual rent escalates to $1,386,100 in July 2018. There is an option to purchase as early as December 2017 (FY 2017-18). The purchase price is expected to be $10.742million.

Sun Theater, located at 3267 Grandel Square, is in a lease which was effective May of 2014 and runs through June 30, 2020. Confluence Academy is the leasing entity. The lease grants Confluence Academy exclusive use of 28,678 sq. ft. Grand Center Arts Academy uses the building for classes five days a week. The annual rent for the 2015-16 school year is $153,000. The annual rent escalates to $314,600 per year beginning July 2020. There is an outstanding loan to Friends of Confluence for $2.218million which was used to finance initial development costs. There is an option to purchase as early as July 2020 (FY 2020-21). The purchase price is expected to be $2.17million assuming the $2.218 million loan from Friends of Confluence is either forgiven or converted to equity at the time. If the loan to Friends of Confluence has to be paid back at the time of purchase, the purchase price increases accordingly.

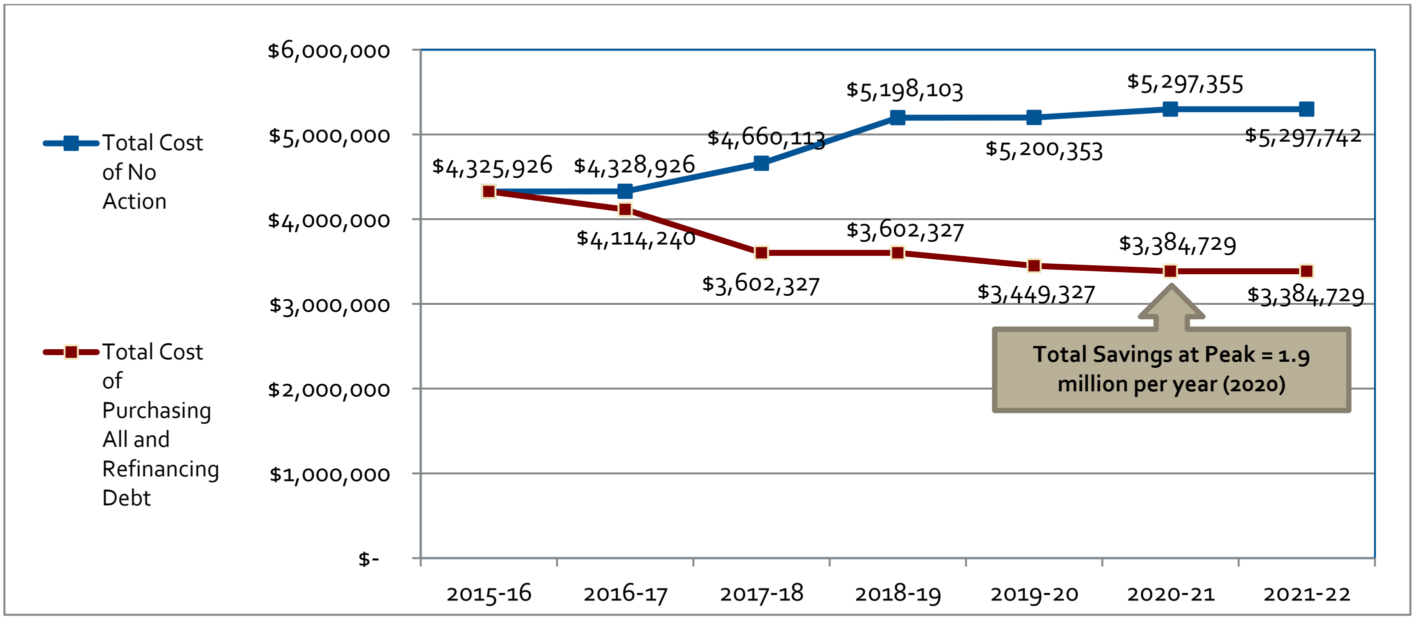
ANALYSIS

Analysis showed cost savings in each purchase scenario. Annual costs savings assume Confluence Charter Schools has the ability to refinance the existing debt. Maintenance and operations costs related to ownership need to be included and considered in any long-term financial model. The Organization's debt to asset ratio increases to 99% if all three (CPA, Sun Theater, and Beaux Arts) are purchased; remains the same if just CPA is purchased; and is reduced to 85% if just Sun Theater and Beaux Arts are purchased.

A side-by-side comparison of the estimated cost savings of the purchase options under consideration is illustrated on the following chart.



Option 2, purchasing CPA, Sun Theater, and Beaux Arts, allows for the greatest annual cost savings going forward as illustrated in the following chart which illustrates the estimated annual costs savings of Option #2 in detail.



RECOMMENDATIONS

1. **Option 2:** Purchase CPA, Sun Theater, and Beaux Arts at beginning of purchase window. Key assumptions are as follows:
   - The organization will refinance existing loans when taking on new facilities-related debt.
   - There will be carrying costs while waiting for purchase windows to open.
   - New debt is obtained at 5% interest rate over 25 years and buildings are depreciated over 30 years.

REVENUE AND COST ANALYSIS

PURPOSE

The purpose of the Revenue and Costs analysis was to determine if the organization was maximizing revenues, realizing cost efficiencies expected of an organization of this size and scope, and to model the effects of the recommendations from this and the other lines of analysis.

RESEARCH METHODOLOGY

CLA reviewed current operating budgets and recent historical performance to understand baseline financials and to integrate research findings and assumptions to build a multi-year operating budget. The following research activities were performed:

Gathered and analyzed relevant background information to understand historical financial performance and inform key drivers for the financial model. Documentation included audited financials, historical budgets and financial performance, building capacity and utilization, and organizational charts.

Analyzed historical federal, state, and local public funding data. Documentation included state reported historic and projected enrollment, state and federal funding formulas, and weighted average daily attendance (WADA) data.

Analyzed historic private fundraising revenue. Reviewed historic fundraising level and trends; anticipated or projected new funding sources; and capacity of fundraising department and staff.

Analyzed historic earned revenue streams. Conducted analysis and financial planning for Sun Theater to understand opportunities for generating earned revenue streams in addition to public and private revenue source.

Benchmarked to industry standards and comparable districts and charter networks. Compared key revenue and costs drivers and metrics with charter school industry standards.

Ongoing conversations with Resource Office financial leadership. The CLA team members were in ongoing conversations with the CFO and finance staff to ensure understanding of historical performance, define key revenue and expense drivers, and to co-develop the financial model to ensure the tool was of value to Confluence going forward.

The financial model created for Confluence Charter Schools presents a multi-year financial plan for the full organization and allows for planning true costs at the school and enterprise level. The following principles were applied to building the financial model:

- Focused on assumptions and drivers, with all inputs made at the driver and assumption level.
- Designed for consistent use by Confluence finance leadership for budgeting and long-term planning, updating assumptions as more information is known.
- Adaptable as the organization and/or situation changes.

OVERVIEW OF FINDINGS

While the elementary school and GCAA's attendance rates were comparable with city-wide average levels, CPA attendance lagged significantly (84.3%) as compared to city-wide averages (92.9%). With revenues tied to enrollment and attendance, a lower attendance rate adversely affects the revenues received from the state. The following chart compares both Confluence high schools (CPA and GCAA) to St. Louis City averages as well as three local, similarly sized, high performing districts.

	Confluence LEA	GCAA LEA	St. Louis City	Webster Groves	University City	Clayton
Total Attendance	91.8	93.9	93.9	95.8	93.6	96.3
K-8 Attendance	93.4	93.8	94.3	96.2	94.3	96.7
HS Attendance	84.3	93.9	92.9	94.9	91.5	95.6

CLA used 2014 audited financials to compare each LEAs financial health to recognized industry standards.[3]

- Current Ratio measures the availability of current assets to cover current liabilities. GCAA LEA had a current ratio of 1.19 and the Confluence LEA had a current ratio of 2.68, both above the recommended target of 1.1.
- Unrestricted Days Cash measures how many day cash an organization has on hand versus the average daily expenses. GCAA LEA had 16 days cash on hand at fiscal year-end; Confluence LEA had 52.5 days cash. The recommended standard target is 30-60 days dependent on the regularity of state payments.
- Debt to Asset Ratio measures how much an organization has borrowed against its assets. GCAA LEA had a debt to asset ratio of 1.68; Confluence LEA had a debt to asset ratio of .90. The recommended standard is .90 (90% of asset value) or lower.
- Debt Service Coverage Ratio measures the cash flow available to pay debt payments over the next 12 months. GCAA LEA has a ratio of -7.79. Confluence LEA has a ratio of 2.53. The recommended target is 1.1 or greater.

[3] National Association of Charter School Authorizers Financial Performance Framework, www.qualitycharters.org

As a whole, the elementary schools have historically run a surplus. Both schools serving high school students have historically run a deficit. Historically Confluence Preparatory Academy deficit has been equal to or greater than GCAA's deficit.

KEY DRIVERS AND ASSUMPTIONS

The following represent key drivers and assumptions identified:

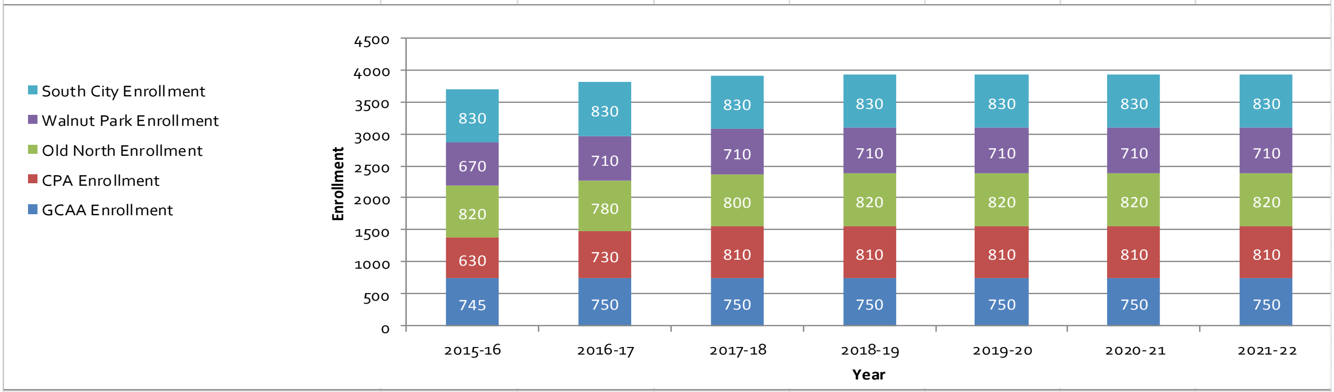
- **WADA:** Target and average enrollment, attrition rates, attendance rates, grade level, student population, etc.
- **Enrollment Strategy:** Plan to maximize enrollment by school.
- **Building Capacity:** Total capacity, goal utilization rates.
- **Pre-K Funding Impact:** Impact of a state funding of Pre-K.
- **Staffing:** Number of staff, salaries, etc.
- **Inflation:** Revenue, Salary, and operating expense.
- **Facilities:** Impact of purchase vs lease scenarios.

ANALYSIS

Excess building capacity presents among the greatest opportunities for increased revenue. Current peak enrollment levels at the beginning of the year fill just 90% of total building capacity. After factoring in attrition, average enrollment levels projected for the current year fill just 83% of enrollment.

Enrollment Summary

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
GCAA Enrollment	745	750	750	750	750	750	750
CPA Enrollment	630	730	810	810	810	810	810
Old North Enrollment	820	780	800	820	820	820	820
Walnut Park Enrollment	670	710	710	710	710	710	710
South City Enrollment	830	830	830	830	830	830	830
Total Enrollment	**3695**	**3800**	**3900**	**3920**	**3920**	**3920**	**3920**



The enrollment plan presented on the previous page gradually increases enrollment by 225 students (approximately 6%) over the course of the next three years. Building capacity allows for this level of growth and more. High School building capacity can be filled by continuing the pilot programs already running with 7-8 graders at CPA (JA Elite). Elementary capacity can be filled by adding Pre-K classes if the state passes funding for Pre-K programming or by increasing K-6 class size if Pre-K funding does not pass. If successful, this could add $2.0-2.5 million of additional revenue to the network; specifically reducing the deficit at CPA.

Increasing high school attendance can further reduce CPA subsidies. Increasing CPA attendance from 84.3% to 90% could result in another 250K in revenue at CPA.

Decreasing attrition rates from peak enrollment directly increase overall revenue. While some attrition is natural and expected, decreasing attrition rates at CPA, Old North, Aspire, and South City from 10% to 8% can generate an estimated additional $600,000 in revenue.

Sun Theater Rental appears to be a viable approach to bring in some additional revenues, however are likely insufficient to make a material impact on the financial health of the enterprise as a whole. Revenue potential is partially limited by the theater's infrastructure—the lights, sound and amenities are not considered to be at professional standard. The greater factor is the use of the building by the school 5 days per week, thus limiting the number of days the theater can be rented. Benchmarks of similar theaters (shown below) show an average rate of $600 for an average length of 5 hours. At the benchmarked rate, the theater would have to be rented 80 times to generate a gross income of $48,000.

Theatre	Location	Seats	Price Per Day	Price Per Hour	Daily Price Per Seat	Other Charges & Provisions
Odyssey	CA	99	$ 385.7	$ 110.2	$ 3.9	$500 for showcases; $300 for small day rentals
El Campanil Theatre	CA	700	$ 466.7	$ 133.3	$ 0.7	Daily use limited to 4 hours. High impact events - $600 per day; Low impact events - $500 per day; Rehearsal - $300 per day
Mamiya Theatre	HI	500	$ 1,073.8	$ 306.8	$ 2.1	Performance $1,325 per day; Technical rehearsal $1,125 per day; Non-tech rehearsal $995 per day; Plaza rental $850 per day
Theatre at Notre Dame High School	PA	768	$ 397.5	$ 113.6	$ 0.5	Price differs for nonprofit versus for-proft groups. Average figure used for this analysis.
Average		**517**	**$ 580.91**	**$ 165.97**	**$ 1.81**	

RECOMMENDATIONS

1. **Enrollment:** Increase CPA enrollment through a combination of higher target levels, reduced attrition, and growing Elite Academy to maximize building capacity utilization.
2. **Capacity:** Maintain elementary schools capacity through Pre-K program (if state-funded) or increased K-6 class sizes.
3. **Attendance:** Increase attendance rates, particularly at CPA.
4. **Staffing:** Continue to manage staff expense in alignment with revenues and areas of need.
5. **Purchase facilities:** full recommendations are included in the facilities financing section.
6. **Further Considerations:** Consider more robust fundraising activities. Fundraising activity is not modeled, although any amount can provide direct opportunity to support specific needs and/or strengthen financial health.

SUMMARY AND CONCLUSION

As indicated through this report, the questions facing Confluence Charter Schools regarding the Resource Office, organizational structure, facilities, revenue maximization and cost efficiencies need to be considered as a whole because of interdependence and related impacts at the school and enterprise level.

A summary of the recommendations are as follows:

Resource Office Assessment

1. Do not pursues outsourcing Resource Office Services at this time.
2. Fully allocate costs associated with the Resource Office to each school to better understand true school-level operating costs.
3. Continue to assess the need for further investment in Resource Office capacity give the low cost structure and related ratios.

Organizational Structure and LEA to LEA Loans

1. Consolidate into one LEA
2. Reconfigure monthly financial management reports to better monitor organization-wide and school level financial performance.

Facilities Financing

1. Take on new debt to purchase CPA, Sun Theater, and Beaux Arts at the beginning of each purchase window.

Revenue Maximization and Cost Efficiency

1. Increase CPA enrollment through a combination of higher target enrollment levels, reduced attrition, and growing Elite Academy to maximize building capacity utilization.
2. Maintain elementary school capacity through state funded Pre-K programming or increased K-6 class sizes.
3. Continue to manage staff expense alignment with revenues and areas of need.
4. Reduce current and future facility-related costs by purchasing the facilities as noted in the facilities financing recommendations.

If all recommendations are adopted, long-term financial projections show an opportunity for steadily improving the organization's overall financial situation. While based in realistic assumptions, the scenario presented below requires effective execution of the multiple interdependent recommendations described. The scenario is a compilation of numerous assumptions housed within the financial model created for management's use. Key levers and assumptions include: managing staff levels to benchmarked standards, enrollment growth, and facilities and financing decisions. This scenario assumes no fundraising dollars as the organizations has not historically participated in enterprise-wide fundraising activities.

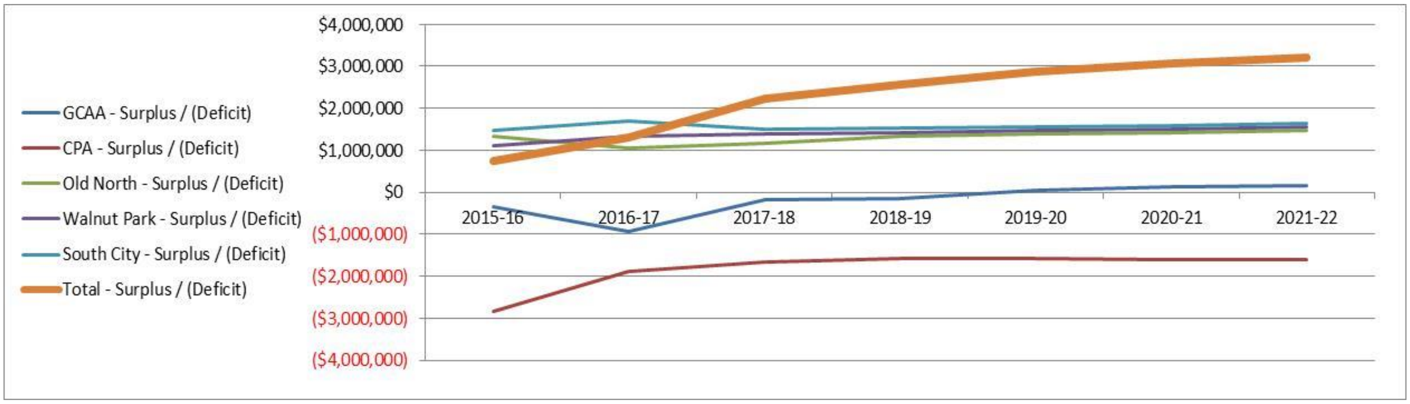
Revenue and Expense Summary

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Revenue							
Total Base State Revenue	$ 33,490,603	$ 35,285,666	$ 36,728,143	$ 37,629,219	$ 38,381,803	$ 39,149,439	$ 39,932,428
Total Additional State Revenue	$ 4,502,023	$ 4,589,463	$ 4,835,317	$ 5,024,157	$ 5,144,575	$ 5,247,467	$ 5,352,416
Total Local Revenue	$ 31,800	$ 42,750	$ 55,080	$ 68,891	$ 79,021	$ 84,490	$ 90,234
Total Federal Revenue	$ 6,529,442	$ 6,844,564	$ 7,132,105	$ 7,307,857	$ 7,454,014	$ 7,603,095	$ 7,755,156
Total Revenue	**$ 44,553,869**	**$ 46,762,443**	**$ 48,750,645**	**$ 50,030,123**	**$ 51,059,413**	**$ 52,084,491**	**$ 53,130,234**
Expense							
Total Compensation Expenses	$ 24,872,378	$ 26,345,682	$ 27,520,390	$ 28,145,613	$ 28,708,526	$ 29,282,696	$ 29,868,350
Total Non-Personnel	$ 15,599,158	$ 15,612,937	$ 15,330,997	$ 15,565,571	$ 15,651,836	$ 15,831,288	$ 16,080,219
Total Resource Office	$ 3,341,540	$ 3,507,183	$ 3,656,298	$ 3,752,259	$ 3,829,456	$ 3,906,337	$ 3,984,768
Total Expense	**$ 43,813,076**	**$ 45,465,802**	**$ 46,507,686**	**$ 47,463,443**	**$ 48,189,817**	**$ 49,020,321**	**$ 49,933,337**
Surplus (Deficit)	**$ 740,792**	**$ 1,296,641**	**$ 2,242,959**	**$ 2,566,680**	**$ 2,869,596**	**$ 3,064,170**	**$ 3,196,898**

The charts below summarize and illustrate the estimated bottom line performance by school through 2021-22.

Bottom Line Performance by School

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
GCAA - Surplus / (Deficit)	($348,715)	($926,949)	($175,691)	($140,376)	$44,985	$138,094	$167,326
CPA - Surplus / (Deficit)	($2,845,846)	($1,884,609)	($1,647,280)	($1,576,951)	($1,589,975)	($1,603,259)	($1,616,809)
Old North - Surplus / (Deficit)	$1,340,351	$1,060,962	$1,169,138	$1,334,651	$1,390,367	$1,428,758	$1,467,916
Walnut Park - Surplus / (Deficit)	$1,111,565	$1,342,729	$1,390,521	$1,428,915	$1,468,077	$1,508,021	$1,548,765
South City - Surplus / (Deficit)	$1,483,438	$1,704,508	$1,506,271	$1,520,441	$1,556,142	$1,592,556	$1,629,699
Total - Surplus / (Deficit)	**$ 740,792**	**$ 1,296,641**	**$ 2,242,959**	**$ 2,566,680**	**$ 2,869,596**	**$ 3,064,170**	**$ 3,196,898**



The findings and recommendations contained in this report were presented to the Board of Directors on October 27, 2015.

APPENDIX: FURTHER CONSULTANT QUALIFICATIONS

THOUGHT LEADERSHIP

Whether through customized seminars, one-on-one coaching, or published resources, we provide our clients' boards and management with practical tools and techniques to effectively managing their organizations and develop as professionals in their fields. Below are examples of our thought leadership in the charter school field.

In 2005, CLA designed and managed **LEAD for Charters, a Cargill Education Partnership**, a grant-making initiative to assist Minneapolis-area charter schools in building strong management and business practices. Recognizing the link between strong business practices and educational excellence, LEAD for Charters works with school leaders, boards, and community members through peer learning, one-on-one coaching, and direct technical assistance. Based on the first round's merits and successes, in 2010 we received a second $2 million grant from The Cargill Foundation to partner with the Center for School Change at Macalester College for a second phase of work. Lead for Charters was recognized as a "promising practice" for enhancing school programs in "Corporations, Chambers, and Charters: How Business Can Support High-Quality Public Charter Schools" published in 2008 by the Institute for a Competitive Workforce, an Affiliate of the U.S. Chamber of Commerce.

In 2009 we authored an issue brief for the National Association of Charter School Authorizers (NACSA) titled **The Bottom Line: Measuring Charter School Financial Health** providing guidance to support charter school authorizers in understanding and conducting the financial due diligence and oversight responsibilities inherent to the authorizing function. We presented this Issue Brief at NACSA's October 2009 Leadership Conference and again in Webinar format—co-presented by NACSA—in February 2010. We have been selected to present a Learning Lab titled "Adapting to Your Financial New Normal" in partnership with Volunteers of America MN at the 2010 NACSA Leadership Conference.


Authorizing Matters

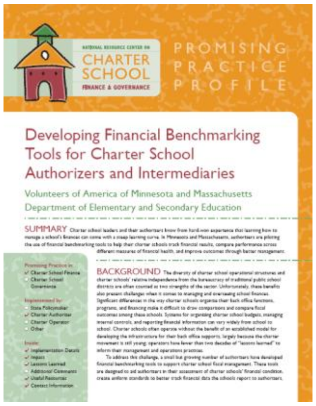
OCTOBER 2009

Issue Brief

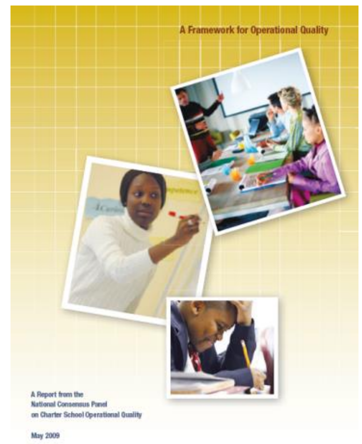
Measuring Charter School Financial Health

The Bottom Line: Measuring Charter School Financial Health

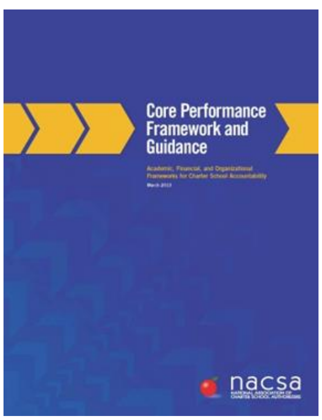
nacsa



In 2009 CLA's benchmarking work with Volunteers of America MN was profiled as a promising practice in charter school finance and governance by **The National Resource Center on Charter School Finance and Governance**, intended to illustrate how other charter school operators, authorizers, and state policymakers have implemented various finance and governance strategies. The content underpinning this profile was also presented at NACSA's 2008 Leadership Conference in a session titled Benchmarking for Financial Success: How do Your Schools Stack Up?



Our staff served on the Finance and Facilities working group that developed core indicators, measures, and metrics that informed **A Framework for Operational Quality, A Report From the National Consensus Panel on Charter School Operational Quality.** This report, published in May 2009 by the Building Charter School Quality project in partnership with the National Alliance for Public Charter Schools and the National Association of Charter School Authorizers, was part of a larger three-year project, "Building Charter School Quality: Strengthening Performance Management among Schools, Authorizers, State Charter Support Organizations, and Funders made possible by a National Leadership Activities grant from the U.S. Department of Education's Charter Schools Program.



In 2012, CLA worked with NACSA to develop the financial portion of their **Core Performance Framework and Guidance.** Additionally, we have worked with NACSA to develop state specific frameworks for authorizers in Louisiana, Colorado, New Mexico, Arizona, Minnesota, Hawaii, Washington and Texas. CLA team members have presented on the topic at several national conferences including the 2012, 2013, and 2014 NACSA conference and the 2012 and 2013 National Charter School Conference.