



North Carolina
Total Retirement Plans



Dale R. Folwell, CPA
STATE TREASURER OF NORTH CAROLINA
DALE R. FOLWELL, CPA

MEMORANDUM

TO: Teachers' and State Employees' Retirement System (TSERS) Board of Trustees

FROM: Patrick Kinlaw, Director of Policy, Planning and Compliance

DATE: July 29, 2021

RE: Application of Charter School for Participation in TSERS

Pursuant to G.S. 135-5.3(b3), Alamance Community School (ACS) of Mebane, NC, was granted provisional entry into TSERS effective August 1, 2020. Approaching the end of its one-year provisional period, ACS has applied for continued participation in TSERS.

Pursuant to G.S. 135-5.3(b7), the Board of Trustees (Board) may grant final approval of a charter school's application to participate in TSERS if it finds the following:

- The school has completed an application using the form approved by the Board;
- All members of the Board of Directors of the school have signed a written statement acknowledging and accepting the estimate of the withdrawal liability performed as described under G.S. 135-5.3(b5);
- The school has not been identified as continually low-performing by the State Board of Education (SBOE) as provided in G.S. 115C-218.94; and
- The school's most recent audited financial statements and independent audit report demonstrate that it is financially sound and can meet the financial obligations of participation in TSERS.

Pursuant to G.S. 135-5.3(b6), if audited financial statements and an independent audit report are not available, the Board's financial review of the school may be based on "functionally equivalent financial statements" provided by the school. Pursuant to G.S. 135-5.3(b8), the Board "may make the final decision for acceptance of the application contingent upon the receipt of a financially sound independent audit report for the fiscal year ending prior to acceptance of the application."

Staff of the Retirement Systems Division (RSD) of the Department of State Treasurer recommends the approval of ACS for continued participation in TSERS, contingent upon the receipt of a financially sound independent audit report for ACS's fiscal year ending June 30, 2021 (coinciding with its first year of operation). Although staff's review of the "functionally equivalent financial statements" did not raise any concerns, a financially sound independent



audit report would more fully demonstrate that ACS can meet the financial obligations of participation in TSERS. ACS has complied with the requirements of G.S. 135-5.3.

Application

ACS submitted a signed and attested Application for Participation dated April 19, 2021. On this application, ACS attested that it is obligated to comply with all provisions governing TSERS pursuant to Article I, Chapter 135 of the NC General Statutes and that it has not been identified as continually low-performing by the SBOE. (RSD staff also confirmed that ACS was not on the SBOE's 2019-2020 list of continually low-performing charter schools.)

Signed Acknowledgement and Acceptance of Withdrawal Liability

ACS submitted a form dated July 1, 2021, signed by each member of its Board of Directors, acknowledging and accepting the payment of a withdrawal liability in the event that ACS elects to cease participation in TSERS in the future. This form included the projected amount of the withdrawal liability after five and ten years of participation in TSERS, as estimated by TSERS' consulting actuary pursuant to G.S. 135-5.3(b5).

Provisional Participation

ACS's provisional participation in TSERS began effective August 1, 2020. During its first year in TSERS, ACS reported \$1,108,407 in retirement-eligible employee compensation to TSERS for twelve (monthly) payroll reporting periods. All contributions owed to TSERS associated with these payroll periods have been paid on time.

Financial Review

Pursuant to G.S. 135-5.3(b3), one year after a charter school is granted provisional entry into TSERS, the charter school shall undergo a financial review. Pursuant to G.S. 135-5.3(b6), the financial review is based on audited financial statements and independent audit reports, or on "functionally equivalent financial statements and independent audit reports" submitted to the Board by the charter school.

Based on information to be used in TSERS' actuarial valuation as of December 31, 2020, ACS had 20 eligible employees. For its provisional participation year, August 2020 through July 2021, ACS reported a total of \$1,108,407 in retirement-eligible compensation to TSERS. The total employer contribution rate for TSERS employers for the fiscal year beginning July 1, 2020, covering TSERS retirement, retiree health, disability, and death benefits, was 21.68% of compensation. It will remain at that rate during the fiscal year beginning July 1, 2021, until a new rate is set through an enacted State budget or other legislation, at which point the total employer contribution rate is expected to increase to at least 22.27% of compensation.

ACS is largely funded by the SBOE and receives funding in an amount equal to the average per pupil allocation for the average daily membership (ADM) from the local school administrative unit allotments in which the school is located (i.e., Alamance-Burlington Board of Education) for



each student attending ACS. The school receives an additional amount for each student with special needs who attends the school. Additionally, for each student who resides outside the local school administrative unit jurisdiction and attends the school, the school receives an amount equal to the per-pupil local current expense appropriation to that respective local school administrative unit.

For the fiscal year ended June 30, 2021, ACS received funding from the Boards of Education for Alamance-Burlington, Guilford County, Orange County, Caswell County, and Rockingham County. ACS also receives funding from state and federal grants, student fees and activities, and contributions and donations.

The independent auditor's report for ACS for the fiscal year ended 2021 is expected to be published later in calendar year 2021. To assist in the Board's financial review, ACS provided its unaudited balance sheet as of May 31, 2021, its unaudited statement of cash flows for the 11 months ended May 31, 2021, and the Financial Policies and Procedures adopted by ACS's Board of Directors.

ACS's unaudited balance sheet shows a fund balance of \$358,651 as of May 31, 2021, one month before the end of the school's first year of operation. The fund balance appears sufficient to provide cash flow and a safety net for the employer, and it does not appear that it is currently being used as a source of funding to meet the school's operating costs.

Assessing Financial Soundness

G.S. 135-5.3(b7)(4) provides that the Board may grant final approval of a charter school's application for participation in TSERS if the Board assesses that the school "is financially sound and can meet the financial obligations of participation in the Retirement System." The Board may make its approval contingent on the receipt of a financially sound independent audit report for the fiscal year ending prior to acceptance of the application.

RSD staff's recommendation to the Board as to the financial soundness of a charter school and its ability to meet the financial obligations of participation in TSERS is based on the following indicators:

- Debt-to-Assets Ratio
 - Target: Debt-to-assets ratio of less than 0.50, which indicates that most of the assets are financed through equity and that total assets exceed total liabilities.
 - Actual: ACS's unaudited balance sheet as of May 31, 2021 indicates that assets exceeded liabilities, resulting in a total net position of \$304,145. The assets in this total include current assets (the fund balance), but do not include the value of fixed assets (e.g., property and equipment), which will be calculated as part of the year-end audit process. Based on this measure, the debt-to-assets ratio was 0.15 as of May 31, 2021.



- Student Enrollment
 - Target: ADM variance, defined as current actual year final ADM divided by actual ADM for the prior year, equals or exceeds 1.0.
 - Actual: Because the 2020-2021 school year was ACS's first year of operation, the ADM variance by definition was equal to 1.0. According to data from Principal's Monthly Reports submitted to the NC Department of Public Instruction, ACS opened the 2020-2021 school year with 136 kindergartners, 67 first-graders, 66 second-graders, and 66 third-graders (335 total students). It ended the eighth month (out of nine) of the 2020-2021 school year with 131 kindergartners, 66 first-graders, 64 second-graders, and 58 third-graders (319 total students).
- Fund Balance
 - Target: The most recent audited financial statement should demonstrate a net surplus with few variances present or, alternatively, a sufficient explanation as to how a negative fund balance will be eliminated in the next fiscal year.
 - Actual: ACS's unaudited statement of cash flows for the 11 months ended May 31, 2021 indicates net additions to cash over that period, resulting in an ending fund balance of \$358,651 as of May 31, 2021.
- Internal Controls and Governance Measures
 - Target: Segregation of duties related to financial transactions and indication of written policies and procedures regarding operations, accounting, personnel, and academics.
 - Actual: The Financial Policies and Procedures adopted by ACS's Board of Directors appear to indicate clear and separate responsibilities for the Finance Officer, Managing Director, and Board of Directors regarding financial transactions. The audit report expected to be published later in 2021 will assess any material weaknesses in the school's internal controls over compliance.
- Cash Flow
 - Target: Positive cash flow and a minimum of one month of operating expenses cash on hand.



North Carolina Total Retirement Plans



Dale R. Folwell, CPA
STATE TREASURER OF NORTH CAROLINA
DALE R. FOLWELL, CPA

- Actual: ACS's unaudited statement of cash flows for the 11 months ended May 31, 2021 indicates net additions to cash over that period, resulting in an ending fund balance of \$358,651 as of May 31, 2021. The audit report expected to be published later in 2021 will provide a clear assessment of the regular level of operating expenses, but based on annual payroll of slightly more than \$1 million, it appears very likely that the cash on hand represents more than one month of operating expenses.
- Presence of Large Loans Outstanding to Fund Operations
 - Target: If present, the charter school must address the paying down of the outstanding obligation.
 - Actual: ACS's unaudited balance sheet as of May 31, 2021 indicates total liabilities of \$54,506. This total amount would not appear to represent a "large loan" relative to the school's net position. In any event, the audited financial statement will further confirm whether any concerns should be present regarding payment of an outstanding obligation.