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The Audit Unit
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Average Daily Membership Audit Report
Friendly House, Inc.
Fiscal Years 2005 and 2006

Report Number 09-02

January 28, 2009

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January 28, 2009

Mr. Luis Ibarra, President and CEO
Friendly House, Inc.
802 S. 1st Ave.
Phoenix, AZ 85003

Dear Mr. Ibarra:

The Arizona Department of Education Audit Unit has conducted an audit of Friendly House, Inc's Average Daily Membership for Fiscal Years 2005 and 2006. The purpose of the audit was to address whether the School properly reported student attendance, offered students sufficient statutorily-mandated instructional hours, and to determine if it received the correct amount of State Aid.

The audit found that the School did not provide the statutorily-required number of instructional hours to its 7th and 8th grade students in FY2005 and FY2006.

We appreciate the excellent cooperation and assistance provided by the Superintendent and staff during the course of the audit. My staff and I will be pleased to discuss or clarify items in the report.

The final report will be issued a week after the meeting. Unless the School files an appeal, the audit will be final 30 days after issuance. Appendix A in the report outlines rules governing the appeals process.

Sincerely,

Arthur E. Heikkila
Chief Auditor

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INTRODUCTION AND BACKGROUND

The Arizona Department of Education (ADE) has conducted a limited scope average daily membership audit of Friendly House, Inc. (School), pursuant to the provisions of Arizona Revised Statutes (A.R.S.). §§ 15-183(E)(6) and 15-901(2). This audit focused on whether the School accurately reported attendance data to ADE and whether it provided sufficient instructional hours to students in FY2005 and FY2006.

Average Daily Membership (ADM) audits help ensure the appropriate distribution of nearly $5 billion in State Aid provided annually to schools in Arizona. Schools receive State Aid based on several factors related to student attendance.[1] To receive funding, schools report attendance data to ADE. ADE then processes that data, determines payment amounts according to the relevant statutory funding formula(s), and distributes payments to schools 10 times per year.

Audit and appeals processes—The ADM audit process determines whether payments were correct or if an adjustment is needed, and provides for an appeal process if the school disagrees with the audit finding(s). ADM audits compare the school's reported information to the original records kept at the school. If the audit finds that the school's reported information does not match the original documentation, the audit will identify and report the funding adjustment needed to the school's State Aid. These funding adjustments can be positive or negative, depending upon the audit finding(s).

After the audit is published, statutes provide schools that disagree with the audit findings the opportunity to file a formal appeal within 30 days after the report was issued. The school and ADE may reach agreement in an informal settlement conference. If not, the appeal will be adjudicated by the Office of Administrative Hearings. If it has been determined that a school received excess State Aid, statutes allow schools to have their future funding adjusted over a 12 month period to compensate for the overpayment. In case of hardship, schools may request that the Superintendent of Public Instruction allow the adjustment to occur over a 24 month period.

[1] Charter schools are funded based on "student count", which is defined in A.R.S. §15-185(B)(2) as Average Daily Membership (ADM) for the current fiscal year as prescribed by A.R.S. §15-901or the adjusted average daily membership as prescribed in A.R.S. §15-902. ADM is determined based on student enrollment and other attendance factors. Schools are required every 20 days to submit daily attendance information to ADE for each student enrolled. Attendance information is used by ADE to calculate Average Daily Membership (ADM). ADE then calculates a school's basic state aid payment.

Financial and other information—The School is located in Phoenix and provides instruction to students from kindergarten through 8th grade. In FY2006, the School enrolled approximately 240 students. Table 1 presents the School's student, staffing, and financial information for FY2004, FY2005, and FY2006.

Table 1

Friendly House, Inc.
Enrollment, Staffing, Revenues, and Expenditures
FY2004, FY2005, and FY2006
(Unaudited)

	FY2004	FY2005	FY2006
Students Enrolled	**212**	**221**	**241**
Staff	**13**	**11**	**12**
Revenue			
Local	$ 10,008	$ 15,581	$ 31,326
State	1,082,321	1,188,288	1,344,754
Intermediate	$6,882	$15,467	14,116
Federal	138,231	172,050	148,384
Total Revenues	**$1,237,442**	**$1,391,386**	**$1,538,580**
Total Expenditures	**$1,287,660**	**$1,510,917**	**$1,574,643**

Source: "Annual Report of the Arizona Superintendent of Public Instruction," for FY2004, FY2005, and FY2006.

SCOPE AND METHODOLOGY

The audit reviewed whether the School provided a sufficient number of instructional hours to students and received the correct amount of State Aid based on the student data it reported to ADE during FY2005 and FY2006.

To determine whether the School was providing sufficient instructional hours to students, auditors reviewed the School's calendars and bell schedules (class schedules) and compared them to the School's approved ADE calendar and other statutory requirements. The bell schedules included class times for regular and early release days and specified any non-instruction time for the students, such as lunch and recess. Based on this information, auditors were able to determine the number of instructional hours the School provided per grade. Auditors then compared instructional hours provided per grade with the annual instructional hours per grade requirements outlined in statute to determine statutory compliance.

The Audit Unit expresses its appreciation to the Friendly House, Inc. administrators and staff for their cooperation and assistance during the audit.

FINDING 1: SCHOOL FAILED TO PROVIDE REQUIRED INSTRUCTIONAL HOURS FOR 7TH AND 8TH GRADE STUDENTS

The School did not provide the statutorily-required number of instructional hours to its 7th and 8th grade students in FY2005 and FY2006. As a result, the School was overpaid State Aid from the Arizona Department of Education (ADE) and ADE needs to recover those monies.

7th and 8th Grade Students Did Not Receive Sufficient Instructional Hours

The School failed to provide the statutorily-mandated amount of instructional hours to its 7th and 8th grade students for FY2005 and FY2006. While several factors contributed to the School's lack to meet the statutory requirements, the School should ensure that it provides all of its students with the statutory required amount of instructional hours.

The School did not meet statutory requirements for instructional hours— Although all school districts and charter schools are required by statute to provide a minimum number of instructional hours to students, the School did not meet this requirement for either FY2005 or FY2006. Specifically, A.R.S. §15-901(A)(2)(b)(i) required school districts and charter schools to provide at least 1,062 instructional hours for 7th and 8th grade students for FY2005 and 1,068 for FY2006. However, as illustrated by Table 2, the School did not meet this requirement for either FY2005 or FY2006. Auditors analyzed the School's bell schedules and calendars and compared them to statutory requirements and found that in FY2005, the School provided students with 97.84 percent of the required number of instructional hours. Similarly, in FY2006, the School provided students with 96.72 percent of the required number of instructional hours.

Table 2

Friendly House, Inc.
Instructional Hours Required and Provided
FY2005 and FY2006

	Instructional Hours		
Fiscal Year	**Required**	**Provided**	**Percentage**
2005	1,062	1,039	97.84
2006	1,068	1,033	96.72

Source: Auditor analysis of the School's bell schedules and calendars from FY2005 and FY2006 and comparison to the requirements in A.R.S. §15-901(A)(2)(b)(i).

Failure to compensate for early release days resulted in insufficient instructional hours—The School did not meet the statutory instructional hour requirement because it did not compensate for the loss of instructional hours due to early release days. Since students are released early from school on those days, instructional hours during these days are also reduced. School administrators designate early release days for a variety of activities, such as parent-teacher conferences. Out of 185 school days for both FY2005 and FY2006, the School had 43 early release days in FY2005 and 45 early release days in FY2006. However, the School failed to add instructional hours to its FY2005 and FY2006 schedules to compensate for the reduction in instructional hours from the early release days.

School should ensure it provides sufficient instructional hours to students—In the future, the School should compensate for any reduction in instructional hours so that its students are provided sufficient education as required by statute. Since the School provided fewer instructional hours than required by statute, it limited the amount and quality of its students' education. Assuming that more instructional hours in school results in more educational opportunities, the School's students' quality of education was reduced compared to what it could have been if the School had provided students with the statutorily-required number of instructional hours. To make sure it provides sufficient instructional hours, the School should either add instructional hours, days, or both to its schedule during weeks with early release days.

Insufficient Instructional Hours Resulted in State Aid Overpayment

Because the School provided fewer than the statutorily-required number of instructional hours, the School's ADM was overstated for FY2005 and FY2006 and it was overpaid State Aid.[2] Since the School did not provide the statutorily-required number of instructional hours, the School's students should not have been claimed as full-time for funding purposes. As a result, the School's student count was overstated, which in turn overstated its ADM. As shown by Table 3 (see page 6), auditors found that the School's ADM was overstated by 0.73 for FY2005 and by 1.36 for FY2006. As shown by Table 4 (see page 7), these amounts translate into $10,633.07 in an overpayment of State Aid that ADE should recover from the School.

[2] Basic state aid payments are computed for each school based on both the amount of instructional hours offered and students' attendance during those hours. The statutorily-mandated minimum instruction hours required for each grade define "full-time student" status for each of the grades.

Table 3

Friendly House, Inc.
Reported, Audited, and Overstated ADM and
State Aid Adjustments
FY2005 and FY2006

	ADM			
Fiscal Year	**Reported**	**Audited**	**Overstated**	**Overpaid State Aid**
2005	198.70	197.97	0.73	$ 3,266.45
2006	220.82	219.46	1.36	7,366.62
Total				$10,633.07

Source: Auditor analysis of statutory requirements for instructional hours as compared to the School's calendar and attendance records.

Recommendations:

1. The School should ensure that it provides sufficient instructional hours to students.

2. ADE should recover $10,633.07 in State Aid that the School should not have received for FY2005 and FY2006.

ADM FUNDING ADJUSTMENTS

The audit identified an overall funding adjustment of $10,633.07 that the School will need to remit to ADE. Statutes allow repayment in 12 months, or 24 months for hardship situations with the approval of the State Superintendent of Public Instruction.

Statutes and rules also provide for a formal appeal process through the Office of Administrative Hearings if the School disagrees with the audit results. The School has 30 days from the issuance of the audit report to request an appeal. Appendix A (see page a-i) presents rules that govern the appeal process.

Table 4 lists the overstated ADM and associated funding adjustments for the School for FY2005 and FY2006.

Table 4

Friendly House, Inc.
ADM Overstatements and Funding Overpaid for
Insufficient Instructional Hours
FY2005 and FY2006

Fiscal Year	ADM Overstated	Funding Overpaid
2005	0.73	$ 3,266.45
2006	1.36	7,366.62
Total	2.09	$10,633.07

APPENDIX A:

State Rules For Appealing Audits

The audit determination pursuant to A.R.S. §15-915 is an agency action for which you can file an appeal. The audit report and cover letter, along with this information serves as notice of your appeal rights under §41-1092.04. Your right to a hearing and right to an informal settlement conference are described below in the Arizona Revised Statutes.

A.R.S. §41-1092.03. Notice of appealable agency action; hearing; informal settlement conference; applicability

A. An agency shall serve notice of an appealable agency action pursuant to section 41-1092.04. The notice shall identify the statute or rule that is alleged to have been violated or on which the action is based and shall include a description of the party's right to request a hearing on an appealable agency action and to request an informal settlement conference pursuant to section 41-1092.06.

B. A party may obtain a hearing on an appealable agency action by filing a notice of appeal with the agency within thirty days after receiving the notice prescribed in subsection A of this section. The notice may be filed by a party whose legal rights, duties or privileges were determined by the appealable agency action. A notice of appeal also may be filed by a party who will be adversely affected by the appealable agency action and who exercised any right to comment on the action provided by law or rule, provided that the grounds for appeal are limited to issues raised in that party's comments. The notice of appeal shall identify the party, the party's address, the agency and the action being appealed and shall contain a concise statement of the reasons for the appeal. The agency shall notify the office of the appeal and the office shall schedule a hearing pursuant to section 41-1092.05, except as provided in section 41-1092.01, subsection F.

C. If good cause is shown an agency head may accept an appeal that is not filed in a timely manner.

A.R.S. §41-1092.06. Appeals of agency actions; informal settlement conferences; applicability

A. If requested by the appellant of an appealable agency action, the agency shall hold an informal settlement conference within fifteen days after receiving the request. A request for an informal settlement conference shall be in writing and shall be filed with the agency no later than twenty days before the hearing. If an informal settlement conference is requested, the agency shall notify the office of the request and the outcome of the conference, except as provided in section 41-1092.01, subsection F. The request for an informal settlement conference does not toll the sixty day period in which the administrative hearing is to be held pursuant to section 41-1092.05.

B. If an informal settlement conference is held, a person with the authority to act on behalf of the agency must represent the agency at the conference. The agency representative shall notify the appellant in writing that statements, either written or oral, made by the appellant at the conference, including a written document, created or expressed solely for the purpose of settlement negotiations are inadmissible in any subsequent administrative hearing. The parties participating in the settlement conference shall waive their right to object to the participation of the agency representative in the final administrative decision.