

# **The Profit Myth**

## **Understanding the Structure of New York Charter Schools**

September 2011

# **The Profit Myth: Understanding the Structure of New York Charter Schools**

Revised August 2011

Charter schools are independently-run public schools that have served at-risk students in New York State since 1999. By the fall of 2011, there will be 136 charter schools in New York City serving 45,000 students, spread across every grade level and borough. Yet even after more than a decade of experience with charter schools, questions and misunderstandings about them persist.

This brief examines a topic that is a frequent source of confusion and misunderstanding: “Do public charter schools create private profits?” The short answer is no.

## **Executive Summary**

Every single New York charter school is organized as a 501(c)(3) non-profit organization.

- There are no exceptions. Charters are not granted to for-profit companies, ever.

46% of New York City charter schools operate independently.

- Some of these schools are longstanding fixtures of their communities. Others are in their first years of operation, and may plan to stay independent or “replicate” into a network of schools.

46% receive centralized services through a non-profit management network.

- The network provides educational and management services. As with any other vendor, the charter school’s board pays a fee for these services, and may terminate the contract at any time.
- Charter school board members are forbidden from having a financial interest in any group that contracts with the school, including management groups.
- The largest non-profit charter school managers in New York are Achievement First, Success Charter Network, and Uncommon Schools.

9% of New York City charter schools work with management networks that are for-profit companies.

- The same rules apply: charter school board members are forbidden to have a financial interest in the management company (no conflicts of interests) and the firm may be fired by the board at any time.

- As of the 2010 state law, new charters may *not* be granted to schools with for-profit managers. There are only six charters left in the state (under the previous law) that may be granted to schools working with for-profit manager.

Some charter schools are linked to large companies—but as beneficiaries, not business partners.

- “Backing” or support of charter schools by hedge fund managers and major corporations takes the form of philanthropic donations, not business investments.
- Such donations typically support facility and scale-up expenses, which are not publicly funded.

### **Non-Profit Status Required**

When one of New York’s charter school authorizers grants a charter to create a new school, the recipient is the board of trustees of a 501(c)(3) non-profit corporation. This board is then responsible for governance of the charter school, including approving budgets, hiring and firing school leaders, and setting the overall direction of the school. Day-to-day operations of the school are left to the school leaders, who must regularly report to the board.

Since charter schools operate independently of the traditional school district, many functions that are typically “central district” responsibilities—from facility planning, to leadership training, to payroll—fall to the charter school to perform itself or through a contractor it hires.

Any group organized under section 501(c)(3) of the Internal Revenue Code is tax-exempt and forbidden from generating private profits. Some charter school critics like to mention that charter schools are “education corporations” for certain purposes in the state education law, with the false implication that this means they are for-profit corporations. In fact, this technical term does not alter a charter school’s non-profit status.

### **Management Organizations**

Some charter schools operate independently. Others choose to affiliate themselves with other charter schools through a common management organization. Such charter school “networks” enter into contracts with the charter school board of trustees. Typically the network provides management services, curriculum, leadership training, and other services to the school, all coordinated around a common philosophy and school design. In return, the charter school pays a fee to the network office. Like any contractor, a management company may be fired by the board for any reason. If a KIPP charter school board were to sour on the KIPP network, for example, the board would terminate its affiliation with the network and change its name, but the charter school would remain.

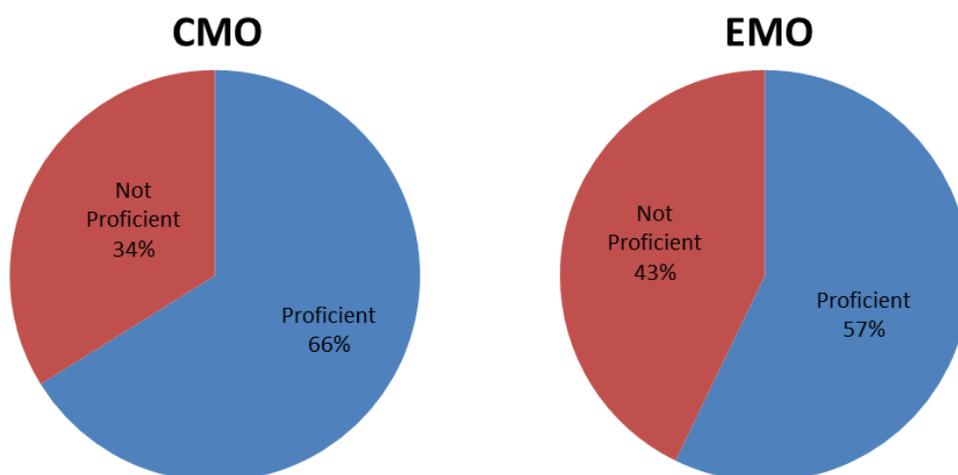
In New York State, 46% of charter schools open in the 2011-12 school year are affiliated with a management organization. For most (68 schools), the network is also a 501(c)(3) non-profit organization. These non-profit managers are commonly known as CMOs (for “charter management organization”). The largest CMOs in New York State are Uncommon Schools (14 charters), Success Charter Network (9 charters), and Achievement First (6 charters).

For a smaller number (16 schools), the management contract is with a for-profit company. As with CMOs, these EMOs (for “education management organization”) are paid for services through a contract with the charter school board, which may be continued or terminated at the board’s discretion. Charter school board members are prohibited from holding any interest in any organization that does business with the school, including an EMO (Education Law §2851(1)).

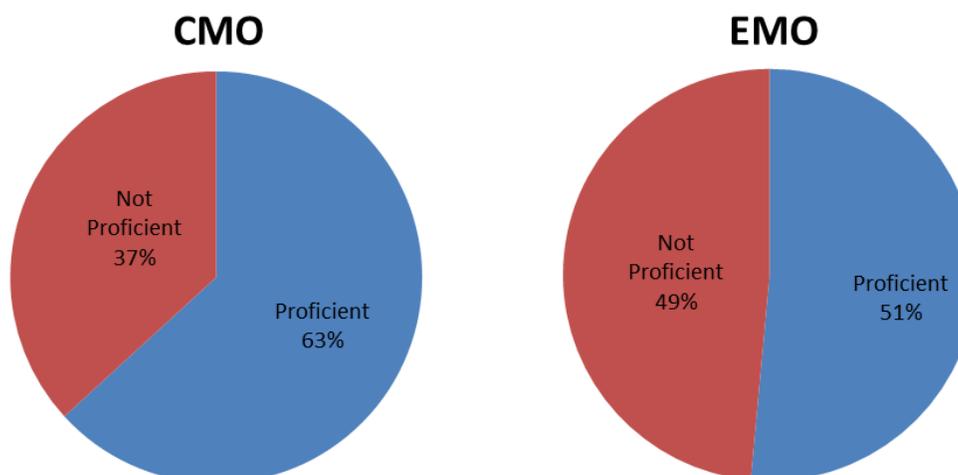
### Charter Schools by Management Type (2011-12)

	New York City	New York State
Independently-managed	62 (46%)	101 (55%)
Contract with non-profit manager ("CMO")	62 (46%)	68 (37%)
Contract with for-profit manager ("EMO")	12 (9%)	16 (9%)
<b>Total</b>	<b>136</b>	<b>185</b>

### Proficiency by Network Type, 4<sup>th</sup> grade 2010-11



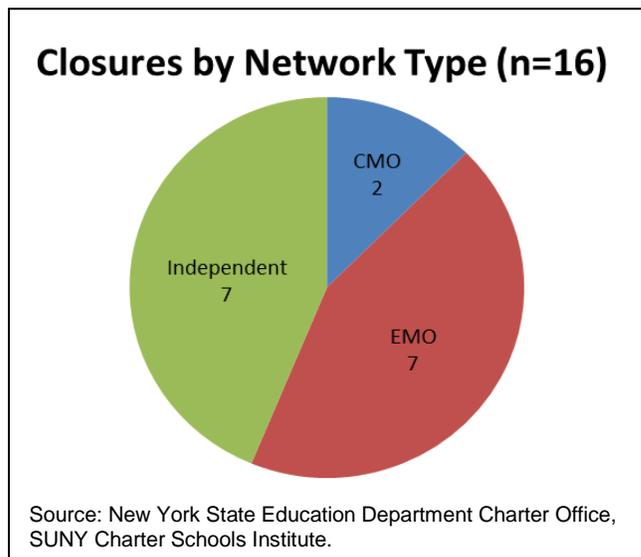
### Proficiency by Network Type, 8<sup>th</sup> grade 2010-11



Source: New York State Education Department School Report Cards

## New Ban on For-Profit Managers

When the New York State Legislature revised the state Charter Schools Act in May 2010, it authorized 260 additional charter school charters. The law included a new stipulation, however: none of the new charters may be used for a school that would contract with a for-profit management firm. Only six charters, under the pre-2010 law, remain to be granted to schools contracting with for-profit management firms. Once those charters are granted, for-profit managers will not be able to open or expand in New York.



## Corporate Philanthropy

Many charter schools do little or no private fundraising, but there are some that do rely on philanthropic support. (This funding is typically used for expansion and facilities costs; charter schools are not guaranteed public funding for either.) As has been widely reported, New York City's financial industry has been strongly supportive of charter schools—but overwhelmingly as *donors*.<sup>1</sup> Wall Street's tax-deductible support of charter networks is purely philanthropic. Any implication that this funding is a covert "investment" is inaccurate and absurd.

## The Big Picture

Charter schools are public schools with a legal mandate to serve children at risk of academic failure. They are funded by state law in proportion to district school spending. They are co-located in district school buildings or left to pay their own rent, and concentrated in the high-need areas of Harlem, the South Bronx, and Central Brooklyn. In order to help their students overcome serious educational obstacles, most charter schools operate with a longer school day and/or longer school year. When people talk about charter schools, this is what they're talking about.

Both district and charter schools contract with for-profit companies for a range of goods and services; similar to a charter school's contract with an EMO, district school principals can contract with partnership

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<sup>1</sup> There is one for-profit network, Victory Education Partners, which is owned by an individual who also runs a hedge fund. EdisonLearning, an EMO that manages a single New York charter school, was traded on Wall Street from 1999 until its stock crashed in 2002. Neither firm is believed to generate large, if any, profits.

support organizations (PSO) to support the delivery of such services as instructional coaching, and data support.

Both district and charter schools sometimes benefit from private donations from individuals and corporations; Bronx Community Charter School, for example, reported over \$380,000 in fundraising in fiscal year 2008-2009, while the parents' organization at PS 334, a gifted and talented district school on the Upper West Side, reported over \$500,000 in revenue during that same year. To be sure, charter schools are unusual in their ability to hire a for-profit firm to manage the school itself, but only a small number of schools do so, and the practice will soon be eliminated in new charter schools.

Reasonable people who care about public education may differ about the role for-profit contractors and private donors play in supporting our schools. Unfortunately, the charter school sector has done a poor job of explaining the difference between the two, leading the ill-informed to speculate that Wall Street donors are trying to profit from poor children. This myth is unfair to the dedicated educators working in public charter schools, and New York's healthy debate over public education would be better off without it.