

SENATE THIRD READING
SB 414 (Ashby)
As Amended September 2, 2025
Majority vote

SUMMARY

Makes changes to charter school law related to audit procedures, financial oversight, and funding determinations.

Major Provisions

- 1) Renames "nonclassroom-based" (NCB) charter schools as "flex-based" charter schools and makes corresponding terminology updates in provisions relating to public meeting requirements and audit procedures.

Auditing and Accounting Standards

- 2) Adds the Charter Schools Development Center and the California Charter Schools Association to the list of stakeholders to be consulted in the audit guide development process.
- 3) Requires chartering authorities to review charter school audit findings and corrective action plans, requires training for local educational agencies (LEAs) auditors, requires the Controller's desk review to be included in the audit guide, requires the Controller to review audits for conformance within 6 months in order to release auditor payments, establishes a weighted risk assessment for determining which audits shall undergo a quality control review reorganizes the dates by which audits are reviewed, certified and corrective action plans are implemented, requires auditors to release pertinent information to audit approving agencies under certain circumstances, requires a LEA to post its annual financial and compliance audit on their website, changes the qualifications needed to be on the State Controller's list of approved auditors, requires if an auditor is terminated, that they shall communicate with the successor auditor as specified.
- 4) Adds charter school-specific procedures that must be included in annual audits, including:
 - a) Review of credit, debit, and electronic payment transactions;
 - b) Review of any single transaction or fund transfer that exceeds \$1 million or 10% of the school's budget;
 - c) Identification of the top 25 payments made to individuals or entities; and
 - d) Review of teacher-to-student ratios in flex-based charter schools.

Oversight

- 5) Requires chartering authorities to:
 - a) Review charter school enrollment and attendance data;
 - b) Review a sample of credit/debit card transactions; and

- c) Notify the California Department of Education (CDE) and the county superintendent of schools if they suspect fraud, misappropriation of funds, or other illegal fiscal practices.

Expands the grounds on which the SBE may revoke a charter to include false claims by a charter school. Requires the SBE or its designee to promptly investigate allegations of false claims or misappropriation of public funds if there is probable cause.

Funding Determination

- 6) Authorizes the SBE to reduce or revoke funding for flex-based charter schools in cases where it makes a formal finding of demonstrable financial abuse, profiteering, or grossly excessive administrative expenses, and requires the SBE, by May 31, 2027, to revise its funding determination regulations to:
 - a) Require cross-checking data submitted by charter schools with independent audits;
 - b) Avoid a requirement to duplicate reporting when data is already available from audits;
 - c) Allow exclusion of unspent one-time funds from instructional spending calculations;
 - d) Count spending on physical school sites as instructional-related expenditures;
 - e) Require disclosure of reserves by accounting category;
 - f) Allow exclusion of reserve increases from revenue if reserves are below 10%; and
 - g) Require explanations for reserves over 10% and notify authorizers when under 5%.
- 7) Clarifies that when a flex-based charter school elects to meet teacher-to-pupil ratio requirements by comparison to the largest unified school district in its county, the applicable ratio shall be based on the district's average daily attendance (ADA) at the second principal apportionment in the prior year and requires the largest unified school district in each county to make its ratio data available upon request.
- 8) Establishes new audit requirements that the State Controller (SCO) must incorporate into the annual audit guide, beginning in the 2027–28 fiscal year, including:
 - a) Requiring auditors to apply materiality thresholds to ADA compliance testing in accordance with Generally Accepted Auditing Standards (GAAS);
 - b) Requiring procedures to identify whether an LEA has material financial relationships with related parties and to ensure compliance with Financial Accounting Standards Board (FASB) disclosure rules;
 - c) Requiring audits of school districts or county offices of education (COEs) that consolidate multiple charter schools to separately track and report financial data for each charter school; and
 - d) Requiring LEAs to report monthly pupil enrollment and attendance, disaggregated by track if applicable.

- 9) Makes changes to the funding determination to establish a definition of a network and require charter schools in a network to apply for a funding determination at the same time.

Contracting

- 10) Establishes the following rules for contracting for all LEAs:
 - a) Prohibiting contracted programs from being sectarian;
 - b) Prohibiting contracts from paying for tuition and fees at a private school, except pursuant to an IEP;
 - c) Prohibiting financial payments or gifts to a pupil or prospective pupil or their family for enrollment, referral, or retention;
 - d) Requires that contracts be at a reasonable market value;
 - e) Prohibits contracting or purchasing season passes to amusement parks, theme parks, zoos or family entertainment activities, but allows for one time admissions that are aligned to teacher assignments or graduation activities funded through parent or student organizations;
 - f) Requires LEA's to only contract with an entity that has a business license or certificate and that holds appropriate insurance for the service;
 - g) Prohibits LEAs from contracting with parents for services provided exclusively to their own child;
 - h) Prohibits LEAs from reimbursing parents for activities or services, except pursuant to an IEP or settlement agreement;
 - i) Requires contractors to have policies and procedures for site safety;
 - j) Requires all contracts to have a valid criminal record summary;
 - k) Requires all contractors to show evidence of qualifications and expertise;
 - l) Prohibits contractors, as part of the contract with the LEA, from charging pupil fees; and
 - m) Requires NCB charter contracts to itemize costs with details to determine a qualifying expense for the funding determination.

COMMENTS

Legislative Analyst Office (LAO)/Fiscal Crisis and Management Assistance Team (FCMAT) report recommends numerous reforms to NCB charter law. In their 2024 report to the Legislature, the LAO and FCMAT made the following recommendations:

- 1) *Several Changes to Improve Funding Determination Process.* We provide several specific recommendations the Legislature could enact to improve the funding determination process.

Our recommendations are intended to narrow the process to a smaller subset of schools, improve the comprehensiveness and quality of data submitted to the CDE, and streamline some aspects of the process. Most significantly, we recommend the Legislature:

- a) *Narrow the Definition of a NCB Charter School.* We recommend narrowing the definition of a NCB charter school so that the designation excludes those schools that provide the majority of their instruction in person. This would exclude charter schools whose programs have cost structures that are similar to traditional classroom-based programs. *This bill does not address this recommendation.*
 - b) *Improve Quality of Data Submitted to CDE.* To assist the CDE in efficiently reviewing and processing funding determination forms, we recommend requiring data submitted by charter schools be consistent with their annual audits. We also recommend several changes that would require information submitted to CDE be subject to annual audits. *This bill does address the recommendation to make the funding determination information consistent with annual audits.*
 - c) *Use Multiple Years of Data for Funding Determinations.* We recommend the funding determinations take into consideration a school's aggregate spending for all years since the previous funding determination. This would ensure school expenditures are aligned with the funding determination thresholds consistently over time. *This bill does not address this recommendation.*
- 2) *Consider Changes to Charter School Oversight.* We also provide several recommendations for the Legislature to consider regarding broader oversight of charter schools. These issues generally apply to all charter schools, though in a few cases, we highlight specific issues related to NCB charter schools and virtual charter schools. Most significantly, we recommend the Legislature consider the following:
- a) *Improvements to Oversight by Charter School Authorizers.* We recommend that the Legislature consider several changes to improve the quality of authorizer oversight. Specifically, we recommend that the Legislature set limits on district authorizers by district size and grade, increase minimum requirements for authorizers, and consider an alternative authorizing structure for virtual schools. *This bill does not address the recommendation to limit NCB charter authorizing by small districts nor address the recommendation to consider alternative authorizing/oversight for virtual schools.*
 - b) *Enhancements to Charter School Audits.* Current audit requirements often do not address the complexities and unique flexibilities of charter school finances. We recommend the Legislature align the audit process for charter schools to that of school districts and add audit requirements that would address issues specific to charter schools. *This bill does address the recommendation to align the audit process for charter schools and school districts, does conform the timing of auditor selection, the requirement to disclose auditor termination or replacement, and the granting of extensions for audits.*

This bill does not fully address the following LAO/FCMAT report recommendations:

- 1) *Small district authorizers.* *This bill does not address the recommendation in the LAO/FCMAT report to limit authorizing by district size.* Most NCB charter schools are authorized by small rural school districts. Many of these small districts are stretched thin with regard to staff, and in some cases, the Superintendent holds many roles like math teacher and school bus driver. These small districts generally do not have the capacity to provide meaningful charter school oversight. In some cases, these small school districts authorize NCB charter schools as a means to balance their district budgets through the

collection of oversight fees. There are very small school districts authorizing large NCB charter schools. The chart below illustrates a sampling of current small school districts that have authorized large numbers of NCB charter schools.

School District Name	School District ADA	Authorized Charter School ADA
New Jerusalem Elementary	22	4,500
Oro Grande	109	3,738
Dehesa Elementary	145	8,532
Maricopa Unified	300	6,067
Julian Union Elementary	311	3,502
Campbell Union	876	6,417
Acton-Agua Dulce Unified	1,080	13,775

(Source: California School Boards Association)

- 2) *Authorizer oversight and oversight fees.* Charter school authorizers play a vital role in providing oversight over both the academic and fiscal aspects of the charter schools they authorize. In order to provide better oversight, this bill requires oversight by authorizers specific to enrollment and attendance accounting and credit card transactions.
This bill does not provide increased oversight fees for authorizers.
- 3) *Funding determination.* NCB charter schools are required to obtain a funding determination that is approved by the SBE. This funding determination establishes the percentage of funding the NCB charter school will receive compared to all other traditional classroom-based schools. Most charter schools apply for a 100% NCB funding determination. To do so, they must meet the following criteria:
 - a) Spend at least 40% of total public revenue on instructional certificated salary and benefits;
 - b) Spend at least 80% of total public revenue on instruction-related services; and
 - c) Not exceed a 25:1 pupil-to-teacher ratio.

Under existing law, if NCB charter schools do not meet these thresholds but meet lower thresholds, they are eligible for 85% funding or 70% funding. If they do not meet minimum thresholds, they are not eligible for funding. With respect to the funding determination process, *this bill does not address the LAO/FCMAT recommendations as follows:*

- 1) Align funding determination with charter renewals; and
- 2) Use the current expense of education to measure spending on certificated staff.

- 4) *Additional recommendations* from the LAO/FCMAT report not included in this bill:
- 3) Establishing a definition of virtual charter network in statute;
- 4) Making the definition of a virtual school subject to the annual audit; and
- 5) Requiring authorizers to participate in regular training.

SCO charter school audits task force makes recommendations on reforms. In response to the A3 Charter School fraud case, described later in this analysis, a San Diego Superior Court Judge signed a court order to approve the formation of a multi-agency task force, known as the Multi-Agency Charter School Audits Task Force, led by the SCO, to combat charter school fraud. The 2024 Task Force report made the following recommendations:

The Task Force extensively discussed the current state of California charter schools and developed recommendations based on the combined expertise, experience, and knowledge of multi-disciplinary Task Force members. These recommendations are intended to foster a culture of transparency and accountability by further strengthening charter school audit function components. The recommendations are organized into the following sections of this report:

- 1) CPA Firm Authorization, Qualifications, Training, Evaluation, and Compliance with K-12 Audit Guide;
- 2) CPA Firm Selection, Rotation, and Late Audit Report Notifications;
- 3) K-12 Audit Guide Procedures; and
- 4) Financial Statement Audit Report Disclosures.

The Task Force determined that most of the recommendations should be applied to all LEAs, including school districts, COEs, and charter schools, providing opportunities to strengthen the audit functions across the entire LEA system. To combat fraud in charter schools, it is important that oversight agencies, in addition to those performing charter school audit functions, implement strong internal and monitoring controls to timely identify and mitigate potential fraud. The control and monitoring functions include the charter school petition and approval process, the charter school accountability systems, the authorizer monitoring of charter schools, and the respective oversight functions of the charter school governing board, COEs, the CDE, and the SCO.

This bill does not address the SCO's Task Force recommendations in the following areas:

- 1) Updating the audit peer review process to include school audits;
- 2) Requirements for CPAs to be removed from the approved auditor directory for significant peer review deficiencies;
- 3) Requiring auditors to increase sample sizes, especially related to NCB attendance;
- 4) Requiring audit procedures to determine whether a NCB charter school submitted the funding determination request, whether it was approved by the SBE and whether the charter school is following the significant terms of the funding determination;
- 5) Requiring audit reports to include the following disclosures:
 - a) Charter management organization management and board members, information about loans between related schools and shared employees;
 - b) The top five highest paid school employees; and
 Funding determination data annually.

This bill includes items that were not in the LAO/FCMAT or SCO reports, as detailed in the following sections.

- 1) *Requiring the SBE to investigate false claims.* This bill requires the SBE or its designee to promptly investigate allegations of false claims or misappropriation of public funds if there is probable cause. There are several flaws to consider in implementing this proposal. To implement such a requirement, the state board would first be required to vote at a public meeting to start an investigation, which will delay the start of any such investigation and create political pressure on the SBE. *The Assembly may wish to consider* whether it is best practice to require a public SBE vote before any fraud investigation commences. Additionally, the proposal requires the SBE to first determine if there is probable cause before it approves an investigation, however, it is unclear how the SBE would determine probable cause without first investigating. Further, the bill does not establish an independent investigation team at the SBE, and without a separate team there is a possibility for conflicts of interest.
- 2) *Changing the name of NCB charters to flex-based charter schools.* This bill replaces the term "NCB" with "flex-based" throughout the Education Code. While the change may be intended to reflect evolving instructional models or reduce negative associations with the term "NCB," it does not alter the underlying instructional model, funding structure, or eligibility requirements for these schools. In effect, the bill rebrands a model that remains substantively unchanged. This name change carries several potential risks, including confusion about the terminology, a potential disruption of oversight and implementation, and a false signaling of reform when none has occurred.

Recent A3 Charter Schools fraud case reveals significant weaknesses in NCB charter school law. Numerous charter school fraud cases have been documented in recent years, including, but not limited to: A3 Charter Schools, Magnolia Charter School, Tri-Valley Learning Corporation, among others.

In *People v. McManus*, the San Diego County District Attorney's Office indicted 11 defendants in a fraud scheme involving nineteen charter schools (A3 Charter Schools). The case revealed many weaknesses in state public charter school law in the areas of pupil data tracking, auditing, school finance, and oversight, which resulted in A3 schools surrendering more than \$210 million, 13 houses, and numerous shares in third-party companies. These weaknesses included the following:

- 1) *Lack of pupil data tracking.* Currently, charter schools submit aggregate attendance data for each school without any information about individual pupils. Oversight agencies do not maintain individual pupil data about enrollments in charter schools they oversee for state funding purposes. One A3 charter school was found to be paying a private company to recruit and collect personal information from pupil athletes. The school then enrolled the athletes in the charter school without their knowledge—thereby fraudulently generating ADA—and paid the recruiting company a portion of the public funds generated as a finder's fee.
- 2) *Multi-track calendar abuses.* The A3 schools were found to have deceived the state into paying them significantly more funds by manipulating the "multi-track year round calendar," which charter schools are currently authorized to use. The A3 schools would (1) run a fake summer school to collect funding for pupils that never knowingly enrolled, (2) inflate their fraudulent summer school attendance numbers—to the tune of about 60%—by offering fewer days of fake summer school instruction, and (3) transfer pupils between different A3 schools, increasing attendance fraudulently by another roughly 40%.

- 3) *Lack of meaningful audit requirements.* The annual audits required by law found little to no malpractice by A3 schools for several reasons. First, auditors are not required to complete any specialized up-front or ongoing training in school finance or law to audit a charter school. Second, charter schools can choose their auditors—A3 schools were shown to have fired their auditing firms and hired less experienced firms in the rare event that audit findings were made. Third, NCB charter schools are allowed to pick their own samples of pupil documentation showing compliance with independent study laws—enabling A3 to hide the fraudulent aspects of their operation from auditors. Fourth, auditors are not required to audit the education program received by pupils, only compliance with documentation. In the A3 schools, many children were enrolled from sports teams, believing they were participating in a fundraiser and had no knowledge they were enrolled in a charter school at all.
- 4) *Flawed funding determination process.* While existing law requires that NCB charter schools only receive full funding in exceptional circumstances—when at least 80% of funding is spent directly serving pupils—the current funding determination process essentially funds all schools at 100%. This is because existing regulations define "instructional and related services" very broadly, and charter schools can meet these spending benchmarks without necessarily spending money on pupils. Further, NCB charter schools are only required to request a funding determination and provide compliance documentation to the SBE every five years.
- 5) *Perverse financial incentives for charter school authorizers.* Existing law allows charter authorizers to collect oversight fees from charter schools under their authority but does not require authorizers to demonstrate that the fees are spent on meaningful school oversight. Small school districts that approve NCB charter schools serving pupils not located in the district can earn significant oversight fees—creating a built-in incentive to overlook poor charter school practices. For example, Dehesa Elementary School District approved over ten charter schools, all providing NCB programs. The district's oversight fees for the 2017-2018 school year were more than its entire expenditures for all employees hired by the district. When the district learned of improprieties from the charter schools it had authorized, it took no meaningful action. Ultimately, the district collected the oversight fees and only acted to revoke the A3 Charter Schools under its authority once law enforcement was involved.

Audit standards identified as flawed as a result of the A3 Charter School Case. The A3 Charter case illustrated many faults in the way that charter schools are audited compared to school districts, including the following:

- 1) Current law allows charter schools to be audited as nonprofit corporations rather than as governmental entities. Nonprofit corporation audits are not nearly as detailed as governmental entity audits.
- 2) Current law does not require school district and charter school auditors to receive any special training on auditing schools.
- 3) Current law does not direct auditors to review many aspects of independent study programs at charter schools.

California Longitudinal Pupil Achievement Data System (CALPADS) and ADA data systems. As noted above, tracking attendance is one of the issues arising out of the A3 case. The State's attendance accounting system is not connected to the CALPADS. In other words, when a charter school or school district submits its ADA information to the State, that ADA is not reported with pupil identification. The State, therefore, does not know which pupils ADA is being claimed when it processes attendance apportionments. Current law prohibits a school from claiming more

than one year of attendance per pupil, however, more than one year of attendance can be paid per pupil if the pupil attends more than one school or if the student is moved between tracks. *This bill does not address this problem.*

Teacher assignments and school calendars. Current law requires independent study programs to operate with specified pupil-to-teacher ratios. Some charter school networks, however, have exceeded these ratios by assigning teachers different groups of pupils at multiple schools. While on paper, it appears that a teacher has a 25:1 pupil-to-teacher ratio at a single school, in reality, the teacher has a much higher pupil-to-teacher ratio across their entire teaching assignment at multiple schools. *This bill does not address this problem.*

The A3 Charter School case demonstrated the ability of schools to manipulate their calendars to collect far more than one year of attendance funding per pupil from the State. The A3 Charter School used the multitrack year-round calendar to run a summer program and erroneously enrolled Little League players over the summer months, enrolled them without their parent's knowledge, and collected attendance funding without providing any instruction to these children. Further, A3 Charter Schools transferred students between multiple schools in their network over the summer months, using the multitrack year-round schedule, and altered their calendar to collect much more than one year of attendance funding per student. *This bill requires schools to include in their annual audit, attendance by month and track, as applicable.*

According to the Author

According to the author, "Charter schools are a part of many communities and often provide alternative educational flexibility for families with a myriad of situations; including medical conditions, special needs, and other unique circumstances. They serve as a resource for families and deliver vital educational programs to our students.

Several fiscal audits conducted by various agencies' have identified opportunities for improvement for various charter schools and charter school authorizers across the state. Most of the negative audit findings point back to a greater need for oversight, transparency, and accountability.

SB 414 addresses these issues specifically by holding charter schools responsible for internal accounting and for educational outcomes for all students. This bill incorporates recommendations from several reports, strengthening oversight and ensuring academic success.

It is vital to implement strong accountability measures and establish proper oversight to ensure that students receive quality education in appropriate, safe, and stable learning environments regardless of whether a school is traditional, chartered, or a hybrid model. SB 414 puts students first and puts into law the important recommendations made through audits from several entities including the Legislative Analyst's Office and State Controller."

Arguments in Support

APLUS+ Personalized Learning Network Association states, "SB 414 will implement several commonsense reforms for NCB (NCB) public charter schools and improve oversight and accountability for these entities. Unlike previous bills introduced in prior legislative sessions under the guise of enacting charter school reforms by threatening their funding and ability to obtain and offer successful alternative education models for hundreds of thousands of families and students that best fit their students' needs, SB 414 is an even-handed, rational approach to solving longstanding issues in the public charter school sector. The bill addresses NCB reforms

and charter school governing board policies in four key areas of accountability and oversight, including 1) vendor relationships, 2) authorizer oversight accountability, 3) auditing practices, auditor training, and expertise, and 4) state oversight and review."

Arguments in Opposition

California Teachers Association states, "Upon the discovery of large-scale fraud perpetrated by a number of NCB charter schools, the Legislature imposed a moratorium on the establishment of new NCB charter schools in 2020, which is set to expire in 2026.

This moratorium gave time for experts from the LAO and FCMAT to investigate these issues and propose comprehensive solutions. In addition, San Diego Superior Court Judge Robert C. Longstreth ordered the State Controller to chair a multi-agency task force to develop audit criteria and best practices for detecting and curtailing future fraud in charter schools.

SB 414 falls short of what is needed, offering incomplete reforms that do not meaningfully resolve the structural issues that contributed to A3. In some sections, the bill creates new problems that undermine charter accountability and legal protections for charter employees.

The bill does not implement core structural reforms recommended in recent oversight reports. For example, it does not adopt the LAO/FCMAT recommendations related to instructional time definitions or real-time enrollment tracking. The LAO and FCMAT also stressed that enhancements to NCB charter oversight by their authorizers are needed in order to prevent fraud and misappropriation of funds. However, SB 414 disregards key report findings and recommendations on that topic as well.

It is critical that the legislature pass comprehensive reforms to NCB charter laws before the moratorium sunset date arrives. Passing incomplete measures that don't fully address all the issues leading to the A3 scandal will result in continue fraud and is deeply problematic."

FISCAL COMMENTS

According to the Assembly Appropriations Committee,

- 1) Ongoing Proposition 98 General Fund costs of an unknown but significant amount, likely in the millions of dollars to tens of millions of dollars statewide, for LEAs, especially charter schools, to comply with the various requirements added by this bill.

This bill makes several changes to charter school audit and charter school authorizer oversight requirements. There are nearly 1,300 charter schools in the state. For audits, each LEA contracts with an independent auditing firm to conduct its annual audit verifying compliance with state law via the K-12 Audit Guide. As statutory requirements for LEAs increase and continue to add procedures, independent auditing firms charge LEAs more to account for increased workload. If an auditing firm increases charges to a charter school by \$500 per year to account for requirements added by this bill, the bill creates \$650,000 in new costs.

- 2) Ongoing General Fund costs of \$174,000 for the CDE to hire one additional staff responsible for fulfilling CDE requirements of the bill. CDE cites potential for significant additional costs to the extent that investigations require existing staff time across multiple divisions.

- 3) Ongoing General Fund costs of an unknown amount, possibly in the low hundreds of thousands to high hundreds of thousands of dollars for the SCO to hire additional staff responsible for determining topics for required auditor training, processing auditor certifications, providing technical assistance to auditors, and processing a potential increase in auditor quality control reviews.

VOTES

SENATE FLOOR: 30-1-9

YES: Allen, Alvarado-Gil, Arreguín, Ashby, Becker, Blakespear, Cabaldon, Caballero, Choi, Dahle, Grayson, Grove, Jones, Laird, Limón, McGuire, McNerney, Menjivar, Niello, Ochoa Bogh, Pérez, Richardson, Rubio, Seyarto, Stern, Strickland, Umberg, Valladares, Weber Pierson, Wiener

NO: Smallwood-Cuevas

ABS, ABST OR NV: Archuleta, Cervantes, Cortese, Durazo, Gonzalez, Hurtado, Padilla, Reyes, Wahab

ASM EDUCATION: 8-1-0

YES: Muratsuchi, Hoover, Addis, Alvarez, Bonta, Castillo, Lowenthal, Patel

NO: Garcia

ASM APPROPRIATIONS: 11-0-4

YES: Wicks, Arambula, Calderon, Caloza, Elhawary, Fong, Mark González, Ahrens, Pacheco, Pellerin, Solache

ABS, ABST OR NV: Sanchez, Dixon, Ta, Tangipa

UPDATED

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CONSULTANT: Chelsea Kelley / ED. / (916) 319-2087

FN: 0001562