Chapter Five
Charter School Finance

The previous chapter examined the persons, organizations, and processes that led to the development and start-up of charter schools. We suggested that founding a charter school requires a great deal of fiscal, human, and political resources. This chapter focuses on fiscal resources. It also moves our discussion from charter start-up to operations. Fiscal resources are, indeed, a crucial input in the educational process.[1] In this chapter we provide answers to three questions:

- What are the sources of charter schools' operating revenues?
- How do charter schools spend their money? How do these expenditure patterns compare with those of other public schools?
- Are charter schools fiscally healthy?

Most of our analysis in this chapter focuses on the 30 schools open during the 1998/99 school year.[2]

5.1 Revenue Sources

Just as LEAs are the primary overseers of charter schools, they are also the primary funding source for most charter schools. With the exception of federal and state funds, and funds raised locally, all charter school funds are funneled through host districts. This distinguishes Pennsylvania from other states such as Michigan, in which charter school funds come directly from the state.

An important part of the charter school and school choice concept is that public revenues follow students, whether they choose to attend district schools or charter schools. In theory, then, students are able to choose whether to attend a charter school solely on educational criteria, without significant concern for finance. As the law is written, however, charter school students in Pennsylvania take with them less than their full per-pupil allotment. For most students, a charter

[1] There is considerable academic debate over the effectiveness of increasing spending on school "production." However, even those who contend that increased expenditures are not a *sufficient* condition of student achievement often agree that it is a *necessary* condition. Moreover, recent studies have begun to find that variations in student achievement are, indeed, associated with variations in expenditures (see RAND, 2000; Weglinsky, 1997). For a more general discussion, see Hanushek, 1997.

[2] Annual Financial Reports for the 1999/2000 school year are due to PDE by the end of October. Once again, we do not have data on the one Pennsylvania charter school that closed – Creative Education Concepts.

school receives from the students' LEA the total budgeted per-pupil amount *minus* expenditures on the following:

- ❍ nonpublic programs
- ❍ adult education programs
- ❍ community and junior college programs
- ❍ transportation
- ❍ special education
- ❍ facilities acquisition
- ❍ construction and improvement services
- ❍ debt service and fund transfers

For each special education student, a charter school receives from the student's LEA the same amount *plus* the district per-pupil allotment for special education. For both special education and non-special education, funding levels are based on the previous year's enrollment. LEAs are required to make payments to charter schools in 12 equal monthly installments. Charter schools may appeal to the Secretary of Education if the LEA fails to make timely payments. The Secretary may then withhold the amount of the missing payment from state payments to the district.

Although relatively few districts actually host charter schools, hundreds send at least one student to a charter school. Thus, estimating precisely the magnitude of the LEA subsidy to charter schools would be an enormous task. We did, however, estimate the typical non-special education subsidy by obtaining from PDE documents showing payments by *host districts* during the 1999/2000 school year.[3] Since host districts can also send students to charter schools in other districts, these estimates include both subsidies payed to charter schools hosted by the district and to out-of-district charter schools. A PDE official warned us that these estimates are tentative and should be used with caution. In the absence of better estimates, we present summary statistics to give policymakers a general sense of the magnitude of the subsidy. We refrain, however, from publishing district-by-district estimates.

According to the estimates, the median per-pupil payment from host districts to charter schools was $5,493. Interestingly, the distribution of payments across host districts is positively skewed, meaning that there are a few districts that pay considerably more per charter school pupil than others.[4] Indeed, payments ranged from a minimum of $4,885 to a maximum of $7,870, with a standard deviation of $762. These variations reflect the fact that LEA subsidies to charter schools are based on the amount districts spend on their own students.

Unfortunately, charter schools' financial reports for the 1999/2000 school year were not available at this writing. Thus, we are unable to provide 1999/2000 estimates of LEA transfers as a percentage of total revenues. We can, however, provide such estimates for the 1998/99 school year using charter schools' Annual Financial Reports. These estimates are found in Appendix C. The median charter school received $880,843 for this year, accounting for approximately 81 percent of all

[3] Data came from the May 3, 2000, version of PDE's *Pennsylvania Charter Schools Operators' Manual*, produced by the Office of Educational Initiatives.

[4] The positive skewness is also evident in the fact that the mean per-pupil payment is considerably higher than the median: $5,849.

revenues. There was, however, considerable variation among the charter schools. The school relying least on LEA payments received just 17 percent of its total fiscal year 1999 revenues from LEA payments, while the school relying most on them received 89 percent.

LEA subsidies for special education students are, of course, larger. Given the importance of special education, we defer discussion of these issues to Chapter 10.

Since LEA transfers to charter schools are calculated based on districts' per-pupil expenditures, it is interesting to compare what LEAs pay charter schools with what they spend on students attending their own schools.[5] For fiscal year 2000, the median per-pupil LEA transfer to charter schools was $2,317 (71 percent) lower than the district's per-pupil expenditures. The differences ranged across districts from a minimum of $1,372 less than the district per pupil expenditure to a maximum of $3,545 less than the district expenditure. In percentage terms the lowest paying district provided a charter school subsidy of 63 percent of its per-pupil expenditures on district students, while the highest paying district provided an 80 percent subsidy.

The fact that LEA transfers comprise only a part of charter schools' revenues leads us to look for other revenue sources. Heavy reliance by charter schools on external funds might raise serious questions for policymakers. Indeed, many foundation funders are happy to provide money for start-up projects but are reluctant to provide operating revenues on a long-term basis. Moreover, if charter schools must rely heavily on outside funders for their operations, this might create a natural limit on the number of potentially viable charter schools and, thus, the range of choices available to Pennsylvania students.

After LEA transfers, the revenue source charters rely upon most is federal funds. The most common federal sources are Title I monies and special charter school grants. Indeed, as illustrated in Appendix C, the median charter school in Pennsylvania received approximately 10 percent of its revenues from federal sources. There is, however, considerable variation among schools, with some schools receiving no federal funds in fiscal year 1999 and others receiving as much as 28 percent of their revenues from federal sources.[6]

The next most important non-LEA source of revenue for charter schools is state funds. Most such funds come in the form of start-up grants. As Appendix C shows, the median charter school relies on state funds for approximately 3 percent of its total revenues. Once again, there is considerable variation among schools, with some schools receiving virtually no state funds and others as much as 12 percent of their total revenues from state sources.

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[5] Once again, these estimates are taken from the 2000 *Charter School Handbook*. The same caveats apply.

[6] Somewhat surprisingly, there appears to be little relationship between the federal funding levels (either Title I or charter school grants) and concentration of low income students in a school. Unfortunately, there are many missing values on the low income variable in the 1998/99 data. Hence, this analysis correlated 1999/2000 income data with 1998/99 fiscal data. While this certainly has an "apples and oranges" quality to it, we judged that imperfect data were better than none. Moreover, it seems unlikely that the concentration of low income students in most charter schools would change dramatically from year to year.

A third source of non-LEA revenues is what state budget officials refer to as "local" revenue sources. These sources include earnings on investments, charitable donations (including foundation grants), and revenues from student activities such as candy sales, car washes, and so on. In the 1998/99 fiscal year the median charter school received just one percent of its total revenues from such sources. Once again, there was much variation among schools–much more than with other revenue sources. Indeed, while some schools received virtually none of their revenues from local sources, several schools received more than 30 percent of their revenues in this way. One school received fully 57 percent of its revenues from local sources. In these latter schools, the lion's share of local revenues came in the form of charitable donations. These estimates are also found in Appendix C.

For most charter schools, LEA, federal, state, and local sources comprise 100 percent of the school's revenue. In a few cases, however, schools relied significantly on proceeds from extended term financing for revenues during the 1998/99 fiscal year. These revenues make up most of the "other" category in Appendix C.

Given the discussion of the resources of charter school founding coalitions in the previous chapter, we performed a number of statistical tests to check for relationships between resources at founding and subsequent revenue flows. Specifically, we found that charter schools with strong backing from nonprofits and other nongovernmental organizations relied slightly more on revenues from charitable donations and from investment activities than other schools. However, the relationship was quite weak.[7] This finding provides some evidence, however, that charter schools whose founding coalitions include nongovernmental organizations have some fiscal advantages over other schools.

5.2 Expenditure Patterns

Under Act 22, each individual charter school is considered a separate local education agency (LEA). As such, they are separate nonprofit entities with the authority to determine their own budgets and expenditure priorities. This distinguishes Pennsylvania's charter school law from many other states in which charter schools legally remain a part of their host districts and in which host districts retain legal liability for debts incurred by charter schools. Given this relative fiscal autonomy, it is important to examine charter schools' spending patterns and whether they differ from those of other public schools. In short, what are Pennsylvania charter schools doing with their fiscal autonomy?

Before focusing on spending priorities, however, we examined the total amount charter schools spend. Table 5:1 shows that the median charter school spent $7,010 per pupil during the 1998/99 academic year. While most charter schools spent between $5,000 and $10,000 per pupil, some spent

[7] Since the distribution was highly and positively skewed, differences between the two groups show up in means (which are more sensitive to outliers) more than in medians. Specifically, the percentage of total school revenues derived from charitable donations for the mean charter school was 5.3 percent for schools with a nongovernmental (NGO) base and 2.1 percent for other schools. The medians for the two groups were 0.006 and 0.4 percent respectively. Given the skewness of the distribution, we relied on a nonparametric test of statistical significance. The difference was not discernible at conventional levels (the Mann-Whitney p-value was 0.19).

as little as $4,000. One school reported spending nearly $30,000 per pupil. This school provides services to troubled teenagers, which might explain the unusually high per-pupil expenditure.

In order to interpret these numbers, however, we need a comparison group. The best readily available comparison is each charter school's host district. Since host districts exist in the same market for labor and other school services as their charter schools, we need not make adjustments for differences in cost of living. Table 5:1 shows that as a group charter schools spent slightly more ($88) more than host districts per pupil. However, when we examine expenditures on a school-by-school basis, we find that the median charter school spent $253 *less* than its host district. The difference in the two estimates accounts for the presence of extreme values (outliers), mainly in the charter school distribution. On balance, then, it appears that charter schools and host districts spent approximately the same amount per pupil.[8] This is somewhat remarkable given that, as indicated above, the typical charter school receives only 71 percent of its district per pupil expenditure in LEA transfers.

Table 5:1 Charter School Per Pupil Expenditures Compared with Host Districts and All Pennsylvania Public Schools, 1998/99 (Medians)[9]

Schools	*Per Pupil Expenditure, 1998/99*	*Coefficient of Variation*[10]
Charter Schools	$7,010	0.59
Host Districts	6,922	0.14
Charter School minus Host District	-253*	22.8

Source: Annual Financial Report (PDE-2057) & School Profiles data.
* Exclusion of highest (outlier) charter school yields a median difference of -92 and a mean difference of -355.

The estimates in Table 5:1, however, do not allow us to assess whether charter schools and host districts have comparable student bodies and, therefore, comparable demands on their resources. For instance, charter schools might have a higher concentration of special needs students than their host districts. One must also bear in mind that charter schools must absorb any number of start up costs (not the least of which is facilities) that their host districts do not. Hence, to say that they spend approximately the same amount per pupil as their host districts might imply that they use their resources more efficiently than host districts. Efficiency, however, involves the relationship between

[8] The charter school mean and median are inflated by one extremely high outlier. Exclusion of this case yields a mean difference of -92 and a median difference of -355. Thus, excluding this unusual school, charter schools as a group spent somewhat less than their host districts.

[9] We calculated total per pupil expenditures by dividing total reported expenditures by average daily membership. Average daily membership estimates for several charter schools are missing from the School Profiles databases linked to the PDE website. We received the missing values, and updated estimates for all charter schools, from Barbara Nelson of PDE.

[10] The coefficient of variation is the standard deviation divided by the mean of a distribution. It is used to compare the amount of variation in samples with different central tendencies.

fiscal (and other) input and various student outcomes. Thus, we defer discussion of these issues until Chapter 11, which deals with student outcomes and their relationship to charter school inputs.

Beyond the total amount of expenditures per pupil, the most important characteristic of a school's overall expenditure patterns is the proportion of its funds spent on instruction versus other functions. In order to estimate the percentage of charter school expenditures devoted to instruction, we examined Annual Financial Reports from the 1998-1999 school year, the most recent year for which such reports are available. Results of this analysis are presented in Table 5:2. We found tremendous variation among charter schools.[11] Three charter schools, for instance, spent less than 40 percent of their total expenditures on instructional items, while four charter schools spent more than 90 percent on such items. One school reports spending 100 percent of its total expenditures on instructional items.[12] Taken as a group, the average charter school spent 59 percent of its total 1998-1999 expenditures on instructional items. The mean value for all Pennsylvania public schools, by comparison, was 66 percent while the mean value for all districts sponsoring charter schools was 65 percent. Taken as a group, then, charter schools spent fewer of their resources on instructional items than other schools during the 1998-1999 school year.

Table 5:2 Percentage of Total Expenditures Devoted to Instructional Items, 1998-1999

Group	*Mean*	*Minimum*	*Maximum*
Charter Schools	59%	35%	100%
Host Districts	66%	61%	73%
All Pennsylvania Public Schools	65%	46%	73%

Source: Annual Financial Report (PDE-2057) & School Profiles data.

Continuing with the charter school-host district comparisons, Table 5:3 provides the frequency distribution for the percentage of charter school expenditures devoted to instruction *minus* the same number for each school host district.[13] The table shows that two-thirds (20) of the 30 charter schools

[11] Throughout the report, we use expenditure category definitions as set out by PDE. "Instructional" expenditures include the following subcategories: regular elementary and secondary programs, special elementary and secondary programs, vocational education programs, other elementary and secondary instructional programs, adult education programs, and community and junior college education programs. Essentially, includes instructional expenditures include salaries and instructional materials.

[12] Such variations raise questions about how consistently accounting categories are applied from one charter school to the next. Some charter schools appear to have limited human resources for budgeting and other administrative functions. Unfortunately, we have no way to independently verify the contents of schools' Annual Financial Reports.

[13] This is a histogram table. Thus, the top row indicates that 8 charter schools spent 20 percent or less than their host districts on instructional items; the second row shows that another 7 charter schools spent between 10 and 20 percent less than their host districts, and so on. For regional charter schools (i.e., those with more than one host district/sponsor), we created composite host district comparisons by averaging the values for all of the host districts. Ideally, one would weight this average by the number of students in the charter school from each district. Given the limits of the project, we were unable to obtain such information on a broad scale.

under examination spent a lower percentage of their total expenditures on instructional items than their host districts–some by more than 20 percentage points.

Table 5:3 Instructional Expenditures as a Percentage of Total for Charter Schools Minus the Same Percentage for Host Districts

Difference	*Number of Schools*
>-20%	8
-20 to -10%	7
-9 to 0%	7
1 to 9%	3
10 to 20%	3
>20%	2
Total	30

Source: Analysis by the Evaluation Center

This finding leads to two interrelated questions. First, why do charter schools as a group devote a smaller share of their total expenditures to instructional items? Second, why is there such wide variation *among* charter schools? We begin with the first question.

One possible answer to the first question is that, as start-up organizations, charter schools must bear many one-time and fixed costs (e.g., renting and/or renovating facilities) that established districts have either covered in the past or have spread out over time by means of capital budgets. If this is true, then the fact that charter schools spend a lower percentage of their total expenditures on instructional items is not necessarily an indication of inefficiency or waste. Rather, it might simply reflect the relative high and fixed start-up costs associated with founding a new school. While available data do not allow us to fully dispose of this issue, we examined the percentage of total expenditures charter schools use for support services. This category includes instructional staff, administration, health, business, maintenance, transportation, and rent payments for school facilities. (The "facilities" category, by contrast, includes expenditures to acquire and improve buildings[14]).

Table 5:4 shows that for the average charter school, "support services"– which include rent and facilities maintenance–comprised 38 percent of total expenditures, compared with 32 percent of host districts and 33 percent for all Pennsylvania public schools. Hence, there is at least some evidence that for charter schools, instructional expenditures are "crowded out" to a certain degree by the need to cover start-up and other related expenses. Another possible explanation is that charter schools typically pay their teachers less than other similar schools (see Chapter 8). This, in turn, would reduce the demand on their instructional budgets. We emphasize, however, that this is only a preliminary answer to the question, and that it deserves further attention. A fuller accounting of charter school expenditure patterns can be found in Appendix C.

[14] Most charter schools spent little or nothing on such services during the 1998/99 school year. Of the 5 schools that reported such expenditures, however, they comprised up to 37 percent of total expenditures. Thus, for some schools, the need to acquire, construct, or improve facilities constitutes a large burden. While Act 22 prohibits charter schools from using public funds to construct new facilities, they may use other funds to do so.

Table 5:4 Expenditure Patterns in Charter School and Other Public Schools (means)[15]

Expenditure Category	*Charter Schools*	*Host Districts*	*All PA Public Schools*
Instruction	59%	66%	65%
Support Services	38	32	33
Noninstructional Services	0	2	2
Facilities Acquisition & Improvement	2	n/a	n/a
Debt Service	1	n/a	n/a

n/a = data not available
Source: Annual Financial Report (PDE-2057) & School Profiles data.

Turning next to the question of why there is so much variation in expenditure patterns among charter schools, once again the data are limited. Nonetheless, there is some evidence that schools with strong backing from nongovernmental organizations devote a larger share of their total expenditures to instruction. These groups might provide facilities and other resources that allow charter schools to devote a larger share of their operating budgets to instructional items. The relationship, however, is weak and somewhat sensitive to choice of statistical technique.[16] We hope that others will examine in greater detail the reasons behind these apparent patterns.

5.3 Fiscal Viability

For charter schools to operate successfully in the long run, they must be fiscally viable. While it is beyond the scope of this report to provide a full fiscal audit of Pennsylvania charter schools, we examined two indicators of fiscal viability. First, we examined charter schools' capacity to develop and execute budgets by looking at variances between budgeted and actual revenues and expenditures. Second, we examined charter schools' end-of-year balance to see if there were any deficits. Finally, as with the earlier sections of this chapter, we tested explanations for observed variations in charter schools' fiscal health.

In order to provide a composite picture of schools' capacity to budget, we calculated the variance between budgeted and actual revenues and between budgeted and actual expenditures. High variances can cast doubt on a school's ability to effectively plan and execute educational and organizational strategies. In operational terms, a revenue variance is the amount of funds actually

[15] As with the other variables, the distributions were skewed. We depart from the normal practice of reporting medians, however, because many of the medians are zero. Readers should bear in mind that means are particularly sensitive to outliers.

[16] The mean proportion of expenditures devoted to instruction for schools with NGO backing was 60.7 percent, compared with 58.5 percent for other schools. The mean is more appropriate than the median in this case, since the distributions are reasonably symmetrical. Looking at the medians, however, produces the opposite result, with NGO-backed schools devoting 55.8 percent and other schools 59.3 percent of their total expenditures to instructional items.

received minus the amount the school budgeted for. The same holds true for expenditures. In order to facilitate comparisons among high- and low-budget schools, we converted these variances into percentages of the total revenues (expenditures) budgeted for. Thus, for instance, a revenue variance of 20 percent means that the school received revenues that were 20 percent higher than those budgeted for, whereas a revenue variance of -20 percent means that the school received revenues that were 20 percent less than those budgeted for. Naturally, it is better for schools to have positive variances in revenue and negative variances in expenditures.

On the revenue side, the median school received 1.7 percent more than it budgeted for (see Table 5:5). Thus, taken as a group, Pennsylvania charter schools budgeted conservatively and received more than expected. As with the other fiscal variables discussed in this chapter, there was great variation among charter schools. Indeed, revenue variances ranged from -47.5 percent (meaning that the school received much less revenue than expected) to 96.7 percent (meaning that the school received much more than it budgeted for). Two schools reported no budgeted revenues for the 1998/99 school year. These were excluded when calculating summary statistics.

Table 5:5 Variances in Revenues and Expenditures as a Percentage of Budgeted Revenues and Expenditures, 1998-1999

Variable	*Median*[17]	*Mean*	*Minimum*	*Maximum*
Revenue Variance	1.7%	7.4%	-47.5%	96.7%
Expenditure Variance	-11.4	-1.4	-46.1	63.2

Source: Annual Financial Records (PDE-2057)

On the expenditure side, Pennsylvania charter schools appear to have been similarly conservative. Indeed, the median charter school spent 11.3 percent less than it budgeted for. Once again, there was great variation among charter schools. Expenditure variances ranged from -46.1 percent (meaning the school spent much less than it expected) to 63.2 percent (meaning the school spent much more than it expected). Once again, two schools reported no budgeted expenditures and we excluded these when calculating summary statistics. A complete listing of revenue and expenditure variances can be found in Appendix C.

In spite of the wide variation in charter schools budgetary precision, we find generally that schools that underestimate their revenues also underestimate their expenditures, and vice versa. Figure 5:1 illustrates the relationship between revenue variances and expenditure variances by means of a scatterplot. The horizontal axis represents the percent variance in revenues while the vertical axis

[17] Readers will note that there are large differences between the mean and median values. This is because each distribution is highly skewed toward the high end. In other words, in each case there are a small number of schools with large positive variances, even though most schools have lower variances. Since the mean is more sensitive to outliers, it is substantially higher than the median in each variable. In such cases, statisticians generally use the median so as to avoid overrepresenting outlying values.

represents the percent variance in expenditures. The graph divides the two-dimensional space into four quadrants. The lower-left quadrant represents schools that underestimated both their revenues and their expenditures. In such cases, even high variances should provide little cause for alarm. Similarly, the upper-right quadrant represents schools that *over*estimated both their revenues and their expenditures. Once again, these cases provide little cause for alarm. The lower-right quadrant represents schools that overestimated their revenues and underestimated their expenditures – once again, no cause for concern. The upper-left quadrant, however, might provide cause for concern, because such schools would have underestimated their revenues and overestimated their expenditures. Fortunately, there are only two schools in this quadrant. Both schools, moreover, lie very close to the intersection of the "zero" lines, indicating that the magnitude of both revenue and expenditure variances was very small.

Pennsylvania charter schools, in sum, did a remarkably good job of budgeting, both on the revenue and expenditure sides of the fiscal equation. Readers should bear in mind, however, that these data represent only one year of expenditures.

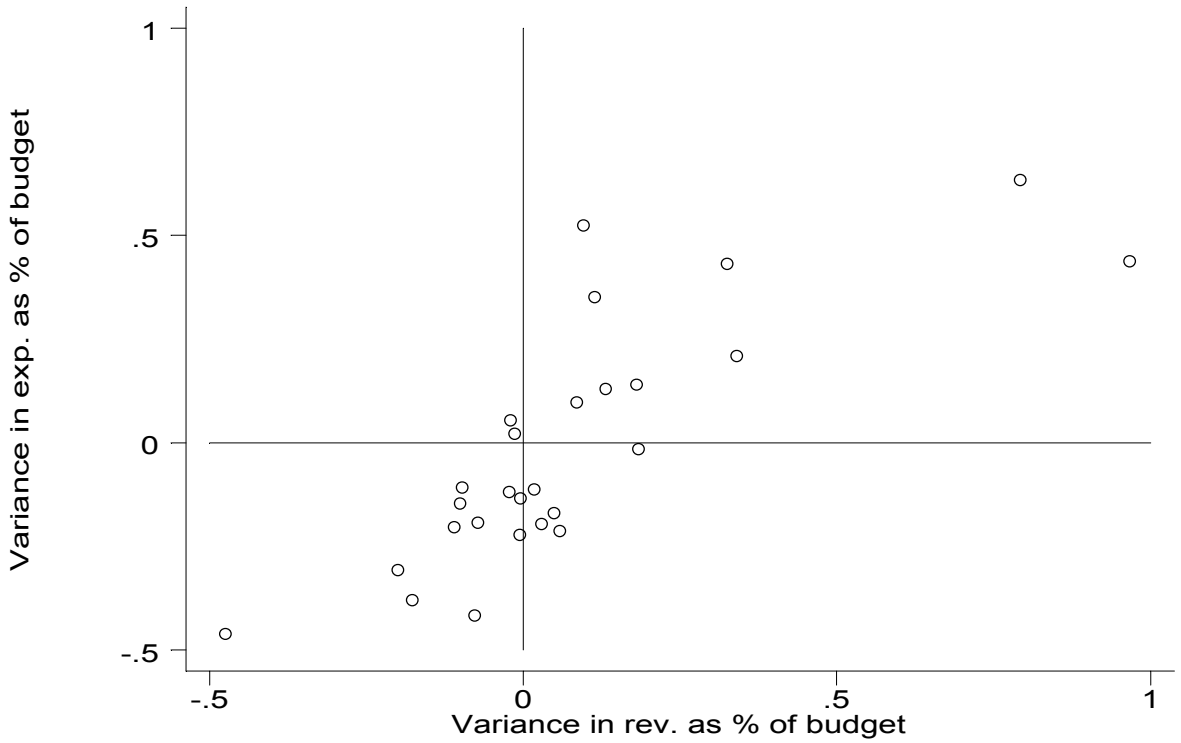

Figure 5:1 Revenue and Expenditure Variance Compared, 1998/99

While providing thorough explanations for these findings lies beyond the scope of this report, we did test a number of explanations that derived from the discussion in Chapter 4. First, we

hypothesized that charter schools in their second year of operation would have more experience at budgeting and thus would have lower variances. The extra year of experience appears to have had no notable impact on budgeting for revenues. However, we did find a modest effect on the expenditure side. Whereas the median expenditure variance for schools in their first year of operation in 1998/99 was -12.7 percent, it was only -2.1 percent for schools in their second year of operation. We tested for similar differences in schools according to whether they were built upon the organizational foundations of preexisting schools. Once again, we found a difference on the expenditure side but not the revenue side. The median expenditure variance for charter schools based on preexisting schools was -6.8 percent, compared with -11.1 for other schools. Finally, we tested whether schools with backing from nongovernmental organizations had lower variances than other schools. Surprisingly, we found that schools with NGO backing had higher variances than other schools. In all the analyses, however, the small number of cases prevented us from controlling sufficiently for variances in target population, community characteristics, and so on. Thus, we cannot rule out the possibility that second year schools were stronger in some unobserved respect than first schools. Indeed, one might theorize that the second year group of schools was stronger since applicants had more time to observe and learn from the experiences of the first round of charter schools. None of the differences reached conventional levels of statistical significance.[18]

The ability to accurately anticipate revenues and expenditures in the budgeting process should enable charter schools to avoid running deficits. Given that charter schools appear to do a good job of budgeting, we should expect that few, if any, would run deficits. Examination of charter schools' 1998/99 Annual Financial Reports (AFRs) reveals that the median balance for all charter schools was $84,380, or 11.4 percent of total expenditures. However, there was significant variation among schools. Seven of the 30 schools (23 percent) we examined showed negative end-of-year balances, the largest of which was over $400,000, or 10.7 percent of that school's total expenditures. On the positive side, some schools showed positive balances of up to 58 percent of their total expenditures for the year. Thus, while most charter schools appeared to be fiscally healthy in the 1998/99 school year, there were a number of trouble spots. A complete listing of end-of-year balances can be found in Appendix C.

Once again, we investigated a number of explanations for variations in end-of-year balances. First, recognizing that secondary schools are generally more expensive to run than elementary schools, we tested whether schools with older students were more likely to run deficits,[19] but found no clear difference. Second, we tested the hypothesis that schools backed by nongovernmental organizations would be more likely to run positive balances, but again found no clear difference. Finally, we tested for an "experience" effect by comparing the balances of first year schools with those in their second year of operation. Surprisingly, we found that schools in their first year of operation were more likely to run positive balances than schools in their second year of operation. This difference

[18] We used Mann-Whitney rank sum tests to assess statistical significance.

[19] In particular, we compared each school's end-of-year balance with the highest grade level it included.

surpassed conventional levels of statistical significance.[20] One might theorize that second year schools had to deplete many of their start-up resources in the first year, or that the first year schools were stronger because they were able to observe and learn from the experiences of the 1997/98 cohort of charter schools. This issue certainly deserves further exploration as policymakers study ways to modify Pennsylvania's charter school law.

5.4 Summary and Conclusions

Like other school choice policies, Act 22 mandates that funding follows students. Thus, schools have an incentive to work to satisfy students and their parents. Under the terms of the Act, this funding is funneled through host districts and other LEAs sending students to a given charter school. The size of the LEA subsidy is based on the LEA's per-pupil expenditure on its own students and differs for special education and non-special education students. We defer detailed discussion of special education finance to chapter10.

The first section of the chapter examined sources of charter schools' revenue. Using PDE data, we estimate that the median charter school received approximately 81 percent of its total revenues from LEAs during the 1998/99 school year. There is, however, a large amount of variation among charter schools. Next to LEA transfers, the largest revenue source for charter schools is the federal government, mostly through Title I monies and special charter school grants. While there is considerable school-by-school variation, the median charter school received approximately 7 percent of its total revenues from the federal government. The remainder of charter school revenues came from state grants (e.g., start-up grants) and "local" sources, such as earnings on investments, charitable donations, and revenues from student activities (e.g., candy sales, car washes, and so on). In addition, a few schools relied on proceeds from extended term financing during the 1998/99 school year. While the scope of the study prevents us from attempting to provide detailed explanations for variations in charter school revenue sources, we did find that schools connected to nongovernmental organizations rely on charitable donations and investment activities slightly more than other schools. This suggests that the advantages of group affiliations in the context of start-up might continue into the early years of the schools' operations. However, the evidence to date is quite weak. Nonetheless, the role of NGOs in charter school operations bears closer examination.

An important policy issue follows from the fact that the typical charter school relies on non-LEA sources for approximately one-fifth of its total revenue. From one point of view, such reliance on nondistrict sources is good inasmuch as it tends to favor schools that bring a great deal of organizational, fiscal, and social capital to the table. In this view, these schools are more likely to realize some of the major goals of privatization–to leverage community resources so that governments can do less with more and to build a sense of collective responsibility for schools and students. From another perspective, charter schools' reliance on non-LEA sources is worrisome,

[20] The median balance for first year schools was positive at 14.2 percent of total expenditures, while the same value for second year schools was negative 1.3 percent. A Mann-Whitney rank sum test showed that the difference was statistically discernible at the .02 level.

since it raises questions about the sustainability and scalability of the reform. There are, after all, a limited number of organizations willing and able to sponsor charter schools. Foundations and other charitable organizations, moreover, are often more sanguine about providing start-up monies than about covering long-term operating expenses. This dependency on externals funds might be especially troubling, from this point of view, if charter schools must use them for operating costs as well as one-time start-up expenses. Thus, what at first blush appears to be a strength of many Pennsylvania charter schools might turn out to place limits on the range of charter-related choices available to students. Ultimately, resolution of this debate depends on how efficiently charter schools are spending their revenues.

The second section of the chapter examined charter schools' expenditure patterns. We estimate that charter schools spent approximately the same amount per pupil as their host districts during 1998/99. Of that total amount, we found that charter schools typically spend a smaller percentage on instructional items than their host districts, and a large percentage on support services (which include renting and maintaining facilities) and on other noninstructional items. The reasons for these differences in expenditure patterns might lie more in the exigencies of starting new schools (e.g., acquiring and maintaining physical facilities) than in any inherent inefficiency in charter schools. However, these are questions that can be answered only with the passage of more time.

The final section of the chapter examined charter schools' fiscal viability using two indicators. First, we found that charter schools appear to be relatively conservative in budgeting, taking in more than expected on the revenue side and spending less than expected on the expenditure side of the ledger. Moreover, there is some evidence that schools benefit from experience, as second year schools had slightly lower expenditure variances than first year schools (there was no discernible relationship on the revenue side). Second, we examined charter schools' end-of-year balances for the 1998/99 school year. We found that 7 schools (23 percent) ran negative balances (deficits), the largest of which constituted 10.7 percent of total expenditures.

In the final analysis, the most important question about charter school finance is how efficiently they spend their resources. Answers to questions about efficiency, however, require evaluators to examine the relationship between fiscal inputs and student outcomes. Chapters 11 and 12 examine student outcomes in charter schools. Unfortunately, the data are insufficient to yield reliable estimates relating costs to outcomes.

Before examining outcomes, however, we turn in the remainder of this section to an evaluation of two important types of nonfiscal inputs and resources. The next chapter provides an overview of the characteristics of charter school students and their families. The final chapter of this section assesses the characteristics of charter school teachers and staff.

As we noted earlier in the chapter, the accuracy of some of the data may not be as high as we would wish. However, compared with other states where we have evaluated charter schools, particularly Michigan, the completeness and accuracy of the Pennsylvania financial data seems quite good. In part this is due the technical assistance and support provided by the Office of Educational Initiatives.