

Office of the Inspector General

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Supplemental Review and Financial Analysis of the South Carolina Governor's School for Science and Mathematics and its Supporting Foundation

I. Executive Summary

In October 2017, the South Carolina Office of the Inspector General (“SIG”) issued a report titled, “*Review of the South Carolina Governor’s School for Science and Mathematics and the Organizational Relationship to its Supporting Foundation.*” (See Appendix A)

This review is supplemental to the SIG’s 2017 review to provide additional transparency of the Foundation’s financial support to the school, and assist SCGSSM leadership, the Foundation’s Board of Directors (“Board”) and the future Foundation CEO in the alignment of the fundraising priorities and reporting hierarchy in support of SCGSSM’s strategic goals and priorities. The scope and objectives of this review were to determine the following:

- Provide a detailed analysis of the Foundation’s annual allocation to SCGSSM and its taxpayer impact, if any;
- Compare the Foundation’s endowment practices to best practices of its national peers;
- Identify best practices in private, nonprofit/foundation financial support and reporting hierarchy to a publicly funded STEM school; and
- Determine the status of the findings and recommendations set forth in the SIG’s 2017 report.

The SIG conducted a detailed analysis of the Foundation’s financial operations and policies for Fiscal Year 2017 (FY2017) since it was the most recent fiscal year in which the Foundation conducted the previously delegated functions for the full year. The detailed financial analysis required a review of the Foundation’s trial balance of accounts, audited financial statements and federal information returns (IRS Form 990), as well as the outside accountant’s supplemental schedules and worksheets associated with the FY2017 year-end closing of its accounting records. The SIG also identified “best practices” in foundation management, reporting framework and relationships to a STEM school; along with obtaining information on the endowment practices of the STEM schools studied as benchmarks in the 2017 review.

Of the seven findings and recommendations set forth in the SIG’s 2017 report, the three most important pertained to the delegation of authority and oversight of specific SCGSSM employees and programs to the Foundation without a formal operating agreement or Memorandum of Understanding (MOU). Two findings and recommendations for the SCGSSM and Foundation are still pending. All other findings have been completed. Set forth in Table A is the status of these three findings and recommendations issued by the SIG in its 2017 review.

Table A: Status of 2017 Report Findings & Recommendations

<u>2017 Report - Finding #</u>	<u>Brief Description</u>	<u>SIG Recommendation</u>	<u>Current Status</u>
1	Delegation of SCGSSM employees and programs was inappropriate & potential violation of state law.	SCGSSM should resume oversight of staff and programs.	Completed during the 2017-18 school year.
2	SCGSSM and Foundation operated without an MOU to ensure fundraising efforts and support aligned with SCGSSM priorities.	SCGSSM and Foundation should adopt a formal MOU.	Incomplete.
4	Lack of transparency of Foundation financial activities in support of SCGSSM.	Foundation should create a process to provide full financial disclosure to SCGSSM.	Pending.

Foundation Trial Balance Review & Analysis

The SIG reviewed the Foundation’s FY2017 final trial balance of accounts as of 6/30/2017, along with supplemental schedules and worksheets. The Foundation Board chair, business manager, and outside

accountant provided detailed financial information and answered supplemental questions posed by the SIG. The Foundation structured its accounting system and year-end closing processes to segregate its net assets into three categories – unrestricted, temporarily restricted, and permanently restricted. At the end of FY2017, the Foundation’s net assets were comprised of the following:

Unrestricted – (deficit)	-	\$ (141,202)
Temporarily Restricted	-	1,989,616
<u>Permanently Restricted</u>	-	<u>10,348,891</u>
Total Net Assets		\$ 12,197,305

The Foundation took steps to ensure each restricted asset was utilized only for its designated purpose. The majority of the Foundation’s FY2017 donations fell into the temporarily restricted category and were received for the support of various SCGSSM programs and activities. The Foundation categorized virtually all of its earnings and appreciation on investments as temporarily restricted funds until they were appropriated.

Foundation FY2017 Income

The majority of the Foundation’s fundraising proceeds was derived from business or corporate contributions, with the majority of those contributions restricted to supporting various programs or activities. The Foundation received several permanently restricted contributions, which added to its endowment (\$18,746). The majority of unrestricted contributions were received from parents, alumni, friends, the Business Leadership Network, and income from two special event fundraising initiatives.

During FY2017, the Foundation assessed an administrative fee (“gift tax”) of 18.55% on approximately \$870,000 of its contributions, which produced unrestricted income of \$161,360. The SIG determined the Foundation first assessed the fee in FY2013 at 8.55% and increased the fee to 18.55% for FY2016. Fees assessed on gifts are becoming more common in nonprofits with the increase in online giving with its associated third party processing fees. A recent survey by the Council for Advancement and Support of Education found 38% of its members assessed fees on non-endowed gifts. Of those assessing fees, the median was 5%, the minimum was 1.2% and the maximum was 10%.

Investment income was the largest source of Foundation income (\$1,177,687) in FY2017 and included dividends, interest, and gains in the value of investments. The total gains for FY2017 represented an increase in the value of the investments of approximately 8%, a significant turnaround from the FY2016 loss in value of approximately 4%. All but \$811 of investment income was recorded as temporarily restricted income, having resulted from the investment of restricted funds.

Other Foundation income included \$66,475 from the Hartsville Development Foundation (HDF) contribution, which pertained to the Foundation’s Startsville Incubator initiative.

Analysis of the Foundation’s Restricted Funds

The Foundation’s total expenses for FY2017 of \$2,458,336 were applied to the different funds, including \$977,269 of expenses applied against the Foundation’s unrestricted funds. The remaining \$1,481,067 of expenses were applied against the temporarily restricted assets based on the Foundation’s determination they satisfied the restrictions associated with the funds (net assets).

Unrestricted Net Assets (Deficit) - The \$977,269 of expenses applied against unrestricted funds was partially offset by unrestricted income of \$870,980 received during FY2017 resulting in a deficit of unrestricted funds. The deficit first arose in FY2016 due to the recorded loss in value of the investments and expanded into FY2017 when expenditures exceeded income in the unrestricted net asset category. A comparison of the Foundation to sixteen similar nonprofits prepared from IRS Form 990 data found the Foundation’s distribution

percentages at the end of FY2017 were 1% unrestricted; 16% temporarily restricted; and 85% permanently restricted. The average distribution percentages for the comparative group of sixteen nonprofits were 43% unrestricted; 28% temporarily restricted; and 29% permanently restricted. (See Exhibit C)

Temporarily Restricted Net Assets - The Foundation's temporarily restricted net assets increased from \$1,435,987 at the end of FY2016 to \$1,989,616 at the end of FY2017. A portion of the increase was related to the unrealized appreciation of investments, which did not represent available funds to the school or the Foundation. Further, there were \$436,000 in uncollected pledge balances at the end of FY2017. However, on a fund-by-fund basis, there were significant fund balances that represented available funds.

Startsville Initiative Funds – Redirection of Temporarily Restricted Funds – The Foundation raised a total of \$304,905 for this initiative and ended FY2017 with a fund balance of \$442,926, with the majority associated with the Career Services undertaking. The SIG determined during its 2017 review concerns were raised by the school this initiative was outside of SCGSSM's strategic plan and not beneficial to the school. While there was possibly some benefit in assisting alumni and students, the SCGSSM Board of Trustees believed resources should meet the current needs of students before the development of a "Launch Fund" to provide financial support to alumni. With the Foundation ceasing the Startsville Incubator operation, three donors who provided \$300,000 toward the Career Services initiative gave permission to redirect their donations to other activities.

Foundation FY2017 Operating Expenses

The Foundation grouped its FY2017 expenses (\$2,458,336) into thirteen groups in its trial balance. The three largest groups were (1) Program Expenses (incl. outreach expenses - \$626,662), (2) Marketing and Public Relations (incl. salaries - \$562,561), and (3) Management and Fundraising Salaries (\$458,900).

The trial balance included separate accounts for each of the Foundation's fourteen salaried employees. A fifteenth position listed in the trial balance for a grant writer received no salary in FY2017. The total FY2017 salaries was \$807,256. At the end of FY2018, the Foundation staff consisted of seven employees. Based on FY2017 salaries, the estimated total salary cost for these seven employees was \$314,000, a reduction of approximately \$493,000 from the total FY2017 salary costs.

Foundation FY2017 Detailed Expense Analysis

The Foundation's outside accountant prepared the year-end worksheets to distribute both income and expenses to the various restricted and unrestricted funds. While a number of expense items were clearly applicable to certain programs or activities, particularly the direct support items provided to SCGSSM, others were not as obvious such as marketing and recruiting expenses, which were grouped together in the Foundation's trial balance. The worksheets separated the recruiting expenses from marketing and public relations, and applied approximately 12% of the remaining marketing expenses to the Foundation's two fundraising events, with the remainder of the marketing expenses applied to the allocation for the benefit of SCGSSM - \$299,709 in total. This amount included the salaries and benefits cost of the director of marketing and the public relations coordinator, but none of the CEO salary cost.

SCGSSM / Foundation Annual Allocation Process

The SCGSSM and Foundation have historically conducted an annual process to determine the necessary funding provided to (or for the benefit of) the school by the Foundation. The school and the Foundation jointly developed this budget allocation process and included a list of items grouped into four categories: (1) Student Development, (2) Academics, (3) Outreach, and (4) General. In FY2017 and prior years, the items of support fell into two broad categories: (1) direct support to SCGSSM - \$309,945 (22% of the total allocation), and (2)

expenditures “for the benefit of” SCGSSM - \$1,115,536 (78% of the total allocation), for a total FY2017 allocation of \$1,425,481 to SCGSSM.

Impact to SCGSSM & Foundation – Delegated Functions

The Foundation Board advised SCGSSM the FY2017 end-of-year deficit and the reduction in fundraising efforts during the search for a new CEO limited the Foundation’s ability to provide any significant funding to support the formerly delegated functions for FY2018. At least 40%, or approximately \$980,000 of the Foundation’s total expenses, were expended on those delegated functions during FY2017. SCGSSM resumed all of these functions during FY2018 and staffed them through hiring additional personnel as well as requiring existing personnel to assume added duties. In the absence of any state funding SCGSSM utilized its reserve funds totaling \$575,000 to carry out the functions. In April 2018, the Foundation Board approved a direct allocation to SCGSSM of \$173,000 for FY2018. The state’s General Assembly approved a supplemental budget request totaling \$400,000 to fund the functions for FY2019.

Comparison of the Foundation’s Endowment Practices

To evaluate the Foundation’s endowment practices, the SIG compared its endowment activity to sixteen other nonprofits by reviewing recent IRS Form 990 reports, utilizing the 990’s Schedule D, Part V, which provides a five-year analysis of endowment activity. The sixteen consisted of the North Carolina School for Science and Mathematics (NCSSM); Illinois Mathematics and Science Academy (IMSA); Louisiana School for Math, Science and the Arts (LSMSA); and thirteen South Carolina nonprofits with endowments of a similar size to that of the Foundation. (*See Exhibit D*)

Based on the Foundation’s Form 990 information, its endowment has not grown in recent years and most of its fundraising focus appeared directed toward supporting current activities and programs. That differed significantly from the other sixteen nonprofits whose average endowment growth was 66% during the five-year period. The supporting foundations of the three STEM schools grew 81% (North Carolina), 94% (Illinois) and 55% (Louisiana), respectively.

The Foundation’s investment earnings and appreciation generated by its endowment totaled \$2,728,983, and its distributions from the endowment totaled \$3,157,942. The Foundation’s investment earnings appeared to be on par with the other sixteen nonprofits during the five-year period. The Foundation’s endowment spending policy is 5% of the fund’s average fair market value over the previous 36 months. The policy has a floor of 3% and a ceiling of 5%, and is subject to Board approval each year. The Foundation appropriated 5% for FY2017 and it appeared to have also done so in each of the past five years. By comparison, the NCSSM foundation’s spending policy is similar to the Foundation’s and based on a 36-month rolling average with a ceiling of 6%, approved annually by the NCSSM foundation board, which is 5% for the current fiscal year.

Best Practices in Foundation Support and CEO Reporting

Prior to April 2016 and the change in SCGSSM leadership, the Foundation’s CEO held the additional title of Executive Vice President for Strategic Direction of SCGSSM and reported to the SCGSSM president for the operation of the previously delegated programs and staff, and to the Foundation Board for other Foundation activities. This dual reporting structure for the Foundation CEO was somewhat similar to the organizational hierarchy and framework in existence at two other STEM schools the SIG surveyed – the NCSSM and IMSA. The difference between the former SCGSSM / Foundation reporting framework and the NCSSM and ISMA frameworks is the SCGSSM / Foundation framework had no governing document or law to ensure the CEO’s

dual reporting framework, relationship, roles and authorities of the school and the Foundation survived any change in leadership at either entity.

The NCSSM and NCSSM Foundation framework and hierarchy relationship was codified in North Carolina state law §116-231, which established the NCSSM as a constituent high school of the University of North Carolina (UNC). (*See Appendix C*) As such, the UNC Policy Manual became the definitive authority on the NCSSM and its foundation's relationship and requirements. Specifically, UNC policy 600.2.5.2(R) sets forth the required elements of a university/associated entity relationship. (*See Appendix D*)

The SIG identified the following key attributes of the NCSSM / NCSSM foundation framework:

- Relationship and reporting structure is created in state law through the UNC system;
- Foundation president jointly reports to NCSSM chancellor and separately to the foundation board;
- Foundation president is part of NCSSM executive leadership team;
- Foundation president and NCSSM leadership jointly prepare fundraising goals to support the school's priorities and strategic plan; and
- Foundation employees are state employees.

A closer review of UNC policy manual, section 600.2.5.2(R) ("*Required Elements of University – Associated Entity Relationship*") sets forth detailed components to ensure the effectiveness of this relationship. (*See Appendix D*) The key points of this policy for associated entities (i.e., foundations) are:

- Associated entities engage in activities that are critical to and aligned with the mission, goal and objectives of the constituent institution;
- Associated entities are subject to the direction of its own governing body and provide funding and support to the approving constituent institution;
- Associated entities are permitted to represent they are affiliated with the constituent institution, in accordance with the regulation and written approval with the approving institution;
- The authority and responsibility for establishing and maintaining cooperative and mutually beneficial relationships between the two entities rests with the approving constituent institution;
- Approving constituent institution maintains oversight and control over its name, marks, resources, and activities that could impact accreditation standards and compliance responsibilities; and
- Funds raised by the associated entity are to be used to support the approving institution consistent with the donor intent and law.

Summary and Recommendations

The Foundation and its outside accountant, maintained extensive documentation on the Foundation's income, expenditures, endowment assets, and allocations to the SCGSSM, as would be expected of a \$12 million nonprofit foundation with the mission of supporting a school of SCGSSM's caliber. While fundraising was strong during FY2017 and early FY2018, the Foundation's mission and focus had drifted away from the priorities of the school.

Most apparent was the Foundation's expenses exceeded its unrestricted income. The fact the unrestricted income was overspent, and the endowment had not grown but in fact, had declined in the last five years, was an indication spending may have been at an unsustainable level.

The bottom line was only 22% (\$309,945) of the Foundation's total allocation and support (\$1,425,481) to SCGSSM was direct support in FY2017. The balance was an allocation "for the benefit of" the school, usually in the form of expenses associated with the delegated functions, to include staff salary apportionment.

Virtually all control and oversight of those functions was lost following the change in SCGSSM leadership and the deterioration of the relationship between the new president and the Foundation's former CEO. It was not possible to judge the cost/value of the services provided by the Foundation in conducting those functions, or to determine appropriate budget amounts to re-assume them.

When the school was informed the Foundation could not provide financial support for its priorities for FY 2017-18, the SCGSSM utilized \$575,000 of its reserve funds to operate these programs. In April 2018, the Foundation provided \$173,000 in direct allocation to the school. In addition, the state General Assembly provided \$400,000 in supplemental funding to the school for FY 2018-19 for these programs.

SIG Recommendations

The SCGSSM and Foundation were on the right trajectory in developing this same framework and reporting hierarchy when the former Foundation CEO reported to the SCGSSM president, held an executive leadership team position at the school, and developed fundraising goals to support SCGSSM priorities. Unfortunately, this dual reporting structure was not formally adopted, either by MOU or state law, and collapsed when a change in school leadership occurred in April 2016.

The success of the NCSSM / NCSSM Foundation relationship can be traced to North Carolina state law, which established the NCSSM as a constituent institution within the UNC system. The UNC policies and regulations established the authorities of the NCSSM and the reporting hierarchy of the NCSSM foundation as an affiliated entity to the school. Equally important to the success of this relationship is the NCSSM Foundation president reports to the NCSSM chancellor on fundraising matters in support of the NCSSM priorities and strategic plan. *(See Appendix C & D)*

The decision to adopt a formal structure of authorities, roles, responsibilities, and accountability for the SCGSSM, the Foundation, and the Foundation CEO is not in dispute. The best practices identified in this review provide two avenues to achieve this goal: (1) agree upon a Memorandum of Understanding; or (2) introduce legislation, which defines the structure for the school and Foundation relationship and reporting hierarchy of the Foundation CEO.

This supplemental review determined there are two recurring findings from the 2017 report associated with the adoption of an MOU by the school and Foundation, and the development of a financial transparency process by the Foundation for the school's use.

It is the SIG's recommendation an MOU be adopted by each board for the SCGSSM and Foundation which recognizes the authorities, roles, responsibilities, and accountability of the SCGSSM, Foundation, and the Foundation CEO; as well as, reestablish a dual reporting role for the Foundation CEO to the SCGSSM president and the Foundation Board. It is also the SIG's recommendation that the General Assembly consider legislation, similar to the North Carolina law, which defines the structure of the SCGSSM and Foundation and reporting hierarchy of the Foundation CEO.

The SIG extends its appreciation to the leadership and staff of the Foundation and SCGSSM, and the Foundation outside accountant for the cooperation and courtesies provided to the SIG during this review.

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II. Background

A. Predicate

In October 2017, the South Carolina Office of the Inspector General (“SIG”) issued a report titled, “*Review of the South Carolina Governor’s School for Science and Mathematics and the Organizational Relationship to its Supporting Foundation.*” (See Appendix A) The SIG determined the South Carolina Governor’s School for Science and Mathematics’ (“SCGSSM”) delegation of supervision of publicly funded state employees along with specific programs and functions to the SCGSSM Foundation’s (“Foundation”) oversight was inappropriate and potentially violated state law. (See Appendix B “*South Carolina Attorney General’s Opinion dated 8/22/2017*”) The SIG recommended the realignment of supervision of those programs, functions, and staff back under SCGSSM’s oversight.

In addition, the SIG determined the poor communication and relationship between the current SCGSSM president and the Foundation’s former chief executive officer (“CEO”) created an environment unconducive to transparency of the Foundation’s past spending and financial support of the school’s priorities. In turn, this created a hardship for SCGSSM to budget for and fund the resumption of the delegated programs and staff.

This review is supplemental to the SIG’s 2017 review to provide additional transparency of the Foundation’s financial support to the school, and assist SCGSSM leadership, the Foundation’s Board of Directors (“Board”) and the future Foundation CEO in the alignment of the fundraising priorities and reporting hierarchy in support of SCGSSM’s strategic goals and priorities.

B. Scope and Objectives

The scope and objectives of this review were to determine the following:

- Provide a detailed analysis of the Foundation’s annual allocation to SCGSSM and its taxpayer impact, if any;
- Compare the Foundation’s endowment practices to best practices of its national peers;
- Identify best practices in private, nonprofit/foundation financial support and reporting hierarchy to a publicly funded STEM school; and
- Determine the status of the findings and recommendations set forth in the SIG’s 2017 report.

C. Methodology

The SIG conducted a detailed analysis of the Foundation’s financial operations and policies. Fiscal Year 2017 (FY2017) was selected for the analysis since it was the most recent fiscal year in which the Foundation conducted the previously delegated functions for the full year. The detailed financial analysis required a review of additional data beyond that found in the Foundation’s audited financial statements and federal information returns (IRS Form 990). The Foundation provided the SIG with supplemental schedules and worksheets associated with the FY2017 year-end closing of its accounting records, and the Foundation provided answers to a number of the SIG’s questions. The SIG sought additional clarification from SCGSSM staff on the Foundation/SCGSSM annual budget allocation process.

The SIG obtained an independent review of the Foundation’s financial statements from the Office of the State Auditor on the Foundation’s overall financial picture.

The SIG identified “best practices” in foundation management, reporting framework and relationships with a STEM school, along with obtaining information on the endowment practices of the STEM schools studied as benchmarks in the 2017 review – the North Carolina School for Science and Mathematics; the Illinois Mathematics and Science Academy; and the Louisiana School for Math, Science and the Arts.

Reviews by the SIG are conducted in accordance with professional standards set forth by the Association of Inspectors General, often referred to as the “Green Book.”

D. Status of the 2017 Review Findings & Recommendations

Of the seven findings and recommendations set forth in the SIG’s 2017 report, the three most important pertained to the delegation of authority and oversight of specific SCGSSM employees and programs to the Foundation without a formal operating agreement or Memorandum of Understanding (MOU). The MOU ensures SCGSSM priorities remain the central focus of the Foundation’s fundraising efforts and support, and provides transparency into Foundation financial support to the school. Set forth in Table A is the status of these three findings and recommendations issued by the SIG in its 2017 review. The SCGSSM and Foundation have addressed all other findings.

Table A: Status of 2017 Report Findings & Recommendations

<u>2017 Report - Finding #</u>	<u>Brief Description</u>	<u>SIG Recommendation</u>	<u>Current Status</u>
1	Delegation of SCGSSM employees and programs was inappropriate & potential violation of state law.	SCGSSM should resume oversight of staff and programs.	Completed during 2017-18 school year.
2	SCGSSM and Foundation operated without an MOU to ensure fundraising efforts and support aligned with SCGSSM priorities.	SCGSSM and Foundation should adopt a formal MOU.	Incomplete.
4	Lack of transparency of Foundation financial activities in support of SCGSSM.	Foundation should create a process to provide full financial disclosure to SCGSSM.	Pending.

III. Foundation Trial Balance Review & Analysis

A. Foundation’s Net Asset Analysis – General

The SIG reviewed the Foundation’s FY2017 final trial balance of accounts as of 6/30/2017, along with supplemental schedules and worksheets. The Foundation Board chair, business manager, and outside accountant provided detailed financial information and answered supplemental questions posed by the SIG.

The Foundation structured its accounting system and year-end closing processes to segregate its net assets into three categories – unrestricted, temporarily restricted, and permanently restricted - based on the existence or absence of any restrictions placed on the portion of those net assets derived from donors, an accepted accounting practice among nonprofit organizations. At the end of FY2017, the Foundation’s net assets were comprised of the following:

Unrestricted – (deficit)	-	\$ (141,202)
Temporarily Restricted	-	1,989,616
<u>Permanently Restricted</u>	-	<u>10,348,891</u>
Total Net Assets		\$ 12,197,305

Temporarily restricted net assets refer to donated assets subject to restrictions on their use. Permanently restricted net assets refer to donated assets subject to donor-imposed restrictions requiring the principal portions

of their donations be preserved and invested with only the income expended. Investment earnings derived from the investment of restricted assets may or may not be restricted, depending on the donor's intent.

The Foundation took steps to ensure each restricted asset was utilized only for its designated purpose. The majority of the Foundation's FY2017 donations fell into the temporarily restricted category and were received for the support of various SCGSSM programs and activities. In most foundation/institution relationships, the transfer of temporarily restricted funds to the supported institution relieved the restriction, with assurance from the institution the funds were utilized as intended by the donor.

However, when the Foundation assumed oversight of specific SCGSSM programs and staff, many of which were supported by the Foundation's fundraising efforts, the Foundation allocated its own expenses to those functions to relieve these temporary restrictions. The expenses of these delegated functions represented two-thirds of the annual SCGSSM allocation the Foundation claimed as expended for the benefit of SCGSSM.

The permanently restricted amount represented the Foundation's endowment and consisted of the fair value of the donors' original gifts, plus any additions, and any other funds designated by the Foundation Board as endowment funds. The Foundation categorized virtually all of its earnings and appreciation on investments as temporarily restricted funds until they were appropriated.

B. Foundation FY2017 Income

1. Fundraising Proceeds

The majority of the Foundation's fundraising proceeds was derived from business or corporate contributions, with the majority of those contributions restricted to supporting various programs or activities. The Foundation received several permanently restricted contributions, which added to its endowment (\$18,746). The majority of unrestricted contributions were received from parents, alumni, friends, the Business Leadership Network, and income from two special event fundraising initiatives.

2. Administrative Fee Income

During FY2017, the Foundation assessed an administrative fee ("gift tax") of 18.55% on approximately \$870,000 of its contributions, which produced unrestricted income of \$161,360. The SIG determined the Foundation first assessed the fee in FY2013 at 8.55% and increased the fee to 18.55% for FY2016. The SIG determined through research and confirmed with the North Carolina School for Science and Mathematics foundation president that fees assessed on gifts are becoming more common in nonprofits with the increase in online giving with its associated third party processing fees. A recent survey by the Council for Advancement and Support of Education found 38% of its members assessed fees on non-endowed gifts. Of those assessing fees, the median was 5%, the minimum was 1.2% and the maximum was 10%.

3. Investment Income

Investment income was the largest source of income (\$1,177,687) and included dividends, interest, and gains in the value of investments. The Foundation followed accepted accounting principles and adjusted the value of its investments to fair market value at year-end. Changes in value were recorded as either gains or losses, and were further subdivided between realized and unrealized gains. The total gains for FY2017 represented an increase in the value of the investments of approximately 10%, which was a significant turnaround from FY2016 where a loss in value of approximately 4% occurred. The investments also sustained a loss in value in FY2015 amounting to approximately 2%. All but \$811 of investment income was recorded as temporarily restricted income, having resulted from the investment of restricted funds.

4. Other Income

Other income included \$66,475 from the Hartsville Development Foundation contribution, which pertained to the Foundation's Startsville Incubator initiative. The Development Foundation previously operated this business incubator as the Hartsville Innovation Center in downtown Hartsville, South Carolina. In obtaining the Innovation Center, the Foundation acquired a combination of assets and liabilities consisting of cash (\$36,587); prepaid contracts (\$20,500); furniture and equipment (\$32,388); and liabilities for unpaid awards (\$23,000), the net of which was \$66,475. A detailed listing of the Foundation's FY2017 income obtained from its 6/30/2017 final trial balance can be found in Exhibit E of this report.

C. Analysis of the Foundation's Restricted Funds

The Foundation undertook a multi-step process at year-end and updated the amount of its net assets in each category. All restricted assets (temporarily restricted and permanently restricted) were recorded and tracked by fund name, and based on purpose or source. The year-end process included the addition of donations and other income received during the year; the distribution of investment income to each fund; and the application of the Foundation's expenses against each fund, which relieved the restrictions on those net assets arising from restricted donations. The expenses applied to each fund represented both direct payments to SCGSSM and those expenses the Foundation considered expended for the benefit of SCGSSM. Investment income was applied to each fund based on the percentage of the fund's invested value to the total invested value of all funds.

Set forth below in Table B is the Foundation's 2017 net asset activity totals taken from Exhibit A to this report.

Table B: Net Asset Activity – FY2017 (Exhibit A)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Assets</u>
<u>Beginning Balances</u>	\$ (81,505)	\$ 1,435,987	\$ 10,330,147	\$ 11,684,629
Donations and Other Income	870,980	903,600	18,746	1,793,326
Invest. Income & Realized Appreciation	811	373,692	---0---	374,503
Unrealized Appreciation	---0---	803,183	---0---	803,183
Expenses Applied	977,269	1,481,067	---0---	2,458,336
FY2016 Fund Deficiency Correction ¹	<u>45,780</u>	<u>(45,780)</u>	<u>---0---</u>	<u>---0---</u>
<u>FY2017 Ending Fund Balances</u>	\$ (141,202)	\$ 1,989,616	\$ 10,348,891	\$ 12,197,305

The Foundation's total expenses for FY2017 of \$2,458,336 are shown as they were applied to the different funds, including \$977,269 of expenses that were applied against the Foundation's unrestricted funds. The remaining \$1,481,067 of expenses were applied against the temporarily restricted assets based on the Foundation's determination they satisfied the restrictions associated with the funds (net assets). This amount approximates the total Foundation allocation to SCGSSM. (*See Exhibit A*)

1. Unrestricted Net Asset (Deficit)

The \$977,269 of expenses applied against unrestricted funds was partially offset by unrestricted income of \$870,980 received during FY2017 resulting in a deficit of unrestricted funds. The deficit first arose in FY2016 due

¹ A portion of the FY2016 loss caused a deficiency in a portion of the Foundation's temporarily restricted funds, where the ending values were below the required amounts by \$45,780. Note 10 of the "Notes to the Financial Statements" in the Foundation's FY2016 & FY2017 audited financial statements addressed these deficiencies. The \$45,780 deficiency was transferred to unrestricted net assets to report the temporarily restricted funds at their correct value. The investments, which caused the deficiency, recovered their value during FY2017 and the transfer was reversed as shown in Exhibit A's column title, "Prior FY-Net Invest. Loss Recovered."

to the recorded loss in value of the investments during that year, and expanded into FY2017 when expenditures exceeded income in the unrestricted net asset category.

A comparison of the Foundation to sixteen similar nonprofits prepared from IRS Form 990 data (*See Exhibit C*) indicated the comparative group had a much different distribution of unrestricted to restricted net assets. The average distribution percentages for the sixteen nonprofits were 43% unrestricted; 28% temporarily restricted; and 29% permanently restricted. The Foundation's percentages at the end of FY2017 were 1% unrestricted; 16% temporarily restricted; and 85% permanently restricted.

2. Temporarily Restricted Net Asset Value

The Foundation's temporarily restricted net assets increased from \$1,435,987 at the end of FY2016 to \$1,989,616 at the end of FY2017. While this increase was significant, a portion of the increase was related to the unrealized appreciation of investments, which did not represent available funds to the school or the Foundation. Further, some of the fund amounts may have been associated with uncollected pledge balances, which totaled \$436,600 at the end of FY2017.

However, on a fund-by-fund basis, there were significant fund balances that represented available funds. This included, the RESP Fund (Research Experience Scholars Program) fund with an ending balance of \$262,720 (only \$23,388 was expended during FY2017), the SPRI (Student Summer Program for Research Interns) fund where only \$21,492 of the \$76,982 donated was expended; as well as minimal expenditures from the Dr. Bill Scholarship Fund; the Brockman Scholarship Fund; and the Memorial Fund.

3. Startsville Initiative Funds – Redirection of Temporarily Restricted Funds

The Startsville Incubator and its related initiatives – Career Services, GSSM Launch, and Project Verge – represented a significant portion Foundation's fundraising focus during FY2017 and the previous fiscal year. A total of \$304,905 was raised for these undertakings during FY2017, and their ending fund balances totaled \$442,926, with the majority associated with the Career Services undertaking.

The SIG determined during its 2017 review that when the Startsville initiative was proposed in April 2016, concerns were raised it was outside of SCGSSM's strategic plan and not beneficial to the school. This concern was further increased by the Foundation's focus on economic development and assisting startup businesses in Hartsville. Several members of the SCGSSM BoT noted economic development was not specifically in the school's mission. While there was possibly some benefit in assisting alumni and students, the SCGSSM Board of Trustees (BoT) believed resources should meet the current needs of students before the development of a "Launch Fund" to provide financial support to alumni.

The Foundation is ceasing the Startsville Incubator operation. As a result, three donors who provided \$300,000 toward the Career Services initiative gave permission to redirect their donations to other activities. In addition, the Foundation obtained the release of restrictions on the Campbell Fund (\$177,684), and used these funds during FY2018 to reduce the unrestricted net asset deficit.

D. Foundation FY2017 Operating Expenses

The Foundation grouped its expenses as follows in its FY2017 trial balance:

Management and Fundraising Salaries	\$ 458,900
Payroll Taxes and Fringe Benefits (for all salaries)	165,625
Professional Fees (audit, accounting, IT, etc.)	55,995
Operations (supplies, telephone, software maint., etc.)	80,727
Facilities and Equipment (rent, utilities, depreciation)	78,801

Insurance (property, D&O, workers' comp.)	6,707
Investment Management Fees	69,768
Marketing & PR (incl. marketing & recruiting salaries)	562,561
Travel & Professional Development	74,843
Fundraising Events (costs)	112,844
Program Expenses (incl. outreach expenses)	626,662
Startsville/Innovation Center (incl. salaries)	128,585
Career Services Expense (incl. salaries)	<u>36,318</u>
Total FY2017 Expenses	<u>\$ 2,458,336</u>

1. Foundation Salaries – FY2017

The trial balance included separate accounts for each of the Foundation's fourteen salaried employees. A fifteenth position listed in the trial balance for a grant writer received no salary in FY2017. Set forth in Table C is a listing of the job titles by the groupings shown in the trial balance along with the total salaries for each grouping.²

Table C: Foundation Salary Groups by Position

<u>Salary Groups</u>	<u>Employee Positions</u>	<u>Total Group Salaries</u>
Management & Fundraising	CEO/Executive Director; business manager; development manager; alumni relations manager; grant coordinator; development coordinator	\$ 458,900
Marketing & Public Relations	director of marketing; public relations coordinator; director of recruitment; diversity recruiting manager; two recruitment coordinators	\$ 292,986
Startsville Incubator & Career Services	Startsville director (part time); Startsville/Career Services assoc. dir.	\$ 55,373
	Total FY2017 Salaries:	\$ <u>807,259</u>

At the end of FY2018, the Foundation staff consisted of seven employees as follows: director of business operations; director of advancement services; director of corporate & foundation relations; director of research & development; and director of Startsville, along with a development manager; and an associate director of Startsville. Based on FY2017 salaries, the estimated total salary cost for these seven employees was \$314,000, a reduction of approximately \$493,000 from the total FY2017 salary costs.

2. Foundation FY2017 Detailed Expense Analysis

The SIG prepared Exhibit B titled, "*Detailed Analysis of Foundation Expenses as Related to the Allocation to SCGSSM*" from the Foundation's FY2017 ending trial balance and supplemental worksheets. This exhibit illustrates how the Foundation applied each expense item to the categories of support allocated to SCGSSM. Two of the Foundation's year-end worksheets whose purpose was to distribute its expenses to those funds and represented restricted net assets and their associated investment earnings supports this data.³

The Foundation's outside accountant prepared the year-end worksheets to distribute both income and expenses to the various restricted and unrestricted funds. A number of expense items were clearly applicable to certain programs or activities, particularly the direct support items provided to SCGSSM shown under the trial

² The career services position was included in "Management and Fundraising" category in the trial balance and shown here under the Startsville Incubator and Career Services listing.

³ **NOTE:** There is an unresolved difference between Exhibit B and the Foundation worksheets of \$3,112, which was not considered material. Total expenses agree.

balance's Program Expenses category. Others were not as obvious such as marketing, public relations, and recruiting expenses, which were grouped together in the Foundation's trial balance.

The worksheets separated the recruiting expenses from marketing and public relations, and applied approximately 12% of the remaining marketing expenses to the Foundation's two fundraising events, with the remainder of the marketing expenses applied to the allocation for the benefit of SCGSSM - \$299,709 in total. This amount included the salaries and benefits cost of the director of marketing and the public relations coordinator, but none of the CEO salary cost. The worksheets included distributions of employees' salaries, as follows:

- Portions of six employees' salary cost were distributed to specific statewide camps (iTeams and CREATEng), a total distribution of \$66,332.
- Based on a Foundation Board action, \$82,500 of the CEO salary was distributed to several of the delegated functions (admissions, recruitment, and the outreach programs).
- The salary cost of the four recruitment employees were distributed to recruitment along with recruitment travel, postage and printing.
- The salary cost of two employees associated with the Startsville initiative were distributed to that function.

Other distributions included the salary cost of the four recruitment employees along with specific recruitment expenses – printing, postage, and travel – that were distributed to the recruitment item in the allocation to the school. The salary, taxes and benefit costs of the two employees involved with the Startsville Incubator and Career Services were distributed to those functions. In addition, the cost of IT equipment, a portion of the professional fees, a portion of the depreciation, and a portion of travel expenses were also distributed to Startsville and Career Services.

E. SCGSSM / Foundation Annual Allocation Process

The SCGSSM and Foundation have historically conducted an annual process to determine the necessary funding provided to (or for the benefit of) the school by the Foundation. The school and the Foundation jointly developed this budget allocation process and included a list of items grouped into four categories: (1) Student Development, (2) Academics, (3) Outreach, and (4) General. Once the school's request was developed, it was submitted to the SCGSSM BoT and upon approval, to the Foundation Board for approval. Depending on the amounts approved, the process may have involved the resubmission of amended requests for approval. Following approval of the allocation by both boards, SCGSSM budgeted the funds and formally invoiced the Foundation from time to time during the year for the specific direct support items.

In FY2017 and prior years, the items of support fell into two broad categories: (1) direct support to SCGSSM - \$309,945 (22% of the total allocation), and (2) expenditures "for the benefit of" SCGSSM - \$1,115,536 (78% of the total allocation). Direct support to SCGSSM typically originated from funds raised by the Foundation for specific SCGSSM needs that were tied to the Foundation's restricted funds, along with other direct support items paid from Foundation unrestricted funds.

The Foundation's final FY2017 allocation report, as summarized in Table D, was prepared prior to the final closing of the Foundation's records and does not agree with the outside accountant's final worksheets as illustrated in Exhibit B to this report.

Table D: 2017 Foundation Allocation & Support to SCGSSM Programs

<u>Direct Support to SCGSSM:</u>		<u>Allocation</u>	<u>Totals</u>	<u>%</u>
	Student Development	\$ 19,173		
	Academics	\$ 113,257		
	Outreach	\$ 87,581		
	General	<u>\$ 89,934</u>	\$ 309,945	22%
<u>Expenditures “for the benefit of SCGSSM”:</u>				
	Outreach (incl. CEO personnel cost distribution)	\$ 364,491		
	Marketing	\$ 263,509		
	Recruitment (including CEO cost distribution)	\$ 322,132		
	Startsville/Verge	\$ 128,966		
	Career Services/SCGSSM Launch	<u>\$ 36,438</u>	<u>\$1,115,536</u>	<u>78%</u>
Total Allocation			<u>\$1,425,481</u>	<u>100%</u>

F. Impact to SCGSSM & Foundation – Delegated Functions

The Foundation ended FY2016 with a deficit of \$81,505 in its unrestricted funds, which increased to \$141,202 at the end of FY2017. The Foundation Board advised SCGSSM the 2017 end of year deficit limited the Foundation’s ability to provide any significant funding to SCGSSM for FY2018. Additionally, a reduction in fundraising efforts occurred while the Foundation Board searched for a new CEO also limited the Foundation’s ability to provide funding.

At least 40%, or approximately \$980,000 of the Foundation’s total expenses, were associated with the delegated functions per the Foundation’s expense distribution to those programs. During FY2018, SCGSSM assumed all of the functions previously delegated to the Foundation, and staffed those functions through hiring additional personnel as well as requiring existing personnel to assume added duties. The SCGSSM requested funding from the Foundation during FY2018 to offset the operating cost of those functions in the absence of state funding. However, the Foundation advised it was unable to assist SCGSSM. This created a hardship for SCGSSM in the absence of any state funding. Consequently, SCGSSM utilized its reserve funds totaling \$575,000 to carry out the functions.

A breakdown of SCGSSM’s budget to assume the delegated functions included \$265,000 for recruitment and admissions; \$55,000 for staffing outreach and \$113,000 for low-income student scholarships for outreach; \$40,000 for marketing print materials; \$50,000 for website design and implementation; and \$53,000 for various staffing changes and other expenses. The school received no financial support from the Foundation during FY2018 for the programs and functions transferred back to SCGSSM.

The SCGSSM adopted a professional recruitment management strategy and hired an experienced professional as director of admissions. The individual had previously served 18 years as a counselor and director of admissions for the North Carolina School for Science and Mathematics. In addition, SCGSSM added two recruiters and budgeted for recruitment travel and additional administrative support. The SCGSSM historically budgeted for two admissions staff previously supervised by the former Foundation CEO. Supervision of these publicly funded employees was transferred back to the new director of admissions.

In April 2018, the Foundation Board approved a direct allocation to SCGSSM of \$173,000, which was approximately one-half of the direct allocation provided in FY2017. None of this amount was to fund the formerly delegated functions. The state’s General Assembly approved a supplemental budget request totaling \$400,000 to fund these SCGSSM functions for FY2019.

G. Comparison of the Foundation's Endowment Practices

To evaluate the Foundation's endowment practices, the SIG reviewed recent IRS Form 990 reports on sixteen nonprofits as shown on Exhibit D. The sixteen consisted of the North Carolina School for Science and Mathematics (NCSSM); Illinois Mathematics and Science Academy (IMSA); Louisiana School for Math, Science and the Arts (LSMSA); and thirteen South Carolina nonprofits with endowments of a similar size to that of the Foundation. IRS Form 990, Schedule D, Part V provides a schedule of endowment activity and related information covering a five-year period. The SIG compared the Foundation's IRS Form 990 endowment information to the other sixteen nonprofits for this analysis. In addition, the SIG obtained the spending and administrative fee policies of the three STEM schools. (*See Exhibit D*)

Based on the Foundation's Form 990 information, the Foundation's endowment has not grown in recent years. In fact, the endowment was slightly less than it was five years ago. The SIG determined during its 2017 review the endowment doubled in size during FYs 2011 and 2012; however, only \$349,000 was added to the endowment over the past five years. Based on fundraising results, it appeared most of the Foundation's fundraising focus was directed toward raising funds to support current activities and programs. That differed significantly from the other sixteen nonprofits whose average endowment growth was 66% during the five-year period. The supporting foundations of the three STEM schools grew 81% (North Carolina), 94% (Illinois) and 55% (Louisiana), respectively.

The Foundation's investment earnings and appreciation generated by its endowment totaled \$2,728,983, and its distributions from the endowment totaled \$3,157,942. The Foundation's endowment spending policy is 5% of the fund's average fair market value over the previous 36 months. The policy has a floor of 3% and a ceiling of 5%, and is subject to Board approval each year. The Foundation appropriated 5% for FY2017 and it appeared to have also done so in each of the past five years. The 5% spending policy based on a 36-month rolling average of an endowment's value is typical of most nonprofits, per Internet research. The Foundation did not assess an administrative fee to manage its endowment; and there appeared to be no consistency among nonprofits on assessing administrative fees to manage an endowment.

The NCSSM foundation's spending policy is similar to the Foundation's and based on a 36-month rolling average with a ceiling of 6%. The NCSSM foundation board also approves the amount to be withdrawn annually and approved 5% for the current fiscal year. The NCSSM foundation president noted their board was considering lowering the spending percentage, which appeared from Internet research to be a trend for many nonprofits in managing endowments. This reevaluation was caused by volatile market conditions and a desire to assure the endowment sustains its inflation-adjusted value going forward.

The Foundation's investment earnings appeared to be on par with the other sixteen nonprofits during the five-year period, and most of the nonprofits in the SIG's Exhibit D comparison incurred investment losses during FY2016, as did the Foundation.

IV. Best Practices in Foundation Support and CEO Reporting

A. Foundation Support & Dual Reporting Framework

As noted in the SIG's 2017 review, SCGSSM delegated specific programs and staff to the Foundation over a period of years, to include the supervision of these programs and staff by the Foundation's CEO, who held the additional title of Executive Vice President for Strategic Direction of SCGSSM. In this role, the Foundation's CEO reported to the SCGSSM president for the operation of the delegated programs and staff, but also reported to the Foundation Board for other Foundation activities.

This dual reporting structure for the Foundation was somewhat similar to the organizational hierarchy and framework in existence at two other STEM schools the SIG surveyed – the NCSSM and IMSA. In those institutions, each foundation chief executive held a leadership position at the STEM school as a state employee, reported directly to each school’s senior executive, and jointly reported to the respective foundation board for foundation activities. This was to ensure foundation fundraising goals and priorities directly supported each school’s strategic goals and priorities.

The difference between the former SCGSSM/Foundation reporting framework and the NCSSM and ISMA frameworks is the SCGSSM/Foundation framework had no governing document or law to ensure the relationship; roles and authorities of the school and the Foundation survived any change in leadership or board composition.

B. NCSSM / NCSSM Foundation Framework and Relationship

The reporting framework and hierarchy relationship between the NCSSM and its foundation was codified in North Carolina state law §116-231, which established the NCSSM as a constituent high school of the University of North Carolina (UNC). (*See Appendix C*) As such, the UNC Policy Manual became the definitive authority on the NCSSM and its foundation’s relationship and requirements. It should be noted the relationship and reporting structure between the NCSSM and its foundation was similar to the SCGSSM/Foundation prior to the North Carolina legislature enacting this law and placing the NCSSM under the UNC system.

Specifically, UNC policy 600.2.5.2(R) sets forth the required elements of a university/associated entity relationship. For definition purposes, the NCSSM is known as a constituent institution, institutional unit, or approving institution; while the NCSSM foundation is known as an “associated entity” within the UNC policy manual (*See Appendix D*)

The SIG and the NCSSM foundation president discussed in great length the attributes and success of the NCSSM and its relationship with the NCSSM foundation. The following are the key points identified:

- Relationship and reporting structure is created in state law through the UNC system
- Foundation president jointly reports to NCSSM chancellor and separately to the foundation board
- Foundation president is part of NCSSM executive leadership team
- Foundation president and NCSSM leadership jointly prepare fundraising goals to support the school’s priorities and strategic plan
- Foundation employees are state employees

A closer review of UNC policy manual, section 600.2.5.2(R) (*“Required Elements of University – Associated Entity Relationship”*) sets forth detailed components to ensure the effectiveness of this relationship. (*See Appendix D*) The key points of this policy are:

- Associated entities (i.e., foundations) engage in activities that are critical to and aligned with the mission, goal and objectives of the constituent institution
- Associated entities become affiliated with a constituent institution by written approval from the constituent institution
- Associated entities are subject to the direction of its own governing body and provide funding and support to the approving institution
- Associated entities are permitted to represent they are affiliated with the constituent institution, in accordance with the regulation and written approval with the approving institution
- The authority and responsibility for establishing and maintaining cooperative and mutually beneficial relationships between the two entities rests with the approving institution

- Approving institution maintains oversight and control over its name, marks, resources, and activities that could impact accreditation standards and compliance responsibilities
- Funds raised by the associated entity are to be used to support the approving institution consistent with the donor intent and law
- Regulations set forth standards of governance and operations of associated entities in their support of and interaction with their approving institutions, create pathways of communication to ensure the constituent institution is informed about the activities of its associated entity so that those activities remain aligned with the mission, goals and objectives of the approving institution.

C. SIG 2017 Report – Best Practices Reaffirmed

The best practices identified in the 2017 report are reaffirmed for this review. The most current and comprehensive report addressing best practices among institutions and affiliated nonprofit support organizations is the University of Texas system’s report titled, “*Advisory Task Force Report on Best Practices Regarding University-Affiliated Foundation Relationships*.”⁴ The three key areas identified as best practices were:

- Mission alignment through the development of an MOU;
- Increase transparency and openness between the institution and the foundation; and
- Good governance and executive board leadership.

These best practices are supported by the accreditation standards utilized by the Southern Association of Colleges and Schools (“SAC”) Commission on Colleges, “*Principles of Accreditation: Foundation for Quality Enhancement, Section 3.2.12 and 3.2.13*.”⁵

V. Summary and Way Forward

The Foundation and its outside accountant, maintained extensive documentation on the Foundation’s income, expenditures, endowment assets, and allocations to the SCGSSM, as would be expected of a \$12 million nonprofit foundation with the mission of supporting a school of SCGSSM’s caliber. While fundraising was strong during FY2017 and early FY2018, the Foundation’s mission and focus had drifted away from the priorities of the school.

Most apparent was the Foundation’s expenses exceeded its unrestricted income. Through this financial analysis, the Foundation appeared financially stretched to sustain its overall level of operation and staffing, particularly carrying out the previously delegated functions. The fact the unrestricted income was overspent, and the endowment had not grown but in fact, had declined in the last five years, was an indication spending may have been at an unsustainable level. Perhaps the cost of conducting the delegated functions was too high resulting in the Foundation utilizing resources better intended for SCGSSM’s direct benefit.

The bottom line was only 22% (\$309,945) of the Foundation’s total allocation and support (\$1,425,481) to SCGSSM was direct support. The balance was an allocation “for the benefit” of the school, usually in form of expenses associated with the delegated functions, to include staff salary apportionment. When the SCGSSM resumed oversight of the previously delegated programs in FY 2017-18, the Foundation’s staffing size was unsustainable and resulted in a reduction in staff during the second half of FY 2017-18.

⁴ University of Texas System’s “*Advisory Task Force Report on Best Practices Regarding University-Affiliated Foundation Relationships*.” (see link [Best Practices Regarding University-Affiliated Foundation Relationships](#))

⁵ Southern Association of Colleges and Schools Commission on Colleges “Principles of Accreditation: Foundation for Quality Enhancement” standard 3.2.12. (see link: <http://www.sacscoc.org/pdf/2012PrinciplesOfAcreditation.pdf>)

Virtually all control and oversight of those functions was lost following the change in SCGSSM leadership and the deterioration of the relationship between the new president and the Foundation's former CEO. The resulting lack of communication and transparency stymied efforts on the part of SCGSSM to determine the cost of carrying out those functions. It was not possible to judge the cost/value of the services provided by the Foundation in conducting those functions, or to determine appropriate budget amounts to re-assume them.

When the school was informed the Foundation could not provide financial support for its priorities for FY 2017-18, the SCGSSM utilized \$575,000 of its reserve funds to operate these programs. In April 2018, the Foundation provided \$173,000 in direct allocation to the school. In addition, the state General Assembly provided \$400,000 in supplemental funding to the school for FY 2018-19 for these programs.

SIG Recommendations

The SCGSSM and Foundation were on the right trajectory in developing this same framework and reporting hierarchy when the former Foundation CEO reported to the SCGSSM president, held an executive leadership team position at the school, and developed fundraising goals to support SCGSSM priorities. Unfortunately, this dual reporting structure was not formally adopted, either by MOU or state law, and collapsed when a change in school leadership occurred in April 2016.

The success of the NCSSM / NCSSM Foundation relationship can be traced to North Carolina state law, which established the NCSSM as a constituent institution within the UNC system. The UNC policies and regulations established the authorities of the NCSSM and the reporting hierarchy of the NCSSM foundation as an affiliated entity to the school. Equally important to the success of this relationship is the NCSSM Foundation president reports to the NCSSM chancellor on fundraising matters in support of the NCSSM priorities and strategic plan. *(See Appendix C & D)*

The best practices identified in the 2017 review for the three STEM schools recognized as national leaders in secondary STEM education – NCSSM, IMSA, and LSMSA – each utilized an MOU with their respective foundations. All three foundation presidents were directly involved with each school's leadership in determining fundraising goals centered on each school's priorities and strategic plan. *(See Appendix A)*

The decision to adopt a formal structure of authorities, roles, responsibilities, and accountability for the SCGSSM, the Foundation, and the Foundation CEO is not in dispute. The best practices identified in this review provide two avenues to achieve this goal: (1) agree upon a Memorandum of Understanding; or (2) introduce legislation, which defines the structure for the school and Foundation relationship and reporting hierarchy of the Foundation CEO.

It is the SIG's recommendation an MOU be adopted by each board for the SCGSSM and Foundation which recognizes the authorities, roles, responsibilities, and accountability of the SCGSSM, Foundation, and the Foundation CEO; as well as, reestablish a dual reporting role for the Foundation CEO to the SCGSSM president and the Foundation Board. It is also the SIG's recommendation that the General Assembly consider legislation, similar to the North Carolina law, which defines the structure of the SCGSSM and Foundation and reporting hierarchy of the Foundation CEO.

VI. Findings and Recommendations

Finding #1: This is a recurring finding from the SIG’s 2017 report (Finding #2). The SCGSSM and Foundation have continued to operate without an operating agreement or memorandum of understanding (MOU), which delineates the roles, responsibilities, authorities, and alignment of each organization’s mission.

Recommendation #1a: Based on the best practices identified in this report, and the previous dual reporting structure of the former Foundation CEO to the SCGSSM president, the respective boards for the SCGSSM and Foundation should complete the adoption of an MOU which recognizes the authorities, roles, responsibilities, and accountability of the SCGSSM, Foundation, and the Foundation CEO; and should include the reestablishment of a dual reporting role for the Foundation CEO to the SCGSSM president and the Foundation Board.

Recommendation #1b: It is recommended that the South Carolina General Assembly consider the introduction of legislation that defines the SCGSSM / Foundation relationship, authorities, roles, accountability, and dual reporting of the Foundation CEO to the SCGSSM president to ensure Foundation priorities and fundraising efforts are aligned with and supportive of SCGSSM priorities and strategic plan.

Finding #2: This a recurring finding from the SIG’s 2017 report (Finding #4). The Foundation has not finalized an affirmative process of providing basic financial information to SCGSSM, including audited financial statements, annual IRS information returns, and final yearly expenditures of those programs and activities managed by the Foundation. As set forth in this report, the Foundation maintained sufficient detail of its financial allocations and operational costs, which would have assisted the SCGSSM in budgeting for the realignment of the previously delegated programs and functions during FY2017-18.

Recommendation #2: The Foundation should affirmatively provide full financial disclosure to the school on Foundation activities, consistent with any need to protect donor privacy. Requests from SCGSSM for supplemental information should be responded to promptly and in the spirit of sharing between affiliated, and collaborative entities working toward a common purpose.

Administrative: SCGSSM’s response to the report located at Internet link:

https://oig.sc.gov/sites/default/files/Documents/Reports/2018/SCGSSM_Response_to_Report.pdf

Foundation’s response to the report located at Internet link:

https://oig.sc.gov/sites/default/files/Documents/Reports/2018/Foundation_Response.pdf

List of Appendices

Appendix A: SIG 2017 review titled, “*Review of the South Carolina Governor’s School for Science and Mathematics and the Organizational Relationship to its Supporting Foundation*”

Appendix B: SC Attorney General’s Opinion, dated 8/22/2017

Appendix C: North Carolina General Statute §116-231 et seq. (Article 29) titled, “*Reestablishment of the North Carolina School of Science and Mathematics as a Constituent High School of the University of North Carolina*”

Appendix D: University of North Carolina Policy Manual, Section 600.2.5.2 (R) titled, “*Required Elements of University-Associated Entity Relationship*”

[Link to Appendices A - D](#)

List of Exhibits

Exhibit A: “Summary of Net Asset Activity from GSSMF’s Spreadsheets for Fiscal Year 2017”

Exhibit B: “Detailed Analysis of Foundation Expenses as Related to the Allocation to GSSM for Fiscal Year 2017”

Exhibit C: “Foundations Comparative Data from IRS Form 990 of Net Assets for Fiscal Year Ending 6/30/2017”

Exhibit D: “Foundations Comparative Data from IRS Form 990 of Endowment Activity for Fiscal Year Ending 6/30/2017”

Exhibit E: “Listing of Income Items for Fiscal Year 2017”

[Link to Exhibits A - E](#)