



SPECIAL INVESTIGATION REPORT OF FINDINGS

**PERTAINING TO:
ECTOR COUNTY ISD (INV2024-05-260)
MIDLAND ISD (INV2024-05-261)
AUSTIN ISD (INV2024-05-262)**

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I. Executive Summary

On May 14, 2024, The Texas Education Agency (TEA or agency) became aware of statements contained in a media report that alleged state funds were being inappropriately diverted from public school students in Texas via partnerships between three Texas school districts and a nonprofit school operator named Third Future Schools – Texas. These three school districts are Austin ISD, Ector County ISD, and Midland ISD and shall be referred to throughout this report by name or as the “Partnering Districts.” The terms of these partnerships were memorialized in contracts or “partnership agreements” between the Partnering Districts and Third Future Schools – Texas. In these partnership agreements, the Partnering Districts agreed to provide funding to Third Future Schools – Texas in exchange for the nonprofit operating a specific district campus in each Partnering District as a Subchapter C charter school.

After becoming aware of the allegations contained in the media report, the Commissioner of Education, via his designee the Associate Commissioner of Compliance and Investigations,¹ issued a special investigation notice to each Partnering District.^{2 3 4} TEA’s Special Investigations Unit (SIU) initiated a special investigation (SI) immediately thereafter. The investigation process and evidence gathered are described in the Investigation Methodology section of this Report.

After analyzing the evidence gathered during the SI (including interviews, financial records, and associated documentation received from Midland ISD, Ector County ISD, Austin ISD and Third Future Schools – Texas), TEA concludes that the Partnering Districts and their operating partner, Third Future Schools – Texas, have not violated any applicable Texas laws. Based on the evidence obtained and analyzed during the investigation, there is no merit to the allegations

¹ Exhibit 1 – Designation of Authority Letter

² Exhibit 2 – Ector County ISD Notice of Special Investigation #INV2024-05-260

³ Exhibit 3 – Midland ISD Notice of Special Investigation #INV2024-05-261

⁴ Exhibit 4 – Austin ISD Notice of Special Investigation #INV2024-05-262

contained in the media reports that state funds were being inappropriately diverted from public school students in Texas via partnerships between the Partnering Districts and Third Future Schools – Texas. This concludes TEA’s investigation. The complaints are hereby closed and no further action will be taken by TEA at this time.

II. Background Information

A. Origin of Complaint

On May 14, 2024, Spectrum News aired a video segment entitled, “Disappearing Dollars: Texas public schools are missing millions” with an accompanying print piece on their website.⁵ The article stated that its reporter identified “millions of Texas public school tax dollars being diverted out of state” arising from partnerships between the Partnering Districts and Third Future Schools – Texas for Third Future Schools – Texas to operate underperforming district campuses. As support, the article references snapshots of public audits, the address listed on checks issued by Ector County ISD to Third Future Schools – Texas, quotations from meetings of the board of directors of an affiliated Colorado nonprofit named Third Future Schools (TFS), and other statements made by representatives of TFS. TEA processed the allegations in the report through the agency’s complaint intake process, and the agency subsequently received additional complaints from a Texas legislator⁶ and other individuals based on the allegations in the Spectrum News report, which were also processed and added to the complaint file for review.

On July 16, 2024, the Texas Observer published an article entitled, “Mike Miles Moved Texas School Funds to Colorado Through a Possible Shell Corporation Without a Paper Trail.”⁷ This article implies that *all* funds transferred by the Partnering Districts to Third Future Schools –

⁵ Exhibit 5 – Spectrum News Article

⁶ Exhibit 6 – Representative’s Letter

⁷ Exhibit 7 – Texas Observer Article

Texas, a total described in the article as being “at least \$49 million in Texas public school funds,” may have been inappropriately transferred out of state. Additionally, beyond the transfer of funds, the article alleges that Third Future Schools – Texas might be a “shell corporation,” existing only to move funds to TFS, the affiliated Colorado nonprofit. As with the allegations in the Spectrum News report, TEA processed the allegations in this article through the agency’s complaint intake process and incorporated the new allegations into the SI.

B. Specific Allegations

The assertions referenced in these media reports, as well as individually directed complaints that the agency received in the time after publication of these media reports on the same subject, covered a broad number of topics that, for purposes of this Report, have been categorized into four categories tied to specific legal standards. Because many of the statements in the articles referenced did not explicitly state a legal violation, instead making broad inferences, SIU has included references to the complaint sources to ensure that this report is comprehensive and includes all possible allegations that may be drawn from these publications.

1. Allegation Category One

The first general category of allegations asserts that, while operating in partnership with the Partnering Districts, Third Future Schools – Texas violated Texas law by misusing state funds. The statutory provision implicated in this allegation is Tex. Educ. Code § 12.107, which requires that state funds be held in trust for the students of the charter school and that state funds cannot be used to support unrelated operations or activities. Within this category, the specific allegations analyzed by the SIU include:

- The Spectrum News article quoted a recording in which it alleged “a TFS official confirmed Colorado charter school deficits were being offset, in part, by money coming from their charter schools in Texas.”

- The Spectrum News article referenced two checks and asserted that they were Texas public school funds sent to a Colorado charter school.
- The Texas Observer article referenced the Spectrum News article and stated that the article raised questions about the transfer of “at least 49 million in Texas public school funds to the Colorado nonprofit.”

2. Allegation Category Two

The second general category of allegations asserts that, while operating in partnership with the Partnership Districts, Third Future Schools – Texas failed to disclose financial information required by Tex. Educ. Code § 12.111(a)(15). Specifically, it is alleged that the transactions and relationship between Third Future Schools – Texas and TFS should have been disclosed to the Agency and Partnering Districts prior to forming the partnership. Within this category, the specific allegations analyzed by the SIU include:

- The Texas Observer article stated, “experts told the Observer that disclosure of pre-existing business deals for administrative expenses are generally required under state law and rules applied to Texas charter schools.”
- The Texas Observer article stated, “While charter schools are allowed to enter into contracts with charter management organizations out of state for professional services, they still have to comply with financial accountability laws that require them to record and disclose to the state each financial transaction with any external organization. “

3. Allegation Category Three

The third general category of allegations asserts that Partnering Districts failed to ensure that Third Future Schools – Texas maintained the state funds received from Partnering Districts in a depository account, as defined and required by Tex. Educ. Code § 12.107. Within this category, the specific allegation analyzed by the SIU is as follows:

- The Texas Observer article stated that “a bank depository certificate obtained by the Observer shows that Third Future Schools-Texas didn’t open a bank account until March 2021,” indicating that the school was operating without a bank account for funds.

4. Allegation Category Four

The fourth general category of allegations asserts that, while serving as an operating partner with Partnering Districts, Third Future Schools – Texas and the board of Third Future Schools – Texas failed to oversee the nonprofit’s finances as required by state and federal law. Within this category, the specific allegations analyzed by the SIU include:

- The Texas Observer stated, “It was another board, the Third Future Schools’ corporate board, that authorized three Colorado-based administrative leaders, including Miles, to be the signatories for Third Future Schools-Texas bank account.”

C. Applicable Legal Standards

1. Legal Authority for TEA Investigations

Texas law grants the Commissioner of Education the authority to authorize special investigations into alleged violations of the Texas Education Code, as set forth Tex. Educ. Code § 39.003. These investigations are governed by procedures adopted by the agency under Tex. Educ. Code § 39.004, which can be found on the agency’s website.⁸ Except as subject to exceptions identified in the Texas Education Code, investigations into conduct relating to other state and federal laws may be reserved to other agencies; where allegations involved in this investigation relate to any such laws, this report notes these limitations.

2. Legal Authority for School Operator Partnerships

The partnership between the Partnering Districts and Third Future Schools – Texas is governed by multiple statutes. In 1995, the Texas Legislature developed a legal framework that allowed for the establishment of charter schools. This framework created multiple types of charter schools, each governed today by separate subsections of Chapter 12 of the Texas Education Code.

⁸ Exhibit 8 – TEA SIU Procedures

Additional types of charter schools have been added to that chapter via distinct subchapters over the years.

The most common type of charter schools are open-enrollment charter schools, established via Subchapter D of Chapter 12 of the Texas Education Code, which are “authorized” – or granted a charter and allowed to operate – by the Commissioner of Education. A charter school authorized by the Commissioner of Education under Subchapter D is subject to the requirements of that Subchapter.

Subchapter C of Chapter 12, however, provides school districts (as opposed to the Commissioner of Education) the ability to authorize a charter for one or more of the district’s own campuses. To operate a charter authorized under Subchapter C, the school district may enter into a school operator partnership with an eligible entity, as defined by Tex. Educ. Code § 12.101(a). The campuses operated by Third Future Schools – Texas via the school operator partnerships with the Partnering Districts are all Subchapter C charter schools. Thus, Subchapter C of Chapter 12 of the Texas Education Code is the primary applicable governing statute for the operation of these campuses.

In 2017, the Texas Legislature passed Senate Bill (SB) 1882, creating Tex. Educ. Code § 11.174, which, in relevant part to this investigation, gives school districts an alternative to state intervention if they use a school operator partnership under Subchapter C of Chapter 12 to address underperforming campuses in their district.⁹ This law requires the school district to grant specific authorities to an operating partner, including full autonomy over campus operations and the campus budget. In return, the district receives additional time for the operating partner to turnaround the campus before state intervention would be invoked. Among other statutory benefits

⁹ Exhibit 9 – SB 1882 - Bill Text

of these partnerships under SB 1882, the district receives an additional state funding entitlement, subject to the provisions of Tex. Educ. Code § 48.252, for the partnership campus.¹⁰ The operating partner must be authorized by the school district as a Subchapter C charter holder to operate a Subchapter C charter school within the district. These Subchapter C charter schools are governed by other state laws *only* as such laws have explicitly been made applicable in statute.¹¹ Additionally, administrative rules provide supplemental guidance and requirements for the approval of the benefits granted in Tex. Educ. Code § 11.174.¹²

In addition, Tex. Educ. Code § 11.174 sets forth requirements for all such school operator partnerships. Specifically, the statute and its associated rules require that any school district entering into a school operator partnership enter into a contract with the operating partner that outlines the terms and conditions under which the operator runs the schools, including the funding structure for any payments to be made by the district to the operator.

Under Texas law, TEA does not have direct authority over those contracts or the terms contained therein, as they are entered into between a school district and its chosen third-party operator. However, TEA does review the contracts to ensure they meet the mandatory legal requirements specified in Tex. Educ. Code § 11.174 and 19 Tex. Admin. Code § 97.1075-1079 in order for the agency to confer the statutory benefits that come along with entering into such a partnership.¹³ Furthermore, while TEA has authority to issue sanctions against a district campus operated by an entity granted a charter under Subchapter C by a school district, TEA lacks authority to issue sanctions against the entity operating the campus. Instead, under the Texas Education Code generally, and Tex. Educ. Code, Chapters 39 and 39A, in particular, TEA has

¹⁰ See Tex. Educ. Code § 48.252.

¹¹ See Tex. Educ. Code § 12.055.

¹² See 19 Tex. Admin. Code § 97.1075-1079.

¹³ See 19 Tex. Admin. Code § 97.1075.

general regulatory authority over the school district that granted the Subchapter C charter, which in turn has authority under Subchapter C over the operator of the campus, to ensure that both the school district and the operator follow Texas law. For this reason, TEA’s investigation notices were issued to the Partnering Districts, not to Third Future Schools – Texas.

The allegations that form the basis of the SI appear to mistakenly attempt to impose legal requirements that apply to open-enrollment charter schools under Subchapter D of Chapter 12 of the Tex. Educ. Code—and specifically Subchapter D requirements for how open-enrollment charter schools spend specific state funding—to the Subchapter C charter school operated under the authority of local school districts. With regard to the use of state funding, different laws apply to Subchapter C and Subchapter D schools. Subchapter D schools receive most state funds through a state funding allocation established in Tex. Educ. Code § 12.106 where funds are paid directly from TEA to the Subchapter D charter holder, whereas Subchapter C charter schools receive funding from a school district via their partnership arrangement and do not receive funding directly from the state. Thus, the use of funds provided by a partnering district to a Subchapter C charter school are governed by the contractual arrangement between the partnering district and operating partner, and are not subject to the financial requirements of Subchapter D.

III. Investigation Methodology

In accordance with division procedures, TEA’s Special Investigation Unit (SIU) initiated an investigation into the processed complaints after a Notice of Special Investigation was sent to the Partnering Districts. SIU investigators reviewed the documentation submitted with the complaints and determined that additional information was needed. Investigators submitted three sets of requests for production of documents to Midland ISD and Ector County ISD, two sets of requests for production of documents to Austin ISD. TFS and Third Future Schools – Texas also

provided a response to requests for documents, as well as follow-up requests for documents and clarification, in order to provide SIU with information necessary to conduct the investigation. The documents that SIU obtained and analyzed during the investigation include, but were not limited to, records outlining district authorization processes, partnership agreements between the Partnering Districts and Third Future Schools – Texas, bylaws and board policies for TFS and Third Future Schools – Texas, board meeting minutes, and school district actions to ensure compliance with the agreements. The records that SIU reviewed to verify financial structures and transactions include, but are not limited to campus budgets, financial audits for the Partnering Districts, Third Future Schools – Texas, and TFS, bank statements and signatory records from Third Future Schools – Texas, samplings of accounting ledgers and journal entries that provided justifications for transfers and payments from the bank accounts of Third Future Schools – Texas, information related to deposits to the Third Future Schools – Texas accounts, ledger entries showing detailed payments to shared services, such as health insurance providers, and federal grant funding information provided by the United States Department of Education. SIU investigators also conducted interviews with individuals at the Partnering Districts, TFS, and Third Future Schools – Texas, including administrators knowledgeable about the financial affairs of the district and partner, board members, and employees. SIU also consulted with internal TEA divisions with expertise relevant to the investigation, including but not limited to the TEA divisions of Charter School Authorizing, Financial Compliance, and Grant Compliance and Administration.

IV. Analysis

A. Allegation Category One

1. Findings of Fact

The first general category of allegations asserts that, while operating in partnership with the Partnering Districts, Third Future Schools – Texas violated Texas law by misusing state funds. The statutory provision implicated in this allegation is Tex. Educ. Code § 12.107, which requires that state funds be held in trust for the students of the charter school and that state funds cannot be used to support unrelated operations or activities. Specifically, it is alleged that Third Future Schools – Texas, during its partnership with the Partnering Districts, improperly sent state funds intended for the students enrolled at the campuses in the Partnering Districts to its out-of-state affiliate, TFS. The agency finds that this allegation is not substantiated by evidence and that no associated legal violations were committed by the Partnering Districts or Third Future Schools – Texas.

TFS is a Colorado nonprofit entity that currently operates 11 charter schools across three states. TFS refers to its operations in each state as a “program” and collectively as the “TFS Network Programs.” TFS has two boards of trustees.¹⁴ The primary TFS board is established as the controlling board in the organizational bylaws. The bylaws require the establishment of a subsidiary advisory board to focus specifically on the Colorado program. Both boards of trustees are organized within the same nonprofit entity, and they share tax-exempt status under § 501(c)(3) of the Internal Revenue Code.¹⁵

¹⁴ Exhibit 10 – Third Future Schools Bylaws

¹⁵ Exhibit 11 – Third Future Schools IRS Letter

Third Future Schools – Texas is a separate nonprofit entity that was established in Texas.¹⁶ The organizational bylaws of Third Future Schools – Texas designate TFS as the sole member of Third Future Schools – Texas.¹⁷ As a distinct organization, Third Future Schools – Texas has a separate board and there is no crossover voting membership between the boards of TFS and Third Future Schools – Texas.

Third Future Schools – Texas has entered into partnerships with several Texas school districts to operate campuses as provided by Tex. Educ. Code § 11.174 and Subchapter C of Chapter 12 of the Texas Education Code, including Austin ISD¹⁸, Ector County ISD¹⁹, and Midland ISD²⁰. Third Future Schools – Texas entered into its first partnership on March 25, 2020, with Midland ISD to operate a Midland ISD elementary school as a Subchapter C charter school for the 2020-2021 school year.²¹

The Third Future Schools – Texas board oversees the school operator partnerships within Texas, Third Future Schools – Texas employs the campus staff at the partnership campuses, and Third Future Schools – Texas has an agreement with TFS to pay TFS for providing the centralized support and administrative services necessary for the operation of the partnership campuses. These supports include, but are not limited to, payroll, accounting, human resources, centralized leadership services, and professional development.

Third Future Schools – Texas maintains its own bank account and has always maintained bank accounts separate from TFS.²² The investigation compared transfers of funds from the Partnering Districts to Third Future Schools – Texas, and the documents reviewed indicate

¹⁶ Exhibit 12 – Third Future Schools – Texas IRS Letter

¹⁷ Exhibit 13 – Third Future Schools – Texas Bylaws

¹⁸ Exhibit 14 – Third Future Schools – Texas Operating Partner Agreement (Austin ISD)

¹⁹ Exhibit 15 – Third Future Schools – Texas Operating Partner Agreement (Ector County ISD)

²⁰ Exhibit 16 – Third Future Schools – Texas Operating Partner Agreement (Midland ISD)

²¹ See Exhibit 16 – Third Future Schools – Texas Operating Partner Agreement (Midland ISD)

²² Exhibit 17 – Third Future Schools – Texas Depository Certificate (2020)

matching deposits in the Third Future Schools – Texas bank accounts. The investigation confirmed that the Partnering Districts did not deposit money into TFS’ bank account.

The allegations in this category focus on the transfer of funds in and out of Third Future Schools – Texas’ bank accounts. The Spectrum News report specifically highlighted that the Colorado address to which the checks from Ector County ISD, as payor, to Third Future Schools – Texas, as payee, were addressed was the address of TFS’ central office. However, the investigation determined that the checks were sent to TFS’ Colorado address because TFS provides accounting services for Third Future School – Texas, a service that includes depositing Third Future Schools – Texas’ checks. The investigation verified the process for check deposits into the Third Future Schools – Texas bank account and confirmed that the Third Future Schools – Texas deposit records matched the payments sent to it by the Partnering Districts. ²³ No evidence gathered during the investigation indicates that any funds from the Partnering Districts were deposited into the bank accounts of TFS, other TFS Network Programs, or any other entity.

Separately, some funds were sent from the Partnering Districts to the bank account of Third Future Schools – Texas via direct deposit. Examples of such transactions include, but are not limited to, monthly payments outlined in the partnership agreement and reimbursement of allowable costs incurred related to various state and federal grant awards. The investigation verified that such direct deposits were deposited directly into the Third Future Schools – Texas bank account and did not flow through a TFS account.

As described above, Third Future Schools – Texas receives many services from TFS. In exchange for these services, Third Future Schools – Texas pays TFS an agreed “administrative fee”. Each partnership agreement with the Partnering Districts contains contractual terms that

²³ Exhibit 18 – Sampled Third Future Schools – Texas Bank Records

permit Third Future Schools – Texas to “contract for any services it deems beneficial in operation of the [s]chool,” a provision that does not violate any Texas law. The administrative fee to obtain such services is budgeted within each partnering campuses’ budget. Each partnership agreement that Third Future Schools – Texas entered into with the Partnering Districts attached a copy of an estimated budget that included a line item for administrative services, and Third Future Schools – Texas provides updated copies of yearly campus budgets to the Partnership Districts. Additionally, the budgets are approved²⁴ by Third Future Schools – Texas’ board of trustees during an annual budget review that is required under administrative rule²⁵ and Third Future Schools – Texas’ bylaws.²⁶ As permitted by the partnership agreements, Third Future Schools – Texas used a portion of the administrative fee to cover the expenses for services described above.

Funds are also transferred from the Third Future Schools – Texas bank account to a TFS bank account as a part of this administrative fee to pay for other shared services provided by TFS to Third Future Schools – Texas, including insurance costs, curriculum and assessment platforms, and pre-paid debit cards for use by campus staff.²⁷ These shared services are provided to all TFS Network Programs, and the costs of the shared services are paid out of TFS’ bank account. All TFS Network Programs, including Third Future Schools – Texas, then reimburse TFS for a pro rata portion of the total costs incurred by TFS based on a per pupil percentage of total TFS Network enrollment. This process was confirmed through evidence gathered as part of the investigation, including the review of pertinent ledger notes.²⁸

²⁴ Exhibit 19 – Third Future Schools – Texas Board Meeting Minutes, June 23, 2022

²⁵ See 19 Tex. Admin. Code § 97.1075(c)(2)(E)

²⁶ See Exhibit 13 – Third Future Schools – Texas Bylaws

²⁷ Exhibit 20 – Evidence of Sampled Financial Transactions

²⁸ See Exhibit 20 – Evidence of Sampled Financial Transactions

Outside of shared services provided to Third Future Schools – Texas, the investigation identified two additional types of transfers from Third Future Schools – Texas’ bank account to TFS’ bank account. First, in the event Partnering Districts did not provide timely transfers of funds owed through the partnership agreements to Third Future Schools – Texas, TFS would make a temporary payment of philanthropic funds to Third Future Schools – Texas. Once the payments from the Partnering District were received, Third Future Schools – Texas would reimburse TFS for the philanthropic funds. The investigation reviewed a sampling of such payments and confirmed that appropriate reimbursements were made. Second, while providing accounting services for Third Future Schools – Texas, TFS employees occasionally made accounting errors in the normal course of business or billed expenses from the incorrect accounts. When this occurred, funds would be transferred between the impacted bank accounts to remedy the error. The investigation also reviewed a sampling of these payments and confirmed that errors were appropriately remedied.

Under Texas law, TEA does not have authority over what TFS does with the funds it is paid by Third Future Schools – Texas for administrative fees or shared services, just as the agency cannot broadly require any other school district vendor to identify how they expend their funds once the vendor has been paid for services provided. As a vendor of Third Future Schools – Texas, TFS may use the funds that they are paid as they see fit, once those funds have been transferred for goods or services rendered.

The Spectrum News article used a screenshot of one portion of a Third Future Schools – Texas financial audit to suggest their administrative expenses were excessive and that such expenses were attributable to TFS. This investigation concludes that the expenses identified in the Third Future Schools – Texas audit were attributable to expenses incurred by Third Future Schools

– Texas and largely were not attributable to the cost of services from TFS. The investigation further concludes that the payment of administrative expenses by Third Future Schools – Texas does not violate Texas law.

Elsewhere in the audit²⁹ referenced by the Spectrum News report, the following breakdown of administrative expenses is provided:

Third Future Schools- Texas Network
Statement of Functional Expenses
June 30, 2023

Expenses	Program Expense	Management and General	TOTAL
Instructional Salaries & Benefits	\$ 13,268,544	\$ -	\$ 13,268,544
Admin Salaries & Benefits	-	3,394,989	3,394,989
Admin Support Costs	-	4,707,379	4,707,379
Supplies and Materials	2,393,914	-	2,393,914
Professional Services	-	1,512,435	1,512,435
Other Operating Services	-	305,270	305,270
Interest	-	11,468	11,468
Amortization	-	283,902	283,902
TOTAL	\$ 15,662,458	\$10,215,442	\$ 25,877,900

In addition to the audit, the investigation also reviewed the budgeted versus actual expenses for each campus operated by Third Future Schools – Texas in the Partnership Districts from 2020 forward.^{30 31} Investigators verified that the “admin salaries & benefits” category was comprised of campus administrative staff such as the principals, assistant principals, counselors, nurses, office managers, and clerks and did not include funding for the salaries of TFS staff.^{32 33} Each of the partnership agreements signed with Third Future Schools – Texas also included a withholding provision permitting the Partnering District to withhold a portion of the overall funding allocation

²⁹ Exhibit 21 – Third Future Schools – Texas Annual Audit, 2023
³⁰ Exhibit 22 – Third Future Schools – Texas Budgeted Expenses 2020-2023 (ECISD and MISD)
³¹ Exhibit 23 – Third Future Schools – Texas Budgeted Expenses 2022-2024 (Austin ISD)
³² See Exhibit 22 – Third Future Schools – Texas Budgeted Expenses 2020-2023 (ECISD and MISD)
³³ See Exhibit 23 – Third Future Schools – Texas Budgeted Expenses 2022-2024 (Austin ISD)

for administrative supports provided by the Partnering Districts; these withholdings are included in the overall administrative services referenced by the Spectrum News article. This amount varied by agreement. In Midland ISD, the agreement provided that the Partnering District would withhold 15 percent of funds for district administrative support, but the amount was renegotiated to six percent in 2023. In Ector County ISD, the Partnering District withheld a “minimum of \$940 per year per enrolled student”. In Austin ISD, the Partnering District withheld 10 percent. Finally, these administrative expenses also include services purchased from the Partnering Districts. For example, in Midland ISD, Third Future Schools – Texas purchased services from the district that included custodial, transportation, copiers, and special education supports.³⁴ While the administrative fee for the TFS services is also counted in this administrative expenses category, it is a fraction of the expenses and has always been capped at ten percent of the total funds released to the campus by the Partnering District.³⁵ Additionally, investigators found TFS reduced or suspended the required payment of the administrative fee when the Third Future Schools – Texas campuses were struggling to make the payment; this occurred on multiple occasions.

2. Legal Analysis

School operator partnerships under Tex. Educ. Code § 11.174, like the agreements between Third Future Schools – Texas and the Partnering Districts, are governed by Subchapter C of Chapter 12 of the Texas Education Code. Subchapter D of Chapter 12, in contrast, governs open-enrollment charter schools authorized by the Commissioner of Education. As described below, there are many important legal differences between charter schools authorized under Subchapter C and those authorized under Subchapter D. The news reports that form the basis of Allegation Category One, however, attempt to mistakenly impose Subchapter D legal requirements on the

³⁴ Exhibit 24 - Menu of Services Midland ISD SY2020-2021

³⁵ See Exhibit 22 – Third Future Schools – Texas Budgeted Expenses 2020-2023 (ECISD and MISD)

Subchapter C charter schools in question. For example, the allegations made in the Texas Observer and Spectrum News articles reference language from provisions under Subchapter D and invoke administrative rules that implement Subchapter D requirements.

The authorization process and requirements for Subchapter C schools are in direct conflict with many provisions of Subchapter D, as they originate from a different source and have different key terms. Specifically, Tex. Educ. Code § 12.107 is a provision in Subchapter D that establishes the status of specific state funds issued to Subchapter D charter schools. These state funds are allotted through Tex. Educ. Code § 12.106, the source for most Subchapter D charter school state funding. Subchapter D charter schools are authorized by the Commissioner of Education and thus receive their state funding directly from the state. The Commissioner of Education has no authority over the authorization of the Subchapter C district campus charter schools, the funding structure between the Partnering District and the operating partner, or how the operating partner implements its program with those funds. The Commissioner of Education's only authority relating to such agreements is to ensure the partnership agreements meet the minimum requirements in Tex. Educ. Code § 11.174 to be eligible for statutory benefits separate from authorization under Subchapter C.

Importantly, no Subchapter C charter school receives funding via Tex. Educ. Code § 12.106. Therefore, when Tex. Educ. Code § 12.107 states, “[f]unds received under Section 12.106 ... by a charter holder”, the subsequent requirements are not applicable to the funds received by a Subchapter C charter school. Instead, the Subchapter C charter schools in question were authorized by the Partnering District and thus receive funds in the form of payments from the Partnering District pursuant to a partnership agreement. The terms of that agreement, approved

by the Partnering Districts' board of trustees, control the money the Subchapter C charter school receives from the district to operate the campus.

Accordingly, the agency finds that the allegations contained in Allegation Category One are unsubstantiated. The agency concludes that the laws contained within Subchapter C of Chapter 12 of the Tex. Educ. Code apply to the operation by Third Future Schools – Texas of the campuses in question, and the agency additionally concludes that neither the Partnering Districts nor Third Future Schools – Texas violated any provisions of Subchapter C through their partnership agreement. Furthermore, the investigation has not identified any misuse of state funds by Third Future Schools – Texas and the agency finds no violations of Texas school law.

B. Allegation Category Two

1. Findings of Fact

The second general category of allegations asserts that, while operating with the Partnering Districts, Third Future Schools – Texas failed to disclose financial information required by Tex. Educ. Code § 12.111(a)(15). Specifically, it is alleged that the transactions and relationship between Third Future Schools – Texas and TFS should have been disclosed to the Agency and the Partnering Districts prior to forming the partnership.

According to TEC § 11.174 and its associated administrative rules, in order to be eligible to enter into a school operator agreement and receive the statutory benefits that come with a school operator partnership, a district must adopt a board policy relating to the authorization of Subchapter C charter schools within the district at district campuses. These local policies, not state law, govern the information that a prospective partner must share with the school district. State law does not dictate what information should or should not be exchanged between the district and the operating partner. TEA does not have authority over a school district's local authorizing policy, beyond

establishing specific information that must be present in the policy to align the partnership with the statute and to qualify the partnership for benefits. Furthermore, the rules and policies by which a school operator must abide are not governed by state law but are contained in the terms of the contract between the school district and the operator. In this case, the board of trustees of each Partnering District adopted a local authorizing policy to govern Subchapter C school operator partnerships. In accordance with the policy, a binding contract was entered into between Third Future Schools – Texas and each of the Partnering Districts that governed the obligations of each party with regard to the operation of the district’s campus. The investigation determined that neither the local authorizing board policies nor the school operator agreements required Third Future Schools – Texas to disclose any existing agreement with TFS or intent to purchase services from TFS (or any other entity), except to the extent that services were being purchased from the district. Additionally, Subchapter C of Chapter 12 of the Tex. Educ. Code does not require the disclosure of the information that the news reports assert should have been disclosed.

Even though there was no legal obligation or local policy requirement for them to do so, the investigation found that Third Future Schools – Texas did provide in each relevant partnership agreement a proposed or estimated campus budget that identified that Third Future Schools – Texas intended to purchase administrative services for the campus.³⁶ In Midland ISD’s operating partner agreement, the estimated budget identified \$150,000 budgeted for “purchased services for admin. support,” just under four percent of the estimated total revenue of the program. In Ector County ISD’s operating partner agreement, the estimated budget identified \$350,000 budgeted for “purchased services for admin. support,” approximately two and a half percent of the estimated total revenue of the program. In Austin ISD’s operating partner agreement, the estimated budget

³⁶ See Exhibits 14-16 – Third Future Schools – Texas Operating Partner Agreement(s)

included a line item for “purchased services for TFS admin. support”. Additionally, in each subsequent operating year, Third Future Schools – Texas submitted a proposed and approved budget for Third Future Schools – Texas to each Partnering District.³⁷ This submission always included a budgeted line item for “Admin – Purchased Services - Network” funds to pay for centralized services provided by TFS.³⁸

Similarly, in two of the three of the partnerships examined in this investigation, Third Future Schools – Texas provided its bylaws to the Partnering Districts as part of the application process. These bylaws clearly show the relationship between Third Future Schools – Texas and TFS, describing TFS as a sole member of Third Future Schools – Texas. The evidence analyzed in this investigation shows no effort to hide the relationship between Third Future Schools – Texas and TFS from the Partnering Districts.

Additionally, in each of its annual audits, Third Future Schools – Texas identified “Third Future Schools Network” as a related party on “Note 4 – Related Party Transactions”, terminology which is defined in Tex. Educ. Code § 12.1166 as, in part, “a charter holder's related organizations, joint ventures, and jointly governed organizations”.³⁹ ⁴⁰ ⁴¹ “Third Future Schools Network” is a term for the combined TFS programs. For example, in 2021 and 2022, the audits identified TFS as providing professional services to the authorized Third Future Schools – Texas campuses, and, in 2021, a campus “reimbursed Third Future Schools Network \$81,736 for expenses paid on their behalf.” Also, Third Future Schools – Texas’ 2023 audit identified that the campuses were “programs of Third Future Schools – Texas and Third Future Schools Network”. Pursuant to a

³⁷ Exhibit 25 – Third Future Schools – Texas Annual Budget Submission

³⁸ Exhibit 26 – FY23 Budget Item Admin Purchased Services Network

³⁹ Exhibit 27 – Third Future Schools – Texas Annual Audit 2021

⁴⁰ Exhibit 28 – Third Future Schools – Texas Annual Audit 2022

⁴¹ See Exhibit 21 – Third Future Schools – Texas Annual Audit 2023,

requirement in the partnership agreements, these audits were provided to the Partnering Districts. The audits are also posted on the TFS website.

2. Legal Analysis

The Texas Observer article did not reference a specific legal requirement related to this category of general allegations, instead stating that “disclosure of pre-existing business deals for administrative expenses are generally required under state law and rules applied to Texas charter schools.” The article also states that there was a failure to disclose a “symbiotic relationship” between Third Future Schools – Texas and TFS.⁴²

As described above, Subchapter C of Chapter 12 of the Texas Education Code governs the operation of the schools in question. Subchapter C does not contain any mandatory reporting requirements, whether related to partnerships with charter management organizations, vendors, or otherwise. While Subchapter D of Chapter 12 does require open-enrollment charters authorized by the state to provide some information to TEA, the Subchapter C charter schools involved in this investigation are not subject to Subchapter D requirements. The local board policies related to charter authorization for each Partnering District also do not require the disclosure of agreements with vendors, service providers, or any other organization, except that these policies specifically require the operating partner to disclose, in advance, any service-related agreements it intends to form with the Partnering District itself.

In conclusion, the agency finds this allegation unsubstantiated, as it appears to reference provisions in statute and rule that are inapplicable to the type of charter school at issue in this case. Additionally, the agency also finds that the Partnering Districts were notified or were aware of the

⁴² Related to this general category of allegations, the Texas Observer article also specifically references federal 990 filings by the TFS and Third Future Schools - Texas. TEA does not have jurisdiction over or authority to investigate alleged inaccuracies in federal tax reporting.

association between TFS and Third Future Schools – Texas. The Partnering Districts were also aware of the intent of Third Future Schools – Texas to purchase administrative services, as it was consistently identified as a line item on the estimated budgets provided to the Partnering Districts during the application process as well as annual budgets produced throughout the operation of the program. The agency concludes that no violations of law occurred related to this category of allegations.

C. Allegation Category Three

1. Findings of Fact

The third general category of allegations asserts that the Partnering Districts failed to ensure that Third Future Schools – Texas maintained the state funds received from the Partnering Districts in a depository account, as defined and required by Tex. Educ. Code § 12.107. The agency finds that this allegation is unsubstantiated and concludes that no violation of law occurred.

The Spectrum News report alleged that checks issued by the Partnering Districts were sent directly to Colorado and that these funds were being diverted to support other TFS schools in Colorado and thus being denied to Texas students. That allegation has been addressed and dismissed as unsubstantiated in Allegation Category One. However, the Texas Observer article cited the response by TFS to the Spectrum News report in alleging that the process for depositing those checks into the Texas bank account was questionable because “a bank depository certificate obtained by the *Observer* shows that Third Future Schools-Texas didn’t open a bank account until March 2021, almost a year after it started receiving Texas tax dollars.”

While the investigation verified that the depository certificate referenced in the Texas Observer article does show that a specific Third Future Schools – Texas bank account was opened in March 2021, the article fails to identify that Third Future Schools – Texas opened a bank account

with the same bank prior to the creation of the account referenced by the Texas Observer. Investigators reviewed the bank depository certificate for the previously existing account and confirmed the account was opened in July 2020, the same month that Third Future Schools – Texas began their first operating partnership in Texas.⁴³ Additionally, investigators confirmed that the account opened in July 2020 was the operating account for the partnership with Midland ISD, which was the only partnership that Third Future Schools – Texas had at that time.

2. Legal Analysis

The general allegations categorized in Allegation Category Three are dismissed as unsubstantiated. First, the statutory provision related to maintaining funds in a depository account, Tex. Educ. Code § 12.107 is contained in Subchapter D of Chapter 12 of the Texas Education Code, which does not apply to Subchapter C charter schools. That is so because the pertinent provision in the statute expressly includes the requirement that “[f]unds received under Section 12.106” must be deposited in a bank “with which the charter holder has entered into a depository contract”. None of the funds received by Third Future Schools – Texas, as a Subchapter C charter school, were provided by the state under Chapter 12; instead, all proceeds received by Third Future Schools – Texas were paid to it by the Partnering District pursuant to the applicable contractual arrangement. As such, Third Future Schools – Texas must comply with the terms of the partnership agreement, and Tex. Educ. Code § 12.107 does not apply.

Despite that, however, Third Future Schools – Texas did in fact maintain bank accounts “with which the charter holder has entered into a depository contract” continuously during the operation of their campuses in the Partnering District. Therefore, the factual assertions in Allegation Category Three have also been disproven.

⁴³ See Exhibit 17 – Third Future Schools – Texas Depository Certification (2020)

D. Allegation Category Four

1. Findings of Fact

The fourth general category of allegations asserts that, while serving as an operating partner for the Partnering Districts, Third Future Schools – Texas and the board of Third Future Schools – Texas failed to oversee the nonprofit’s finances as required by Texas law. Specific allegations include that the board of Third Future Schools – Texas are not signatories on the entity’s bank account and that the board of TFS, not Third Future Schools – Texas, authorized signatory access to the bank account, enabling the transfer of funds. The agency finds that no violations of applicable Texas law occurred.

TFS is the sole member of Third Future Schools – Texas pursuant to the bylaws of Third Future Schools – Texas. The bylaws of Third Future Schools – Texas govern the responsibilities of its sole member. The bylaws can also impose restrictions on the authority of the sole member and designate exclusive responsibilities to the Third Future Schools – Texas board. For example, the bylaws expressly reserve for the Third Future Schools – Texas board the authority to approve the organization’s budget. There are no express restrictions contained in the bylaws related to the management of depository accounts.

Additionally, an agreement exists between Third Future Schools – Texas and TFS whereby Third Future Schools – Texas pays TFS for specific services. One of those services includes accounting. In that capacity, among other tasks, TFS deposits checks for Third Future Schools – Texas, makes payments on behalf of the Texas entity, and conducts payroll services for Third Future Schools – Texas. To provide these services, TFS’ Director of Finance is a signatory on the Texas entity’s bank account.

The bank account signatories for Third Future Schools – Texas do not include its board members. The board members of Third Future Schools – Texas do not issue checks, withdraw money, or engage in the day-to-day financial operations on behalf of the organization. While the Texas Observer article asserts this fact and implies that the Texas entity is violating a law, no such Texas law exists. Similarly, the article asserts that the Texas board was not the board that approved the Texas account’s signatories; while true, this fact does not create a violation of applicable Texas law. Lastly, the article states that Mike Miles, founder and former CEO of TFS, remains a signatory on the Third Future Schools – Texas bank account, despite no longer being employed by or serving on the board of either organization. The investigation confirmed there is a segregation of duties, and that multiple Third Future staff members are involved with the process for making a check-request, reviewing the request, and approving the request. While the investigation confirmed that Mr. Miles remains a signatory on the Third Future Schools – Texas bank account, this fact does not constitute a violation of Texas law. Furthermore, the investigation uncovered no evidence of any wrongdoing by Mr. Miles or anyone else associated with Third Future Schools – Texas or TFS.

2. Legal Analysis

The fourth general category of allegations asserts that, while serving as an operating partner for the Partnering Districts, Third Future Schools – Texas and its board failed to oversee the nonprofit’s finances as required by Texas law. After investigation, the agency has concluded that no violation of the applicable Texas law or any other applicable rule or policy occurred.

To begin, the Texas Observer article incorrectly states: “Both Texas charter school laws and federal laws governing nonprofit organizations require a nonprofit board of directors to be in charge of the organization’s finances.” This is not an accurate statement of the law. The Texas

Observer article linked to a document from the Internal Revenue Service (IRS) that describes best practices for nonprofit organizations regarding the authorities of governing bodies. This IRS document contains *guidance* for nonprofits, but it does not reference or cite any specific federal law that requires nonprofit directors be signers on their accounts or be involved in the decision regarding the authorized signers. In fact, this document states, “tax law generally does not mandate particular management structures, operational policies, or administrative practices.”

Elsewhere in Subchapter D, Tex. Educ. Code § 12.107 and its associated administrative rule 19 Tex. Admin. Rule § 100.1063 contain requirements related to depository accounts that apply to Subchapter D charter schools but do not apply to Third Future Schools – Texas because it is a Subchapter C charter holder. As discussed in the analysis for Allegation Category One, the funds referenced in Tex. Educ. Code § 12.107 are specifically issued through Tex. Educ. Code § 12.106, which is the funding mechanism by which the state directly funds Subchapter D charter schools authority by the Commissioner of Education, but it is not the funding mechanism for Subchapter C charter schools like the school in question, which receives funding through a contractual agreement with a school district. Similarly, 19 Tex. Admin. Code § 100.1063 is used to administer the legal requirements of Tex. Educ. Code § 12.107 and cannot be made broadly applicable to other funds or entities by agency authority alone.

Instead of these statutes, a Subchapter C charter school is bound by the terms of its partnership agreement with the school district and the local authorizing policy of the school district. While the agency does not have authority over the terms of these contracts or the local authorizing policies adopted by school districts, evidence analyzed during the investigation establishes that neither the partnership agreement at issue or the district’s local authorizing policy has requirements related to depository accounts.

In the absence of an applicable law or policy, either in the operating partnership agreement, the school district's charter authorizing policy, or in Subchapter C, there is no applicable requirement in the agency's jurisdiction to indicate that the funds issued in the partnership must be held in an account with sole operating partner control. No evidence was obtained during the investigation that supports the allegation that funds were being transferred from the account by TFS signers that were not for expenses approved by the Third Future Schools – Texas board in the partnership budgets.

V. Conclusion

The allegations regarding the Partnering Districts and their partnership with Third Future Schools – Texas have been investigated by the agency, and the agency concludes that no violations of applicable laws have occurred by either the Partnering Districts or Third Future Schools – Texas. The allegations contained in the media reports described herein and related complaints either reference requirements that are inapplicable to the partnership or cannot be substantiated, or have been proven to be false. Accordingly, the agency is concluding its review of these matters and closing the investigation.