

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED FINANCIAL
STATEMENTS WITH INDEPENDENT
AUDITOR'S REPORT**

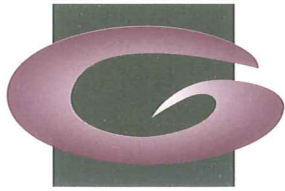
**YEAR ENDED
JUNE 30, 2009
AND
PERIOD ENDED
JUNE 30, 2008**

ROCKETSHIP EDUCATION AND ITS AFFILIATES

JUNE 30, 2009 AND 2008

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Gilbert Associates, Inc.
CPAs and Advisors

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Rocketship Education
San Jose, California

We have audited the accompanying consolidated statements of financial position of Rocketship Education and its Affiliates (RSED), a California non-profit public benefit corporation, as of June 30, 2009 and 2008 and the related consolidated statements of activities and changes in net assets and of cash flows for the year ended June 30, 2009 and the period from inception (October 16, 2006) through June 30, 2008. These consolidated financial statements are the responsibility of RSED's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of RSED as of June 30, 2009 and 2008 and the changes in its net assets and its cash flows for the year ended June 30, 2009 and the period from inception (October 16, 2006) through June 30, 2008, in conformity with accounting principles generally accepted in the United States of America.

Our audits were performed for the purpose of forming an opinion on the consolidated financial statements of RSED as a whole. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements of RSED. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, such information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Gilbert Associates, Inc.

GILBERT ASSOCIATES, INC.
Sacramento, California

December 14, 2009

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2009 AND 2008**

| | ASSETS | |
|---|---------------------------|---------------------|
| | <u>2009</u> | <u>2008</u> |
| CURRENT ASSETS | | |
| Cash and equivalents | \$ 4,525,789 | \$ 1,320 |
| Cash and equivalents - restricted | 90,000 | |
| Investments | 1,000,123 | |
| Accounts receivable | 689,432 | 132,089 |
| Prepaid expenses and deposits | <u>127,932</u> | <u>53,930</u> |
| Total current assets | 6,433,276 | 187,339 |
| PROPERTY AND EQUIPMENT - Net | <u>11,093,436</u> | <u>4,227,191</u> |
| TOTAL ASSETS | <u>\$ 17,526,712</u> | <u>\$ 4,414,530</u> |
| LIABILITIES AND NET ASSETS | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 1,578,162 | \$ 131,797 |
| Accrued expenses | 92,726 | 36,771 |
| Accrued interest | 22,360 | |
| Notes payable, current portion | <u>436,245</u> | <u>100,207</u> |
| Total current liabilities | 2,129,493 | 268,775 |
| LONG-TERM LIABILITIES | | |
| Accrued long-term liabilities | | 2,515,663 |
| Accrued interest | 23,321 | |
| Notes payable | <u>14,360,313</u> | <u>1,233,742</u> |
| Total liabilities | <u>16,513,127</u> | <u>4,018,180</u> |
| NET ASSETS | | |
| Unrestricted | 1,013,585 | 393,886 |
| Temporarily restricted | <u> </u> | <u>2,464</u> |
| Total net assets | <u>1,013,585</u> | <u>396,350</u> |
| TOTAL LIABILITIES AND NET ASSETS | <u>\$ 17,526,712</u> | <u>\$ 4,414,530</u> |

The accompanying notes are an integral part of these financial statements.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED JUNE 30, 2009 AND PERIOD FROM INCEPTION
(OCTOBER 16, 2006) THROUGH JUNE 30, 2008**

| | 2009 | 2008 |
|---|---------------------|-------------------|
| CHANGES IN UNRESTRICTED NET ASSETS: | | |
| SUPPORT AND REVENUE | | |
| Private grants and contributions | \$ 791,887 | \$ 405,402 |
| In-kind contributions | 156,000 | 126,118 |
| Federal revenue | 367,023 | 582,481 |
| State revenue: | | |
| State aid portion of general purpose block grant | 30,690 | 63,249 |
| Categorical block grant | 216,738 | 142,653 |
| Lottery revenue | 35,301 | 17,710 |
| All other state revenue | 549,345 | 178,704 |
| Local revenue: | | |
| Cash in-lieu of property taxes | 1,672,359 | 799,978 |
| Interest income | 4,542 | 454 |
| All other local revenue | 12,981 | 22,918 |
| Subtotal | 3,836,866 | 2,339,667 |
| Net assets released from restrictions | 275,480 | |
| Total support and revenue | 4,112,346 | 2,339,667 |
| EXPENSES | | |
| PROGRAM EXPENSES | | |
| Educational programs | 2,839,800 | 1,800,994 |
| SUPPORTING SERVICES | | |
| Site support | 198,060 | 144,787 |
| Development and expansion | 300,165 | |
| Management and general | 154,622 | |
| Total supporting services | 652,847 | 144,787 |
| Total expenses | 3,492,647 | 1,945,781 |
| Increase in Unrestricted Net Assets | 619,699 | 393,886 |
| CHANGES IN TEMPORARILY RESTRICTED NET ASSETS: | | |
| State revenue | 159,975 | 2,464 |
| Federal revenue | 113,041 | |
| Net assets released from restrictions | (275,480) | |
| Increase (Decrease) in Temporarily Restricted Net Assets | (2,464) | 2,464 |
| INCREASE IN NET ASSETS | 617,235 | 396,350 |
| NET ASSETS - Beginning of Year | 396,350 | |
| NET ASSETS - End of Year | \$ 1,013,585 | \$ 396,350 |

The accompanying notes are an integral part of these financial statements.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS
YEAR ENDED JUNE 30, 2009 AND PERIOD FROM INCEPTION
(OCTOBER 16, 2006) THROUGH JUNE 30, 2008**

| | 2009 | 2008 |
|--|--------------|-------------|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Increase in net assets | \$ 617,235 | \$ 396,350 |
| Adjustments to reconcile to net cash provided by operating activities: | | |
| Depreciation | 285,270 | 15,898 |
| Unrealized gain on investments | (122) | |
| Debt forgiven through grant agreement | (400,000) | |
| Changes in assets: | | |
| Accounts receivable | (557,343) | (132,089) |
| Prepaid expenses and deposits | (74,002) | (53,930) |
| Changes in liabilities: | | |
| Accounts payable | 24,329 | 131,797 |
| Accrued expenses | 101,636 | 36,771 |
| Net cash provided by (used in) operating activities | (2,997) | 394,797 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of investment | (1,000,001) | |
| Purchases of property and equipment | (5,729,479) | (4,243,089) |
| Net cash used in investing activities | (6,729,480) | (4,243,089) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Borrowings on notes payable | 14,254,483 | 3,849,612 |
| Borrowings on line of credit | 435,000 | 752,042 |
| Payments on lines of credit | (435,000) | (752,042) |
| Principal payments on notes payable | (2,907,537) | |
| Net cash provided by financing activities | 11,346,946 | 3,849,612 |
| Net increase in cash | 4,614,469 | 1,320 |
| Cash and cash equivalents, beginning of year | 1,320 | |
| Cash and cash equivalents, end of year | \$ 4,615,789 | \$ 1,320 |
| NON-CASH INVESTING ACTIVITIES: | | |
| Property and equipment financed through accounts payable | \$ 1,422,036 | |
| CASH PAID FOR INTEREST (net of capitalized amount) | \$ 290,260 | \$ 21,384 |

The accompanying notes are an integral part of these financial statements.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

1. OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Rocketship Education (RSED or Rocketship) is a California non-profit public benefit corporation that was incorporated in May 2006 and is organized to manage, operate, guide, direct, and promote a network of outstanding inner-city college preparatory elementary charter schools.

In addition to managing school operations, RSED is creating a network of schools (the Network) that currently includes construction and ownership of its own school facilities. Each school facility is owned and managed by a single-member limited liability company (LLC). The managing member of each LLCs is RSED which treats the LLCs as a consolidated wholly-owned subsidiary. For tax and financial reporting purposes, the LLCs are considered a disregarded entity and its operations are consolidated with RSED corporate. Plans are currently underway to spin-off the facility LLCs into a separate organization during the 2009/10 fiscal year.

Principles of Consolidation – The accompanying financial statements include the accounts of RSED and its wholly-owned LLCs. All significant intercompany accounts and transactions have been eliminated in consolidation. Listed below are the affiliated organizations included in these financial statements:

- **Rocketship Education**

RSED operates its first school as a division of its corporate office (Rocketship National). Its first school, Rocketship Mateo Sheedy Elementary (RMS), charter number 0850, is funded principally through State of California public education monies received through the California Department of Education and the Santa Clara County Office of Education (SCCOE), the Sponsoring District. RSED is governed by a Board of Directors consisting of seven members.

SCCOE approved the Charter for RMS for a 3-year term through the 2009/10 school year. The charter may be revoked by SCCOE for material violations of the charter, failure to meet generally accepted standards of fiscal management, or violation of any provision of the law.

RSED opened its second school, Rocketship Si Se Puede Academy (RSSP), charter number 1061, on August 31, 2009. RSSP is operated as a division of RSED's corporate office and is funded principally through State of California public education monies received through the California Department of Education and SCCOE.

SCCOE approved the Charter for RSSP for a 5-year term through the 2013/14 school year. The charter may be revoked by SCCOE for material violations of the charter, failure to meet generally accepted standards of fiscal management, or violation of any provision of the law.

SCCOE additionally approved 5 charters including Rocketship Three Elementary (RS3), charter number 1127, scheduled to begin operations in the 2010/11 school year.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

- **Rocketship Locust Property, LLC** - RSED organized Rocketship Locust Property, LLC (Locust LLC) to construct, hold, and manage the facility used in the school operations of RMS. RMS started serving K-3 grades in the 2007/08 school year at a temporary facility with 160 enrolled students. RMS expanded to serving K-4 grades in the 2008/09 school year in its new permanent facility with 320 enrolled students, and it will expand further to serving K-5 grades in the 2009/10 school year to reach its full enrollment capacity of 450 students.
- **Rocketship Dobern Property, LLC** - RSED organized Rocketship Dobern Property, LLC (Dobern LLC) to construct, hold, and manage the facility used in the school operations of RSP. RSP started serving grades K-4 on August 31, 2009 with an initial enrollment of 422 students. RSP will expand in the 2010/11 school year to reach its full enrollment capacity of 450 students.
- **Rocketship Three Property, LLC** - RSED organized Rocketship Three Property, LLC (RS3 LLC) to construct, hold, and manage the facility used in the school operations of Rocketship 3, scheduled to open in the 2010/11 school year.

Basis of presentation – The financial statements are presented in conformity with Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-For-Profit Organizations*. Under SFAS No. 117, RSED reports information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. RSED had no temporarily restricted or permanently restricted net assets at June 30, 2009.

Revenue recognition – Contributions and grants are recognized when the donor/grantor makes an unconditional promise to give to Rocketship or when received, in accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*. Donor-restricted contributions and grants are reported as increases in temporarily or permanently restricted net assets, depending on the nature of the restrictions. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as “Net Assets Released from Restriction.” Government grants are recognized as revenue in accordance with the terms of the applicable grant agreement, which is generally upon the incurrence of expenditures related to the required services.

Cash and cash equivalents – For financial statement purposes, Rocketship considers investments with maturity at purchase of three months or less to be cash equivalents.

Restricted cash consists of a Certificate of Deposit (CD) for \$90,000 which matured on July 29, 2009. This CD is maintained in an RSED bank account and is payable to the City of San Jose. It is used as collateral for public improvements being performed during construction at Rocketship Dobern, LLC.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

Donated materials, services and facilities – In-kind contributions are recorded at their estimated fair values at the date of donation. Donated services are recorded when they create or enhance non-financial assets or require a specialized skill that RSED would otherwise need to purchase. During the year ended June 30, 2009 and period ended June 30, 2008, in-kind contributions of management services valued at \$156,000 and \$126,118, respectively, were received.

Land, Buildings, and equipment – Land, buildings, and equipment are stated at cost if purchased or at estimated fair market value if donated. Depreciation of buildings and equipment is provided on a straight-line basis over estimated useful lives of the assets. RSED capitalizes all expenditures for land, buildings, and equipment equal to or in excess of \$5,000.

Income taxes – Rocketship is publicly supported and has received tax-exempt status under Internal Revenue Code Section 501(c)(3) and Section 23701(d) of the California Revenue and Taxation Code. There is no unrelated taxable income and, accordingly, there is no provision for income taxes in these financial statements. RSED has elected to defer the application of Financial Accounting Standard Board (FASB) Interpretation 48, *Accounting for Uncertainty in Income Taxes* as allowed until July 1, 2009. RSED will evaluate any uncertain tax positions in conjunction with the preparation of the tax returns.

Use of estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Functional allocation of expenses – The cost of providing various programs and other activities has been summarized on a functional basis in the Statement of Activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Recent accounting pronouncements – In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes guidelines for measuring fair value, and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. The adoption of SFAS 157 for financial assets and liabilities on July 1, 2008 did not have a material impact on the Organization's statement of financial position or the related statements of activities and of cash flows.

Fair value measurements – Assets and liabilities measured at fair value are recorded in accordance with SFAS 157, which clarifies that fair value is an exit price, representing the amount that would be received upon sale of an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, SFAS 157 establishes a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

- Level 1 Inputs Unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.
- Level 2 Inputs Inputs other than quoted prices in active markets that are observable either directly or indirectly.
- Level 3 Inputs Unobservable inputs in which there is little or no market data, which require us to develop our own assumptions.

Subsequent events were reviewed through the date of the audit report.

Reclassification – Certain reclassifications have been made to the 2008 balances to conform to the 2009 presentation. These reclassifications had no effect on the Organization’s total net assets.

2. CONCENTRATION OF CREDIT RISK

RSED maintains its cash in bank deposit accounts that at times may exceed federally insured limits. RSED has not experienced any losses in such accounts and management believes RSED is not exposed to any significant credit risk related to cash.

3. INVESTMENTS

Investments consist of a US Treasury bill maturing on November 5, 2009. As of June 30, 2009, investments consisted of balances classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices in an active market. Investment income for the year ending June 30, 2009 includes \$1 of interest income and \$122 of unrealized gain.

4. ACCOUNTS RECEIVABLE

Accounts receivable primarily consist of funds due from various governmental agencies. Management believes all of these amounts are collectible; therefore, no provisions for uncollectible accounts were recorded.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008**

5. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30:

| | <u>2009</u> | <u>2008</u> |
|-------------------------------|----------------------|---------------------|
| Land | \$ 1,858,359 | |
| Buildings and improvements | 5,850,377 | |
| Furniture and equipment | 59,865 | \$ 59,865 |
| Construction in progress | <u>3,625,928</u> | <u>4,183,149</u> |
| Subtotal | 11,394,529 | 4,243,014 |
| Less accumulated depreciation | <u>(301,093)</u> | <u>(15,823)</u> |
| Property and equipment, net | <u>\$ 11,093,436</u> | <u>\$ 4,227,191</u> |

Depreciation expense was \$285,270 and \$15,823 for the year ended June 30, 2009 and period ended June 30, 2008, respectively.

In August 2008, RSED completed building RMS's new site in San Jose, CA. As of June 30, 2009, a total of approximately \$5.85 million in expenditures had been incurred for this project and RSED had a commitment for an additional \$200,000.

As of June 30, 2009, RSED was in the process of building a new facility for RSSP in San Jose, California through Dobern, LLC. At that time, a total of approximately \$5.44 million in expenditures had been incurred for this project, including \$1.86 million to purchase land at 2249 Dobern Avenue in San Jose, CA. RSED had a commitment to completion of approximately \$1.6 million. The facilities were completed in August 2009.

Additionally, as of June 30, 2009, RSED had begun planning for the construction of a new facility for RS3 in San Jose, CA through RS3, LLC. At that time, a total of approximately \$48,000 in expenditures had been incurred for this project.

While a facility is under construction, a portion of interest is capitalized into its cost in accordance with SFAS No. 34, *Capitalization of Interest Costs*. In summary, the capitalization of interest is applicable to the amount of interest that could have been avoided had the Organization not undertaken the building of a capital asset. The amount of capitalizable interest is determined by applying the debt interest rate to the average amount of accumulated expenditures for the building during the year. Interest costs of \$347,411 and \$18,090 were incurred related to debt during the years ended June 30, 2009 and 2008, respectively. During the years ended June 30, 2009 and 2008, \$38,165 and \$0 of interest was capitalized, respectively.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008**

6. LEASES

Operating Leases

Related to the site development of RMS's facility, on October 1, 2007, Locust LLC entered into a 10 year land lease payable at \$10,400 monthly. This lease was modified on December 1, 2007 to increase the term of the lease to 20 years with gradually increasing financial commitments. Annual commitments on this lease are as follows:

| Year Ending June 30, | |
|---------------------------------|---------------------|
| 2010 | \$ 124,800 |
| 2011 | 125,320 |
| 2012 | 131,040 |
| 2013 | 131,040 |
| 2014 | 131,586 |
| Thereafter | <u>2,102,106</u> |
| Total | <u>\$ 2,745,892</u> |

Lease expense recognized as of June 30, 2009 and 2008 was \$124,800 and \$15,600, respectively. As part of this lease agreement, Rocketship Education has provided a \$250,000 Letter of Credit payable to the Lessor as additional securitization. The current Letter of Credit expires in May 2010 but will be renewed as a condition of the lease.

Each school rents equipment under various operating leases. As of June 30, 2009, RMS and RSSP each had operating leases with approximately 3 year terms. The following is a schedule of future minimum lease payments required under operating leases that have initial noncancelable lease terms in excess of one year:

| Year Ending June 30, | <u>RMS</u> | <u>RSSP</u> | <u>Total</u> |
|---------------------------------|-------------------|--------------------|---------------------|
| 2010 | \$ 26,388 | \$ 17,941 | \$ 44,329 |
| 2011 | 26,388 | 19,572 | 45,960 |
| 2012 | 26,388 | 19,572 | 45,960 |
| 2013 | <u>2,199</u> | <u>1,631</u> | <u>3,830</u> |
| Total | <u>\$ 81,363</u> | <u>\$ 58,716</u> | <u>\$ 140,079</u> |

Lease expense recognized as of June 30, 2009 and 2008 was approximately \$30,800 and \$13,500, respectively.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

7. DEBT

CDFI Facilities Construction Loans

As of June 30, 2009, Locust LLC has two facilities construction loans payable with a Community Development Financial Institution (CDFI). Two of them were entered into during the 2007-2008 fiscal year and as of June 30, 2009 had principal balances of \$4,688,432 on the primary loan and \$683,126 on the subordinate loan with effective interest rates of 5.0 percent and 5.25 percent, respectively. The loan agreement with the CDFI allows RSED to borrow up to \$5,000,000 on the primary loan and \$700,000 on the subsidiary loan. Both loans are for seven years with the primary loan structured as interest-only over the term of the loan and the subsidiary loan structured as interest-only until 10/1/08 at which point it amortizes over a 20 year period. RSED used the proceeds of these loans to construct permanent facilities for its San Jose campus for Rocketship Mateo Sheedy Elementary School. Both loans use the completed facilities as collateral. As of June 30, 2008, RSED incurred \$2,511,426 in construction costs that were accrued as long term liabilities because all costs incurred on the facilities project were to be funded by the CDFI loans. The entire \$2.5 million of accrued expenses at June 30, 2008 was funded by the loans in July 2008.

As of June 30, 2009, Dobern, LLC has a facilities construction loan payable with a CDFI totaling \$6.8 million. This loan is structured as interest-only for seven years with an effective interest rate of 5.5 percent. A modification signed in May 2009 lowered the effective rate to 4.5 percent for the period from May 1, 2009 through November 30, 2009, after which time it returns to 5.5 percent. Rocketship Dobern LLC is using the proceeds of this loan to construct permanent facilities for the San Jose campus for Rocketship Si Se Puede Academy. The loan will use the completed facilities as collateral.

For each of these loans, the CDFI requires the borrower to maintain a debt service ratio [EBITDA / (Principal + Interest)] of 1.1, calculated quarterly. As of June 30, 2009, Locust LLC and Dobern LLC had both met the covenants of these loans.

Future minimum principal payments under these loans as of June 30, 2009 are as follows:

| Year Ending June 30, | Locust LLC | Dobern LLC | Total |
|---------------------------------|-----------------------|-----------------------|---------------------|
| 2010 | \$ 21,245 | | \$ 21,245 |
| 2011 | 22,382 | | 22,382 |
| 2012 | 23,572 | | 23,572 |
| 2013 | 24,813 | | 24,813 |
| 2014 | 26,106 | | 26,106 |
| Thereafter | <u>5,253,440</u> | <u>\$ 6,800,000</u> | <u>12,053,440</u> |
| Total | <u>\$5,371,558</u> | <u>\$ 6,800,000</u> | <u>\$12,171,558</u> |

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

California Department of Education Revolving Loan Program

As of June 30, 2009, RMS has a \$200,000 unsecured loan payable under the California Department of Education Revolving Loan Program with an effective interest rate of 5.0 percent. The repayment terms require annual principal payments of \$50,000, and the loan matures on June 30, 2014.

As of June 30, 2009, RSSP has a \$200,000 unsecured loan payable under the California Department of Education Revolving Loan Program with an effective interest rate of 1.47 percent. The repayment terms require annual principal payments of \$40,000, and the loan matures on June 30, 2015.

Future minimum principal payments under this revolving loan as of June 30, 2009 are as follows:

| Year Ending June 30, | <u>RMS</u> | <u>RSSP</u> | <u>Total</u> |
|---------------------------------|-------------------|--------------------|---------------------|
| 2010 | \$ 50,000 | \$ 40,000 | \$ 90,000 |
| 2011 | 50,000 | 40,000 | 90,000 |
| 2012 | 50,000 | 40,000 | 90,000 |
| 2013 | 50,000 | 40,000 | 90,000 |
| 2014 | <u> </u> | <u>40,000</u> | <u>40,000</u> |
| Total | <u>\$ 200,000</u> | <u>\$ 200,000</u> | <u>\$ 400,000</u> |

California Charter Schools Association Growth Loan Program

As of June 30, 2009, RMS has a \$325,000 loan payable under the California Charter Schools Association's (CCSA) Growth Loan Program with an annual interest rate of 6.5 percent. This loan pledges public revenue earned from the State of California but not yet received (Receivables) as collateral. The loan agreement with CCSA allowed RMS to borrow up to \$650,000. The \$325,000 remaining balance plus accrued interest was paid in July 2009.

Convertible Loans

In February 2009, RSED entered into a \$2.3 million Subordinate Loan Agreement with Charter School Growth Fund at an effective interest rate of 4.0 percent. Of this amount, \$2 million plus associated interest will be forgiven and converted into a grant provided that RSED meet specified educational, financial and growth outcomes. In the event that these annual benchmarks are not met, the loan is to be repaid in \$500,000 annual increments, starting October 1, 2014 through October 1, 2017 with all remaining principal and accrued, unpaid interest due on October 1, 2018.

As of June 30, 2009, RSED had substantively met the 2008/09 school year benchmarks and converted \$400,000 of principal and \$4,910 in interest into a grant, resulting in \$1.9 million remaining note payable. In addition to the interest converted into a grant, RSED accrued \$23,321 in interest payable as a long-term liability.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

Commercial Bank Line of Credit

RSED also has a line of credit with a commercial bank effective November 1, 2006 through November 30, 2009, which provides borrowings up to \$1,000,000. Interest on outstanding balances is the LIBOR plus 2.25 percent or prime minus 0.25%, whichever is less. For the year ended June 30, 2009 there were four borrowings on this line of credit, and there is no balance outstanding as of June 30, 2009 and 2008. The line of credit is secured by the personal property of the Co-Founder and CEO.

8. EMPLOYEE BENEFIT PLANS

Qualified employees are covered under multiple-employer defined benefit pension plan maintained by an agency of the State of California. Certificated employees are members of the California State Teachers' Retirement System (CalSTRS). All employees who are not members of CalSTRS must contribute to the federal Social Security system.

California State Teachers' Retirement Systems (CalSTRS):

Plan Description

RSED contributes to the California State Teachers' Retirement Systems (CalSTRS), a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalSTRS. The plan provides retirement, disability, and survivor benefits to beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the State Teachers' Retirement Law. CalSTRS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalSTRS annual financial report may be obtained from CALSTRS, 100 Waterfront Place, West Sacramento, California 95605.

Funding Policy

Active plan members are required to contribute 8% of their salary and RSED is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the CalSTRS Teachers' Retirement Board. The required employer contribution rate for fiscal year 2008-09 was 8.25% of annual payroll. The contribution requirements of the plan members are established by state statute. RSED's contributions to CalSTRS for the fiscal year ending June 30, 2009 and the period ending June 30, 2008 were \$66,485 and \$33,547, respectively, and equal 100% of the required contributions for each year.

ROCKETSHIP EDUCATION AND ITS AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2009 AND 2008

9. AGREEMENT WITH SPONSORING DISTRICT

RSED has a Memorandum of Understanding (MOU) with SCCOE from July 1, 2007 through June 30, 2010 which outlines the supervisory oversight provided by the SCCOE. As stated in the Education Code, up to 1% of all Charter School State revenues (excluding grants and private monies outside of the funding model), can be paid to the sponsoring district for the actual expenses incurred in monitoring and overseeing RMS. The fees accrued to SCCOE for oversight in accordance with this agreement were approximately \$19,000 and \$15,000 for the year ended June 30, 2009 and the period ended June 30, 2008, respectively, and is included in accrued expenses on the statements of financial position.

10. RELATED PARTY TRANSACTIONS

RSED's Co-Founder and CEO voluntarily did not receive any form of compensation in fiscal year 2007-08 and 2008-09, but the equivalent value of his performance as the CEO was estimated at \$126,118 and \$156,000, respectively. The value of his work was recorded as a component of revenues under in-kind contributions and recorded as supporting services on the schedule of functional expense. The net effect of these transactions to the changes in net assets was zero.

Personal property of the Co-Founder and CEO is used as collateral for the RSED bank line of credit in the amount of \$1,000,000. At June 30, 2009 and 2008, there was no balance on this line of credit.

11. CONTINGENCIES

RSED has received state and federal funds for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate disallowances under terms of the grants, management believes all compliance requirements have been met.

SUPPLEMENTARY INFORMATION SECTION

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED SCHEDULE OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2009**

| | <u>Program Expenses</u> | | | | | <u>Support Expenses</u> | | | | |
|---------------------------------------|---|---------------------------------------|--|-----------------------|-----------------------|--------------------------|-------------------------|--|---|--------------------------|
| | <u>Rocketship Mateo Sheedy Elementary</u> | <u>Rocketship Si Se Puede</u> | <u>Rocketship Three Elementary</u> | <u>Locust LLC</u> | <u>Eliminations</u> | <u>Total Program</u> | <u>Site Support</u> | <u>Rocketship National Program Development and Expansion</u> | <u>Administrative and General</u> | <u>Total Support</u> |
| Certificated salaries | \$ 843,809 | \$ 62,865 | | | | \$ 906,674 | | | | |
| Classified salaries | 142,540 | 8,936 | | | | 151,476 | \$ 157,490 | | | \$ 157,490 |
| Employee benefits | 204,370 | 15,017 | | | | 219,387 | 29,190 | | | 29,190 |
| Books and supplies | 363,559 | 2,163 | | | | 365,722 | 11,380 | | | 11,380 |
| Services and other operating expenses | 1,227,216 | 337,936 | \$ 45,648 | \$ 133,488 | \$ (1,139,617) | 604,671 | | \$ 270,824 | \$ 154,622 | 425,446 |
| Depreciation and amortization | 44,042 | | | 241,228 | | 285,270 | | | | |
| Interest Expense | 59,677 | | | 246,923 | | 306,600 | | 29,341 | | 29,341 |
| Total expenses | <u>\$ 2,885,213</u> | <u>\$ 426,917</u> | <u>\$ 45,648</u> | <u>\$ 621,639</u> | <u>\$ (1,139,617)</u> | <u>\$ 2,839,800</u> | <u>\$ 198,060</u> | <u>\$ 300,165</u> | <u>\$ 154,622</u> | <u>\$ 652,847</u> |

The accompanying notes are an integral part of these financial statements.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATED SCHEDULE OF FUNCTIONAL EXPENSES
YEAR ENDING JUNE 30, 2008**

| | <u>Program expenses</u> | <u>Supporting services</u> | <u>Total expenses</u> |
|---------------------------------------|-----------------------------|--------------------------------|---------------------------|
| Certificated salaries | \$ 511,657 | | \$ 511,657 |
| Classified salaries | 73,443 | \$ 9,583 | 83,026 |
| Employee benefits | 126,094 | 1,725 | 127,819 |
| Books and supplies | 273,767 | | 273,767 |
| Services and other operating expenses | 778,751 | 133,479 | 912,230 |
| Interest | 21,384 | | 21,384 |
| Depreciation | <u>15,898</u> | <u> </u> | <u>15,898</u> |
| Total expenses | <u>\$ 1,800,994</u> | <u>\$ 144,787</u> | <u>\$ 1,945,781</u> |

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATING STATEMENT OF FINANCIAL POSITION
JUNE 30, 2009**

| ASSETS | | | | | | | | | | |
|---|--------------------------------|---|---------------------------------------|--|---|--------------------|-----------------------|-----------------------|---------------------|-------------------------------|
| | <u>Rocketship National</u> | <u>Rocketship Mateo Sheedy Elementary</u> | <u>Rocketship Si Se Puede</u> | <u>Rocketship Three School</u> | <u>Total Rocketship Education</u> | <u>RS3 LLC</u> | <u>Dobern LLC</u> | <u>Locust LLC</u> | <u>Eliminations</u> | <u>Consolidated Total</u> |
| CURRENT ASSETS | | | | | | | | | | |
| Cash and cash equivalents | \$ 1,292,590 | \$ 111,279 | \$ 52,038 | \$ 79,352 | \$ 1,535,259 | \$ 3,150 | \$ 2,943,433 | \$ 43,947 | | \$ 4,525,789 |
| Cash and cash equivalents - restricted | | | | | | | 90,000 | | | 90,000 |
| Investments | 1,000,123 | | | | 1,000,123 | | | | | 1,000,123 |
| Accounts receivable | | 689,432 | | | 689,432 | | | | | 689,432 |
| Intraorganization receivables | 50,000 | | | | 50,000 | | | | \$ (50,000) | |
| Prepaid expenses and deposits | 5,870 | 51,347 | 49,915 | | 107,132 | | | 20,800 | | 127,932 |
| Total current assets | <u>2,348,583</u> | <u>852,058</u> | <u>101,953</u> | <u>79,352</u> | <u>3,381,946</u> | <u>3,150</u> | <u>3,033,433</u> | <u>64,747</u> | <u>(50,000)</u> | <u>6,433,276</u> |
| PROPERTY AND EQUIPMENT - Net | | | | | | <u>47,935</u> | <u>5,436,352</u> | <u>5,609,149</u> | | <u>11,093,436</u> |
| TOTAL ASSETS | <u>\$ 2,348,583</u> | <u>\$ 852,058</u> | <u>\$ 101,953</u> | <u>\$ 79,352</u> | <u>\$ 3,381,946</u> | <u>\$ 51,085</u> | <u>\$ 8,469,785</u> | <u>\$ 5,673,896</u> | <u>\$ (50,000)</u> | <u>\$ 17,526,712</u> |
| LIABILITIES AND NET ASSETS | | | | | | | | | | |
| CURRENT LIABILITIES | | | | | | | | | | |
| Accounts payable | \$ 53,162 | \$ 88,073 | \$ 14,381 | | \$ 155,616 | \$ 1,085 | \$ 1,418,713 | \$ 2,748 | | \$ 1,578,162 |
| Intraorganization payables | | | | | | 50,000 | | | \$ (50,000) | |
| Accrued expenses | 5,432 | 85,305 | 1,989 | | 92,726 | | | | | 92,726 |
| Accrued interest | | 3,521 | | | 3,521 | | 18,839 | | | 22,360 |
| Debt, current portion | | 375,000 | 40,000 | | 415,000 | | | 21,245 | | 436,245 |
| Total current liabilities | <u>58,594</u> | <u>551,899</u> | <u>56,370</u> | | <u>666,863</u> | <u>51,085</u> | <u>1,437,552</u> | <u>23,993</u> | <u>(50,000)</u> | <u>2,129,493</u> |
| LONG-TERM DEBT | | | | | | | | | | |
| Accrued interest | 23,321 | | | | 23,321 | | | | | 23,321 |
| Notes payable | 1,900,000 | 150,000 | 160,000 | | 2,210,000 | | 6,800,000 | 5,350,313 | | 14,360,313 |
| Total liabilities | <u>1,981,915</u> | <u>701,899</u> | <u>216,370</u> | | <u>2,900,184</u> | <u>51,085</u> | <u>8,237,552</u> | <u>5,374,306</u> | <u>(50,000)</u> | <u>16,513,127</u> |
| NET ASSETS: | | | | | | | | | | |
| Unrestricted | <u>366,668</u> | <u>150,159</u> | <u>(114,417)</u> | <u>\$ 79,352</u> | <u>481,762</u> | | <u>232,233</u> | <u>299,590</u> | | <u>1,013,585</u> |
| Total net assets | <u>366,668</u> | <u>150,159</u> | <u>(114,417)</u> | <u>79,352</u> | <u>481,762</u> | | <u>232,233</u> | <u>299,590</u> | | <u>1,013,585</u> |
| TOTAL LIABILITIES AND NET ASSETS | <u>\$ 2,348,583</u> | <u>\$ 852,058</u> | <u>\$ 101,953</u> | <u>\$ 79,352</u> | <u>\$ 3,381,946</u> | <u>\$ 51,085</u> | <u>\$ 8,469,785</u> | <u>\$ 5,673,896</u> | <u>\$ (50,000)</u> | <u>\$ 17,526,712</u> |

The accompanying notes are an integral part of these financial statements.

**ROCKETSHIP EDUCATION
AND ITS AFFILIATES**

**CONSOLIDATING SCHEDULE OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED JUNE 30, 2009**

| | Rocketship National | Rocketship Mateo Sheedy Elementary | Rocketship Si Se Puede | Rocketship Three Elementary | Total Rocketship Education | RS3 LLC | Dobern LLC | Locust LLC | Eliminations | Consolidated Total |
|--|--------------------------------|---|---------------------------------------|--|---|--------------------|-----------------------|-----------------------|---------------------|-------------------------------|
| CHANGES IN UNRESTRICTED NET ASSETS: | | | | | | | | | | |
| SUPPORT AND REVENUE | | | | | | | | | | |
| Private grants and contributions | \$ 857,352 | \$ 7,148 | \$ 250,000 | \$ 125,000 | \$ 1,239,500 | | \$ 232,000 | \$ 460,004 | \$ (1,139,617) | \$ 791,887 |
| In-kind contributions | 156,000 | | | | 156,000 | | | | | 156,000 |
| Federal revenue | | 304,523 | 62,500 | | 367,023 | | | | | 367,023 |
| State revenue: | | | | | 0 | | | | | |
| State aid portion of general purpose block grant | | 30,690 | | | 30,690 | | | | | 30,690 |
| Categorical block grant | | 216,738 | | | 216,738 | | | | | 216,738 |
| Lottery revenue | | 35,301 | | | 35,301 | | | | | 35,301 |
| All other state revenue | | 549,345 | | | 549,345 | | | | | 549,345 |
| Local revenue: | | | | | | | | | | |
| Cash in-lieu of property taxes | | 1,672,359 | | | 1,672,359 | | | | | 1,672,359 |
| Interest income | 4,309 | | | | 4,309 | | 233 | | | 4,542 |
| All other local revenue | 1,854 | 11,127 | | | 12,981 | | | | | 12,981 |
| Subtotal | 1,019,515 | 2,827,231 | 312,500 | 125,000 | 4,284,246 | | 232,233 | 460,004 | (1,139,617) | 3,836,866 |
| Net assets released from restrictions | | 275,480 | | | 275,480 | | | | | 275,480 |
| Total support and revenue | 1,019,515 | 3,102,711 | 312,500 | 125,000 | 4,559,726 | | 232,233 | 460,004 | (1,139,617) | 4,112,346 |
| PROGRAM EXPENSES | | | | | | | | | | |
| Educational programs | | 2,885,213 | 426,917 | 45,648 | 3,357,778 | | | 621,639 | (1,139,617) | 2,839,800 |
| SUPPORTING SERVICES | | | | | | | | | | |
| Site support | 198,060 | | | | 198,060 | | | | | 198,060 |
| Program development and expansion | 300,165 | | | | 300,165 | | | | | 300,165 |
| Administration and general | 154,622 | | | | 154,622 | | | | | 154,622 |
| Total supporting services | 652,847 | | | | 652,847 | | | | | 652,847 |
| Total expenses | 652,847 | 2,885,213 | 426,917 | 45,648 | 4,010,625 | | | 621,639 | (1,139,617) | 3,492,647 |
| Increase (Decrease) in Unrestricted Net Assets | 366,668 | 217,498 | (114,417) | 79,352 | 549,101 | | 232,233 | (161,635) | | 619,699 |
| CHANGES IN TEMPORARILY RESTRICTED NET ASSETS: | | | | | | | | | | |
| State revenue | | 159,975 | | | 159,975 | | | | | 159,975 |
| Federal revenue | | 113,041 | | | 113,041 | | | | | 113,041 |
| Net assets released from restrictions | | (275,480) | | | (275,480) | | | | | (275,480) |
| Increase (Decrease) in Temporarily Restricted Net Assets | | (2,464) | | | (2,464) | | | | | (2,464) |
| INCREASE (DECREASE) IN NET ASSETS | 366,668 | 215,034 | (114,417) | 79,352 | 546,637 | | 232,233 | (161,635) | | 617,235 |
| NET ASSETS - Beginning of Year | | 396,350 | | | 396,350 | | | | | 396,350 |
| Reclassifications** | | (461,225) | | | (461,225) | | | 461,225 | | |
| NET ASSETS (DEFICIT) - End of Year | \$ 366,668 | \$ 150,159 | \$ (114,417) | \$ 79,352 | \$ 481,762 | \$ | \$ 232,233 | \$ 299,590 | \$ | \$ 1,013,585 |

** \$461,225 of beginning assets was transferred from Rocketship Mateo Sheedy to Locust LLC

The accompanying notes are an integral part of these financial statements.