

**KIPP STAR COLLEGE PREP
CHARTER SCHOOL**

FINANCIAL STATEMENTS

JUNE 30, 2006

KIPP STAR COLLEGE PREP CHARTER SCHOOL

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GOLDSTEIN GOLUB KESSLER LLP

Certified Public Accountants and Consultants

INDEPENDENT AUDITOR'S REPORT

The Board of Trustees
KIPP STAR College Prep Charter School

We have audited the accompanying statement of financial position of KIPP STAR College Prep Charter School (the "School") as of June 30, 2006 and 2005, and the related statements of activities, functional expenses, and cash flows for the years then ended. These financial statements are the responsibility of the School'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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those 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 financial statements referred to above present fairly, in all material respects, the financial position of KIPP STAR College Prep Charter School as of June 30, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report, dated September 26, 2006, on our consideration of the School's internal control over financial reporting, and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and on compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Goldstein Golub Kessler LLP

GOLDSTEIN GOLUB KESSLER LLP

September 26, 2006

KIPP STAR COLLEGE PREP CHARTER SCHOOL

STATEMENT OF FINANCIAL POSITION

June 30,	2006	2005
ASSETS		
Cash and Cash Equivalents	\$ 950,205	\$673,160
Grants and Contracts Receivable	146,449	184,995
Property and Equipment, net	255,217	131,423
Prepaid Expenses and Other Assets	28,049	8,075
Total Assets	\$1,379,920	\$997,653
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable and accrued expenses	\$ 132,708	\$234,535
Capital lease obligation	76,063	
Due to related parties	54,553	25,328
Total liabilities	263,324	259,863
Contingency		
Net Assets:		
Unrestricted	986,616	737,790
Temporarily Restricted	129,980	
Total net assets	1,116,596	737,790
Total Liabilities and Net Assets	\$1,379,920	\$997,653

See Notes to Financial Statements

KIPP STAR COLLEGE PREP CHARTER SCHOOL

STATEMENT OF ACTIVITIES

Year ended June 30,	2006			2005		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
Operating revenue:						
State and local per pupil operating revenue	\$2,230,288		\$2,230,288	\$1,444,175		\$1,444,175
Government grants	250,116		250,116	71,666		71,666
Total operating revenue	2,480,404		2,480,404	1,515,841		1,515,841
Operating expenses:						
Program services:						
School operations	2,219,843		2,219,843	1,276,879		1,276,879
Total program services	2,219,843		2,219,843	1,276,879		1,276,879
Supporting services:						
Management and general	182,982		182,982	316,172		316,172
Fund-raising	74,405		74,405	64,864		64,864
Total supporting services	257,387		257,387	381,036		381,036
Total operating expenses	2,477,230		2,477,230	1,657,915		1,657,915
School surplus (operating deficit)	3,174		3,174	(142,074)		(142,074)
Other revenue and expenses:						
Contributions and grants	5,019	\$ 299,980	304,999	259,125		259,125
Interest and other income - net	33,252		33,252	1,089		1,089
Donated services	37,381		37,381	31,275		31,275
Net assets released from restrictions	170,000	(170,000)		316,201	\$(316,201)	
Change in net assets	248,826	129,980	378,806	465,616	(316,201)	149,415
Net assets at beginning of year	737,790		737,790	272,174	316,201	588,375
Net assets at end of year	\$ 986,616	\$ 129,980	\$1,116,596	\$ 737,790	\$ - 0 -	\$ 737,790

See Notes to Financial Statements

KIPP STAR COLLEGE PREP CHARTER SCHOOL

STATEMENT OF FUNCTIONAL EXPENSES

Year ended June 30, 2006

	Program Services		Supporting Services		Total Expenses
	School Operations	Management and General	Fund-raising	Total Supporting Services	
Salaries	\$1,176,885	\$105,716	\$59,690	\$165,406	\$1,342,291
Payroll taxes and employee benefits	229,545	21,143	11,938	33,081	262,626
Equipment	23,663				23,663
Professional fees	149,480	54,095	124	54,219	203,699
Supplies and materials	141,236	966	2,285	3,251	144,487
Telephone and internet	26,372	133		133	26,505
Insurance	37,550				37,550
Food	28,390	144	37	181	28,571
Field lessons	269,921				269,921
Staff development	37,076	688	193	881	37,957
Fees	3,224	97	138	235	3,459
Other					
Depreciation	96,501				96,501
	<u>2,219,843</u>	<u>\$182,982</u>	<u>\$74,405</u>	<u>\$257,387</u>	<u>\$2,477,230</u>
Management and general	182,982				
Fund-raising	74,405				
Subtotal	<u>\$2,477,230</u>				
Total number of students	248				
Average cost per student	<u>\$ 9,989</u>				

See Notes to Financial Statements

KIPP STAR COLLEGE PREP CHARTER SCHOOL

STATEMENT OF FUNCTIONAL EXPENSES

Year ended June 30, 2005

	Program Services		Supporting Services		Total Expenses
	School Operations	Management and General	Fund-raising	Total Supporting Services	
Salaries	\$ 716,471	\$213,133	\$57,774	\$270,907	\$ 987,378
Payroll taxes and employee benefits	139,598	17,299	4,311	21,610	161,208
Equipment	19,501	1,755	1,756	3,511	23,012
Professional fees	34,322	43,836	8	43,844	78,166
Building costs	4,653				4,653
Supplies and materials	146,871	4,557		4,557	151,428
Telephone and internet	8,117	2,465	1,015	3,480	11,597
Insurance	26,175				26,175
Food	14,885				14,885
Field lessons	116,776				116,776
Staff development	16,730				16,730
Fees		3,267		3,267	3,267
Other		29,860		29,860	29,860
Depreciation	32,780				32,780
	<u>1,276,879</u>	<u>\$316,172</u>	<u>\$64,864</u>	<u>\$381,036</u>	<u>\$1,657,915</u>
Management and general	316,172				
Fund-raising	64,864				
Subtotal	<u>\$ 1,657,915</u>				
Total number of students	167				
Average cost per student	<u>\$ 9,928</u>				

See Notes to Financial Statements

KIPP STAR COLLEGE PREP CHARTER SCHOOL

STATEMENT OF CASH FLOWS

Year ended June 30,	2006	2005
Cash flows from operating activities:		
Change in net assets	\$ 378,806	\$ 149,415
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	96,501	32,780
Write-off of property and equipment		15,273
Write-off of uncollectible receivables		29,860
Changes in operating assets and liabilities:		
Decrease (increase) in grants and contracts receivable	38,546	(5,508)
(Increase) decrease in prepaid expenses and other assets	(19,974)	2,153
(Decrease) increase in accounts payable and accrued expenses	(101,827)	195,495
Increase in due to related parties	29,225	25,328
Net cash provided by operating activities	421,277	444,796
Cash used in investing activity - purchases of property and equipment	(114,137)	(123,925)
Cash used in financing activity - payments made on capital lease obligations, net of proceeds	(30,095)	
Net increase in cash and cash equivalents	277,045	320,871
Cash and cash equivalents at beginning of year	673,160	352,289
Cash and cash equivalents at end of year	\$ 950,205	\$ 673,160
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	\$ 4,257	
Supplemental schedule of noncash investing and financing activity:		
Purchase of equipment financed by capital lease	\$ 106,158	

See Notes to Financial Statements

KIPP STAR COLLEGE PREP CHARTER SCHOOL

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

**1. PRINCIPAL
BUSINESS
ACTIVITY AND
SUMMARY OF
SIGNIFICANT
ACCOUNTING
POLICIES:**

KIPP STAR College Prep Charter School (the "School") is an education corporation that operates as a charter school in the borough of Manhattan (Harlem), New York City. On March 25, 2003, the Board of Regents of the University of the State of New York for and on behalf of the State Education Department granted the School a provisional charter valid for a term of five years from the effective date of March 25, 2003 and renewable upon expiration. The School's mission is to equip students with the academic and character skills necessary to succeed in high school, college and the competitive world beyond.

In fiscal year 2006, the School operated classes for students in grades five through seven.

The New York City Department of Food Services provides free and reduced-price lunches and New York City Department of Transportation provides transportation vouchers directly to a majority of the School's students. Amounts with respect to these items are not included in these financial statements.

The financial statements of the School have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America.

The financial statements of the School reflect contributions received from the public and other organizations.

The School reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. 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 restrictions.

Unrestricted net assets are not restricted by donors or the donor-imposed restrictions have expired.

Temporarily restricted net assets contain donor-imposed restrictions that permit the organization to use or expend the assets as specified. The restrictions are satisfied either by the passage of time or by action of the organization.

Permanently restricted net assets contain donor-imposed restrictions that stipulate the resources be maintained permanently, but permit the organization to use, or expend, part or all of the income derived from the donated assets for either specified or unspecified purposes.

Revenue from the state and local governments resulting from the School's charter status and based on the number of students enrolled is recorded when services are performed in accordance with the charter agreement. Federal and state funds are recorded by the School when expenditures are incurred and billable.

Revenue from other government grants to which the School is entitled is recognized mostly on student enrollment. Some grants are provided for specific educational endeavors which are not based on student enrollment and are recorded when related expenditures are incurred by the School.

KIPP STAR COLLEGE PREP CHARTER SCHOOL

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

A number of volunteers have made a contribution of their time to the School. These in-kind contributions have not been reflected in the financial statements since they do not meet the criteria for recognition under Statement of Financial Accounting Standards No. 116, *Accounting for Contributions Received and Contributions Made*.

The School maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The School has not experienced any losses in such accounts.

The School considers all highly liquid instruments purchased with a maturity of six months or less to be cash equivalents. Cash equivalents consist of a United States Treasury Bill.

Property and equipment is recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the respective assets. Property and equipment acquired with certain government contract funds are recorded as expenses pursuant to the terms of the contract.

Fixed assets acquired under capital leases are recorded in property and equipment with corresponding obligations carried in liabilities. The amount capitalized is the lower of the present value of the minimum lease payments or the fair value of the leased asset. Amortization on assets leased under capital leases is recorded on a straight-line basis over the estimated useful life of the asset or the term of the lease, depending on the criteria used to capitalize the lease.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates by management. Actual results could differ from those estimates and the differences could be significant.

2. RELATED PARTY TRANSACTIONS:

The Knowledge is Power Program Foundation ("KIPP Foundation") is a national, nonprofit organization that trains school leaders to open and run academically rigorous public schools.

The School is a member of KIPP Foundation's KIPP Network of Schools and, as such, is eligible for a range of benefits and fee-based services.

The School has entered into a trademark license agreement with KIPP Foundation subject to a license fee of 1% of annual per pupil operating revenue not to exceed \$30,000. For the year ended June 30, 2006, the School incurred trademark license fees amounting to \$22,074.

The back-office functions are centralized and handled by KIPP NYC's shared services team, whose salaries are paid by KIPP Academy Charter School. Amounts due to related parties represent short-term timing differences of pending settlements.

KIPP STAR COLLEGE PREP CHARTER SCHOOL

NOTES TO FINANCIAL STATEMENTS June 30, 2006

3. PROPERTY AND EQUIPMENT, NET:

Property and equipment, net, at cost, consists of the following:

	2006	2005	Estimated Useful Life
Furniture and fixtures	\$ 19,261	\$ 17,250	5 years
Equipment and other	385,480	167,196	3 to 5 years
	404,741	184,446	
Less accumulated depreciation and amortization	(149,524)	(53,023)	
	\$ 255,217	\$131,423	

Property and equipment includes two copiers acquired under capital leases. As of June 30, 2006, the leased copiers are reflected at a cost of \$106,158 and related accumulated amortization amounted to \$24,018.

4. TAX STATUS:

The Internal Revenue Service has determined that the School is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

5. AGREEMENT FOR SCHOOL FACILITY:

The School occupies 24,000 square feet of space in its original facility since inception. The School is still negotiating formal terms with the New York City Department of Education for this dedicated and shared space at PS 125, a New York City public school, located at West 123rd Street, New York, New York. The facility is provided to the School at no cost. The School will be responsible for any overtime-related costs for services provided beyond regular opening hours.

6. OPERATING EXPENSES:

Operating expenses are presented in the statement of functional expenses classified according to the significant program activity related to the purpose for which the School exists or supporting service.

The significant activities are:

School operations

Represents work (time and materials) that is specifically related to or necessary for the programming aspects of the School. If the activities and related costs directly affect students or parents then it falls under this program.

The significant supporting services are:

Management and general

Represents work (time and materials) that is specifically related to running the non-programmatic/back-end operational functions of the School including, but not limited to human resources, finance, technology and payroll.

KIPP STAR COLLEGE PREP CHARTER SCHOOL

NOTES TO FINANCIAL STATEMENTS June 30, 2006

Fund-raising

Represents work (time and materials) associated with the School's fund-raising efforts including but not limited to annual mailings, donor meetings and events.

7. CAPITAL LEASE OBLIGATIONS:

The School leases two copiers under capital leases expiring in July 2008. The leases require monthly payments of principal and interest ranging from \$1,009 - \$1,475, at imputed interest rates of 5.7% and 6.0% per annum. Future minimum lease payments under the leases are as follows:

Year ending June 30,

2007	\$29,814
2008	29,814
2009	18,708
2010	4,424

	82,760
Less amount representing interest	(6,697)
	\$76,063

8. CONTINGENCY:

Certain grants and contracts may be subject to audit by the funding sources. Such audits might result in disallowances of costs submitted for reimbursement. Management is of the opinion that such cost disallowances, if any, will not have a material effect on the accompanying financial statements. Accordingly, no amounts have been provided in the accompanying financial statements for such potential claims.

9. TEMPORARILY RESTRICTED NET ASSETS:

Temporarily restricted net assets are available for the following purpose or periods:

June 30, 2006

Time restricted for future period	\$129,980
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During the years ended June 30, 2006 and 2005, respectively, net assets were released from donor restrictions by incurring expenses satisfying the following temporarily restricted purposes:

School programming for fiscal '04-'05 school year	\$ 63,156
Startup and implementation grant	250,545
Student orchestra	2,500
Extended day and year and special education programs	\$160,000
Literacy program	10,000
	\$170,000
	\$316,201



GOLDSTEIN GOLUB KESSLER LLP

Certified Public Accountants and Consultants

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Board of Trustees
KIPP STAR College Prep Charter School

We have audited the financial statements of KIPP STAR College Prep Charter School (the "School") as of June 30, 2006 and 2005 and for the years then ended, and have issued our report thereon dated September 26, 2006. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting - In planning and performing our audits, we considered the School's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

We noted other matters involving the internal control over financial reporting which have been reported to management in a separate letter dated September 26, 2006.

Compliance and Other Matters - As part of obtaining reasonable assurance about whether the School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, board of trustees, management, the New York State Education Department and the Board of Regents of the University of the State of New York and is not intended to be and should not be used by anyone other than these specified parties.

Goldstein Golub Kessler LLP

GOLDSTEIN GOLUB KESSLER LLP

September 26, 2006