



NEWSCHOOLS VENTURE FUND

Financial Statements

August 31, 2003

(With Independent Auditors' Report Thereon)



Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

The Board of Directors
NewSchools Venture Fund:

We have audited the accompanying balance sheet of NewSchools Venture Fund (the Fund) as of August 31, 2003, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior eight-month period summarized comparative information has been derived from NewSchools Venture Fund's 2002 financial statements which were audited by other auditors whose report thereon dated June 10, 2003 expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 audit provides 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 NewSchools Venture Fund as of August 31, 2003, and the change in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

November 21, 2003



NEWSCHOOLS VENTURE FUND

Balance Sheet

August 31, 2003

(with comparative financial information as of August 31, 2002)

	<u>2003</u>	<u>2002</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 5,978,827	2,777,444
Short-term investments	—	1,842,861
Contributions receivable	15,262,000	—
Interest in net assets of support organization	1,000,000	—
Other current assets	—	10,472
Total current assets	<u>22,240,827</u>	<u>4,630,777</u>
Property and equipment, net	51,848	43,502
Contributions receivable, noncurrent portion, net	6,854,041	—
Note receivable	1,000,000	1,000,000
Investment securities	417,581	332,890
Other assets	12,263	12,263
Total assets	<u>\$ 30,576,560</u>	<u>6,019,432</u>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	\$ 42,847	39,967
Grants payable	483,000	—
Accrued compensation	207,129	46,524
Total liabilities	<u>732,976</u>	<u>86,491</u>
Net assets:		
Unrestricted	4,365,607	5,431,563
Temporarily restricted	25,477,977	501,378
Total net assets	<u>29,843,584</u>	<u>5,932,941</u>
Total liabilities and net assets	<u>\$ 30,576,560</u>	<u>6,019,432</u>

See accompanying notes to financial statements.

NEWSCHOOLS VENTURE FUND

Statement of Activities

Year ended August 31, 2003

(with summarized financial information for the eight-month period ended August 31, 2002)

	2003			2002
	Unrestricted	Temporarily restricted	Total	
Revenues, gains and other support:				
Contributions	\$ 2,029,826	27,141,041	29,170,867	1,558,630
Program service fees	119,732	—	119,732	—
Investment income	126,234	—	126,234	(1,831,300)
Net assets released from restrictions	2,164,442	(2,164,442)	—	—
Total revenues, gains and other support	4,440,234	24,976,599	29,416,833	(272,670)
Expenses:				
Program services	3,100,842	—	3,100,842	1,964,955
Supporting services	2,405,348	—	2,405,348	1,260,698
Total expenses	5,506,190	—	5,506,190	3,225,653
Increase (decrease) in net assets	(1,065,956)	24,976,599	23,910,643	(3,498,323)
Net assets, beginning of year	5,431,563	501,378	5,932,941	9,431,264
Net assets, end of year	\$ 4,365,607	25,477,977	29,843,584	5,932,941

See accompanying notes to financial statements.

NEWSCHOOLS VENTURE FUND

Statement of Cash Flows

Year ended August 31, 2003

(with comparative financial information for the eight-month period ended August 31, 2002)

	<u>2003</u>	<u>2002</u>
Cash flows from operating activities:		
Increase (decrease) in net assets	\$ 23,910,643	(3,498,323)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	26,161	12,820
Net unrealized and realized (gain) loss on investments	(34,982)	1,905,147
Changes in operating assets and liabilities:		
Contribution receivable	(22,116,041)	—
Interest in net assets of support organization	(1,000,000)	—
Other current assets	10,472	2,028
Other assets	—	(9,659)
Accounts payable	2,880	15,638
Grants payable	483,000	—
Accrued compensation	160,605	11,373
Net cash provided by (used in) operating activities	<u>1,442,738</u>	<u>(1,560,976)</u>
Cash flows from investing activities:		
Purchases of property and equipment	(34,507)	(22,894)
Purchases of securities	(84,691)	(64,169)
Purchases of short-term investments	(1,691,619)	(10,480,314)
Proceeds from sale of short-term investments	1,179,099	5,889,699
Proceeds from maturity of short-term investments	2,390,363	3,898,949
Net cash provided by (used in) investing activities	<u>1,758,645</u>	<u>(778,729)</u>
Net increase (decrease) in cash and cash equivalents	3,201,383	(2,339,705)
Cash and cash equivalents at beginning of year	<u>2,777,444</u>	<u>5,117,149</u>
Cash and cash equivalents at end of year	\$ <u><u>5,978,827</u></u>	<u><u>2,777,444</u></u>

See accompanying notes to financial statements.

NEWSCHOOLS VENTURE FUND

Notes to Financial Statements

August 31, 2003

(with summarized comparative information as of August 31, 2002)

(1) Organization and Nature of Operations

NewSchools Venture Fund (the Fund) was founded in 1998 under the laws of the State of California. The Fund's mission is to improve public education by identifying and supporting the most promising education ventures in the country and by creating a nationwide network of education entrepreneurs, educators, leaders and others committed to improving schools. In furtherance of these goals, the Fund makes grants and loans to nonprofit entities engaged in improving public education and makes investments in for-profit businesses engaged in improving public education. The Fund also provides technical assistance to both nonprofit entities and for-profit enterprises, working to improve public education. The Fund is supported through donor contributions.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting. Balances and transactions are reported according to the existence or absence of donor-imposed restrictions. Accordingly, balances and transactions are reported in the following classes of net assets:

Permanently Restricted Net Assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Fund.

Temporarily Restricted Net Assets – Net assets subject to donor-imposed stipulations that may or will be met by actions of the Fund and/or the passage of time. When a donor-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 – Net assets not subject to donor-imposed stipulations.

Revenues are reported as increases in unrestricted net assets unless use of related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations or temporary restrictions in net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

(b) Contributions

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of the discount is recorded as additional contribution revenue over the payment period.

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Notes to Financial Statements

August 31, 2003

(with summarized comparative information as of August 31, 2002)

All contributions are considered to be available for the general programs of the Fund unless specifically restricted by the donor. The Fund reports contributions of cash and other assets as restricted support if they are received with donor stipulations that limit the use of donated assets. Donor-restricted contributions are recorded in the temporarily restricted net asset class and then reclassified to the unrestricted class as the restrictions are met.

(c) *Contributed Services*

The Fund records revenue for voluntary donations of services when those services create or enhance nonfinancial assets or require specialized skills provided by individuals possessing those skills and which would be typically purchased if not provided by donation. Contributed services reported for the year ended August 31, 2003 amounted to \$29,826. During the period ended August 31, 2002, there were no contributed services meeting the requirements for recognition in the financial statements.

(d) *Grants*

Unconditional grants made by the Fund are accrued as expenses and are recognized in the year in which they are approved by the Board of Directors. Conditional grants are not recorded until the conditions are substantially met.

(e) *Cash and Cash Equivalents*

Cash and cash equivalents include cash on hand and money market accounts. The Fund considers all investments with an original maturity of ninety days or less to be cash equivalents.

(f) *Investments*

Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the balance sheet. Investments without readily determinable fair values are reported at historical cost, unless it can reasonably be expected that the organization will suffer a loss on the disposition of an investment, in which case a provision for the loss is made in the period in which the decline in value occurs. Unrealized gains and losses are included in the change in net assets in the period such gains and losses are incurred.

(g) *Property and Equipment*

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is provided using the straight-line method over the estimated useful lives of the assets, ranging from three to seven years. Renewals and betterments that amend the economic useful lives of the related assets are capitalized. Other expenditures for repairs and maintenance are charged to expense as incurred.

NEWSCHOOLS VENTURE FUND

Notes to Financial Statements

August 31, 2003

(with summarized comparative information as of August 31, 2002)

(h) 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(i) Tax-Exempt Status

The Fund has been granted tax-exempt status by the Internal Revenue Service under Internal Revenue Code (IRC) Section 501(c)(3). Gifts to the Fund are deductible for income tax purposes under IRC Section 170(b)(1)(A).

(i) Reclassifications

Certain reclassifications have been made in the 2002 financial statements to conform to the presentation used in the 2003 financial statements.

(3) Contributions Receivable

Contributions receivable as of August 31, 2003 consists of the following:

Receivable due in less than one year	\$ 15,262,000
Receivable due in one to five years	<u>7,000,000</u>
Total contributions receivable	22,262,000
Less:	
Amount representing discount at 1.59% and 2.15% for receivables due in one to two years and two to three years, respectively	<u>(145,959)</u>
Net contributions receivable	<u>\$ 22,116,041</u>

The Fund received conditional promises from two foundations amounting to \$13.45 million. Both grants will be awarded to the Fund based on the acceptability of the projects proposed by the Fund to the foundations.

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(4) Property and Equipment

Property and equipment as of August 31, 2003 and 2002 are as follows:

	<u>2003</u>	<u>2002</u>
Computer equipment	\$ 64,637	48,410
Printers	7,978	7,978
Furniture and fixtures	38,969	20,689
	<u>111,584</u>	<u>77,077</u>
Accumulated depreciation	<u>(59,736)</u>	<u>(33,575)</u>
Property and equipment, net of depreciation	\$ <u>51,848</u>	<u>43,502</u>

(5) Program Related Investments

The Fund has created a pool of capital used to make loans to nonprofits (predominantly, but not exclusively IRC Section 501(c)(3) organizations) engaged in working to improve public education; and to invest in for-profit businesses with a strong potential to improve public education.

Program related investments as of August 31, 2003 and 2002 were as follows:

	<u>2003</u>	<u>2002</u>
Note receivable from a foundation, bearing interest at 3%, due on September 21, 2004	\$ <u>1,000,000</u>	<u>1,000,000</u>
Investment in educational enterprise, 454,545 shares of preferred stock and 45,455 shares of common stock	\$ 143,731	143,731
Investment in educational enterprise, 166,667 shares of preferred stock	125,000	125,000
Investment in educational enterprise, 198,467 and 85,546 shares of preferred stock in 2003 and 2002, respectively	<u>148,850</u>	<u>64,159</u>
Total investment securities	\$ <u>417,581</u>	<u>332,890</u>

(6) Lease Commitments

The Fund leases an office under a noncancelable lease agreement expiring May 31, 2005. Rental expense for this lease was \$72,309 for 2003. Future minimum lease payments under this lease are:

2004	\$ 71,368
2005	<u>55,181</u>
Total	\$ <u>126,549</u>

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(with summarized comparative information as of August 31, 2002)

(7) **Related Party Transactions**

During the year ended August 31, 2003, the Fund recognized contribution revenue of \$2,000,000 from a member of the Board of Directors of the Fund, through NewSchools Fund Supporting Organization, Inc. (Support Organization). The members of the Board of the Support Organization are the members of the Executive Committee of the Board of Directors of the Fund. In accordance with Statement of Financial Accounting Standards (SFAS) No. 136, *Transfer of Assets to a Not-for-Profit Organization or Charitable Trust that Raises or Holds Contributions for Others*, this entire contribution has been recognized as revenue of the Fund for the year ended August 31, 2003. The portion not yet received by the Fund of \$1 million has been recorded under interest in net assets of support organization as of August 31, 2003.

The Fund received legal services contributed by a law firm, which amounted to \$29,826 and was reported as an unrestricted contribution for the year ended August 31, 2003. One of the partners of the law firm serves as a member of the Board of Directors of the Fund.

During the fiscal year ended August 31, 2002, the Fund received a contribution totaling \$500,000 from a member of the Board of Directors of the Fund.