

**CHARTER SCHOOL FACILITIES PROGRAM  
PROP 1D-2014 FUNDING ROUND  
STAFF SUMMARY REPORT – APRIL 2015**

<b>Applicant/Obligor:</b>	KIPP Bay Area Schools
<b>Project School:</b>	KIPP Heartwood Academy
<b>CDS (County – District – School) Code:</b>	43-60369-0106633
<b>School Address/Proposed Site:</b>	1250 S. King Road, San Jose, CA, 95122
<b>Type of Project:</b>	Rehabilitation
<b>County:</b>	Santa Clara
<b>District in which Project is Located:</b>	Alum Rock Union Elementary School District
<b>Charter Authorizer:</b>	Alum Rock Union Elementary School District
<b>Total OPSC Project Cost:</b>	\$8,807,194
<b>State Apportionment (50% Project Cost):</b>	\$4,403,597
<b>Lump Sum Contribution:</b>	N/A
<b>Total CSFP Financed Amount:</b>	\$4,403,597
<b>Length of CSFP Funding Agreement:</b>	30 years
<b>Assumed Interest Rate:</b>	3.00%
<b>Estimated Annual CSFP Payment:</b>	\$224,668
<b>First Year of Occupancy of New Project:</b>	2017-18

**Staff Recommendation:** Staff recommends that the California School Finance Authority (CSFA) Board determine that KIPP Bay Area Schools (KIPP), on behalf of KIPP Heartwood Academy (Heartwood) is financially sound for the Charter School Facilities Program (Program) Preliminary and/or Advance Apportionment, but not Final Apportionment, under the Program. This determination as it relates to a Preliminary Apportionment is in place for six months and assumes no financial, operational, or legal material findings within this time period. This determination of financial soundness also is contingent upon KIPP agreeing to have its CSFP payments intercepted at the state level, pursuant to sections 17199.4 and 17078.57(a)(1)(A) of the Education Code. Staff recommends that the CSFA Board direct staff to immediately notify the Office of Public School Construction (OPSC) and the State Allocation Board regarding this determination.

**Background:** KIPP has previously applied, and received CSFP funds, for one other charter school, KIPP King Collegiate High (King). In May 2008, King received a Proposition 1D preliminary apportionment in the amount of \$11,041,874 for new construction and \$3,607,942 for rehabilitation. The total project costs for the new construction project was reassessed at \$8,282,844, and OPSC issued a Final Release of Funds on August 16, 2012. An Advance Release was issued in September 2013 for the rehabilitation project; however, the Final Release is pending with a Final Conversion deadline of November 13, 2015. In evaluating KIPP's ability to repay the local matching share in the form of a loan, the annual loan payment amount will be based on project costs represented by the sum of the preliminary apportionment amount for Heartwood, \$8,807,194, and total project costs (both new construction and rehabilitation for King), which is \$11,890,786, or \$20,697,980. The

amortized loan payment amount will also be based on a 30-year loan at a fixed 3% annual interest rate.

**Application Highlights:** Below staff has highlighted key criteria that were evaluated when conducting our financial soundness review of KIPP, on behalf of Heartwood. Detailed information is contained in the body of the report.

<b>Criteria</b>	<b>Comments</b>
<b>EMO Information</b>	
Demographic Information	<ol style="list-style-type: none"> <li>1. KIPP has shown substantial and consistent growth since 2010-11, growing from 2,299 students in 2010-11, across seven schools, to 3,285 students across 10 schools in 2014-15, representing growth of 43% over four years, or an average of approximately 11% per year</li> <li>2. Largely through the addition of new schools and addition of new grades each subsequent year (for all new schools, 12 in total), for 2015-16 through 2018-19, KIPP is projecting aggregate enrollment of 3,965, 5,065, 6,701, and 8,267, respectively, representing overall growth of approximately 250%, or approximately 62% per year over four years .</li> </ol>
Debt Service Coverage	Based on KIPP’s financial projections, the projected debt service coverage levels for the anticipated combined CSFP lease payment in 2018-19 and 2019-20 are 199.3% and 1,384%, respectively. KIPP will need to receive at least 94% (\$8.76 million) of expected contributions in 2017-18 in order to meet the 100% projected debt service coverage ratio threshold. In 2019-20, KIPP will need to receive at least 49% (\$6.44 million) of contributions to maintain 100% projected debt service coverage.
Other Financial Factors	<ol style="list-style-type: none"> <li>1. Measured as a percentage of total revenues, contributions from 2018-19 and 2019-20 are projected to average 10% annually.</li> <li>2. KIPP’s net working capital (NWC) as of June 30, 2014 was exceptionally high at \$33.90 million, or 130.2% of total expenses, up from \$23.01 million, or 97.2% of total expenses as of June 30, 2013. Staff considers NWC equivalent to at least 5.0% of total expenses to be sufficient.</li> </ol>
Student Performance	<ol style="list-style-type: none"> <li>1. With respect to API growth scores and meeting of API growth targets, for 2009-10 through 2012-13, where data was available, 100% of KIPP schools achieved API growth scores of greater than 800, and 100% met their API growth targets.</li> <li>2. With respect to KIPP’s statewide and similar schools rankings (base API scores), during the reported years, 2009-10 through 2012-13, where data was available, 100% of schools (7 schools) had statewide and similar schools rankings of “5” or greater In addition, during each of 2011-12 and 2012-13, 100%</li> </ol>

	of schools (7 schools) had both rankings of “8” or greater.
<b>School Information</b>	
Eligibility Criteria	Heartwood has met all eligibility criteria: (1) Heartwood commenced operations in 2004-05; (2) KIPP’s charter was renewed in 2011 and is in place through June 2019; (3) KIPP is in good standing with its chartering authority, and in compliance with the terms of its charter.
Student Performance	<ol style="list-style-type: none"> <li>Heartwood met its API growth targets in each of the four most recent reported years, 2009-10 through 2012-13, and had API growth scores of 915, 900, 906, and 922 for each of these years, respectively.</li> <li>In all years reported by CDE based on API base scores, Heartwood had statewide and similar schools rankings of “9” or “10” (“10” = best) with “10” in both rankings in 2009-10, 2010-11, and 2013-14.</li> </ol>
Demographic Information	<ol style="list-style-type: none"> <li>Heartwood’s student enrollment has remained level over the past five years, and KIPP is projecting Heartwood’s enrollment to remain constant at about 414 students through 2018-19.</li> <li>Heartwood’s year-to-year retention rate for 2014-15 was 98.5%, and Heartwood’s ADA rates for 2012-13 and 2013-14 were 98.0% and 98.8%, respectively.</li> </ol>

**Program Eligibility:** On January 12, 2015, at CSFA staff’s request, verification was received from Alum Rock Union Elementary School District (District) confirming that Heartwood (1) is in compliance with the terms of its charter agreements, and (2) is in good standing with its chartering authority. Heartwood’s charter is effective through June 30, 2019.

**Legal Status Questionnaire:** Staff reviewed KIPP’s responses, on behalf of Heartwood, to the questions contained in the Legal Status Questionnaire (LSQ) signed on March 13, 2015. KIPP answered “None” to each of the two questions, indicating that it has no material information to disclose relating to legal or regulatory proceedings, or legal action in which it or any of its affiliates is a named party.

**Project Description:** KIPP is requesting CSFP funding for rehabilitation of an existing facility at 1250 S. King Road, San Jose. The project is expected to include 17 classrooms for grades 5-8. The anticipated project completion date is January 2017, and the anticipated first full year of occupancy of the renovated classrooms is 2017-18, even though the facility will be in use during the process.

**School Organizational Information:** Heartwood began operations in 2004 with 73 fifth graders in July 2004 and was the first public charter school under Alum Rock Union Elementary School District. Heartwood currently serves 413 students in grades 5-8. Heartwood has had its charter renewed twice with its current charter effective through 2019. Heartwood’s target population is represented by a largely underserved community in east Palo Alto, which is reflected by 84% of Heartwood students are eligible for free or reduced-price meals. Heartwood’s demographic profile includes an ethnicity mix of 82%, Latino,

18% Asian, 1% African-American, and 1% “others.” In addition 20% of Heartwood students are considered “English Language Learners.”

**Management Experience for Schools Open Less than Two Years:** Not applicable as Heartwood began operations in 2004-05, exceeding the two years of instruction requirement.

**School Management:** Susana Mena currently is the Principal at KIPP Heartwood Academy. Ms. Mena started her career at KIPP as a founding Business Manager in 2004 and moved into the classroom two years later. During her 10 years at Heartwood, she has had the opportunity to be part of the administration team and the teaching staff. In November of 2010, Ms. Mena served as Interim Principal leading a staff during a transitional phase while maintaining a strong team and high student achievement. Prior to becoming Principal, Ms. Mena made the decision to step down as Interim Principal in order to temporarily go back into the classroom and receive more training. Before her career at KIPP, Ms. Mena worked at the YWCA of Silicon Valley as a Program Manager for Youth Programs that serviced schools in the East Side of San Jose. Ms. Mena holds a Bachelor's degree in Spanish from the University of California, Santa Barbara.

**CMO Organization and Management:** KIPP is a non-profit, public benefit corporation with 501(c)(3) status, founded in 2008 through the consolidation of seven charter schools, which currently operates the following ten public charter schools (middle schools and high schools) in the San Francisco Bay Area: KIPP Bridge Charter; KIPP Bayview Academy; KIPP San Francisco Bay Academy; KIPP San Francisco College Preparatory Academy; KIPP Heartwood Academy; KIPP Heritage Academy; KIPP Prize Preparatory Academy; KIPP San Jose Collegiate; KIPP King Collegiate; and KIPP Summit Academy.

The following table depicts, for each school under KIPP, the opening year, grade levels served, and current student enrollment.

<b>School</b>	<b>Opened</b>	<b>Grades Served</b>	<b>2014-15 Enrollment</b>
KIPP Bridge Charter	Aug. 2007	5-8	340
KIPP Bayview Academy	July 2003	5-8	287
KIPP San Francisco Bay Academy	Aug. 2003	5-8	367
KIPP San Francisco College Prep	Aug. 2013	9-12	255
KIPP Heartwood Academy	Aug. 2004	5-8	414
KIPP Heritage Academy	Aug. 2014	5-8	105
KIPP Prize Preparatory Academy	Aug. 2014	5-8	106
KIPP King Collegiate	Sept. 2007	9-12	529
KIPP San Jose Collegiate	Aug. 2008	9-12	475
KIPP Summit Academy	Aug. 2003	5-8	407
<b>Total</b>			<b>3,285</b>

KIPP Bay Area Schools is associated with the KIPP national network of schools, which has 109 schools across the nation all managed by local, regionalized nonprofits. The KIPP Foundation, located in San Francisco, provides professional development, evaluation, and

advocacy support for all KIPP schools nationwide. KIPP's mission is to operate high-achieving public schools in educationally underserved communities, developing knowledge, skills, and character essential to thrive in college, shape the future, and positively impact the world.

Heartwood was established following the national KIPP model, as set forth by the KIPP Foundation. The hallmarks of the KIPP program include the following five pillars: 1) High Expectations: KIPP schools have clearly defined and measurable high expectations for academic achievement and conduct that make no excuses based on the students' backgrounds. Students, parents, teachers, and staff create and reinforce a culture of achievement and support through a range of formal and informal rewards and consequences for academic performance and behavior; 2) Choice & Commitment: Students, their parents, and the faculty of each KIPP school choose to participate in the program. No one is assigned or forced to attend a KIPP school. Everyone must make and uphold a commitment to the school and to each other to put in the time and effort required to achieve success; 3) More Time: KIPP schools know that there are no shortcuts when it comes to success in academics and life. With an extended school day, week, and year, students have more time in the classroom to acquire the academic knowledge and skills that will prepare them for competitive high schools and colleges, as well as more opportunities to engage in diverse extracurricular experiences; 4) Power to Lead: The principals of KIPP schools are effective academic and organizational leaders who understand that great schools require great school leaders. They have control over their school budget and personnel. They are free to swiftly move dollars or make staffing changes, allowing them maximum effectiveness in helping students learn; 5) Focus on Results: KIPP schools relentlessly focus on high student performance on standardized tests and other objective measures. Just as there are no shortcuts, there are no excuses. Students are expected to achieve a level of academic performance that will enable them to succeed at the nation's best high schools and colleges.

**CMO Management:** Beth Sutkus-Thompson, Executive Director of KIPP Bay Area Schools, is the founding Executive Director of KIPP Bay Area Schools. Previously, she was the West Coast Trailblazer at the KIPP Foundation, where she was responsible for creating and implementing a west coast strategic growth plan for KIPP schools. Prior to her work at the KIPP Foundation, Ms. Sutkus-Thompson was on the founding team of NewSchools Venture Fund. Ms. Sutkus-Thompson is a graduate of The Broad Residency in Urban Education, a management development program for emerging executives working in urban school districts and charter management organizations. Ms. Sutkus-Thompson holds a B.A. in Education, and an MBA with a certificate in nonprofit management, all from Stanford University.

Cindy Tsai joined KIPP Bay Area Schools in 2010. As the Director of Regional Operations, she leads the development and sustainability of high-quality operational systems at our schools to support teaching and learning. This includes managing the process for opening new sites, implementing cohesive policies and procedures, and partnering with schools to solve operational challenges. She also negotiates services and contracts on behalf of schools for food service, facilities, insurance, and other necessary materials. Additionally, Cindy leads the recruitment of school-based operations staff and their ongoing professional

development. She received her B.A. in Economics from Pomona College and lives in San Francisco.

**Board Experience:** KIPP Bay Area is governed by a Board of Trustees and currently includes members with a variety of occupations and experiences, as noted below. The Board of Trustees is responsible for variety of functions, which include: Define and refine the organization’s mission, vision, and strategic direction; recruit, support, and evaluate the executive director (e.g., including hire and fire authority); monitor and evaluate the organizations programs and services; and ensure fiscal, legal and ethical integrity and maintain accountability.

<b>Name</b>	<b>Occupation</b>	<b>County of Residence</b>	<b>Term</b>
Jay Allen	EVP, Human Resources, Charles Schwab & Co., Inc.	San Francisco	2012-15
John Philip Coghlan	Former president and CEO of VISA USA	San Francisco	2014-17
Lauren Dutton (Board Chair)	Education consultant	Alameda	2014-17
Chuck Daggs (Board Vice Chair)	Executive Vice President of Wells Fargo's Wealth Management Group	Alameda	2013-16
Andrea Evans	Commissioner, San Francisco Fire Dept.	San Francisco	2013-16
Doris Fisher	Founder Gap, Inc.	San Francisco	Director for life
Laura Fisher	Community Volunteer	San Francisco	2013-16
Abe Friedman	Managing Partner, CamberView Partners	Alameda	2012-15
Ron Gonzales	CEO, Hispanic Foundation Silicon Valley	Santa Clara	2013-16
Sukey Grousbeck	Community Volunteer	Santa Clara	2013-16
Andrea Higuera-Ballard	Community Volunteer	San Mateo	2013-16
Ken Hirsch	Managing Director and Partner, Goldman Sachs	Santa Clara	2012-15
Tom Holland	COO, Sunrun, Inc.	San Francisco	2012-15
Rick Intrater	Founder and CEO of Long Term Solutions	San Francisco	2012-15
Tonia Karr	Community Volunteer	San Francisco	2013-16
Mimi Kingsley	Community Volunteer	San Francisco	2012-15
Katie Paige	Grants Chair, Charles and Helen Schwab Foundation	San Francisco	2013-16
Satya Patel	Director at Twitter Inc.	San Mateo	2014-17
David Paulson	Partner with Jones Day LLP	San Francisco	2013-16
Jenny Shimizu Risk	Community Volunteer	San Mateo	2012-15
Mary Robinson	Fund development consultant	Marin	2012-15
Lisa Sobrato Sonsini	Board President, Sobrato	Santa Clara	2013-16

	Family Foundation		
Grace Voorhis	Former Partner at Morgan Stanley Venture Partners	San Mateo	2012-15
Ted Williams	Managing Partner, Springbok Partners	Marin	2013-16

**Student Performance:** Pursuant to SB X51 (2010), a designated California State Commission was given the authority to review the Common Core State Standards (Standards), as promulgated by the U.S. Department of Education, and make recommendations to the California Board of Education (Board). This resulted in the Board’s adoption of the Standards for purposes of statewide accountability on academic performance. Although this adoption does not directly require all Local Educational Agencies to adopt the standards, pursuant to Education Code, Sections 52060 through 52077, in order for districts to receive funding through their Local Control Funding Formulas (LCFFs), school districts must submit “Local Control and Accountability Plans” (LCAPs) to their respective county offices of education that address State and local educational priorities, and, pursuant to Education Code, Section 52060(d)(2), these priorities must include Common Core State Standards.

Assessments based on the Standards are derived from the “Smarter Balanced Assessment System,” a test that has been field tested during 2014 and is planned for initial implementation in spring 2015 for purposes of establishing a baseline for comparing academic performance between schools, and subsequent improvement. As such, the Standards do not currently provide metrics for comparing academic performance between schools.

As a result of the transition to Common Core Standards, CDE’s Accountability Progress Reporting has significantly changed in that, since 2012-13, Growth Academic Performance Index (API) and Base API reporting has been temporarily suspended, API rankings are no longer being reported, and Adequate Yearly Progress (AYP) reporting pursuant the No Child Left Behind Act of 2001 has been limited to public high schools receiving Title 1 funding when they meet specific enrollment criteria.

Although staff recognizes the limitation in the lack of current available academic performance reports, because of the implications for student enrollment stability and growth, staff is nevertheless considering academic performance as an indicator for financial soundness with this limitation in mind.

Staff notes that the percent-proficient threshold requirement for AYP, both for English-language arts and mathematics, in accordance with the Elementary and Secondary Education Act (ESEA), has reflected increases each year up to 2012-13 when the percent-proficient requirement in both mathematics and English-language arts reached approximately 89%.<sup>[1]</sup> Therefore, with each successive year, charter schools have been increasingly challenged in meeting all AYP criteria. This requirement applies to both school

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<sup>[1]</sup> Information regarding AYP requirements are derived from the California Department of Education’s “2013 Adequate Yearly Progress Report Information Guide.”

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wide performance and performance of each numerically significant subgroup within any school.

Heartwood has more than four years of reported API scores and AYP results, allowing a review of progress and comparison to similar schools. The following table summarizes Heartwood’s student performance for 2009-10 through 2012-13, the four most recent years for which CDE has reported API and AYP results.

KIPP Heartwood Academy	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
<b>ADEQUATE YEARLY PROGRESS (AYP)</b>				
Met All AYP Criteria?	Yes	No	Yes	No
Criteria Met / Required Criteria	21 / 21	16 / 17	17 / 17	16 / 17
Met API Indicator for AYP?	Yes	Yes	Yes	Yes
Met Graduation Rate?	N/A	N/A	N/A	N/A
<b>ACADEMIC PERFORMANCE INDEX (API)</b>				
Met Schoolwide Growth Target?	Yes	Yes	Yes	Yes
Met Comparable Improvement Growth Target?	Yes	Yes	Yes	Yes
Met Both Schoolwide & CI Growth Targets?	Yes	Yes	Yes	Yes
API Base Statewide Rank (10 = best)	10	10	9	9
API Base Similar Schools Rank (10 = best)	10	10	10	10
School's Actual Growth	22	-16	6	15
Similar Schools Median of Actual Growth	11	9	5	N/A
Did School's Growth Exceed Median?	Yes	No	Yes	N/A

Heartwood met its API growth targets in each of the four most recent reported years, 2009-10 through 2012-13, and had API growth scores of 915, 900, 906, and 922 for each of these years, respectively. In all years, based on API base scores, Heartwood had statewide and similar schools rankings of “9” or “10” (“10” = best) with “10” in both rankings in 2009-10 and 2010-11. Heartwood met all AYP criteria in two of the four most recent years reported, 2009-10 and 2012-13. Though not in the table, Heartwood had “10” in both rankings in 2013-14.

Staff also reviewed academic performance data that was available for seven of the ten KIPP schools for 2009-10 through 2012-13, the four most recent years reported by CDE, as shown in the tables below.

<b>KIPP Bay Area Schools - API Growth Scores/Met Schoolwide API Growth Target</b>				
<b>School</b>	<b>2009-10</b>	<b>2010-11</b>	<b>2011-12</b>	<b>2012-13</b>
KIPP Bridge Charter (5-8)	864/Yes	911/Yes	901/Yes	905/Yes
KIPP Bayview Academy (5-8)	825/Yes	867/Yes	864/Yes	838/Yes
KIPP San Francisco Bay Academy (5-8)	845/Yes	859/Yes	907/Yes	868/Yes
KIPP Heartwood Academy (5-8)	915/Yes	900/Yes	906/Yes	922/Yes
KIPP San Jose Collegiate (9-12)	893/Yes	909/Yes	900/Yes	875/Yes
KIPP King Collegiate (9-12)	N/A / N/A	819/ N/A	833/Yes	833/Yes
KIPP Summit Academy (5-8)	845/Yes	859/Yes	912/Yes	933/Yes

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With respect to API growth scores and meeting of API growth targets, for 2009-10 through 2012-13, where data was available, 100% of KIPP schools achieved API growth scores of greater than 800, and 100% met their API growth targets.

<b>KIPP Bay Area Schools - Base API Score Statewide Ranking / Similar School Ranking (10 = best)</b>				
<b>School</b>	<b>2009-10</b>	<b>2010-11</b>	<b>2011-12</b>	<b>2012-13</b>
KIPP Bridge Charter (5-8)	7/10	9/10	10/10	9/10
KIPP Bayview Academy (5-8)	5/9	8/10	9/10	8/10
KIPP San Francisco Bay Academy (5-8)	8/10	8/10	8/10	9/10
KIPP Heartwood Academy (5-8)	10/10	10/10	9/10	9/10
KIPP San Jose Collegiate (9-12)	10/ N/A	10/10	10/10	10/10
KIPP King Collegiate (9-12)	10/10	N/A / N/A	8/10	9/10
KIPP Summit Academy (5-8)	8/8	8/10	8/8	9/10

With respect to KIPP’s statewide and similar schools rankings (base API scores), during the reported years, 2009-10 through 2012-13, where data was available, 100% of schools (7 schools) had statewide and similar schools rankings of “5” or greater. In addition, during each of 2011-12 and 2012-13, 100% of schools (7 schools) had both rankings of “8” or greater.

<b>KIPP Bay Area Schools - Met All AYP Targets</b>				
<b>School</b>	<b>2009-10</b>	<b>2010-11</b>	<b>2011-12</b>	<b>2012-13</b>
KIPP Bridge Charter (5-8)	Yes	No	No	No
KIPP Bayview Academy (5-8)	Yes	Yes	No	No
KIPP San Francisco Bay Academy (5-8)	Yes	No	Yes	No
KIPP Heartwood Academy (5-8)	Yes	No	Yes	No
KIPP San Jose Collegiate (9-12)	Yes	Yes	Yes	No
KIPP King Collegiate (9-12)	No	Yes	Yes	No
KIPP Summit Academy (5-8)	Yes	No	Yes	Yes

As shown in the above table, in spite of the increasingly difficult task of meeting all AYP criteria over successive years, 71% of the KIPP schools (5 of 7) continued to meet such criteria during 2011-12. Staff acknowledges the challenge for schools in meeting the percent-proficient requirement of approximately 89% in 2012-13 in both mathematics and English-language arts, and does not consider results for this year to be indicative of general performance.

Overall, staff considers KIPP’s consistently high academic performance across all schools, as well as Heartwood’s performance individually, to be supportive of a recommendation for financial soundness.

**Enrollment Trends and Projections:** The table below depicts KIPP’s growth in enrollment over the past five years. KIPP has shown substantial and consistent growth since 2010-11,

growing from 2,299 students in 2010-11, across seven schools, to 3,285 students across 10 schools in 2014-15, representing growth of 43% over four years, or an average of approximately 11% per year. This growth is primarily due to the growth of individual schools (contributing to about 32% of total growth), and secondarily due to the addition of three new schools (contributing to about 11% of total growth).

**Student Enrollment by School and by Year**

School	2010-11	2011-12	2012-13	2013-14	2014-15
	Actual	Actual	Actual	Actual	Actual
KIPP Bayview	249	255	253	267	287
KIPP Bridge	256	262	323	317	340
KIPP Heartwood	394	401	398	403	414
KIPP Heritage	0	0	0	0	105
KIPP Prize	0	0	0	0	106
KIPP San Francisco Bay	333	351	348	363	367
KIPP Summit	396	397	397	405	407
KIPP King Collegiate	405	448	474	497	529
KIPP San Jose Collegiate	266	356	409	449	475
KIPP San Francisco College Prep	0	0	0	120	255
<b>Total</b>	<b>2,299</b>	<b>2,470</b>	<b>2,602</b>	<b>2,821</b>	<b>3,285</b>

For 2015-16 through 2018-19, KIPP is projecting aggregate enrollment of 3,965, 5,065, 6,701, and 8,267, respectively, representing overall growth of approximately 250%, or approximately 62% per year over four years. Upon requesting KIPP’s substantiation of such expansion, KIPP indicated the following:

- (1) In the first year (2015-16), KIPP anticipates adding one new school and the addition of new grades in three schools;
- (2) In the second year (2016-17), KIPP anticipates adding five new schools and the addition of new grades in four schools;
- (3) In the third year (2017-18), KIPP anticipates adding four new schools and the addition of new grades in eight schools: and
- (4) in the fourth year (2018-19), KIPP anticipates adding two new schools and the addition of new grades in ten schools.

Overall, KIPP is anticipating the addition of 12 new schools and the addition of new grades within each school each subsequent year through student promotion, starting with the lowest grade first. KIPP’s average daily attendance for 2012-13 and 2013-14 were 95.6% and 96.8%, which are supportive of the assumption of an ADA rate of 95% in the multi-year budget projections. Staff considers KIPP’s enrollment projections to be highly aggressive. However, the academic performance results and consistent enrollment growth over the past five years provide reasonable support for KIPP’s anticipated growth.

Heartwood’s student enrollment has remained relatively constant over the past five years, with student enrollment of 394, 401, 398, 403, and 414 for 2010-11 through 2014-15, respectively. In addition, KIPP is projecting that Heartwood’s enrollment remain the same

throughout the projected years in the multi-year budget projections. Heartwood’s year-to-year retention rate for 2014-15 was 98.5%. Based on the P-2 reports, Heartwood’s ADA rates for 2012-13 and 2013-14 were 98.0% and 98.8%, respectively. KIPP has a current wait list with 291 students.

**Financial Analysis:** Staff’s financial analysis of KIPP is based upon review of the following documents: (1) three years of audited financial statements (2011-12 through 2013-14), (2) 2014-15 budgeted financials, (3) multi-year budget projections from 2015-16 through 2019-20. Additionally, KIPP provided enrollment projections through 2019-20.

KIPP’s financial projections are based upon the following assumptions: (1) occupancy of the construction CSFP project in 2017-18; (2) increases in enrollment as described above under the Enrollment Trends and Projections section; (3) 2014-15 LCFF per ADA funding rates and revenue growth (cost of living adjustments) to LCFF of 2.0% from 2015-16 through 2019-20 (4) projected ADA rates of 95%, which is consistent with KIPP’s historical performance; (5) Cost of living adjustments for expense categories of 2.4% in 2014-15 and 2.6% from 2015-16 and thereafter (6) and additional 4.7% salary increases in 2015-16 through 2017-18.

Highlighted in this section are financial data and credit indicators used to evaluate KIPP’s ability to meet its CSFP obligations for its projects funded by Proposition 1D. Staff’s financial analysis is based on information for KIPP as an organization and not for KIPP Heartwood on a stand-alone basis. Please note that the revenue, expenditure and changes to net assets recorded in financial audits and provided in KIPP’s financial projections have been modified by staff, where necessary, to include capital outlays, operating leases and repayment of debt and other significant obligations, and to exclude non-cash items such as depreciation.

KIPP Bay Area Schools	Actual FY 2012/13	Actual FY 2013/14	Budget FY 2014/15	Projected FY 2015/16	Projected FY 2016/17	Projected FY 2017/18	Projected FY 2018/19	Projected FY 2019/20
<b>ENROLLMENT PROJECTIONS</b>								
Enrollment	2,602	2,821	3,280	3,985	5,065	6,701	8,267	9,589
Average Daily Attendance	2,494	2,730	3,116	3,786	4,812	6,366	7,854	9,110
Average Daily Attendance (%)	96%	97%	95%	95%	95%	95%	95%	95%
<b>FINANCIAL PROJECTIONS</b>								
Total Revenues Available for CSFP Payment	\$ 40,992,936	\$ 37,207,586	\$ 53,866,723	\$ 61,003,684	\$ 67,109,120	\$ 78,742,839	\$ 98,295,443	\$ 120,095,734
Total Expenses Paid Before CSFP Payment	23,670,188	26,038,176	36,679,986	44,242,909	57,252,149	77,790,801	97,240,655	112,769,919
Accounting Adjustments	-	-	-	-	-	-	-	-
Net Revenues Available for CSFP Payment	\$ 17,322,748	\$ 11,169,410	\$ 17,186,737	\$ 16,760,775	\$ 9,856,971	\$ 952,038	\$ 1,054,788	\$ 7,325,815
CSFP Payment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 529,271	\$ 529,271
Net Revenues After CSFP Payment	\$ 17,322,748	\$ 11,169,410	\$ 17,186,737	\$ 16,760,775	\$ 9,856,971	\$ 952,038	\$ 525,517	\$ 6,796,544
<b>FINANCIAL INDICATORS</b>								
Net Revenues Available for CSFP Payment	\$ 17,322,748	\$ 11,169,410	\$ 17,186,737	\$ 16,760,775	\$ 9,856,971	\$ 952,038	\$ 1,054,788	\$ 7,325,815
Debt Service Coverage by Net Revenues	N/A	N/A	N/A	N/A	N/A	N/A	199.3%	1384.1%
Contributions	\$ 18,500,219	\$ 16,784,743	\$ 24,233,334	\$ 23,384,633	\$ 17,385,000	\$ 9,318,000	\$ 9,290,000	\$ 13,238,000
Debt Service Coverage by Net Revenues (w/out Contributions)	N/A	N/A	N/A	N/A	N/A	N/A	-1556.0%	-1117.0%
CSFP Lease Payment / Revenues	N/A	N/A	N/A	N/A	N/A	N/A	0.5%	0.4%
Contributions / Revenues	45.1%	45.1%	45.0%	38.3%	25.9%	11.8%	9.5%	11.0%
Net Revenues After CSFP Payment / Revenues	42.3%	30.0%	31.9%	27.5%	14.7%	1.2%	0.5%	5.7%
Revenues / ADA	\$ 16,439	\$ 13,627	\$ 17,287	\$ 16,114	\$ 13,947	\$ 12,369	\$ 12,516	\$ 13,183
Expenses / ADA	\$ 9,492	\$ 9,537	\$ 11,771	\$ 11,687	\$ 11,898	\$ 12,220	\$ 12,449	\$ 12,437
Surplus (Deficit) / ADA	\$ 6,947	\$ 4,091	\$ 5,516	\$ 4,427	\$ 2,049	\$ 150	\$ 67	\$ 746
Net Working Capital	\$ 23,012,735	\$ 33,897,164						
Net Working Capital / Expenses	97.2%	130.2%						

Long-Term Liabilities – No long-term debt was outstanding through June 30, 2014 or indicated by the school’s financial projections other than the CSFP obligations from KIPP King.

Short-Term Liabilities: KIPP has a commercial card line of credit with a financial institution for up to \$400,000. This line of credit is associated with KIPP’s credit cards and is settled monthly. The line of credit is set to expire in April 2016. KIPP also has a revolving line of credit with a financial institution for \$1,000,000. It carries a variable interest rate of prime plus 1.75% with a 5% minimum rate and expires May 2016. KIPP Bay Area Schools currently has no amounts outstanding under this line of credit.

School Facilities: KIPP leases various facilities under operating leases. The aggregate rental payments required under the terms of their operating leases were \$728,783 in 2013-14 and is expected to be \$867,510 in 2014-15.

The facility costs for all KIPP schools incorporated into the financial projections are as follows: \$1.37 million (2014-15), \$1.79 million (2015-16), \$3.20 million (2016-17), \$5.93 million (2017-18), \$8.90 million (2018-19), and \$11.01 million (2019-20). The facilities cost estimates are generally based on \$1,300 per pupil and are not inclusive of SB740 State facility cost subsidies. These estimated expenses are equivalent to an average of 9% of annual total revenues including contributions. These levels are below the 10-15% affordability range and these commitments are not expected to impact the organization’s flexibility to respond to any unforeseen costs.

Non-Operating Revenues from Contributions - Over the last three years, KIPP received the following total amounts of private grants and contributions, averaging \$13.92 million per year: \$6.47 million (2011-12), \$18.5 million (2012-13), and \$16.78 million (2013-14). KIPP anticipates \$23.8 million in contributions in both 2014-15 and 2015-16. The financial projections estimate donations averaging \$12.3 million per year from 2016-17 through 2019-20. Historically, fundraising annual receipts averaged 45.0% of revenues for years 2012-13 and 2013-14, but this average is expected to slightly decrease to 11% from 2017-18 through 2019-20.

A significant trend that staff has identified through its review of KIPP’s historical performance, current year’s budget, and multi-year budget projections is that, in spite of KIPP’s ability to substantiate its projected private contributions, KIPP relies on such contributions in order to operate on at least a break even basis and that without such contributions, KIPP would be operating at a deficit. Based on a stress test of KIPP’s reliance on private contributions, KIPP would need to receive at least 94% (\$8.76 million) of expected contributions in 2018-19 and 49% (\$6.44 million) of contributions in 2019-20 to maintain debt service coverage ratios of greater than 100.0%. When looking at KIPP’s historical average (\$13.92 million) and future projections in regards to their contributions, staff believes that the school will be able to raise their projected contributions in the future. However, due to the large percentage of contributions that must be realized, if any unforeseen decrease in private contributions occurs, KIPP would have to reduce services. Given KIPP’s strong track record of fundraising and the broad base of contributors, Staff finds KIPP’s sizable projected contributions to be reasonable.

Staff Adjusted Changes in Net Assets - KIPP's historical and projected financial operations incorporate the aforementioned described enrollment trends, facility costs and non-operating revenues from contributions.

Staff notes that KIPP has been able to maintain positive ending fund balances due to receipt of sizeable donations. Factoring in their contribution revenues, KIPP experienced net revenues of \$17.32 million in 2012-13 and \$11.17 million in 2013-14. KIPP's estimates for 2014-15 project net revenue of \$17.19 million. In 2015-16, KIPP projects net revenue of \$16.76 million, based on operating revenue of \$53.87 million (including contributions of \$24.23 million) and expenses of \$36.68 million. The financial projections indicate net revenue of \$9.86 million and \$952,038 in 2016-17 and 2017-18, respectively. KIPP projects net revenues available after the CSFP lease payments to be \$525,517 and \$6.80 million, respectively, in 2018-19 and 2019-20.

Projected Debt Service Coverage – Debt service coverage ratios on CSFP payments are calculated using net revenues available after payment of debt service on any existing and projected indebtedness. KIPP does have debt outstanding, which has been incorporated into their financial projections.

Assuming a 3.0% interest rate, a 30-year repayment period, and an estimated combined project cost of \$20,747,882, KIPP's annual CSFP payment is projected to be \$529,271 beginning 2018-19, the year following project occupancy. KIPP's projected net revenues of \$1.05 million for 2018-19 and \$7.33 million for 2019-20 would provide debt service coverage of 199.3% and 1,384%, respectively. Staff notes higher net revenue projected in 2019-20 which in turn increases debt service coverage considerably. The increases in projected coverage are primarily due to an increase in projected contributions to be received in 2019-20. However, if projected contributions are not realized in either 2018-19 or 2019-20, debt service coverage would be well below 0%.

The CSFP payments in addition to the projected facilities costs would represent 9.6% of projected revenues for each of these years, which is well below the preferred maximum range of 10-15%.

Liquidity – Liquidity measured in terms of net working capital (NWC) is calculated by subtracting current liabilities from current assets. KIPP's NWC for 2013-14 of \$33.9 million, or 130.2% of total expenses, increased from \$23.0 million in 2012-13, or 97.2% of total expenses. As of June 30, 2014, KIPP maintained \$23.6 million in cash. KIPP's liquidity position remains exceptional. Staff considers NWC equivalent to at least 5.0% of total expenses to be sufficient.

### **Strengths, Weaknesses and Mitigants**

- + KIPP Bay Area schools have consistently met all AYP criteria, scored in the 800's in regards to their API growth scores, and rank among the highest schools in the state, both in the similar school and statewide rankings.

- + Staff projects debt service coverage ratios for 2018-19 and 2019-20 of 199.3% and 1,384%, respectively.
- + KIPP has demonstrated strong management and leadership with support of local districts. The KIPP organization is well established throughout the nation, with significant experience within the charter school area and providing a network of support. KIPP King also has strong local school leadership.
- KIPP would need to receive at least 94% (\$8.76 million) of expected contributions in 2018-19 and 49% (\$6.44 million) of expected contributions 2019-20 to maintain debt service coverage ratios of greater than 100.0%.

**Staff Recommendation:** Staff recommends that the California School Finance Authority (CSFA) Board determine that KIPP Bay Area Schools (KIPP), on behalf of KIPP Heartwood Academy (Heartwood) is financially sound for the Charter School Facilities Program (Program) Preliminary and/or Advance Apportionment, but not Final Apportionment, under the Program. This determination as it relates to a Preliminary Apportionment is in place for six months and assumes no financial, operational, or legal material findings within this time period. This determination of financial soundness also is contingent upon KIPP agreeing to have its CSFP payments intercepted at the state level, pursuant to sections 17199.4 and 17078.57(a)(1)(A) of the Education Code. Staff recommends that the CSFA Board direct staff to immediately notify the Office of Public School Construction and the State Allocation Board regarding this determination.