

FINANCIAL STATEMENTS

EDUCATION SECTOR, INC.

**FOR THE YEAR ENDED DECEMBER 31, 2007
WITH SUMMARIZED FINANCIAL
INFORMATION FOR 2006**

EDUCATION SECTOR, INC.

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GELMAN, ROSENBERG & FREEDMAN
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Education Sector, Inc.
Washington, D.C.

We have audited the accompanying statement of financial position of the Education Sector, Inc. as of December 31, 2007, and the related statements of activities and change in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Education Sector, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the organization's financial statements for the year ended December 31, 2006 and, in our report dated May 2, 2007, we expressed an unqualified opinion on those 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 the Education Sector, Inc. as of December 31, 2007, and its change in net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Gelman Rosenberg & Freedman

September 8, 2008

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EDUCATION SECTOR, INC.
STATEMENT OF FINANCIAL POSITION
AS OF DECEMBER 31, 2007
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2006

ASSETS		<u>2007</u>	<u>2006</u>
CURRENT ASSETS			
Cash and cash equivalents		\$ 2,547,872	\$ 1,139,366
Certificate of deposit - restricted (Note 7)		92,968	92,975
Grants receivable		342,000	442,808
Prepaid expenses and security deposits		<u>14,227</u>	<u>12,708</u>
Total current assets		<u>2,997,067</u>	<u>1,687,857</u>
FIXED ASSETS			
Equipment		35,446	35,446
Furniture and fixtures		55,873	54,097
Leasehold improvements		66,322	66,322
Software		<u>42,868</u>	<u>42,868</u>
		200,509	198,733
Less: Accumulated depreciation and amortization		<u>(72,355)</u>	<u>(28,659)</u>
Net fixed assets		<u>128,154</u>	<u>170,074</u>
TOTAL ASSETS		<u>\$ 3,125,221</u>	<u>\$ 1,857,931</u>
LIABILITIES AND NET ASSETS			
CURRENT LIABILITIES			
Accounts payable and accrued liabilities		\$ 14,409	\$ 57,253
Accrued salaries and related benefits		69,948	61,622
Deferred rent (Note 4)		<u>12,864</u>	<u>4,927</u>
Total current liabilities		<u>97,221</u>	<u>123,802</u>
NET ASSETS			
Unrestricted		626,323	482,036
Temporarily restricted (Note 2)		<u>2,401,677</u>	<u>1,252,093</u>
Total net assets		<u>3,028,000</u>	<u>1,734,129</u>
TOTAL LIABILITIES AND NET ASSETS		<u>\$ 3,125,221</u>	<u>\$ 1,857,931</u>

See accompanying notes to financial statements.

EDUCATION SECTOR, INC.

**STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2007
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2006**

	2007			2006
	Unrestricted	Temporarily Restricted	Total	Total
REVENUE				
Foundation grants	\$ 5,000	\$ 2,985,800	\$ 2,990,800	\$ 455,437
Research income	15,000	-	15,000	-
Interest/dividend income	50,811	-	50,811	54,244
Contributed services and materials	16,094	-	16,094	10,051
Other revenue	(194)	-	(194)	534
Net assets released from donor restrictions (Note 3)	<u>1,836,216</u>	<u>(1,836,216)</u>	<u>-</u>	<u>-</u>
Total revenue	<u>1,922,927</u>	<u>1,149,584</u>	<u>3,072,511</u>	<u>520,266</u>
EXPENSES (Note 8)				
Salaries	1,026,622	-	1,026,622	930,263
Benefits	39,946	-	39,946	35,130
Retirement plan contribution (Note 6)	30,006	-	30,006	25,981
Payroll taxes	67,961	-	67,961	59,893
Printing and production	12,022	-	12,022	33,502
Professional fees	263,846	-	263,846	223,796
Occupancy (Note 4)	162,349	-	162,349	119,721
Insurance	13,821	-	13,821	15,056
Depreciation and amortization	43,696	-	43,696	28,659
Telephone	21,369	-	21,369	27,971
Travel and entertainment	36,019	-	36,019	57,431
Postage and delivery	4,251	-	4,251	7,277
Supplies	5,419	-	5,419	9,366
Subscriptions and publications	10,078	-	10,078	8,320
Meetings and conventions	19,210	-	19,210	18,906
Advertising and promotion	1,634	-	1,634	4,277
Equipment	8,395	-	8,395	33,934
Other	8,859	-	8,859	6,236
Bank fees	1,937	-	1,937	1,996
Repairs and maintenance	<u>1,200</u>	<u>-</u>	<u>1,200</u>	<u>-</u>
Total expenses	<u>1,778,640</u>	<u>-</u>	<u>1,778,640</u>	<u>1,647,715</u>
Change in net assets	144,287	1,149,584	1,293,871	(1,127,449)
Net assets at beginning of year	<u>482,036</u>	<u>1,252,093</u>	<u>1,734,129</u>	<u>2,861,578</u>
NET ASSETS AT END OF YEAR	<u>\$ 626,323</u>	<u>\$ 2,401,677</u>	<u>\$ 3,028,000</u>	<u>\$ 1,734,129</u>

See accompanying notes to financial statements.

EDUCATION SECTOR, INC.

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2007
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2006**

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 1,293,871	\$ (1,127,449)
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:		
Depreciation and amortization	43,696	28,659
(Increase) decrease in:		
Grants receivable	100,808	1,007,192
Prepaid expenses and security deposits	(1,519)	(6,820)
Increase (decrease) in:		
Accounts payable and accrued liabilities	(42,844)	31,340
Accrued salaries and related benefits	8,326	19,158
Deferred rent	<u>7,937</u>	<u>4,927</u>
Net cash provided (used) by operating activities	<u>1,410,275</u>	<u>(42,993)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of fixed assets	(1,776)	(155,865)
Purchases of Certificate of Deposit	<u>7</u>	<u>(92,975)</u>
Net cash used by investing activities	<u>(1,769)</u>	<u>(248,840)</u>
Net increase (decrease) in cash and cash equivalents	1,408,506	(291,833)
Cash and cash equivalents at beginning of year	<u>1,139,366</u>	<u>1,431,199</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 2,547,872</u>	<u>\$ 1,139,366</u>

See accompanying notes to financial statements.

EDUCATION SECTOR, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION

Organization -

The Education Sector, Inc. (Education Sector) is a nonprofit organization, incorporated in the State of Maryland and located in Washington, DC. The Education Sector is an independent education think tank. It is nonprofit and nonpartisan, both a dependable source of sound thinking on policy and an honest broker of evidence in key education debates. The Education Sector produces original research and policy analysis and promotes outstanding work by the nation's most respected education analysts.

Basis of presentation -

The accompanying financial statements are presented on the accrual basis of accounting, and in accordance with Statement of Financial Accounting Standards No. 117, "Financial Statements of Not-for-Profit Organizations".

Cash and cash equivalents -

The Education Sector considers all cash and other highly liquid investments with initial maturities of three months or less to be cash equivalents.

At times during the year, the Education Sector maintains cash balances at financial institutions in excess of the Federal Deposit Insurance Corporation (FDIC) limits. Management believes the risk in these situations to be minimal.

Fixed assets -

Fixed assets are stated at cost. Fixed assets are depreciated on a straight-line basis over the estimated useful lives of the related assets, generally three to five years. The Education Sector capitalizes all property and equipment with a cost of \$2,000 or more. The cost of maintenance and repairs is recorded as expenses are incurred.

Income taxes -

The Education Sector is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision for income taxes has been made in the accompanying financial statements. The Education Sector is not a private foundation.

Net asset classification -

The net assets are reported in two self-balancing groups as follows:

- **Unrestricted net assets** include unrestricted revenue and contributions received without donor-imposed restrictions. These net assets are available for the operation of the Education Sector and include both internally designated and undesignated resources.

EDUCATION SECTOR, INC.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION**
(Continued)

Net asset classification (continued) -

- **Temporarily restricted net assets** include revenue and contributions subject to donor-imposed stipulations that will be met by the actions of the Education Sector and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities and Change in Net Assets as net assets released from restrictions.

Contributions and grants -

Contributions and grants are recorded as revenue in the year notification is received from the donor. Contributions and grants are recognized as unrestricted support only to the extent of actual expenses incurred in compliance with the donor-imposed restrictions and satisfaction of time restrictions. Contributions and grants received in excess of expenses incurred are shown as temporarily restricted net assets in the accompanying financial statements. The organization does not feel an allowance for uncollectable grants is necessary as of December 31, 2007

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 at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

Reclassification -

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation.

In-kind contributions -

The Education Sector, Inc. receives donated legal services that are recorded as in-kind contributions at their estimated fair value at the date of donation. Donated legal services for the year ended December 31, 2007 totaled \$16,094.

2. **TEMPORARILY RESTRICTED NET ASSETS**

Temporarily restricted net assets consisted of the following at December 31, 2007:

Accountability	\$ 468,750
Teacher Quality	96,667
Undergrad Education	327,927
Time Restricted	<u>1,508,333</u>
	<u>\$2,401,677</u>

EDUCATION SECTOR, INC.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007

3. NET ASSETS RELEASED FROM RESTRICTIONS

The following temporarily restricted net assets were released from donor restrictions by incurring expenses which satisfied the restricted purposes specified by the donors:

Accountability	\$ 381,250
Develop New Ideas	78,332
Educational Choice	114,131
Policy Making	9,975
Teacher Quality	320,512
Undergrad Education	77,849
Time Restricted	<u>854,167</u>
	<u>\$1,836,216</u>

4. LEASE COMMITMENT

On July 1, 2006, the Education Sector entered into a non-cancelable operating lease for its office space that terminates on June 30, 2012. Under the terms of the lease, the base rent increases annually on an incremental basis as stated in the lease. Under accounting principles generally accepted in the United States of America (GAAP), all rental payments, including fixed rent increases, less any rental abatements, are recognized on a straight-line basis over the term of the lease. The difference between the GAAP rent expense and the required lease payments is reflected as deferred rent in the accompanying Statement of Financial Position.

The future minimum payments under this lease are as follows:

<u>Year Ended December 31,</u>	
2008	\$ 158,268
2009	162,211
2010	166,263
2011	170,424
2012	<u>86,268</u>
	<u>\$ 743,434</u>

Rent expense for the year ended December 31, 2007 was \$162,349.

5. EMPLOYMENT CONTRACTS

The Education Sector has entered into four-year employment agreements with its Co-Directors. The agreements terminate on December 31, 2008, and call for a fixed annual salary, retirement plan contribution and potential bonuses. In addition, they stipulate that the Co-Directors shall receive six months severance pay if terminated without cause.

EDUCATION SECTOR, INC.

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2007**

6. RETIREMENT PLAN

The Education Sector maintains a defined contribution plan under Section 401(k) of the Internal Revenue Code for employees who have attained certain age and length of service requirements. Under the terms of the plan, eligible employees may elect to contribute up to the Federal tax limitation annually. The Education Sector makes contributions of three percent (3%) of participant's compensation to the plan. Additionally, the Education Sector may elect to make additional discretionary contributions to the plan. During the year ended December 31, 2007, the Education Sector contributed \$30,006 to the plan.

7. LETTER OF CREDIT/CERTIFICATE OF DEPOSIT

The Education Sector has a \$60,000 restricted use letter of credit secured by a Certificate of Deposit for \$90,000 with PNC Bank. The terms of the office lease agreement stipulate that the Education Sector maintain this letter of credit in lieu of a security deposit. Only the landlord may draw on this letter of credit and only if the Education Sector is in default and has been notified. This may be reduced over the life of the lease when certain conditions are met. At December 31, 2007, the letter of credit had no balance outstanding. As the Certificate of Deposit is collateral for this letter of credit, it may not be drawn upon.

8. FUNCTIONAL EXPENSES

The costs of providing the various programs and other activities have been summarized on a functional basis in the Statement of Activities and Change in Net Assets. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

The organization's functional expenses were comprised of the following at December 31, 2007:

Program services:	<u>\$1,486,057</u>
Supporting services:	
Management and general	159,279
Fundraising	<u>133,304</u>
Total supporting services	<u>292,583</u>
TOTAL	<u>\$1,778,640</u>