

**Explanatory Notes to ESF Educational Services Limited ('ESL') Accounts
for the year ended 31 August 2008**

Explanatory Notes

These explanatory notes do not form part of the audited accounts and are provided to put the numbers into context with some background information. There are sections on the income and expenditure account, balance sheet and cash flow statement.

Income and expenditure

	<u>2007/08</u>		<u>2006/07</u>		<u>2005/06</u>	
	\$M	% of total income	\$M	% of total income	\$M	% of total income
Income						
Course fees	47.1	22.6	40.5	29.7	31.6	35.4
Tuition fees	149.1	71.5	88.0	64.6	53.9	60.4
Other income	12.3	5.9	7.8	5.7	3.7	4.1
	<u>208.5</u>	100.0	<u>136.3</u>	100.0	<u>89.2</u>	100.0
Expenditure						
Staff cost	145.2	69.6	94.8	69.6	64.7	72.5
Depreciation	2.2	1.1	2.6	1.9	4.5	5.0
Management & administrative expenses	2.5	1.2	2.2	1.6	1.8	2.0
Rent, rates & building management fees	14.5	7.0	9.9	7.3	9.1	10.2
Other expenses	41.0	19.7	28.4	20.8	14.4	16.1
	<u>205.4</u>	98.5	<u>137.9</u>	101.2	<u>94.5</u>	105.9
Surplus/(Deficit)	<u>3.1</u>	1.5	<u>(1.6)</u>	-1.2	<u>(5.3)</u>	-5.9
Average student enrolment						
Kindergartens	706		695		676	
Renaissance College	1,308		885		426	
Discovery College	440		n/a		n/a	
	<u>2,473</u>		<u>1,580</u>		<u>1,102</u>	

Income:

1. The overall increase in course fees of \$6.6M represents a 16% increase over the previous year as a result of a) hourly fee increase of 14% and 6% for Language and Sports Sections, respectively; and b) increase in enrolment numbers of 7.4% and 17% for Language and Sports Sections, respectively.
2. The increase in tuition fees of \$61.1M is attributed to the first year operation of Discovery College ('DC') with an average enrolment of 459 and increase in enrolment at Renaissance College ('RCHK') from 885 in 06/07 to 1308 in 07/08. A slight increase of 20 students in the Kindergartens also contributed to the increase in income.
3. Included in the \$12.3M other income for 2007/08 were \$1.9M in registration fees charged by RCHK and DC, \$3.9 in income derived from the rental of school premises to outside parties, \$5.0M in resale of school items including uniforms, and \$1.5M in miscellaneous items. The increase in 2007/08 relates mostly to RCHK operations.

Expenditure:

1. The \$50.4M increase in staff cost during 2007/08 is due to a) the first year of operation at DC (\$22.0M); b) the increase in staff members at RCHK to meet its growth (net increase of \$22.4M); c) the increase in hourly teachers for Sports Section (net increase of \$3.3M); d) the increase in staff at ESL administration office (net increase of \$1.0M); and e) salary point increments of kindergarten teachers (net increase of \$0.9M).
2. The \$4.7M increase in rent, rates and building management fees is mainly a result of RC's first payment for rates and government rent (\$3.3M) and the increase in rental of \$0.7M paid by Language Section to ESF schools during the year (from \$113 to \$200 per hour per classroom). Action has been taken to recover the \$3.3M in rates and rent from the Education Bureau as of November 2008.
3. Other expenses were \$12.6M higher largely due to a) \$4.7M increase in payment from RCHK and DC to the English Schools Foundation ("ESF") in return for its financing part of the cost of the school buildings under the Development and Operating Agreement between ESL and ESF; b) office and teaching material expenses of DC in its first year of operations (\$4.6M); c) increase in office and teaching material expenses of RCHK to meet its growth (net increase of \$1.7M).

Business segment performance:

The operating surplus of \$3.1M in 2007/08 can be better explained by business segment information as follows:

(in \$ million)	Language	Sports	Kinder-gartens	RCHK	DC	Total
Surplus after allocation of administration cost	4.3	0.8	1.8	(1.6)	(2.2)	3.1

DC's deficit is due to its first year of operation and preparation for the new school site in Discovery Bay. The deficit at RCHK is a result of paying first-time rates and government rent of \$3.3M in 2007/08.

Balance sheet

	<u>2007/08</u>	<u>2006/07</u>	<u>2005/06</u>
	\$M	\$M	\$M
Assets employed			
Non-current assets	3.1	36.6	38.9
Current assets and others	81.9	20.2	4.6
	<u>85.0</u>	<u>56.8</u>	<u>43.5</u>
Less: current liabilities	(81.6)	(56.5)	(41.5)
Net assets employed	<u><u>3.4</u></u>	<u><u>0.3</u></u>	<u><u>2.0</u></u>
 Reserves			
Accumulated fund	3.1	0.1	1.7
Schools' donation fund	0.3	0.2	0.3
	<u>3.4</u>	<u>0.3</u>	<u>2.0</u>

The \$33.5M decrease in non-current assets in 2007/08 is largely due to the transfer of the entire balance of construction-in-progress to ESF pertaining to the DC project (\$32.9M).

The \$61.7M increase in current assets can be attributed to a) the increase in cash on hand of \$54.8M as a result of increases in RCHK's and DC's scholarship funds, payment of schools' advance fees, and transfer of construction-in-progress to ESF; and b) increase in grant receivable from the government for the construction of DC of \$4.1M.

Cashflow and capital commitments

	<u>2007/08</u>	<u>2006/07</u>	<u>2005/06</u>
	\$M	\$M	\$M
Operating activities			
(Deficit)/Surplus for the year	3.1	(1.6)	(5.3)
Depreciation	2.2	2.6	4.5
Interest Income	(0.5)	(0.1)	-
	<u>4.8</u>	<u>0.9</u>	<u>(0.8)</u>
Change in working capital	18.2	12.9	7.6
Cash generated from operations	<u>23.0</u>	<u>13.8</u>	<u>6.8</u>
 Investing activities			
(Capital expenditure)/ construction in progress transferred to ESF	31.4	(0.4)	(15.1)
Other	0.3	0.1	-
	<u>31.7</u>	<u>(0.3)</u>	<u>(15.1)</u>
 Increase / (Decrease) in cash	<u><u>54.7</u></u>	<u><u>13.5</u></u>	<u><u>(8.3)</u></u>

Change in working capital is largely a result of setting aside the scholarship funds in the amount of \$11.4M and fees received in advance of \$10.9M at RC and DC and the increase in creditors and accruals of \$13.6M, offset by a decrease in amount due to ESF of \$12.0M and an increase in debtors of \$5.3M.

The relationship between ESF and ESL

ESL was set up in 1994 to provide kindergarten education, language classes and extra curricula activities. It also operates two Private Independent Schools, RCHK and DC and has common management with ESF although it is not a legal subsidiary of ESF.

ESL is the qualified sponsoring body to run RCHK in Ma On Shan and DC in Discovery Bay under separate service agreements with the Education Bureau.

ESF and ESL have entered into a Development and Operating Agreement such that the funds made available by ESF to build the RCHK and DC school premises and other related provisions will be compensated by fees based on student enrolment. ESL also pays for the services which ESF provides to it. Refer to [here](#) for details of the relationship between ESF and ESL.

Governance

Effective 15th February 2007, the ESF Audit Committee (“Committee”) has expanded its scope of coverage to include ESL. Prior to the ESL board meeting to discuss and approve the audited accounts, the Committee has met to discuss and monitor the preparation of ESL accounts and the work performed by external and internal auditors. The Committee reports to the ESF Board of Governors chaired by Professor Felice Lih Mak.

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