

ESF Educational Services Limited ('ESL') Accounts **for the year ended 31 August 2014**

Explanatory Notes

These explanatory notes provide information on ESF Educational Services Limited ("ESL") only. ESL is a controlled subsidiary of the English Schools Foundation ("ESF"). For more information, please refer to the section "The relationship between ESF and ESL" at the end of this document. These notes do not form part of the audited accounts and are provided to put the numbers into context with some background information.

Income and expenditure

	<u>2013/14</u>		<u>2012/13</u>		<u>2011/12</u>	
	\$M	% of total income	\$M	% of total income	\$M	% of total income
Income						
Operating Income						
Tuition fees	409.1	78.0	365.8	76.1	326.3	78.2
Course fees	58.2	11.1	55.0	11.4	53.3	12.8
Others	23.8	4.5	27.9	5.8	22.9	5.5
	<u>491.1</u>	<u>93.6</u>	<u>448.7</u>	<u>93.3</u>	<u>402.5</u>	<u>96.5</u>
Capital Income						
Non-refundable building levy	19.3	3.7	13.9	2.9	4.4	1.1
Nomination rights	14.2	2.7	18.3	3.8	10.4	2.5
	<u>33.5</u>	<u>6.4</u>	<u>32.2</u>	<u>6.7</u>	<u>14.8</u>	<u>3.5</u>
	<u>524.6</u>	<u>100.0</u>	<u>480.9</u>	<u>100</u>	<u>417.3</u>	<u>100</u>
Expenditure						
Staff cost	367.6	70.1	331.5	68.9	296.7	71.1
Depreciation	7.5	1.4	3.4	0.7	2.1	0.5
Management & administrative expenses	7.9	1.5	7.7	1.6	5.4	1.3
Rent, rates & building management fees	20.1	3.8	18.5	3.8	19.0	4.6
Development and operating agreement payment	21.2	4.0	20.2	4.2	15.6	3.7
Teaching materials & resources	14.0	2.7	13.1	2.7	12.4	3.0
Scholarship fund & hardship allowance	33.6	6.4	29.9	6.2	26.3	6.3
Office, general and other expenses	42.0	8.0	41.5	8.6	32.6	7.8
	<u>513.9</u>	<u>98.0</u>	<u>465.8</u>	<u>96.9</u>	<u>410.1</u>	<u>98.3</u>
Surplus	<u>10.7</u>	<u>2.0</u>	<u>15.1</u>	<u>3.1</u>	<u>7.2</u>	<u>1.7</u>
Represented by:						
Operating deficit	(22.8)		(17.0)		(7.6)	
Capital fund surplus	33.5		32.1		14.8	
	<u>10.7</u>		<u>15.1</u>		<u>7.2</u>	

Student enrolment

	<u>2013/14</u>	<u>2012/13</u>	<u>2011/12</u>
Average student enrolment (Schools)			
Kindergartens	1,214	1,198	1,183
Renaissance College	2,041	1,996	1,963
Discovery College	1,243	1,120	981
	<u>4,498</u>	<u>4,314</u>	<u>4,127</u>
Average student enrolment (Courses)			
Language	1,434	1,404	1,344
Sports	3,474	2,912	2,838
	<u>4,908</u>	<u>4,316</u>	<u>4,182</u>

Income:

1. The increase in Tuition fees income of \$43.3M is mainly attributed to an average 5.7% fee increase for the kindergartens and an average 7.6% fee increase for the Private Independent Schools ('PIS'). Additional enrolment at Renaissance College ('RCHK'), from 1,996 in 12/13 to 2,041 in 13/14, and at Discovery College ('DC'), from 1,120 in 12/13 to 1,243 in 13/14 was also a contributing factor.
2. Course fees income saw a rise of 5.8% to HK\$58.2m, which was a direct result of higher sign-up rates in the sports and language programs.
3. Other operating income comprises rental income, application fees, retained deposits, income from re-sale of school items, interest income, school activity income, and transfer from prior years' scholarship fund surplus. Decrease in other operating income of \$4.1M can mainly be attributed to a reduction in transfer from prior years' scholarship fund and hardship allowance surplus into income. Such transfer has been based on actual available surplus in either the scholarship fund or the hardship allowance each year.
4. Non-refundable building levy of \$19.3M came from students of Renaissance College and Discovery College.
5. Nomination rights income of \$14.2M came from newly enrolled students of Renaissance College and Discovery College who were part of the nomination rights scheme.

Expenditure:

1. The \$36.1M increase in Staff cost during 2013/14 is mainly due to a 3.5% overall salary increment, increased staff numbers at the PIS to match the respective growth in student enrolment, and increased staffing at the kindergartens.
2. Management and administrative expenses of \$7.9M represents the amount paid to ESF during the year for providing management and administrative support to ESL.
3. In consideration for the provision of the school buildings and facilities by ESF, the PIS paid a fee of \$21.2M to ESF in 2013/14 in accordance with the Development and operating agreement (DOA) between ESL and ESF.
4. Scholarship fund & hardship allowance represents 10% of total tuition fees received by PIS which have been set aside for the provision of scholarship and financial assistance.

Business segment performance:

The surplus, after allocation of central administrative costs, may be split into business segments as follows:

	<u>2013/14</u>	<u>2012/13</u>	<u>2011/12</u>
	\$M	\$M	\$M
Language	6.4	6.3	6.7
Sports	4.0	3.9	5.3
Kindergartens	(4.0)	(0.4)	1.3
Renaissance College	14.8	16.6	2.9
Discovery College	(10.5)	(11.3)	(9.0)
	<u>10.7</u>	<u>15.1</u>	<u>7.2</u>

2013/14 deficit in the kindergartens is a result of increase in staffing and accelerated depreciation of major leasehold improvements to match lease terms. Discovery College remains in a deficit position as the school has yet to reach full student capacity. 2013/14 average student enrolment at Discovery College was 1,243 compared to a future capacity of between 1,400 to 1,500 students.

Balance sheet:

	<u>2013/14</u>	<u>2012/13</u>	<u>2011/12</u>
	\$M	\$M	\$M
Assets employed			
Properties, plant and equipment	58.5	50.6	19.8
Restricted cash and bank deposits			
with original maturities over three months	3.9	3.4	3.4
Cash and cash equivalents	90.6	85.2	116.4
Other assets	47.6	43.3	17.3
	<u>200.6</u>	<u>182.5</u>	<u>156.9</u>
Less: current liabilities	(172.5)	(165.1)	(158.9)
Less: refundable debenture	(4.3)	(4.3)	-
Net assets / (liabilities)	<u>23.8</u>	<u>13.1</u>	<u>(2.0)</u>
Reserves			
Accumulated fund	(56.7)	(33.9)	(16.9)
Capital fund	80.5	47.0	14.9
	<u>23.8</u>	<u>13.1</u>	<u>(2.0)</u>

The \$7.9M increase in Properties, plant and equipment includes capital asset additions of converted classrooms and a new sports field. There is a \$7.4M increase in Current liabilities of which \$4.1m is related to the current portion of the kindergarten refundable debenture, with the rest relating to fees received in advance. Capital fund consists of income accumulated from non-refundable building levy and nomination rights.

Cash flow and capital commitments

	<u>2013/14</u>	<u>2012/13</u>	<u>2011/12</u>
	\$M	\$M	\$M
Operating activities			
(Deficit)/Surplus for the year	10.7	15.1	7.2
Adjustments for:			
Depreciation	7.5	3.4	2.1
Interest Income	(0.3)	(0.5)	(0.7)
Nomination rights	(14.2)	(18.2)	(10.4)
Non-refundable building levy	(19.3)	(13.9)	(4.4)
Other	-	0.3	0.2
	<u>(15.6)</u>	<u>(13.8)</u>	<u>(6.0)</u>
Change in working capital	5.2	(42.7)	10.8
Cash generated from operations	<u>(10.4)</u>	<u>(56.5)</u>	<u>4.8</u>
Investing activities			
Payments for purchase of plant & equipment	(22.6)	(11.1)	(5.9)
Interest received	0.3	0.5	0.7
Other	(0.5)	-	(1.9)
	<u>(22.8)</u>	<u>(10.6)</u>	<u>(7.1)</u>
Financing activities			
Proceeds from nomination rights	15.2	17.7	11.4
Proceeds from non-refundable building levy	19.3	13.9	4.4
Proceeds from refundable debenture	4.1	4.3	-
	<u>38.6</u>	<u>35.9</u>	<u>15.8</u>
Increase/(decrease) in cash	<u>5.4</u>	<u>(31.2)</u>	<u>13.5</u>

Operating activities: Change in working capital of \$5.2M is mainly a result of decrease in receivables and increase in creditors.

Investing activities: Payments for purchase of plant & equipment of \$22.6M relate largely to the settlement of the costs of RC ICT Suite and other school works during the year.

Financing activities: Proceeds from the issuance of nomination rights and non-refundable building levy come from RC and DC. Proceeds from refundable debenture relate to admissions at the kindergartens.

The relationship between ESF and ESL

ESL was set up in 1994 to provide kindergarten education, language classes and extra-curricular activities. It currently operates four kindergartens and two Private Independent Schools. ESL has common management with ESF and is a controlled subsidiary of ESF.

ESF charges ESL an annual fee for providing management and administration services to ESL at cost.

ESL is the qualified sponsoring body to run Renaissance College (“RCHK”) in Ma On Shan and Discovery College (“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 reimbursed together with a return of 1% over the higher of the actual borrowing cost incurred by ESF or the Hong Kong Inter-bank Offer Rates (HIBOR) for 3 months. Such fee income has been collected by ESF from RCHK since 2006/07 and from DC since 2007/08 and will serve to provide a steady stream of revenue to ESF in the future.

At the directors’ meeting held on 21 May 2012, it was proposed and endorsed that RCHK and DC would pay for their own capital expenditure with effect from 1 July 2012. Any related depreciation charge would be recorded in the books of the Company accordingly. The proposal was agreed and ratified by the Board of ESF on 13 December 2012.

Governance

Effective 15 February 2007, the ESF Audit Committee (“Committee”) expanded its role, at the request of the ESF Chief Executive, to review ESL’s financial statements and work done on ESL by external and internal auditors. The Committee reports to the ESF Board of Governors which makes these comments available to the ESL Board of Directors.

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