

New Oriental Education & Technology Group Inc.

Form 20-F

September 27, 2013

[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 20-F**

(Mark One)

**REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OR 12(G) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended May 31, 2013.**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

**SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

**Date of event requiring this shell company report**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-32993

## **NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.**

(Exact name of Registrant as specified in its charter)

N/A

(Translation of Registrant's name into English)

**Cayman Islands**

(Jurisdiction of incorporation or organization)

**No. 6 Hai Dian Zhong Street**

**Haidian District, Beijing 100080**

**People's Republic of China**

(Address of principal executive offices)

**Louis T. Hsieh, President and Chief Financial Officer**

**Tel: +(86 10) 6090-8000**

**E-mail: louishsieh@xdf.cn**

**Fax: +(86 10) 6260-5511**

**No. 6 Hai Dian Zhong Street**

**Haidian District, Beijing 100080**

**People's Republic of China**

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

**Table of Contents**

**Securities registered or to be registered pursuant to Section 12(b) of the Act:**

Title of Each Class	Name of Exchange on Which Registered
American depositary shares, each representing one common share*	New York Stock Exchange
Common shares, par value US\$0.01 per share**	New York Stock Exchange

\* Effective August 18, 2011, the ratio of ADSs to our common shares was changed from one ADS representing four common shares to one ADS representing one common share.

\*\* Not for trading, but only in connection with the listing on New York Stock Exchange of the American depositary shares.

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

None

(Title of Class)

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

None

(Title of Class)

Indicate the number of outstanding shares of each of the Issuer's classes of capital or common stock as of the close of the period covered by the annual report. **156,695,987 common shares, par value US\$0.01 per share, as of May 31, 2013.**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934. Yes  No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

## Edgar Filing: New Oriental Education & Technology Group Inc. - Form 20-F

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP

International Financial Reporting Standards as issued

Other

by the International Accounting Standards Board

If  Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.  Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.  Yes  No

**Table of Contents**

**TABLE OF CONTENTS**

<u>INTRODUCTION</u>	1
<u>FORWARD-LOOKING STATEMENTS</u>	2
<u>PART I</u>	3
ITEM 1. <u>IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS</u>	3
ITEM 2. <u>OFFER STATISTICS AND EXPECTED TIMETABLE</u>	3
ITEM 3. <u>KEY INFORMATION</u>	3
ITEM 4. <u>INFORMATION ON THE COMPANY</u>	32
ITEM 4A. <u>UNRESOLVED STAFF COMMENTS</u>	57
ITEM 5. <u>OPERATING AND FINANCIAL REVIEW AND PROSPECTS</u>	57
ITEM 6. <u>DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</u>	82
ITEM 7. <u>MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS</u>	90
ITEM 8. <u>FINANCIAL INFORMATION</u>	90
ITEM 9. <u>THE OFFER AND LISTING</u>	93
ITEM 10. <u>ADDITIONAL INFORMATION</u>	94
ITEM 11. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	102
ITEM 12. <u>DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u>	103
<u>PART II</u>	105
ITEM 13. <u>DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u>	105
ITEM 14. <u>MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS</u>	105
ITEM 15. <u>CONTROLS AND PROCEDURES</u>	105
ITEM 16A. <u>AUDIT COMMITTEE FINANCIAL EXPERT</u>	106
ITEM 16B. <u>CODE OF ETHICS</u>	106
ITEM 16C. <u>PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	107
ITEM 16D. <u>EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u>	107
ITEM 16E. <u>PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS</u>	107
ITEM 16F. <u>CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANTS</u>	107
ITEM 16G. <u>CORPORATE GOVERNANCE</u>	108
ITEM 16H. <u>MINE SAFETY DISCLOSURE</u>	108
<u>PART III</u>	108
ITEM 17. <u>FINANCIAL STATEMENTS</u>	108
ITEM 18. <u>FINANCIAL STATEMENTS</u>	108
ITEM 19. <u>EXHIBITS</u>	109

**Table of Contents**

**INTRODUCTION**

Unless otherwise indicated and except where the context otherwise requires, references in this annual report on Form 20-F to:

we, us, our company or our refers to New Oriental Education & Technology Group Inc., its predecessor entities and subsidiaries and in the context of describing our operations and consolidated financial data, also includes New Oriental China (as defined below);

China or PRC refers to People's Republic of China, and for the purpose of this annual report, excludes Taiwan, Hong Kong and Macau;

New Oriental China refers to Beijing New Oriental Education & Technology (Group) Co., Ltd., which is a domestic PRC company and our variable interest entity whose financial results are consolidated into our consolidated financial statements in accordance with U.S. GAAP;

student enrollments refers to the cumulative total number of courses enrolled in and paid for by our students, including multiple courses enrolled in and paid for by the same student but excluding courses offered at our primary and secondary schools;

shares or common shares refers to our common shares, par value US\$0.01 per share;

ADSs refers to our American depositary shares. Prior to August 18, 2011, each of our ADSs represented four common shares. On August 18, 2011, we effected a change in the ratio of our ADSs to common shares from one ADS representing four common shares to one ADS representing one common share. Except as otherwise noted, this change in our ADS to common share ratio has been retroactively reflected in this annual report on Form 20-F; and

RMB or Renminbi refers to the legal currency of China and \$, dollars, US\$ or U.S. dollars refers to the legal currency of the United States.

We refer to our teaching facilities in this annual report as either schools or learning centers, based primarily on a facility's functions. Generally, our schools consist of classrooms and administrative facilities with student and administrative services, while our learning centers consist primarily of classroom facilities. Each of our schools, including kindergartens, has received a Permit for Operating a Private School from the relevant local government authority.

Our financial statements are expressed in U.S. dollar, which is our reporting currency. Certain of our financial data in this annual report on Form 20-F are translated into U.S. dollars solely for the reader's convenience. Unless otherwise noted, all convenient translations from Renminbi to U.S. dollars in this annual report on Form 20-F were made at a rate of RMB6.1340 to US\$1.00, the exchange rate set forth in the H.10 statistical release of the Federal Reserve Board on May 31, 2013. We make no representation that any Renminbi or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or Renminbi, as the case may be, at any particular rate, at the rate stated above, or at all.

**Glossary of Major Admissions and Assessment Tests**

ACT	American College Test (US)
BEC	Business English Certificate (US)
CET 4	College English Test Level 4 (PRC)
CET 6	College English Test Level 6 (PRC)
GMAT	Graduate Management Admission Test (US)

## Edgar Filing: New Oriental Education & Technology Group Inc. - Form 20-F

GRE	Graduate Record Examination (US)
IELTS	International English Language Testing System (Commonwealth countries)
LSAT	Law School Admission Test (US)
PETS	Public English Test System (PRC)
SAT	SAT College Entrance Test (US)
TOEFL	Test of English as a Foreign Language (US)
TOEIC	Test of English for International Communication (US)
TSE	Test of Spoken English (US)

**Table of Contents**

**FORWARD-LOOKING STATEMENTS**

This annual report contains forward-looking statements that involve risks and uncertainties. All statements other than statements of historical facts are forward-looking statements. These forward-looking statements are made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements.

You can identify these forward-looking statements by words or phrases such as may, will, expect, is expected to, anticipate, aim, estimate, intend, plan, believe, is/are likely to or other similar expressions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. These forward-looking statements include, but are not limited to:

our anticipated growth strategies;

our future business development, results of operations and financial condition;

expected changes in our revenues and certain cost and expense items;

our ability to increase student enrollments and course fees and expand program, service and product offerings;

competition in each type of educational program, service and product we provide;

risks associated with our offering of new educational programs, services and products and the expansion of our geographic reach;

the expected increase in expenditures on education in China; and

PRC laws, regulations and policies relating to private education and providers of private educational services.

You should read thoroughly this annual report and the documents that we refer to herein with the understanding that our actual future results may be materially different from and/or worse than what we expect. We qualify all of our forward-looking statements by these cautionary statements. Other sections of this annual report include additional factors which could adversely impact our business and financial performance. Moreover, we operate in an evolving environment. New risk factors emerge from time to time and it is not possible for our management to predict all risk factors, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

You should not rely upon forward-looking statements as predictions of future events. The forward-looking statements made in this annual report relate only to events or information as of the date on which the statements are made in this annual report. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by applicable law.



**Table of Contents****PART I****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

**ITEM 3. KEY INFORMATION****A. Selected Financial Data*****Our Selected Consolidated Financial Data***

The following tables present the selected consolidated financial data of our company. The selected consolidated statement of operations data for the fiscal years ended May 31, 2011, 2012 and 2013 and the consolidated balance sheet data as of May 31, 2012 and 2013 have been derived from our audited consolidated financial statements, which are included in this annual report beginning on page F-1. The selected consolidated statement of operations data for the fiscal years ended May 31, 2009 and 2010 and the selected consolidated balance sheet data as of May 31, 2009, 2010 and 2011 have been derived from our audited consolidated financial statements for the fiscal years ended May 31, 2009, 2010 and 2011, which are not included in this annual report. Our historical results do not necessarily indicate results expected for any future periods. The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements and related notes included elsewhere in this annual report and Item 5 A. Operating and Financial Review and Prospects. Our audited consolidated financial statements are prepared and presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP.

<i>(in thousands of US\$ except share, per share and per ADS data)</i>	<b>For the Years Ended May 31,</b>				
	<b>2009<sup>(4)</sup></b>	<b>2010<sup>(4)</sup></b>	<b>2011<sup>(4)</sup></b>	<b>2012<sup>(4)</sup></b>	<b>2013</b>
<b>Consolidated Statement of Operations Data:</b>					
Net revenues:					
Educational programs and services	258,682	341,954	490,418	675,189	857,685
Books and others	26,178	33,450	49,433	78,006	102,169
<b>Total net revenues</b>	<b>284,860</b>	<b>375,404</b>	<b>539,851</b>	<b>753,195</b>	<b>959,854</b>
Operating costs and expenses: <sup>(1)</sup>					
Cost of revenues	(108,395)	(142,344)	(213,779)	(293,063)	(384,177)
Selling and marketing	(38,327)	(57,787)	(81,954)	(113,568)	(142,098)
General and administrative	(77,872)	(99,153)	(148,409)	(226,404)	(311,014)
Loss on disposal of subsidiaries			(1,537)		
<b>Total operating costs and expenses</b>	<b>(224,594)</b>	<b>(299,284)</b>	<b>(445,679)</b>	<b>(633,035)</b>	<b>(837,289)</b>
<b>Operating income</b>	<b>60,266</b>	<b>76,120</b>	<b>94,172</b>	<b>120,160</b>	<b>122,565</b>
Other income, net:					
Interest income	6,599	6,474	13,017	25,488	30,121
Investment loss					(1,427)
Miscellaneous income, net	561	(283)	1,241	1,040	772

Edgar Filing: New Oriental Education & Technology Group Inc. - Form 20-F

Provision for income taxes:					
Current	(8,399)	(7,845)	(9,390)	(14,027)	(18,985)
Deferred	1,143	1,871	1,154	3,255	3,630
Provision for income taxes	<b>(7,256)</b>	<b>(5,974)</b>	<b>(8,236)</b>	<b>(10,772)</b>	<b>(15,355)</b>
Income from continuing operations	<b>60,170</b>	<b>76,337</b>	<b>100,194</b>	<b>135,916</b>	<b>136,676</b>
Gain (Loss) from discontinued operations, net of tax	<b>683</b>	<b>1,225</b>	<b>1,345</b>	<b>(3,228)</b>	<b>(407)</b>
Net income	<b>60,853</b>	<b>77,562</b>	<b>101,539</b>	<b>132,688</b>	<b>136,269</b>
Add: Net loss attributable to noncontrolling interest <sup>(2)</sup>	163	227	235		
Net income attributable to New Oriental Education & Technology Group Inc.	61,016	77,789	101,774	132,688	136,269

**Table of Contents**

<i>(in thousands of US\$ except share, per share and per ADS data)</i>	<b>For the Years Ended May 31,</b>				
	<b>2009<sup>(4)</sup></b>	<b>2010<sup>(4)</sup></b>	<b>2011<sup>(4)</sup></b>	<b>2012<sup>(4)</sup></b>	<b>2013</b>
Net income from continuing operation per ADS attributable to shareholders of New Oriental Education & Technology Group Inc. <sup>(3)</sup>					
- Basic	0.40	0.51	0.65	0.88	0.88
- Diluted	0.39	0.49	0.64	0.87	0.87
Net income (loss) from discontinued operation per ADS attributable to shareholders of New Oriental Education & Technology Group Inc. <sup>(3)</sup>					
- Basic	0.01	0.01	0.01	(0.02)	(0.00)
- Diluted	0.00	0.01	0.01	(0.02)	(0.00)
Shares used in calculating basic net income per share	149,090,088	150,952,249	153,253,065	154,627,784	155,762,959
Shares used in calculating diluted net income per share	153,528,383	154,831,633	156,071,833	156,872,441	157,823,792

(1) Share-based compensation expenses are included in our operating costs and expenses as follows:

<i>(in thousands of US\$)</i>	<b>For the years Ended May 31,</b>				
	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>
Cost of revenues	316	657	900	216	
Selling and marketing	225	117			
General and administrative	16,209	15,409	14,145	23,909	27,242
Total	16,750	16,183	15,045	24,125	27,242

(2) Amounts in relation to noncontrolling interests, formerly named minority interest, for the years ended May 31, 2009 are reclassified in accordance with authoritative guidance regarding the noncontrolling interests, which we adopted on June 1, 2009.

(3) Each ADS represents one common share.

(4) Historical financial statements were adjusted retrospectively to reflect the discontinued operations of Elite English in the year ended May 31, 2013. Please see Note 6 to our consolidated financial statements included in this annual report for further information.

The following table presents our selected consolidated balance sheet data as of May 31, 2009, 2010, 2011, 2012 and 2013:

<i>(in thousands of US\$)</i>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>
<b>Selected Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	254,772	281,104	317,260	428,261	417,166
Total assets	469,402	596,420	863,370	1,128,817	1,353,441
Total current liabilities	117,761	168,705	288,000	438,303	489,835
Total liabilities	117,918	168,842	289,147	438,415	496,189
Total shareholders' equity	351,246	427,567	574,223	690,402	857,252
Noncontrolling interest	238	11			
Total equity	351,484	427,578	574,223	690,402	857,252

**B. Capitalization and Indebtedness**

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

**Risks Related to Our Business**

*If we are not able to continue to attract students to enroll in our courses without a significant decrease in course fees, our revenues may decline and we may not be able to maintain profitability.*

The success of our business depends primarily on the number of student enrollments in our courses and the amount of course fees that our students are willing to pay. Therefore, our ability to continue to attract students to enroll in our courses without a significant decrease in course fees is critical to the continued success and growth of our business. This in turn will depend on several factors, including our ability to develop new programs and enhance existing programs to respond to changes in market trends and student demands, expand our geographic reach, manage our growth while maintaining the consistency of our teaching quality, effectively market our programs to a broader base of prospective students, develop and license additional high-quality educational content and respond to competitive pressures. If we are unable to continue to attract students to enroll in our courses without a significant decrease in course fees, our revenue may decline and we may not be able to maintain profitability.

## **Table of Contents**

***We depend on our dedicated and capable faculty, and if we are not able to continue to hire, train and retain qualified teachers, we may not be able to maintain consistent teaching quality throughout our school network and our brand, business and operating results may be materially and adversely affected.***

Our teachers are critical to maintaining the quality of our programs, services and products and maintaining our brand and reputation. It is critical for us to continue to attract qualified teachers who have a strong command of the subject areas to be taught and meet our qualification. We also need to hire teachers who are capable of delivering innovative and inspirational instruction. The number of teachers in China with the necessary experience and language proficiency to teach our courses is limited and we must provide competitive compensation packages to attract and retain qualified teachers. In addition, criteria such as commitment and dedication are difficult to ascertain during the recruitment process, in particular as we continue to expand and add teachers to meet rising student enrollments. We must also provide continuous training to our teachers so that they can stay up to date with changes in student demands, admissions and assessment tests, admissions standards and other key trends necessary to effectively teach their respective courses. We may not be able to hire, train and retain enough qualified teachers to keep pace with our anticipated growth while maintaining consistent teaching quality across many different schools, learning centers and programs in different geographic locations. Shortages of qualified teachers or decreases in the quality of our instruction, whether actual or perceived, in one or more of our markets may have a material and adverse effect on our business.

***Our business depends on our New Oriental brand, and if we are not able to maintain and enhance our brand, our business and operating results may be harmed.***

We believe that market awareness of our New Oriental brand has contributed significantly to the success of our business. We also believe that maintaining and enhancing the New Oriental brand is critical to maintaining our competitive advantage. We offer a diverse set of programs, services and products to primary and middle school students, college students and other adults throughout many provinces and cities in China. As we continue to grow in size, expand our program, service and product offerings and extend our geographic reach, maintaining quality and consistency may be more difficult to achieve.

We have invested significantly in brand promotion initiatives. We cannot assure you that these or our other marketing efforts will be successful in promoting our brand to remain competitive. If we are unable to further enhance our brand recognition and increase awareness of our programs, services and products, or if we incur excessive marketing and promotion expenses, our business and results of operations may be materially and adversely affected. In addition, any negative publicity relating to our company or our programs and services, regardless of its veracity, could harm our brand image and in turn materially and adversely affect our business and operating results.

***Our reputation and the trading price of our ADSs may be negatively affected by adverse publicity or other detrimental conduct against us.***

Adverse publicity concerning our failure or perceived failure to comply with legal and regulatory requirements, alleged accounting or financial reporting irregularities, regulatory scrutiny and further regulatory action or litigation could harm our reputation and cause the trading price of our ADSs to decline and fluctuate significantly. For example, after we issued a press release on July 17, 2012 disclosing that we were subject to the investigation by the U.S. Securities & Exchange Commission, or the SEC, and Muddy Waters LLC, an entity unrelated to us, issued a report containing various allegations about us on July 18, 2012, the trading price of our ADSs declined sharply and we were inundated by numerous investor inquiries. The negative publicity and the resulting decline of the trading price of our ADSs also led to the filing of shareholder class action lawsuits against us and some of our senior executive officers.

We may continue to be the target of adverse publicity and other detrimental conduct against us. Such conduct includes complaints, anonymous or otherwise, to regulatory agencies regarding our operations, accounting, revenues and regulatory compliance. Additionally, allegations against us may be posted on the internet by any person or entity which identifies itself or on an anonymous basis. We may be subject to government or regulatory investigation or inquiries as a result of such third-party conduct and may be required to incur significant time and substantial costs to defend ourselves, and there is no assurance that we will be able to conclusively refute each of the allegations within a reasonable period of time, or at all. Our reputation may also be negatively affected as a result of the public dissemination of allegations or malicious statements about us, which in turn may materially and adversely affect the trading price of our ADSs.

---

## **Table of Contents**

***We face risks related to health epidemics and other outbreaks, which could result in reduced attendance or temporary closure of our schools, learning centers and bookstores.***

Our business could be materially and adversely affected by the outbreak of avian influenza, severe acute respiratory syndrome, or SARS, or other epidemics. In April 2009, a new strain of influenza A virus subtype H1N1, commonly referred to as swine flu, was first discovered in North America and quickly spread to other parts of the world, including China. In early June 2009, the World Health Organization declared the outbreak to be a pandemic, while noting that most of the illnesses were of moderate severity. The PRC Ministry of Health subsequently reported several hundred deaths caused by the influenza A (H1N1). The influenza A (H1N1) outbreak adversely affected our business and results of operations in the first and second fiscal quarters of 2010 as we experienced slower-than-usual student enrollment growth and large numbers of cancellations and deferments in enrollments from registered students. In addition, we had to cancel classes whenever an enrolled student was diagnosed with influenza A (H1N1), as required by applicable health regulations. Starting from March 2013, H7N9 bird flu, a new strain of animal influenza, has been spreading in China and has infected more than a hundred people. While the spread of the avian virus H7N9 has not materially affected our student enrollments as of the date of this annual report, any future outbreak of avian influenza, SARS, the influenza A (H1N1), H7N9 bird flu or other adverse public health developments in China may have a material and adverse effect on our business operations. These occurrences could cause cancellations or deferments of student enrollments and require the temporary closure of our schools, learning centers and bookstores while we remain obligated to pay rent and other expenses for these facilities, thus severely disrupting our business operations and materially and adversely affecting our liquidity, financial condition and results of operations.

***Failure to effectively and efficiently manage the expansion of our school network may materially and adversely affect our ability to capitalize on new business opportunities.***

We have increased the number of our schools in China from 25 as of May 31, 2006 to 57 as of May 31, 2013, and we increased the number of our learning centers in China from 111 as of May 31, 2006 to 669 as of May 31, 2013. We may continue to expand our operations in different geographic locations in China. Our expansion has resulted, and will continue to result, in substantial demands on our management, faculty and operational, technological and other resources. Our expansion will also place significant demands on us to maintain the consistency of our teaching quality and our culture to ensure that our brand does not suffer as a result of any decreases, whether actual or perceived, in our teaching quality. To manage and support our growth, we must continue to improve our existing operational, administrative and technological systems and our financial and management controls, and recruit, train and retain additional qualified teachers, management personnel and other administrative and sales and marketing personnel, particularly as we expand into new markets. We cannot assure you that we will be able to effectively and efficiently manage the growth of our operations, recruit and retain qualified teachers and management personnel and integrate new schools and learning centers into our operations. Any failure to effectively and efficiently manage our expansion may materially and adversely affect our ability to capitalize on new business opportunities, which in turn may have a material adverse impact on our financial condition and results of operations.

***If we fail to successfully execute our growth strategies, we may not be able to continue to attract students to enroll in our courses without a significant decrease in course fees, and our business and prospects may be materially and adversely affected.***

Our growth strategies include expanding our program, service and product offerings and our network of schools, learning centers and bookstores, updating and expanding the content of our programs, services and products in a cost-effective and timely manner, as well as maintaining and continuing to establish strategic relationships with complementary businesses. The expansion of our programs, services and products in terms of types of offerings and geographic locations may not succeed due to competition, failure to effectively market our new programs, services and products and maintain their quality and consistency, or other factors. In addition, we may be unable to identify new cities with sufficient growth potential to expand our network, and we may fail to attract students and increase student enrollments or recruit, train and retain qualified teachers for our new schools and learning centers. Some cities in China have undergone development and expansion for several decades while others are still at an early stage of urbanization and development. In more developed cities, it may be difficult to increase the number of schools and learning centers because we and/or our competitors already have extensive operations in these cities. In recently developed and developing cities, demand for our programs, services and products may not increase as rapidly as we expect. Furthermore, we may be unable to develop or license additional content on commercially reasonable terms and in a timely manner, or at all, to keep pace with changes in market demands. If we fail to successfully execute our growth strategies, we may not be able to continue to attract students to enroll in our courses without a significant decrease in course fees, and our business and prospects may be materially and adversely affected.

## **Table of Contents**

***We are subject to the SEC investigation and we cannot predict the timing, outcome or consequences of the investigation.***

On July 13, 2012, we were informed that the SEC had issued a formal order of investigation captioned *In the Matter of New Oriental Education & Technology Group Inc.* In that investigation the SEC's enforcement staff has requested documents and information concerning, among other things, the basis for the consolidation of New Oriental China, a variable interest entity of our company, and its schools and subsidiaries, into our consolidated financial statements and other issues related to certain allegations about us contained in a report issued on July 18, 2012 by Muddy Waters LLC. We are cooperating fully with the SEC in its investigation. We cannot predict the timing, outcome or consequences of the SEC investigation.

***We have been named as a defendant in several putative shareholder class action lawsuits that could have a material adverse impact on our business, financial condition, results of operation, cash flows and reputation.***

We will have to defend against the putative shareholder class action lawsuits described in *Item 8. Financial Information - A. Consolidated Statements and Other Financial Information - Legal and Administrative Proceedings - Litigation*, including any appeals of such lawsuits should our initial defense be successful. We are currently unable to estimate the possible loss or possible range of loss, if any, associated with the resolution of these lawsuits. In the event that our initial defense of these lawsuits is unsuccessful, there can be no assurance that we will prevail in any appeal. Any adverse outcome of these cases, including any plaintiff's appeal of the judgment in these lawsuits, could have a material adverse effect on our business, financial condition, results of operation, cash flows and reputation. In addition, there can be no assurance that our insurance carriers will cover all or part of the defense costs, or any liabilities that may arise from these matters. The litigation process may utilize a significant portion of our cash resources and divert management's attention from the day-to-day operations of our company, all of which could harm our business. We also may be subject to claims for indemnification related to these matters, and we cannot predict the impact that indemnification claims may have on our business or financial results.

***We may not be able to achieve the benefits we expect from recent and future acquisitions, and recent and future acquisitions may have an adverse effect on our ability to manage our business.***

As part of our business strategy, we have pursued and intend to continue to pursue selective strategic acquisitions of businesses that complement our existing businesses. Acquisitions expose us to potential risks, including risks associated with the diversion of resources from our existing businesses, difficulties in successfully integrating the acquired businesses, failure to achieve expected growth by the acquired businesses and an inability to generate sufficient revenue to offset the costs and expenses of acquisitions. If the revenue and cost synergies that we expect to achieve from our acquisitions do not materialize, we may have to recognize impairment charges. For example, in June 2008 we acquired a 60% equity stake in Beijing Haidian Mingshitang Exam Training Education School, or Mingshitang School, a Beijing-based private school that specializes in tutoring students seeking to retake the Chinese college entrance examination, and in September 2008 we acquired Changchun Tongwen Gaokao Training Education School, or Tongwen Gaokao School, which provides services similar to those of Mingshitang School. In the fiscal year ended May 31, 2010, we recognized a goodwill impairment loss of US\$76,000 arising from the acquisitions of Mingshitang School and Tongwen Gaokao School. We disposed Mingshitang School in April 2011 and recorded a loss of US\$1.2 million on the disposal. As another example, in September 2010, we completed the acquisition of a 100% equity interest in Newave Education, a K-12 English language school in Shanghai. Due to breach of contract by the seller of Newave Education, we submitted a request for arbitration to the China International Economic and Trade Arbitration Commission for full refund of the purchase consideration which we had paid. The case was closed in December 2011, and we received the full refund by the end of the fiscal year ended May 31, 2012.

## **Table of Contents**

If any one or more of the aforementioned risks associated with acquisitions materialize, our acquisitions may not be beneficial to us and may have a material adverse effect on our business, financial condition and results of operations.

*Third parties have in the past brought intellectual property infringement claims against us based on the content of the books and other teaching or marketing materials that we or our teachers authored and/or distributed and may bring similar claims against us in the future.*

We may be subject to claims by educational institutions and organizations, content providers and publishers, competitors and others on the ground of intellectual property rights infringement, defamation, negligence or other legal theories based on the content of the materials that we or our teachers author and/or distribute as course materials. These types of claims have been brought, sometimes successfully, against print publications and educational institutions in the past, including ourselves. For example, in January 2001, the Graduate Management Admission Council, or GMAC, and Educational Testing Service, or ETS, filed three separate lawsuits against us in the Beijing No. 1 Intermediate People's Court, alleging that we had violated the copyrights and trademarks relating to the GMAT test owned by GMAC and relating to the GRE and TOEFL tests owned by ETS by duplicating, selling and distributing their test materials without their authorization. In September 2003, the trial court found that we had violated GMAC's and ETS's respective copyrights and trademarks in connection with those admissions tests. The trial court's judgment was partially affirmed in a final judgment issued by the Beijing Higher People's Court in December 2004. The Beijing Higher People's Court held that we had not misused the trademarks of GMAC or ETS. However, it also found that the TOEFL and GRE tests were the original works of ETS and the GMAT test was the original work of GMAC, all of which are protected under the PRC Copyright Law. The Beijing Higher People's Court held that our duplication, sale and distribution of the test materials relating to these tests without ETS's and GMAC's prior permission were not a reasonable use of the test materials under the PRC Copyright Law, and that we, therefore, had infringed upon ETS's and GMAC's respective copyrights. We were ordered to pay damages in an aggregate of approximately RMB6.5 million, cease all infringing activities and destroy all copyright-infringing materials in our possession, all of which we have done. Since the Beijing Higher People's Court issued the final judgment in 2004, we have endeavored to comply with the court order and applicable PRC laws and regulations relating to intellectual property, and we have adopted policies and procedures to prohibit our employees and contractors from engaging in any copyright, trademark or trade name infringing activities. However, we cannot assure you that every teacher or other personnel will strictly comply with these policies at our schools, learning centers or other locations or media through which we provide our programs, services and products.

We have also been involved in other claims and legal proceedings against us relating to infringement of third parties' copyrights in materials distributed by us and the unauthorized use of a third party's name in connection with the marketing and promotion of one of our programs, and may be subject to further claims in the future, particularly in light of the uncertainties in the interpretation and application of intellectual property laws and regulations. Furthermore, if printed publications or other materials that we or our teachers author and/or distribute contain materials that government authorities find objectionable, these publications may have to be recalled, which could result in increased expenses, loss in revenues and adverse publicity. Any claims against us, with or without merit, could be time-consuming and costly to defend or litigate, divert our management's attention and resources or result in the loss of goodwill associated with our brand. If a lawsuit against us is successful, we may be required to pay substantial damages and/or enter into royalty or license agreements that may not be based upon commercially reasonable terms, or we may be unable to enter into such agreements at all. We may also lose, or be limited in, the rights to offer some of our programs, services and products or be required to make changes to our course materials or websites. As a result, the scope of our course materials could be reduced, which could adversely affect the effectiveness of our teaching, limit our ability to attract new students, harm our reputation and have a material adverse effect on our results of operations and financial position.



## **Table of Contents**

***We may lose our competitive advantage and our reputation, brand and operations may suffer if we fail to prevent the loss or misappropriation of, or disputes over, our intellectual property rights.***

We consider our trademarks and trade name invaluable to our ability to continue to develop and enhance our brand recognition. We have spent 20 years building our New Oriental brand by emphasizing quality and consistency and building trust among students and parents. From time to time, our trademarks and trade name have been used by third parties for or as part of other branded programs, services and products unrelated to us. We have sent cease and desist letters to such third parties in the past and will continue to do so in the future. However, preventing trademark and trade name infringement, particularly in China, is difficult, costly and time-consuming and continued unauthorized use of our trademarks and trade name by unrelated third parties may damage our reputation and brand. In addition, we have spent significant time and expense developing or licensing and localizing the content of certain educational materials, such as books, software, CD-ROMs, magazines and other periodicals, to enrich our product offerings and meet students' needs. The measures we take to protect our trademarks, copyrights and other intellectual property rights, which presently are based upon a combination of trademark, copyright and trade secret laws, may not be adequate to prevent unauthorized use by third parties. Furthermore, the application of laws governing intellectual property rights in China and abroad is uncertain and evolving, and could involve substantial risks to us. If we are unable to adequately protect our trademarks, copyrights and other intellectual property rights, we may lose these rights, our brand name may be harmed, and our business may suffer materially.

***We face significant competition in each major program we offer and each geographic market in which we operate, and if we fail to compete effectively, we may lose our market share and our profitability may be adversely affected.***

The private education sector in China is rapidly evolving, highly fragmented and competitive, and we expect competition in this sector to persist and intensify. We face competition in each major program we offer and each geographic market in which we operate. For example, we face nationwide competition for our IELTS preparation courses from Global IELTS School, which offers IELTS preparation courses in many cities in China. We face regional competition for our English for children program from several competitors that focus on children's English training in specific regions, including English First. We face competition from companies that focus on providing international and/or PRC test preparation courses in specific geographic markets in China. We also face competition from companies that focus on providing after-school tutoring services, including TAL Education Group and Xueda Education Group.

Our student enrollments may decrease due to intense competition. Some of our competitors may have more resources than we do. These competitors may be able to devote greater resources than we can to the development, promotion and sale of their programs, services and products and respond more quickly than we can to changes in student needs, testing materials, admissions standards or new technologies. In addition, we face competition from many different smaller sized organizations that focus on some of our targeted markets, and they may be able to respond more promptly to changes in student preferences in these markets. In addition, the increasing use of the internet and advances in internet- and computer-related technologies, such as web video conferencing and online testing simulators, are eliminating geographic and cost-entry barriers to providing private educational services. As a result, many of our international competitors that offer online test preparation and language training courses may be able to more effectively penetrate the China market. Many of these international competitors have strong education brands, and students and parents in China may be attracted to the offerings of international competitors based in the country that the student wishes to study in or in which the selected language is widely spoken. Moreover, many smaller companies are able to use the internet to quickly and cost-effectively offer their programs, services and products to a large number of students with less capital expenditure than previously required. We may have to reduce course fees or increase spending in response to competition in order to retain or attract students or pursue new market opportunities. As a result, our revenues and profitability may decrease. We cannot assure you that we will be able to compete successfully against current or future competitors. If we are unable to maintain our competitive position or otherwise respond to competitive pressures effectively, we may lose our market share and our profitability may be adversely affected.

***Failure to adequately and promptly respond to changes in testing materials, admissions standards and technologies could cause our programs, services and products to be less attractive to students.***

Admissions and assessment tests undergo continuous change, in terms of the focus of the subjects and questions tested, the format of the tests and the manner in which the tests are administered. For example, certain admissions and assessment tests in the United States now include an essay component, which required us to hire and train teachers to be able to analyze written essays that tend to be more subjective in nature and require a higher level of English proficiency. In addition, some admissions and assessment tests that were previously offered in paper format only are now offered in a computer-based testing format. These changes require us to continually update and enhance our test preparation materials and our teaching methods. Further, the Chinese Ministry of Education, or the MOE, promulgated new curriculum standards on December 28, 2011 for primary and secondary schools in China covering 19 subjects, including mathematics, Chinese and English. These new curriculum standards have taken effect in the fall semester of 2012, and we had finished adapting our tutoring programs and materials to these changes in curriculum standards in July 2013. Any inability to track and respond to these changes in a timely and cost-effective manner would make our programs, services and products less attractive to students, which may materially and adversely affect our reputation and ability to continue to attract students without a significant decrease in course fees.



## **Table of Contents**

***If colleges, universities and other higher education institutions reduce their reliance on admissions and assessment tests, we may experience a decrease in demand for our test preparation courses and our business may be materially and adversely affected.***

We provide preparation courses for both overseas and domestic admissions and assessment tests. In the fiscal year ended May 31, 2013, we derived a significant portion of our revenues from test preparation courses. The success of our test preparation courses depends on the continued use of admissions and assessment tests as a requirement for admission or graduation. However, the use of admissions tests in China may decline or fall out of favor with educational institutions and government authorities. For example, educational institutions and government authorities in China have recently initiated discussions and conducted early experiments in China on school admissions. Generally, these discussions and experiments exhibit a trend of basing admissions decisions less on entrance exam scores and more on a combination of other factors, such as past academic record, extracurricular activities and comprehensive aptitude evaluations. There have been certain changes in some geographic areas in the way the high school entrance exam is administered. In 2013, 90 universities and colleges were allowed to recruit up to 5% of their students through independently administered tests according to a notice promulgated by the MOE. Students admitted through such independently administered tests still need to meet certain thresholds in the national college entrance exam. If the use of admissions tests in China declines or falls out of favor with educational institutions and government authorities and if we fail to respond to these changes, the demand for certain of our services may decline, and our business may be materially and adversely affected.

In the United States, there has been a continuing debate regarding the usefulness of admissions and assessment tests to assess qualifications of applicants and many people have criticized the use of admissions and assessment tests as unfairly discriminating against certain test takers. If a large number of educational institutions abandon the use of existing admissions and assessment tests as a requirement for admission, without replacing them with other admissions and assessment tests, we may experience a decrease in demand for our test preparation courses and our business may be seriously harmed.

***We have experienced and may continue to experience a decrease in our margins.***

Many factors may cause our gross and net margins to decline. For example, there is a recent trend that the short-term language training and test preparation markets are moving towards smaller class sizes, especially for students between the ages of five and 12. This may have resulted from discretionary income increases for families in China, which cause students to be more willing and able to pay higher course fees for the more individualized attention that smaller classes can offer. In our fiscal year ended May 31, 2013, the average class size for our short-term language training and test preparation courses was approximately 10 students per class, which decreased from approximately 13 students per class in the previous fiscal year. Although our smaller-sized classes are highly profitable, they are marginally less profitable on average than our large classes. Our net margin for our fiscal year ended May 31, 2013 was 14.2%, down from 17.6% in the previous fiscal year. This decrease was partly due to the increase in demand for our smaller-sized classes. In addition, new investments and acquisitions may cause our margins to decline before we successfully integrate the acquired businesses into our operations and realize the full benefits of these investments and acquisitions. There is a risk that our margins could continue to decline in the future due to increasing demand for our smaller-sized classes and/or other factors.

***New programs, services and products that we develop may compete with our current offerings.***

We are constantly developing new programs, services and products to meet changes in student demands and respond to changes in testing materials, admissions standards, market needs and trends and technological changes. While some of the programs, services and products that we develop will expand our current offerings and increase student enrollments, others may compete with or make irrelevant our existing offerings without increasing our total student enrollments. For example, our online courses may take away students from our existing classroom-based courses, and our new schools and learning centers may take away students from our existing schools and learning centers. If we are unable to expand our program, service and product offerings while increasing our total student enrollments and profitability, our business and growth may be adversely affected.

## **Table of Contents**

***Our business is subject to fluctuations caused by seasonality or other factors beyond our control, which may cause our operating results to fluctuate from quarter to quarter. This may result in volatility and adversely affect the price of our ADSs.***

We have experienced, and expect to continue to experience, seasonal fluctuations in our revenues and results of operations, primarily due to seasonal changes in student enrollments. Historically, our courses tend to have the largest student enrollments in our first fiscal quarter, which runs from June 1 to August 31 of each year, primarily because many students enroll in our courses during the summer vacation to enhance their foreign language skills and/or prepare for admissions and assessment tests in subsequent school terms. In addition, we have generally experienced larger student enrollments in our third fiscal quarter, which runs from December 1 to February 28 of each year, primarily because many students enroll in our language training and other courses during the winter school holidays. However, our expenses vary, and certain of our expenses do not necessarily correspond with changes in our student enrollments and revenues. For example, we make investments in marketing and promotion, teacher recruitment and training, and product development throughout the year and we pay rent for our facilities based on the terms of the lease agreements. In addition, other factors beyond our control, such as special events that take place during a quarter when our student enrollment would normally be high, may have a negative impact on our student enrollments. We expect quarterly fluctuations in our revenues and results of operations to continue. These fluctuations could result in volatility and adversely affect the price of our ADSs. As our revenues grow, these seasonal fluctuations may become more pronounced.

***Our historical financial and operating results are not indicative of our future performance; and our financial and operating results are difficult to forecast.***

Our financial and operating results may not meet the expectations of public market analysts or investors, which could cause the price of our ADSs to decline. In addition to the fluctuations described above, our revenues, expenses and operating results may vary from quarter to quarter and from year to year in response to a variety of other factors beyond our control, including:

general economic conditions;

regulations or actions pertaining to the provision of private educational services in China;

detrimental negative publicity about us, our competitors or our industry;

changes in consumers' spending patterns; and

non-recurring charges incurred in connection with acquisitions or other extraordinary transactions or unexpected circumstances.

Due to these and other factors, we believe that quarter-to-quarter comparisons of our operating results may not be indicative of our future performance, and therefore you should not rely on them to predict the future performance of our ADSs. In addition, our past results may not be indicative of future performance because of new businesses developed or acquired by us.

***Our business is difficult to evaluate because we have limited experience generating net income from some of our newer services.***

Historically, our core businesses have been English language training for adults and test preparation courses for college and graduate students. We have launched many new services to expand our business and student base. For example, in 2008, we launched our New Oriental U-Can (Non-English) training program, which targets middle and high school students in China from ages 13 to 18 who are preparing for the college entrance examination in China, known as the gaokao. The gaokao is required for admission to bachelor degree programs and most associate degree programs at colleges and universities in China. In January 2010, we established a small pilot program whereby we permit third parties in certain small cities to offer our Pop Kids English program and New Oriental Star kindergarten program under a brand name cooperation model. The cooperation facilities operated by such third parties are not included in the counts of our schools and learning centers, and student enrollments from these facilities are not included as our student enrollments.



## **Table of Contents**

Some of these operations have not generated significant or any profit to date, and we have less experience responding quickly to changes, competing successfully and maintaining and expanding our brand in these areas without jeopardizing our brand in other areas. Consequently, there is limited operating history on which you can base your evaluation of the business and prospects of these relatively more recent operations.

***The continuing efforts of our senior management team and other key personnel are important to our success, and our business may be harmed if we lose their services.***

It is important for us to have the continuing services of our senior management team, in particular, Michael Minhong Yu, our founder, chairman and chief executive officer, who has been our leader since our inception in 1993. If one or more of our senior executives or other key personnel are unable or unwilling to continue in their present positions, we may not be able to replace them easily, and our business may be disrupted. Competition for experienced management personnel in the private education sector is intense, the pool of qualified candidates is very limited, and we may not be able to retain the services of our senior executives or key personnel, or attract and retain high-quality senior executives or key personnel in the future. In addition, if any member of our senior management team or any of our other key personnel joins a competitor or forms a competing company, we may lose teachers, students, key professionals and staff members. Each of our executive officers and key employees is subject to the duty of confidentiality and non-competition restrictions. However, if any disputes arise between any of our senior executives or key personnel and us, it may be difficult to successfully pursue legal actions against these individuals because of the uncertainties of China's legal systems.

***We generate a significant portion of our revenues from four cities in China. Any event negatively affecting the private education industry in these cities could have a material adverse effect on our overall business and results of operations.***

We derived approximately 41.6% of our total net revenues for the fiscal year ended May 31, 2013 from our operations in Beijing, Shanghai, Wuhan and Guangzhou, and we expect these four cities to continue to constitute important sources of our revenues. If any of these cities experiences an event negatively affecting its private education industry, such as a serious economic downturn, a natural disaster or an outbreak of contagious disease, or if any of these cities adopts regulations relating to private education that place additional restrictions or burdens on us, our overall business and results of operations may be materially and adversely affected.

***If we are not able to continually enhance our online programs, services and products and adapt them to rapid technological changes and student needs, we may lose market share and our business could be adversely affected.***

The market for internet-based educational programs, services and products is characterized by rapid technological changes and innovation, unpredictable product life cycles and user preferences. We have limited experience with generating revenues from online programs, services and products, and their results are largely uncertain. The increasing adoption of computer-based testing formats for admissions testing may lead more students to seek online test preparation courses. We must quickly modify our programs, services and products to adapt to changing student needs and preferences, technological advances and evolving internet practices. Ongoing enhancement of our online offerings and related technology may entail significant expense and technical risk. We may fail to use new technologies effectively or adapt our online products or services and related technology on a timely and cost-effective basis. If our improvements to our online offerings and the related technology are delayed, result in systems interruptions or are not aligned with market expectations or preferences, we may lose market share and our business could be adversely affected.

## **Table of Contents**

### ***Failure to maintain effective internal control over financial reporting could have a material and adverse effect on the trading price of our ADSs.***

We are subject to the reporting obligations under the U.S. securities laws. Although our management concluded, and our independent registered public accounting firm reported, that we maintained effective internal control over financial reporting as of May 31, 2013, we cannot assure you that we will maintain effective internal control over financial reporting on an ongoing basis. If we fail to maintain effective internal control over financial reporting, we will not be able to conclude and our independent registered public accounting firm will not be able to report that we have effective internal control over financial reporting in accordance with the Sarbanes-Oxley Act of 2002 in our future annual report on Form 20-F covering the fiscal year in which this failure occurs. Effective internal control over financial reporting is necessary for us to produce reliable financial reports. Any failure to maintain effective internal control over financial reporting could result in the loss of investor confidence in the reliability of our financial statements, which in turn could have a material and adverse effect on the trading price of our ADSs. Furthermore, we may need to incur additional costs and use additional management and other resources as our business and operations further expand or in an effort to remediate any significant control deficiencies that may be identified in the future.

### ***We do not have any liability or business disruption insurance, and a liability claim against us due to injuries suffered by our students or other people at our facilities could adversely affect our reputation and our financial results.***

We could be held liable for accidents that occur at our schools, learning centers and other facilities, including indoor facilities where we organize certain summer camp activities and temporary housing facilities that we lease for our students from time to time. In the event of on-site food poisoning, personal injuries, fires or other accidents suffered by students or other people, we could face claims alleging that we were negligent, provided inadequate supervision or were otherwise liable for the injuries. We currently do not have any liability insurance or business disruption insurance. A successful liability claim against us due to injuries suffered by our students or other people at our facilities could adversely affect our reputation and our financial results. Even if unsuccessful, such a claim could cause unfavorable publicity, require substantial cost to defend and divert the time and attention of our management.

### ***Capacity constraints or system disruptions to our computer systems or websites could damage our reputation, limit our ability to retain students and increase student enrollments and require us to expend significant resources.***

The performance and reliability of our online program infrastructure is critical to our reputation and ability to retain students and increase student enrollments. Any system error or failure, or a sudden and significant increase in traffic, could result in the difficulty of accessing our websites by our students or unavailability of our online programs. We cannot assure you that we will be able to timely expand our online program infrastructure to meet demand for such programs. Our computer systems and operations could be vulnerable to interruption or malfunction due to events beyond our control, including natural disasters and telecommunications failures. If the computer center at our headquarters is damaged by natural disaster, there could be a service delay of up to four hours until our offsite data backup center restores service on our website. We are planning to build an off-site computer center which is expected to restore service within several minutes following significant damage to our on-site computer center.

Our computer networks may also be vulnerable to unauthorized access, hacking, computer viruses and other security problems. A user who circumvents security measures could misappropriate proprietary information or cause interruptions or malfunctions in operations. Any interruption to our computer systems or operations could have a material adverse effect on our ability to retain students and increase student enrollments. Furthermore, we may be required to expend significant resources to protect against the threat of security breaches or to alleviate problems caused by these breaches.

---

## **Table of Contents**

***Terrorist attacks, geopolitical uncertainty and international conflicts involving the U.S. and elsewhere may discourage more students from studying in the United States and elsewhere outside of China, which could cause declines in the student enrollments for our courses.***

Terrorist attacks, geopolitical uncertainty and international conflicts involving the U.S. and elsewhere, such as the attacks on September 11, 2001 and the Boston marathon bombings on April 15, 2013, could have an adverse effect on our overseas test preparation courses and English language training courses. Such attacks may discourage students from studying in the United States and elsewhere outside of China and may also make it more difficult for Chinese students to obtain visas to study abroad. These factors could cause declines in the student enrollments for our test preparation and English language training courses and could have an adverse effect on our overall business and results of operations.

### **Risks Related to Our Corporate Structure**

***If the PRC government finds that the agreements that establish the structure for operating our China business do not comply with applicable PRC laws and regulations, we could be subject to severe penalties.***

PRC laws and regulations currently require any foreign entity that invests in the education business in China to be an educational institution with relevant experience in providing educational services outside China. Our offshore holding companies are not educational institutions and do not provide educational services outside China. In addition, in the PRC, foreign ownership of high schools for students in grade ten to twelve is restricted and foreign ownership of primary and middle schools for students in grades one to nine is prohibited. As a result, our offshore holding companies are not allowed to directly own and operate schools in China. We conduct substantially all of our education business in China through a series of contractual arrangements with New Oriental China and its schools and subsidiaries and New Oriental China's shareholder. These contractual arrangements enable us to (1) have power to direct the activities that most significantly affect the economic performance of New Oriental China and its schools and subsidiaries; (2) receive substantially all of the economic benefits from New Oriental China and its schools and subsidiaries in consideration for the services provided by our wholly owned subsidiaries in China; and (3) have an exclusive option to purchase all or part of the equity interests in New Oriental China, when and to the extent permitted by PRC law, or request any existing shareholder of New Oriental China to transfer all or part of the equity interest in New Oriental China to another PRC person or entity designated by us at any time in our discretion. For a description of these contractual arrangements, see Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, its Schools and Subsidiaries and its Shareholder.

Tian Yuan Law Firm, our PRC legal counsel, is of the opinion that the corporate structure of New Oriental China and its schools and subsidiaries and our wholly owned subsidiaries in China are in compliance with existing PRC laws and regulations; and the contractual arrangements among our wholly owned subsidiaries in China, New Oriental China and its schools and subsidiaries and the shareholder of New Oriental China are valid, binding and enforceable under, and do not violate, PRC laws or regulations currently in effect. We have been advised by our PRC legal counsel, however, that there are substantial uncertainties regarding the interpretation and application of current and future PRC laws and regulations. Accordingly, there can be no assurance that the PRC regulatory authorities will not in the future take a view that is contrary to the above opinion of our PRC legal counsel. We have been further advised by our PRC counsel that if we, any of our wholly owned subsidiaries, New Oriental China or any of its schools or subsidiaries are found to be in violation of any existing or future PRC laws or regulations or fail to obtain or maintain any of the required permits or approvals, the relevant PRC regulatory authorities, including the Ministry of Education, which regulates the education industry, would have broad discretion in dealing with such violations, including:

revoking the business and operating licenses of our PRC subsidiaries, New Oriental China or New Oriental China's schools and subsidiaries;

discontinuing or restricting the operations of any related-party transactions among our PRC subsidiaries and New Oriental China and its schools and subsidiaries;

limiting our business expansion in China by way of entering into contractual arrangements;



---

**Table of Contents**

imposing fines or other requirements with which we may not be able to comply;

requiring us to restructure our corporate structure or operations; or

restricting or prohibiting our use of the proceeds of our future offering to finance our business and operations in China.

The imposition of any of these penalties could result in a material and adverse effect on our ability to conduct our business and on our results of operations. If any of these penalties results in our inability to direct the activities of New Oriental China and its schools and subsidiaries that most significantly impact their economic performance, and/or our failure to receive the economic benefits from New Oriental China and its schools and subsidiaries, we may not be able to consolidate New Oriental China and its schools and subsidiaries in our consolidated financial statements in accordance with U.S. GAAP. However, we do not believe that such actions would result in the liquidation or dissolution of our company, our wholly owned subsidiaries in China or New Oriental China or its schools or subsidiaries.

***We rely on contractual arrangements for our operations in China, which may not be as effective in providing operational control as direct ownership.***

We have relied and expect to continue to rely on contractual arrangements with New Oriental China, its schools and subsidiaries and its shareholder to operate our education business. These contractual arrangements may not be as effective in providing us with control over New Oriental China as direct ownership. From the legal perspective, if New Oriental China, any of its schools and subsidiaries or its shareholder fails to perform its respective obligations under the contractual arrangements, we may have to incur substantial costs and spend other resources to enforce such arrangements, and rely on legal remedies under PRC law, including seeking specific performance or injunctive relief and claiming damages. For example, if Beijing Century Friendship Education Investment Co., Ltd., or Century Friendship, the sole shareholder of New Oriental China, were to refuse to transfer its equity interest in New Oriental China to us or our designee when we exercise the call option pursuant to the option agreement, or if it otherwise acts in bad faith toward us, then we may have to take legal action to compel it to fulfill its contractual obligations, which could be time consuming and costly.

These contractual arrangements are governed by PRC law and provide for the resolution of disputes through arbitration in the PRC or through the PRC courts. The legal environment in the PRC is not as developed as in some other jurisdictions, such as the United States. As a result, uncertainties in the PRC legal system could limit our ability to enforce these contractual arrangements. In the fiscal years ended May 31, 2011, 2012 and 2013, New Oriental China and its schools and subsidiaries contributed in aggregate 97.2%, 97.2% and 99.1%, respectively, of our total net revenues. In the event we are unable to enforce these contractual arrangements, we may not be able to have the power to direct the activities that most significantly affect the economic performance of New Oriental China and its schools and subsidiaries, and our ability to conduct our business may be negatively affected, and we may not be able to consolidate the financial results of New Oriental China and its schools and subsidiaries into our consolidated financial statements in accordance with U.S. GAAP.

Within the existing contractual arrangements, seven of our wholly owned subsidiaries in China have entered into a series of service agreements with New Oriental China and its schools and subsidiaries to enable them to receive substantially all of the economic benefits of New Oriental China and its schools and subsidiaries. However, under certain service agreements, the renewal of the agreements requires both parties' consents, and in a number of other service agreements, the schools and subsidiaries to New Oriental China may terminate the relevant agreements according to provisions without our consent if our wholly owned subsidiaries breach the terms of the service agreements. See Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, its Schools and Subsidiaries and its Shareholder for more information. We believe that our exclusive option to purchase all or part of the equity interests in New Oriental China, when and to the extent permitted by PRC law, or request any existing shareholder of New Oriental China to transfer all or part of the equity interest in New Oriental China to another PRC person or entity designated by us at any time in our discretion, and the power of attorney that New Oriental China's shareholder has granted to us, effectively enable us to have the ability to cause the related service contracts to be renewed when needed. However, if we are not able to renew these service agreements when they expire or the school and subsidiaries of New Oriental China terminate these agreements according to terms and conditions thereunder, our ability to receive the economic benefits of New Oriental China and its schools and subsidiaries may be adversely affected.

---

**Table of Contents**

***Our ability to enforce the equity pledge agreements between us and New Oriental China's shareholder may be subject to limitations based on PRC laws and regulations.***

Pursuant to the equity pledge agreements among New Oriental China, Century Friendship and five of our wholly owned subsidiaries in China, Century Friendship, as New Oriental China's sole shareholder, agrees to pledge its equity interests in New Oriental China to our subsidiaries to secure New Oriental China's and its schools and subsidiaries' performance of their obligations under the relevant contractual arrangements. The equity pledges of Century Friendship under these equity pledge agreements have been registered with the relevant local branch of the State Administration for Industry and Commerce, or SAIC. According to the PRC Property Law and PRC Guarantee Law, the pledgee and the pledgor are prohibited from making an agreement prior to the expiration of the debt performance period to transfer the ownership of the pledged equity to the pledgee when the obligor fails to pay the debt due. However, under the PRC Property Law, when an obligor fails to pay its debt when due, the pledgee may choose to either conclude an agreement with the pledgor to obtain the pledged equity or seek payments from the proceeds of the auction or sell-off of the pledged equity. If New Oriental China or its shareholder fails to perform its obligations secured by the pledges under the equity pledge agreements, one remedy in the event of default under the agreements is to require the pledgor to sell the equity interests of New Oriental China in an auction or private sale and remit the proceeds to our wholly owned subsidiaries in China, net of related taxes and expenses. Such an auction or private sale may not result in our receipt of the full value of the equity interests in New Oriental China. We consider it very unlikely that the public auction process would be undertaken since, in an event of default, our preferred approach is to ask Shanghai Smart Words Software Technology Co., Ltd., or Shanghai Smart Words, which is one of our PRC wholly owned subsidiaries and a party to the option agreement with New Oriental China's shareholder, to designate another PRC person or entity to replace the existing shareholder of New Oriental China pursuant to the direct transfer option we have under the option agreement.

In addition, in the registration forms of the local branch of State Administration for Industry and Commerce for the pledges over the equity interests under the equity pledge agreements, the amount of registered equity interests pledged to our wholly owned subsidiaries was stated as RMB3,000,000, RMB18,500,000, RMB9,500,000, RMB14,000,000 and RMB5,000,000, respectively, which in aggregate represent 100% of the registered capital of New Oriental China. The equity pledge agreements with New Oriental China's shareholder provide that the pledged equity interest shall constitute continuing security for any and all of the indebtedness, obligations and liabilities under all of the principal service agreements and the scope of pledge shall not be limited by the amount of the registered capital of New Oriental China. However, it is possible that a PRC court may take the position that the amount listed on the equity pledge registration forms represents the full amount of the collateral that has been registered and perfected. If this is the case, the obligations that are supposed to be secured in the equity pledge agreements in excess of the amount listed on the equity pledge registration forms could be determined by the PRC court as unsecured debt, which takes last priority among creditors and often does not have to be paid back at all. We do not have agreements that pledge the assets of New Oriental China and its schools and subsidiaries for the benefit of us or our wholly owned subsidiaries.

***The controlling shareholder of Century Friendship, which is the sole shareholder of New Oriental China, may have potential conflicts of interest with us, and if any such conflicts of interest are not resolved in our favor, our business may be materially and adversely affected.***

New Oriental China is wholly owned by Century Friendship, a PRC domestic company which is beneficially owned by Mr. Michael Minhong Yu, our founder, chairman and chief executive officer. The interests of Mr. Yu as the controlling shareholder of the entity which owns New Oriental China may differ from the interests of our company as a whole, since Mr. Yu is only one of the beneficial owners of our company, holding 16.4% of our total common shares issued and outstanding as of September 20, 2013. We cannot assure you that when conflicts of interest arise, Mr. Yu will act in the best interests of our company or that conflicts of interests will be resolved in our favor. In addition, Mr. Yu may breach or cause New Oriental China and its schools and subsidiaries to breach or refuse to renew the existing contractual arrangements with us. Currently, we do not have existing arrangements to address potential conflicts of interest Mr. Yu may encounter in his capacity as a beneficial owner and director of New Oriental China, on the one hand, and as a beneficial owner and director of our company, on the other hand; provided that we could, at all times, exercise our option under the option agreement with Century Friendship to cause it to transfer all of its equity ownership in New Oriental China to a PRC entity or individual designated by us, and this new shareholder of New Oriental China could then appoint a new director of New Oriental China to replace Mr. Yu. In addition, if such conflicts of interest arise, Beijing Pioneer Technology Co., Ltd., or Beijing Pioneer, our wholly owned PRC subsidiary, could also, in the capacity of Century Friendship's attorney-in-fact as provided under the proxy agreement and power of attorney, directly appoint a new director of New Oriental China to replace Mr. Yu. We rely on Century Friendship and Mr. Yu to comply with the laws of China, which protect contracts, including the contractual arrangements New Oriental China and its schools and subsidiaries and its shareholder have entered into with us, which provide that directors and executive officers owe a duty of loyalty to our company and require them to avoid conflicts of interest and not to take advantage of their positions for personal gains. We also rely on Mr. Yu to abide by the laws of the Cayman Islands, which provide that directors have a duty of care and a duty of loyalty to act honestly in good faith with a view to our best interests. However, the legal frameworks of China and the Cayman Islands do not provide guidance on resolving conflicts in the event of a conflict with another corporate governance regime. If we cannot resolve any conflicts of interest or disputes between us and Century Friendship and Mr. Yu, we would have to rely on legal proceedings, which could result in disruption of our business and subject us to substantial uncertainty as to the outcome of any such legal proceedings.



## **Table of Contents**

*If the custodians or authorized users of our controlling non-tangible assets, including chops and seals, fail to fulfill their responsibilities, or misappropriate or misuse these assets, our business and operations could be materially and adversely affected.*

Under PRC law, legal documents for corporate transactions, including agreements and contracts such as the leases and sales contracts that our business relies on, are executed using the chop or seal of the signing entity or with the signature of a legal representative whose designation is registered and filed with the relevant local branch of the SAIC. We generally execute legal documents by affixing chops or seals, rather than having the designated legal representatives sign the documents.

We have three major types of chops corporate chops, contract chops and finance chops. We use corporate chops generally for documents to be submitted to government agencies, such as applications for changing business scope, directors or company name, and for legal letters. We use contract chops for executing leases and commercial, contracts. We use finance chops generally for making and collecting payments, including, but not limited to issuing invoices. Use of corporate chops and contract chops must be approved by our legal department and administrative department, and use of finance chops must be approved by our finance department. The chops of our subsidiaries and New Oriental China and its schools and subsidiaries are generally held by the relevant entities so that documents can be executed locally. Although we usually utilize chops to execute contracts, the registered legal representatives of our PRC subsidiaries, New Oriental China and its schools and subsidiaries have the apparent authority to enter into contracts on behalf of such entities without chops. All designated legal representatives of our PRC subsidiaries and New Oriental China and its schools and subsidiaries are members of our senior management who have signed employment agreements with us under which they agree to abide by duties they owe to us.

In order to maintain the physical security of our chops, we generally have them stored in secured locations accessible only to the department heads of the legal, administrative or finance departments. Our designated legal representatives generally do not have access to the chops. Although we monitor our employees, including the designated legal representatives of our PRC subsidiaries and New Oriental China and its schools and subsidiaries, the procedures may not be sufficient to prevent all instances of abuse or negligence. There is a risk that our employees or designated legal representatives could abuse their authority, for example, by binding the relevant subsidiary or New Oriental China and its schools and subsidiaries with contracts against our interests, as we would be obligated to honor these contracts if the other contracting party acts in good faith in reliance on the apparent authority of our chops or signatures of our legal representatives. If any designated legal representative obtains control of the chop in an effort to obtain control over the relevant entity, we would need to have a shareholder or board resolution to designate a new legal representative and to take legal action to seek the return of the chop, apply for a new chop with the relevant authorities, or otherwise seek legal remedies for the legal representative's misconduct. If any of the designated legal representatives obtains and misuses or misappropriates our chops and seals or other controlling intangible assets for whatever reason, we could experience disruption to our normal business operations. We may have to take corporate or legal action, which could involve significant time and resources to resolve while distracting management from our operations.

## **Table of Contents**

*Our ability to operate private schools may be subject to significant limitations or may otherwise be materially and adversely affected by changes in PRC laws and regulations.*

The principal regulations governing private education in China are The Law for Promoting Private Education (2003) and The Implementation Rules for the Law for Promoting Private Education (2004). Under these regulations, a private school may elect to be a school that does not require reasonable returns or a school that requires reasonable returns. As of May 31, 2013, 22 of our schools elected as schools not requiring reasonable returns, 30 of our schools elected as schools requiring reasonable returns, and the remaining schools are not classified.

At the end of each fiscal year, every private school is required to allocate a certain amount to its development fund for the construction or maintenance of the school or procurement or upgrade of educational equipment. In the case of a private school that requires reasonable returns, this amount shall be no less than 25% of annual net income of the school, while in the case of a private school that does not require reasonable returns, this amount shall be equivalent to no less than 25% of the annual increase in the net assets of the school, if any. A private school that requires reasonable returns must publicly disclose such election and additional information required under the regulations. A private school shall consider factors such as the school's tuition, ratio of the funds used for education-related activities to the course fees collected, admission standards and educational quality when determining the percentage of the school's net income that would be distributed to the investors as reasonable returns. However, none of the current PRC laws and regulations provides a formula or guidelines for determining reasonable returns. In addition, none of the current PRC laws and regulations sets forth different requirements or restrictions on a private school's ability to operate its education business based on such school's status as a school that requires reasonable returns or a school that does not require reasonable returns.

In some cities, our schools are registered as schools that require reasonable returns, while in other cities, our schools are registered as schools that do not require reasonable returns. The current PRC laws and regulations governing private education may be amended or replaced by new laws and regulations that (1) impose significant limitations on the ability of our schools to operate their business, charge course fees or make payments to related parties for services received, (2) specify the formula for calculating reasonable returns, (3) change the preferential tax treatment policies applicable to private schools, or (4) restrict a private school's ability to make payments to related parties for services. We cannot predict the timing and effects of any such amendments or new laws and regulations. Changes in PRC laws and regulations governing private education or otherwise affecting our schools' operations could materially and adversely affect our business prospects and results of operations. For example, if the PRC government imposes additional limitations on private schools' ability to operate their business or restricts private schools from making payments to related parties for services, our ability to receive service fees from our affiliated schools may be limited or we may have to reorganize our group structure.

On July 29, 2010, the PRC central government promulgated the Outline of China's National Plan for Medium- and Long-Term Education Reform and Development, which for the first time announced the policy that the government will implement a reform to divide private education entities into two categories: (1) for-profit private education entities and (2) not-for-profit private education entities. However, this outline is still new and no further law or regulation has been promulgated to implement the outline. If upon the implementation of this reform, our schools choose to be for-profit private education entities, they may be subject to income tax at the rate of 25% and other taxes as if they were enterprises. For the year ended May 31, 2013, schools that accounted for approximately 62.3% of our consolidated net revenues were subject to a 25% income tax rate. Historically, the effective income tax rates for all our schools were 10.98%, 9.93% and 10.26% in the fiscal years ended May 31, 2011, 2012 and 2013, respectively. Additionally, if our schools choose to be not-for-profit private education entities, our contractual arrangements with New Oriental China and its schools and subsidiaries may be subject to more stringent scrutiny. As a result, implementation of this reform policy may adversely affect our results of operations.

## **Table of Contents**

***Our contractual arrangements may be subject to scrutiny by the PRC tax authorities, and a finding that we owe additional taxes could substantially reduce our consolidated net income and the value of your investment.***

Under PRC laws and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. We could face material and adverse tax consequences if the PRC tax authorities determine that the contractual arrangements among our wholly owned subsidiaries in China and New Oriental China and its schools and subsidiaries do not represent an arm's-length price and adjust New Oriental China or any of its schools or its subsidiaries' income in the form of a transfer pricing adjustment. A transfer pricing adjustment could, among other things, result in a reduction, for PRC tax purposes, of expense deductions recorded by New Oriental China or any of its schools or its subsidiaries, which could in turn increase its tax liabilities. In addition, the PRC tax authorities may impose late payment fees and other penalties to New Oriental China and its schools and subsidiaries for under-paid taxes. Our consolidated net income may be materially and adversely affected if our tax liabilities increase or if we are found to be subject to late payment fees or other penalties.

***Regulatory agencies may commence investigations of the private primary and secondary schools controlled and operated by New Oriental China. If the results of the investigations are unfavorable to us, we may be subject to fines, penalties, injunctions or other censure that could have an adverse impact on our results of operations.***

PRC laws and regulations currently prohibit foreign ownership of primary and middle schools for students in grades one to nine in China, and restrict foreign ownership of high schools for students in grades ten to twelve. New Oriental China controls and operates a private primary and secondary school in Yangzhou and a private secondary school in Beijing. As the provision of private primary and middle school services is a heavily regulated industry in China, our existing and any new primary or middle schools we establish or acquire in the future may be subject from time to time to investigations, claims of non-compliance or lawsuits by governmental agencies, which may allege statutory violations, regulatory infractions or other causes of action. If the results of the investigations are unfavorable to us, we may be subject to fines, injunctions or other penalties that could have an adverse impact on our results of operations. Even if we adequately address the issues raised by a government investigation, we may have to devote significant financial and management resources to resolve these issues, which could harm our business.

***We may rely on dividends and other distributions on equity paid by our wholly owned subsidiaries to fund any cash and financing requirements we may have, and any limitation on the ability of our subsidiaries or New Oriental China and its schools and subsidiaries to make payments to us could have a material adverse effect on our ability to conduct our business.***

We are a holding company, and we may rely on dividends from our wholly owned subsidiaries in China and service, license and other fees paid to our wholly owned subsidiaries by New Oriental China and its schools and subsidiaries for our cash requirements, including any debt we may incur. Current PRC regulations permit our subsidiaries to pay dividends to us only out of their accumulated profits, if any, determined in accordance with Chinese accounting standards and regulations. In addition, each of our subsidiaries and New Oriental China and its subsidiaries in China is required to set aside at least 10% of its after-tax profits each year, if any, to fund a statutory reserve until such reserve reaches 50% of its registered capital, and each of our subsidiaries is required to further set aside a portion of its after-tax profits to fund the employee welfare fund at the discretion of its board of directors. These reserves are not distributable as cash dividends. Furthermore, if our subsidiaries and New Oriental China and its schools and subsidiaries in China incur debt on their own behalf in the future, the instruments governing the debt may restrict their ability to pay dividends or make other payments to us. In addition, the PRC tax authorities may require us to adjust our taxable income under the contractual arrangements we currently have in place in a manner that would materially and adversely affect our subsidiaries' ability to pay dividends and other distributions to us. Moreover, at the end of each fiscal year, every private school in China is required to allocate a certain amount to its development fund for the construction or maintenance of the school or procurement or upgrade of educational equipment. In the case of a private school that requires reasonable returns, this amount shall be no less than 25% of the annual net income of the school, while in the case of a private school that does not require reasonable returns, this amount shall be equivalent to no less than 25% of the annual increase in the net assets of the school, if any. Any limitation on the ability of our subsidiaries to distribute dividends to us or on the ability of New Oriental China and its schools and subsidiaries to make payments to us could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our businesses, pay dividends, or otherwise fund and conduct our business.

---

**Table of Contents**

***PRC regulation of loans to, and direct investment in, PRC entities by offshore holding companies and governmental control of currency conversion may restrict or prevent us from making loans to our PRC subsidiaries or New Oriental China and its schools and subsidiaries or making additional capital contributions to our PRC subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business.***

We are an offshore holding company conducting our operations in China through our PRC subsidiaries and New Oriental China and its schools and subsidiaries. We may need to make loans to our PRC subsidiaries or New Oriental China and its schools and subsidiaries, or we may make additional capital contributions to our PRC subsidiaries.

Any loans to our PRC subsidiaries or New Oriental China and its schools and subsidiaries are subject to PRC regulations. For example, loans by us to our wholly-owned subsidiaries in China, each of which is a foreign-invested enterprise, to finance their activities cannot exceed statutory limits and must be registered with the PRC State Administration of Foreign Exchange, or SAFE, or its local counterparts. Loans by us to New Oriental China and its schools and subsidiaries, which are domestic PRC entities, must be approved by the relevant government authorities and must also be registered with SAFE or its local counterparts.

We may also decide to finance our PRC subsidiaries by means of capital contributions. These capital contributions must be approved by the PRC Ministry of Commerce or its local counterparts. We are unlikely, however, to finance the activities of New Oriental China and its schools and subsidiaries by means of capital contributions due to regulatory issues related to foreign investment in domestic PRC entities, as well as the licensing and other regulatory issues. SAFE promulgated the Circular on the Relevant Operating Issues Concerning the Improvement of the Administration of the Payment and Settlement of Foreign Currency Capital of Foreign Invested Enterprises, or SAFE Circular 142, on August 29, 2008 to regulate the conversion by a foreign-invested company of its capital contribution in foreign currency into RMB. SAFE Circular 142 requires that the paid-in capital of a foreign-invested company settled in RMB converted from foreign currencies shall be used only for purposes within the business scope as approved by the authorities in charge of foreign investment or by other competent authorities and as registered with the local branch of the SAIC and, unless set forth in the business scope or in other regulations, may not be used for equity investments within the PRC. In addition, SAFE strengthened its oversight of the flow and use of the paid-in capital of a foreign-invested company settled in RMB converted from foreign currencies. The use of such RMB paid-in capital may not be changed without SAFE's approval. Violations of Circular 142 will result in severe monetary or other penalties. In strengthening Circular 142, SAFE promulgated the Circular on Further Clarifying and Regulating Relevant Issues Concerning the Administration of Foreign Exchange under Capital Account, or SAFE Circular 45, on November 9, 2011, which expressly prohibits a foreign invested company from converting registered capital in foreign exchange into RMB for the purpose of equity investment, granting certain loans, repayment of inter-company loans, or repayment of bank loans which have been transferred to a third party. As a result, Circular 142 and Circular 45 may significantly limit our ability to transfer capital to New Oriental China and its schools and subsidiaries through our subsidiaries in the PRC, which may adversely affect our ability to expand our business, and we may not be able to convert capital into RMB to invest in or acquire any other PRC companies, or establish other variable interest entities in the PRC. See also Item 4. Information on the Company B. Business Overview Regulation. We cannot assure you that we will be able to obtain these government registrations or approvals on a timely basis, if at all. If we fail to receive such registrations or approvals, our ability to capitalize our PRC operations may be negatively affected, which could adversely affect our liquidity and our ability to fund and expand our business.

***If any of New Oriental China and its schools and subsidiaries becomes the subject of a bankruptcy or liquidation proceeding, we may lose the ability to use and enjoy their assets, which could reduce the size of our operations and materially and adversely affect our business, ability to generate revenue and the market price of our ADSs.***

To comply with PRC laws and regulations relating to foreign ownership restrictions in the education business, we currently conduct substantially all of our operations in China through contractual arrangements with New Oriental China and its schools and subsidiaries as well as its shareholder. As part of these arrangements, New Oriental China and its schools and subsidiaries hold assets that are important to the operation of our business.

---

## **Table of Contents**

We do not have priority pledges and liens against New Oriental China's assets. As a contractual and property right matter, this lack of priority pledges and liens has remote risks. If New Oriental China undergoes an involuntary liquidation proceeding, third-party creditors may claim rights to some or all of its assets and we may not have priority against such third-party creditors on New Oriental China's assets. If New Oriental China liquidates, we may take part in the liquidation procedures as a general creditor under the PRC Enterprise Bankruptcy Law and recover any outstanding liabilities owed by New Oriental China to our PRC subsidiaries under the applicable service agreements. To ameliorate the risks of an involuntary liquidation proceeding initiated by a third-party creditor, we closely monitor the operations and finances of New Oriental China through carefully designed budgetary and internal controls to ensure that New Oriental China is well capitalized and is highly unlikely to trigger any third party monetary claims in excess of its assets and cash resources. Furthermore, our PRC subsidiaries have the ability, if necessary, to inject capital in Renminbi into New Oriental China to prevent such an involuntary liquidation.

If the shareholder of New Oriental China were to attempt to voluntarily liquidate New Oriental China without obtaining our prior consent, we could effectively prevent such unauthorized voluntary liquidation by exercising our right to request New Oriental China's shareholder to transfer all of its equity ownership interest to a PRC entity or individual designated by us in accordance with the option agreement with the New Oriental China shareholder. In addition, under the equity pledge agreements signed by the shareholder of New Oriental China and the PRC Property Law, the shareholder of New Oriental China does not have the right to issue dividends to itself or otherwise distribute the retained earnings or other assets of New Oriental China without our consent. Also, under the proxy agreement and power of attorney, the shareholder of New Oriental China undertakes to Beijing Pioneer, our wholly owned PRC subsidiary, that if it receives, among other things, any dividends, residual assets upon liquidation or proceeds from the transfer of its equity interest in New Oriental China, it will, to the extent permitted under applicable law, remit all such dividends, residual assets and proceeds to Beijing Pioneer without any compensation or other consideration. In the event that the shareholder of New Oriental China initiates a voluntary liquidation proceeding without our authorization or attempts to distribute the retained earnings or assets of New Oriental China without our prior consent, we may need to resort to legal proceedings to enforce the terms of the contractual agreements. Any such litigation may be costly and may divert our management's time and attention away from the operation of our business, and the outcome of such litigation would be uncertain.

### **Risks Related to Doing Business in China**

***Adverse changes in economic and political policies of the PRC government could have a material adverse effect on the overall economic growth of China, which could adversely affect our business.***

Substantially all of our business operations are conducted in China. Accordingly, our results of operations, financial condition and prospects are subject to a significant degree to economic, political and legal developments in China. China's economy differs from the economies of most developed countries in many respects, including with respect to the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth for over three decades, growth has been uneven across different regions and among various economic sectors of China. The PRC government has implemented various measures to encourage economic development and guide the allocation of resources. While some of these measures benefit the overall PRC economy, they may also have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments, conversion of foreign exchange into Renminbi or changes in tax regulations that are applicable to us. In addition, future actions or policies of the PRC government to control the pace of economic growth may cause a decrease in the level of economic activity in China, which in turn could materially affect our liquidity and access to capital and our ability to operate our business.

***Our business, financial condition and results of operations, as well as our ability to obtain financing, may be adversely affected by the downturn in the global or PRC economy.***

The global financial markets experienced significant disruptions in 2008 and the United States, Europe and other economies went into recession. The recovery from the lows of 2008 and 2009 was uneven and it is facing new challenges, including the escalation of the European sovereign debt crisis since 2011 and the slowdown of the Chinese economy in 2012 and the first half of 2013. It is unclear whether the European sovereign debt crisis will be contained and when the Chinese economy will resume the high growth rate. There is considerable uncertainty over the long-term effects of the expansionary monetary and fiscal policies that have been adopted by the central banks and financial authorities of some of the world's leading economies, including China's. There have also been concerns over unrest in the Middle East and Africa, which have resulted in higher oil prices and significant market volatility, and over the possibility of a war involving Iran. There have also been concerns about the economic effect of the earthquake, tsunami and nuclear crisis in Japan and the relationship between China and Japan.



## **Table of Contents**

Economic conditions in China are sensitive to global economic conditions and also have their own challenges, and our business, results of operations and financial condition are sensitive to PRC and global economic conditions. Any prolonged slowdown in the PRC or global economy may have a negative impact on our business, results of operations and financial condition, and continued turbulence in the international markets may adversely affect our ability to access the capital markets to meet liquidity needs.

### ***Uncertainties with respect to the PRC legal system could adversely affect us.***

Our operations in China are governed by PRC laws and regulations. Our subsidiaries are generally subject to laws and regulations applicable to foreign investments in China and, in particular, laws applicable to wholly foreign-owned enterprises. The PRC legal system is based on written statutes. Prior court decisions may be cited for reference but have limited precedential value. China has not developed a fully integrated legal system and recently enacted laws and regulations may not sufficiently cover all aspects of economic activities in China. In particular, because many of these laws and regulations are relatively new, and because of the limited volume of published decisions and their nonbinding nature, the interpretation and enforcement of these laws and regulations involve uncertainties. In addition, the PRC legal system is based in part on government policies and internal rules and interpretations (some of which are not published on a timely basis or at all) that may have a retroactive effect. As a result, we may not be aware of our violation of these policies, rules and interpretations until sometime after the violation. In addition, any litigation in China may be protracted and may result in substantial costs and diversion of resources and management attention.

### ***Regulation and censorship of information disseminated over the internet in China may adversely affect our business and reputation and subject us to liability for information displayed on our websites.***

The PRC government has adopted regulations governing internet access and the distribution of news and other information over the internet. Under these regulations, internet content providers and internet publishers are prohibited from posting or displaying over the internet content that, among other things, violates PRC laws and regulations, impairs the national dignity of China, or is reactionary, obscene, superstitious, fraudulent or defamatory. Failure to comply with these requirements may result in the revocation of licenses to provide internet content and other licenses, and the closure of the concerned websites. In the past, failure to comply with such requirements has resulted in the closure of certain websites. The website operator may also be held liable for such censored information displayed on or linked to the websites. If any of our websites, including those used for our online education business, are found to be in violation of any such requirements, we may be penalized by relevant authorities, and our operations or reputation could be adversely affected.

### ***We are required to obtain various operating licenses and permits and to make registrations and filings for our business operations in China; failure to comply with these requirements may materially adversely affect our business and results of operations.***

We are required to obtain and maintain various licenses and permits and fulfill registration and filing requirements in order to conduct and operate our business. For instance, to establish and operate a school to provide language training and test preparation services, we are required to obtain a private school operating permit and to make necessary filings for each learning center with the local counterparts of the Ministry of Education and the Ministry of Civil Affairs. Our business is also subject to various health, safety and other regulations that affect various aspects of our business in the cities in which we operate and we must obtain various licenses and permits under these regulations for our operations. We have been making efforts to ensure compliance with applicable rules and regulations in all material respects. In addition, we follow internal guidelines to make necessary registrations and filings and obtain necessary licenses and permits on a timely basis. If we fail to comply with applicable legal requirements, we may be subject to fines, confiscation of the gains derived from our noncompliant operations or the suspension of our noncompliant operations, which may materially and adversely affect our business and results of operations.

---

**Table of Contents**

***PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident shareholders to personal liability and limit our ability to inject capital into our PRC subsidiaries, limit our PRC subsidiaries' ability to distribute profits to us or otherwise adversely affect us.***

SAFE issued a public notice in October 2005 and its new implementation rules in April 2011, requiring PRC residents to register with the local SAFE branch before establishing or controlling any company outside of China for the purpose of capital financing with assets or equities of PRC companies, referred to in the notice as an offshore special purpose company. PRC residents that are shareholders of offshore special purpose companies established before November 1, 2005 were required to register with the local SAFE branch before March 31, 2006. Our beneficial owners immediately before our initial public offering who are PRC residents had registered with the local SAFE branch prior to our initial public offering as required under the SAFE notice. The failure of these beneficial owners to timely amend their SAFE registrations, if required, or the failure of future beneficial owners of our company who are PRC residents to comply with the registration procedures set forth in the SAFE notice may subject such beneficial owners to fines and legal sanctions and may also limit our ability to contribute additional capital into our PRC subsidiaries, limit our PRC subsidiaries' ability to distribute dividends or repay loans in foreign exchange to our company or otherwise adversely affect our business.

***We face regulatory uncertainties in China concerning our employees' participation in our share incentive plan.***

On February 15, 2012, SAFE issued the Notices on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in a Stock Incentive Plan of an Overseas Publicly-Listed Company, or Circular No. 7. According to Circular No. 7, if PRC individuals (meaning both PRC residents and non-PRC residents who reside in the PRC for a continuous period of not less than one year, excluding the foreign diplomatic personnel and representatives of international organizations) participate in any share incentive plan of an overseas listed company, a qualified PRC domestic agent, which could be the PRC subsidiaries of such overseas listed company, shall, among other things, file, on behalf of such individuals, an application with SAFE to conduct the SAFE registration with respect to such share incentive plan, and obtain approval for an annual allowance with respect to the purchase of foreign exchange in connection with the share purchase or share option exercise. Such PRC individuals' foreign exchange income received from the sale of shares and dividends distributed by the overseas listed company and any other income shall be fully remitted into a collective foreign currency account in the PRC opened and managed by the PRC domestic agent before distribution to such individuals. In addition, such PRC individuals must also retain an overseas entrusted institution to handle matters in connection with the exercise of their share options and their purchase and sale of shares.

Since Circular No. 7 is relatively new, interpretations and application of this circular involves uncertainties. We are in the process of making application on behalf of the PRC individuals who participate in our company's share incentive plan with SAFE in compliance with Circular No. 7; however, we cannot assure you that such application will be successful. If it is determined that we or the participants of our share incentive plan who are PRC individuals do not fully comply with Circular No. 7 or other applicable regulations, we and participants of our share incentive plan who are PRC individuals may be subject to fines and legal sanctions and government agencies may prevent us from further granting options under our share incentive plan to our employees who are PRC individuals. Such events could adversely affect our ability to retain talented employees.

***The M&A rules establish complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.***

On August 8, 2006, six PRC regulatory agencies, namely the Ministry of Commerce, the State Assets Supervision and Administration Commission, the State Administration for Taxation, the State Administration for Industry and Commerce, the China Securities Regulatory Commission, or the CSRC, and SAFE, jointly adopted the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, commonly referred to as the M&A Rules, which became effective on September 8, 2006. The M&A Rules establish procedures and requirements that could make some acquisitions of Chinese companies by foreign investors more time-consuming and complex, including requirements in some instances that the Ministry of Commerce be notified in advance of any change-of-control transaction in which a foreign investor takes control of a Chinese domestic enterprise. We may expand our business in part by acquiring complementary businesses. Complying with the requirements of the M&A Rules to complete such transactions could be time-consuming, and any required approval processes, including obtaining approval from the Ministry of Commerce, may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

## **Table of Contents**

### ***Increases in labor costs in the PRC may adversely affect our business and our profitability.***

The economy of China has been experiencing significant growth, leading to inflation and increased labor costs. According to the National Bureau of Statistics of China, the year-over-year percent change in the consumer price index in China, the broadest measure of inflation, was 2.1% for May 2013. China's overall economy and the average wage in the PRC are expected to continue to grow. As a result, the average wage level for our employees has also increased in recent years. Future increases in China's inflation and material increases in the cost of labor may diminish our competitive advantage and, unless we are able pass on these increased labor costs to our students by increasing prices for our services, our profitability and results of operations could be materially and adversely affected.

### ***Governmental control of currency conversion may affect the value of your investment.***

The PRC government imposes controls on the convertibility between the RMB and foreign currencies and, in certain cases, the remittance of currency out of China. We receive substantially all of our revenues in RMB. Under our current corporate structure, our income at the holding company level may be primarily derived from dividend payments from our PRC subsidiaries. Shortages in the availability of foreign currency may restrict the ability of our PRC subsidiaries and New Oriental China and its schools and subsidiaries to remit sufficient foreign currency to pay dividends or other payments to us, or otherwise satisfy their foreign currency denominated obligations. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade-related transactions, can be made in foreign currencies without prior approval from SAFE by complying with certain procedural requirements. However, approval from appropriate government authorities is required where RMB is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of loans denominated in foreign currencies. The PRC government may also at its discretion restrict access in the future to foreign currencies for current account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currency to satisfy our currency demands, we may not be able to pay dividends in foreign currencies to our shareholders, including holders of our ADSs.

### ***Fluctuation in the value of the RMB may have a material adverse effect on your investment.***

The value of the Renminbi against the U.S. dollar and other currencies is affected by, among other things, changes in China's political and economic conditions and China's foreign exchange policies. The conversion of the Renminbi into foreign currencies, including the U.S. dollar, has been based on exchange rates set by the People's Bank of China. The PRC government allowed the Renminbi to appreciate by more than 20% against the U.S. dollar between July 2005 and July 2008. Between July 2008 and June 2010, this appreciation was halted and the exchange rate between the Renminbi and the U.S. dollar remained within a narrow band. As a consequence, the RMB fluctuated significantly during that period against other freely traded currencies, in tandem with the U.S. dollar. Since June 2010, the PRC government has allowed the Renminbi to appreciate slowly against the U.S. dollar again, though there have been periods when the U.S. dollar has appreciated against the Renminbi. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future. In addition, there remains significant international pressure on the PRC government to adopt a substantial liberalization of its currency policy, which could result in further appreciation in the value of the RMB against the U.S. dollar.

Our revenues and costs are mostly denominated in the RMB, and a significant portion of our financial assets are also denominated in RMB. We may rely entirely on dividends and other fees paid to us by our subsidiaries and New Oriental China and its schools and subsidiaries in China. Any significant revaluation of the RMB may materially and adversely affect our cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, our ADSs in U.S. dollars. For example, a further appreciation of the RMB against the U.S. dollar would make any new RMB-denominated investments or expenditures more costly to us, to the extent that we need to convert U.S. dollars into the RMB for such purposes. Conversely, a significant depreciation of the RMB against the U.S. dollar may significantly reduce our reported earnings in U.S. dollars, which in turn could adversely affect the price of our ADSs.

**Table of Contents**

*The discontinuation of any preferential tax treatments currently available to us could materially and adversely affect our results of operations.*

On March 16, 2007, the National People's Congress passed the Enterprise Income Tax Law, or the EIT Law, which took effect on January 1, 2008. The EIT Law applies a uniform 25% enterprise income tax rate to both foreign-invested enterprises and domestic enterprises. The EIT Law provides that preferential tax treatments will be granted to industries and projects that are strongly supported and encouraged by the state, and that enterprises otherwise classified as high and new technology enterprises strongly supported by the state will be entitled to a preferential enterprise income tax rate. The implementation rules of the EIT Law promulgated by the State Council in December 2007 and other supplemental rules promulgated by the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation in April 2008 and July 2008, respectively, have stipulated new criteria for such high and new technology enterprises, and all enterprises which had been granted such status before the effectiveness of the EIT Law are required to be re-examined according to such new rules before they can continue to be entitled to such preferential tax treatments.

In December 2008, two of our wholly owned subsidiaries in China, Beijing Hewstone Technology Co., Ltd., or Beijing Hewstone, and Beijing Decision Education & Consulting Co., Ltd., or Beijing Decision, and one subsidiary of New Oriental China, Beijing New Oriental Xuncheng Network Technology Co., Ltd., or Xuncheng Network, were recertified as high and new technology enterprise in Beijing. All of them are entitled to a 15% tax rate as long as they continue to qualify as a high and new technology enterprise. Enterprises that qualify as a newly established software enterprise are exempt from enterprise income tax for two years beginning in the enterprise's first profitable year followed by a tax rate of 12.5% for the succeeding three years. Beijing Pioneer, Shanghai Smart Words and Beijing Smart Wood qualified as newly established software enterprises and were exempt from income taxes from January 2010 through December 31, 2011, from January 2011 through December 31, 2012 and from January 2012 through December 31, 2013, respectively, and a tax rate of 12.5% through December 31, 2014, through December 31, 2015 and through December 31, 2016, respectively.

According to The Implementation Rules for the Law for Promoting Private Education (2004), private schools that do not require reasonable returns enjoy the same preferential tax treatment as public schools, while the preferential tax treatment policies applicable to private schools requiring reasonable returns shall be separately formulated by the relevant authorities under the State Council. As of May 31, 2013, 22 of our schools elected as schools not requiring reasonable returns, 30 of our schools elected as requiring reasonable returns and the remaining schools were not classified. The implementing rules of the EIT Law provide certain conditions under which not-for-profit entities may be exempted from enterprise income tax. According to such conditions, our schools may not be entitled to income tax exemption. To date, however, no separate specific regulations or policies have been promulgated by the relevant authorities in this regard and whether our schools can be entitled to any preferential income tax treatment remains unclear. In practice, tax treatments for private schools vary across different cities in China. For example, private schools in certain cities are subject to a 25% standard enterprise income tax starting from January 1, 2008, while in other cities, private schools are subject to a fixed amount of enterprise income tax each year as determined by the local tax authority in lieu of the 25% standard enterprise income tax or are not required to pay enterprise income tax. On July 8, 2013, Shanghai promulgated the Interim Measures for the Registration of Operational Private Training Institutions, or Measure No. 5, which requires for-profit private training institutions to register with local administration of industry and commerce bureau. The Measure No. 5 came into effect on August 8, 2013 and will remain effective for two years. Our school in Shanghai has been subject to 25% standard enterprise income tax, and is thus not affected by Measure No. 5. However, if similar regulations or policies are promulgated in other cities where we operate, and our schools choose to be or are required to be registered as for-profit private training institutions, they may be required to pay 25% standard enterprise income tax, which may be higher than the tax rates they are currently subject to, and our results of operations may be materially and adversely affected. Beijing Haidian School was not required by the governing tax bureau to pay any EIT since its establishment through May 31, 2013. Preferential tax treatments granted to us by governmental authorities are subject to review and may be adjusted or revoked at any time in the future. The discontinuation of any preferential tax treatments currently available to us, especially to those schools in major cities, will cause our effective tax rate to increase, which will increase our income tax expenses and in turn decrease our net income.

---

**Table of Contents**

***We may be treated as a resident enterprise for PRC tax purposes under the EIT Law, which may subject us to PRC income tax for our global income and withholding for any dividends we pay to our non-PRC shareholders and ADS holders.***

Under the EIT Law, enterprises established outside of China whose de facto management bodies are located in China are considered resident enterprises, and will generally be subject to the uniform 25% enterprise income tax rate for their global income. Although the term de facto management bodies is defined as management bodies which has substantial and overall management and control power on the operation, human resources, accounting and assets of the enterprise, the circumstances under which an enterprise's de facto management body would be considered to be located in China are currently unclear. A circular issued by the State Administration of Taxation on April 22, 2009 provides that a foreign enterprise controlled by a PRC company or a PRC company group will be classified as a resident enterprise with its de facto management bodies located within China if the following requirements are satisfied: (1) the senior management and core management departments in charge of its daily operations function mainly in the PRC; (2) its financial and human resources decisions are subject to determination or approval by persons or bodies in the PRC; (3) its major assets, accounting books, company seals, and minutes and files of its board and shareholders meetings are located or kept in the PRC; and (4) at least half of the enterprise's directors or senior management with voting rights reside in the PRC. In addition, the State Administration of Taxation recently promulgated the Interim Provisions on Administration of Income Tax of Chinese-Controlled Resident Enterprise Registered Overseas, effective from September 1, 2011, which clarified certain matters concerning the determination of resident status, administrative matters following this determination, and competent tax authorities. These interim provisions also specify that when an enterprise which is both Chinese-controlled and incorporated outside of mainland China receives PRC-sourced incomes such as dividends and interests, no PRC withholding tax is applicable if such enterprise has obtained a certificate evidencing its status as a PRC resident enterprise which is registered overseas and controlled by Chinese.

Most members of our management team are based in China and are expected to remain in China. Although our offshore holding companies are not controlled by any PRC company or company group, we cannot assure you that we will not be deemed to be a PRC resident enterprise under the EIT Law and its implementation rules. If we are deemed to be a PRC resident enterprise, we will be subject to PRC enterprise income tax at the rate of 25% on our global income. In that case, however, dividend income we receive from our PRC subsidiaries may be exempt from PRC enterprise income tax because the EIT Law and its implementation rules generally provide that dividends received by a PRC resident enterprise from its directly invested entity that is also a PRC resident enterprise is exempt from enterprise income tax. Accordingly, if we are deemed to be a PRC resident enterprise and earn income other than dividends from our PRC subsidiaries, a 25% enterprise income tax on our global income could significantly increase our tax burden and materially and adversely affect our cash flow and profitability.

In addition, the EIT Law and its implementation rules are relatively new and ambiguities exist with respect to the interpretation of the provisions relating to identification of PRC-sourced income. If we are deemed to be a PRC resident enterprise, dividends distributed to our non-PRC entity investors by us, or the gain our non-PRC entity investors may realize from the transfer of our common shares or ADSs, may be treated as PRC-sourced income and therefore be subject to a 10% PRC withholding tax pursuant to the EIT Law and, as a result, the value of your investment may be materially and adversely affected.

***Dividends we receive from our subsidiaries located in the PRC are subject to the PRC withholding tax.***

The EIT Law provides that a maximum income tax rate of 20% may apply to dividends payable to non-PRC investors that are non-resident enterprises, to the extent such dividends are derived from sources within the PRC. The State Council has reduced such rate to 10%, in the absence of any applicable tax treaties that may reduce such rate. We are a Cayman Islands holding company and may derive our income from dividends we receive from our operating subsidiaries located in the PRC. If we are required under the EIT Law to pay income tax for any dividends we receive from our PRC subsidiaries, the amount of dividends, if any, we may pay to our shareholders and ADS holders may be materially and adversely affected.

**Table of Contents**

According to The Arrangement between the PRC and the Hong Kong Special Administrative Region on the Avoidance of Double Taxation and Prevention of Fiscal Evasion with respect to Taxes on Income, or the Double Taxation Arrangement (Hong Kong), which became effective on January 1, 2007, The Notice of the State Administration of Taxation on Negotiated Reduction of Dividends and Interest Rates, which was issued on January 29, 2008, and The Notice of the State Administration of Taxation Regarding Interpretation and Recognition of Beneficial Owners under Tax Treaties, which became effective on October 27, 2009, dividends paid to enterprises incorporated in Hong Kong are subject to a withholding tax of 5% provided that a Hong Kong resident enterprise owns over 25% of the PRC enterprise distributing the dividend and can be considered as a beneficial owner and entitled to treaty benefits under the Double Taxation Arrangement (Hong Kong). Elite Concept Holdings Limited, Winner Park Limited and Smart Shine International Limited, our Hong Kong wholly owned subsidiaries, own 100% of our PRC subsidiaries. Thus, dividends paid by our PRC subsidiaries to us through our Hong Kong wholly owned subsidiaries may be subject to the 5% withholding tax if we and our Hong Kong subsidiaries are considered as non-resident enterprises under the EIT Law and our Hong Kong subsidiaries are considered as beneficial owners and entitled to treaty benefits under the Double Taxation Arrangement (Hong Kong). If our Hong Kong subsidiaries are not regarded as the beneficial owners of any such dividends, they will not be entitled to the treaty benefits under the Double Taxation Arrangement (Hong Kong). As a result, such dividends would be subject to regular withholding tax of 10% as provided by the PRC domestic law rather than the favorable rate of 5% applicable under the Double Taxation Arrangement (Hong Kong).

*We face uncertainties with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies.*

Pursuant to the Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprises, or Circular 698, issued by the State Administration of Taxation on December 10, 2009, where a foreign investor transfers the equity interests in a PRC resident enterprise indirectly via disposition of the equity interests of an overseas holding company, or an Indirect Transfer, and such overseas holding company is located in a tax jurisdiction that (1) has an effective tax rate less than 12.5% or (2) does not tax foreign income of its residents, the foreign investor shall report the Indirect Transfer to the competent PRC tax authority. The PRC tax authority will examine the nature of such Indirect Transfer, and if the tax authority considers that the foreign investor has adopted an abusive arrangement in order to reduce, avoid or defer PRC taxes, it may disregard the existence of the overseas holding company and re-characterize the Indirect Transfer such that gains derived from such Indirect Transfer may be subject to PRC withholding tax at a rate of up to 10%. Circular 698 also provides that, where a non-PRC resident enterprise transfers its equity interests in a PRC resident enterprise to its related parties at a price lower than the fair market value, the competent tax authority has the power to make a reasonable adjustment to the taxable income of the transaction. Circular 698 is retroactively effective from January 1, 2008. There is uncertainty as to the application of Circular 698. For example, while the term Indirect Transfer is not clearly defined, it is understood that the relevant PRC tax authorities have jurisdiction regarding requests for information over a wide range of foreign entities having no direct contact with China. Moreover, the relevant authority has not yet promulgated any formal provisions or formally declared or stated how to calculate the effective tax rates in foreign tax jurisdictions, and the process and format of the reporting of an Indirect Transfer to the competent tax authority of the relevant PRC resident enterprise remain unclear. In addition, there are not formal declarations with regard to how to determine whether a foreign investor has adopted an abusive arrangement in order to reduce, avoid or defer PRC tax. As a result, we and our non-resident investors may have the risk of being taxed under Circular 698 and may be required to spend valuable resources to comply with Circular 698 or to establish that we or our non-resident investors should not be taxed under Circular 698, which may have a material adverse effect on our financial condition and results of operations or such non-resident investors' investments in us.

*Our auditor, like other independent registered public accounting firms operating in China, is not permitted to be subject to inspection by the Public Company Accounting Oversight Board, and as such, investors may be deprived of the benefits of such inspection.*

Our independent registered public accounting firm that issues the audit reports included in our annual reports filed with the US Securities and Exchange Commission, as auditors of companies that are traded publicly in the United States and a firm registered with the US Public Company Accounting Oversight Board (United States) (the PCAOB), is required by the laws of the United States to undergo regular inspections by the PCAOB to assess its compliance with the laws of the United States and professional standards. Because our auditors are located in the Peoples Republic of China, a jurisdiction where the PCAOB is currently unable to conduct inspections without the approval of the Chinese authorities, our auditors are not currently inspected by the PCAOB.

## **Table of Contents**

Inspections of other firms that the PCAOB has conducted outside China have identified deficiencies in those firms' audit procedures and quality control procedures, which may be addressed as part of the inspection process to improve future audit quality. This lack of PCAOB inspections in China prevents the PCAOB from regularly evaluating our auditor's audits and its quality control procedures. As a result, investors may be deprived of the benefits of PCAOB inspections.

The inability of the PCAOB to conduct inspections of auditors in China makes it more difficult to evaluate the effectiveness of our auditor's audit procedures or quality control procedures as compared to auditors outside of China that are subject to PCAOB inspections. Investors may lose confidence in our reported financial information and procedures and the quality of our financial statements.

***We may be adversely affected by the outcome of the administrative proceedings brought by the SEC against five accounting firms in China.***

Recently, the SEC commenced administrative proceedings under Rule 102(e) of its Rules of Practice and also under the Sarbanes-Oxley Act of 2002 against the Chinese affiliates of the big four accounting firms, including our auditors, and another accounting firm in China. The Rule 102(e) proceedings initiated by the SEC relate to these firms' failure to produce documents, including audit work papers, to the request of the SEC pursuant to Section 106 of the Sarbanes-Oxley Act of 2002, as the auditors located in the PRC are not in a position lawfully to produce documents directly to the SEC because of restrictions under PRC law and specific directives issued by the CSRC. On May 24, 2013, the PCAOB announced that it had entered into a Memorandum of Understanding on Enforcement Cooperation, or the MOU, with the CSRC and the PRC Ministry of Finance, or MOF, which establishes a cooperative framework between the parties for the production and exchange of audit documents relevant to investigations in the United States and China. The PCAOB continues to be in discussions with the CSRC and MOF to permit joint inspections in China of audit firms that are registered with the PCAOB and audit Chinese companies that trade on stock exchanges in the United States. It is likely that how the administrative proceedings will develop will depend in substantial part on how the MOU is applied in practice and whether the parties to the MOU can make further progress with regard to the cooperation in joint inspection. Therefore, it is difficult to determine the outcome of the administrative proceedings and the consequences thereof to us. Any negative news about the proceedings against these audit firms may erode investor confidence in China-based, United States listed companies and the market price of our ADSs may be adversely affected.

## **Risks Related to Our ADSs**

***The market price for our ADSs may be volatile.***

The market price for our ADSs has fluctuated significantly since our ADSs became listed on the New York Stock Exchange, or the NYSE, on September 7, 2006. See Item 9. The Offer and Listing C. Markets for more information. The market price for our ADSs is likely to be highly volatile and subject to wide fluctuations in response to factors such as:

actual or anticipated fluctuations in our operating results,

changes in financial estimates by securities research analysts,

changes in the economic performance or market valuation of other education companies,

announcements by us or our competitors of material acquisitions, strategic partnerships, joint ventures or capital commitments,

addition or departure of our executive officers,

detrimental negative publicity about us, our competitors or our industry,

regulatory investigation or other governmental proceedings against us,

substantial sales or perception of sales of our ADSs in the public market, and

general economic, regulatory or political conditions in China and the U.S.



## **Table of Contents**

In addition, the stock market in general, and the market prices for companies with operations in China in particular, have experienced volatility that often has been unrelated to the operating performance of such companies. In addition, any negative news or perceptions about inadequate corporate governance practices or fraudulent accounting, corporate structure or other matters of other Chinese companies may also negatively affect the attitudes of investors towards Chinese companies in general, including us, regardless of whether we have conducted any inappropriate activities. Further, the global financial crisis and the ensuing economic recessions in many countries and the slowing Chinese economy have contributed and may continue to contribute to extreme volatility in the U.S. stock market. These broad market and industry fluctuations may adversely affect our operating performance. Volatility or a lack of positive performance in our ADS price may also adversely affect our ability to retain key employees, some of whom have been granted options and other share incentives under our share incentive plan.

***We may need additional capital, and the sale of additional ADSs or other equity securities could result in additional dilution to our shareholders.***

We believe that our current cash and cash equivalents and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs for the near future. We may, however, require additional cash resources to finance our continued growth or other future developments, including any investments or acquisitions we may decide to pursue. The amount and timing of such additional financing needs will vary principally depending on the timing of new school and learning center openings, investments and/or acquisitions, and the amount of cash flow from our operations. If our existing cash resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity securities could result in additional dilution to our shareholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations.

Our ability to obtain additional capital on acceptable terms is subject to a variety of uncertainties, including:

investors' perception of, and demand for, securities of educational service providers;

conditions of the U.S. and other capital markets in which we may seek to raise funds;

our future results of operations, financial condition and cash flows;

PRC governmental regulation of foreign investment in education in China;

economic, political and other conditions in China; and

PRC governmental policies relating to foreign currency borrowings.

We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all, especially in the event of a severe and prolonged global economic recession. If we fail to raise additional funds, we may need to reduce our growth to a level that can be supported by our cash flow. Without additional capital, we may not be able to open additional schools and learning centers, acquire necessary technologies, products or businesses, hire, train and retain teachers and other employees, market our programs, services and products, or respond to competitive pressures or unanticipated capital requirements.

***If securities or industry analysts publish negative reports about our business, the price and trading volume of our ADSs securities could decline.***

The trading market for our ADSs is influenced by the research reports and ratings that securities or industry analysts or ratings agencies publish about us, our business and the private education market in China in general. We do not have any control over these analysts or agencies. If one or more of the analysts or agencies who cover us downgrades us or our securities, the price of our ADSs may decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could

cause the price of our ADSs or trading volume to decline.

## **Table of Contents**

***You may not have the same voting rights as the holders of our common shares and may not receive voting materials in time to be able to exercise your right to vote.***

Except as described in the deposit agreement, holders of our ADSs will not be able to exercise voting rights attaching to the common shares evidenced by our ADSs on an individual basis. Holders of our ADSs will appoint the depository or its nominee as their representative to exercise the voting rights attaching to the common shares represented by the ADSs. You may not receive voting materials in time to instruct the depository to vote, and it is possible that you, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote. Upon our written request, the depository will mail to you a shareholder meeting notice which contains, among other things, a statement as to the manner in which your voting instructions may be given, including an express indication that such instructions may be given or deemed given to the depository to give a discretionary proxy to a person designated by us if no instructions are received by the depository from you on or before the response date established by the depository. However, no voting instruction shall be deemed given and no such discretionary proxy shall be given with respect to any matter as to which we inform the depository that (1) we do not wish such proxy given, (2) substantial opposition exists or (3) such matter materially and adversely affects the rights of shareholders.

***You may not be able to participate in rights offerings and may experience dilution of your holdings as a result.***

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement for the ADSs, the depository will not offer those rights to ADS holders unless both the rights and the underlying securities to be distributed to ADS holders are either registered under the Securities Act, or exempt from registration under the Securities Act with respect to all holders of ADSs. We are under no obligation to file a registration statement with respect to any such rights or underlying securities or to endeavor to cause such a registration statement to be declared effective. In addition, we may not be able to take advantage of any exemptions from registration under the Securities Act. Accordingly, holders of our ADSs may be unable to participate in our rights offerings and may experience dilution in their holdings as a result.

***You may be subject to limitations on transfer of your ADSs.***

Your ADSs are transferable on the books of the depository. However, the depository may close its transfer books at any time or from time to time when it deems expedient in connection with the performance of its duties. In addition, the depository may refuse to deliver, transfer or register transfers of ADSs generally when our books or the books of the depository are closed, or at any time if we or the depository deems it advisable to do so because of any requirement of law or of any government or governmental body, or under any provision of the deposit agreement, or for any other reason.

***You may experience difficulties in effecting service of legal process, enforcing foreign judgments or bringing original actions in the Cayman Islands or China based on United States or other foreign laws against us or our management.***

We are incorporated in the Cayman Islands and conduct substantially all of our operations in China. Substantially all of our assets are located in China. All of our executive officers reside in China and some or all of the assets of those persons are located outside of the United States. As a result, it may be difficult for you to effect service of process within the United States or elsewhere outside the Cayman Islands and China upon us or our executive officers, including with respect to matters arising under U.S. federal securities laws or applicable state securities laws. It may also be difficult or impossible for you to bring an action against us or against our executive officers in the Cayman Islands or in China in the event that you believe that your rights as an ADS holder have been infringed under the securities laws of the United States or otherwise. Even if you are successful in bringing an action of this kind in the United States, the respective laws of the Cayman Islands and China may render you unable to enforce a judgment against our assets or the assets of our directors and officers. There is no statutory recognition in the Cayman Islands of judgments obtained in the United States, although the courts of the Cayman Islands will generally recognize and enforce a non-penal judgment of a foreign court of competent jurisdiction without retrial on the merits. Moreover, our PRC counsel has advised us that the PRC does not have treaties with the United States or many other countries providing for the reciprocal recognition and enforcement of judgment of courts.

## **Table of Contents**

***We are a Cayman Islands company and, because judicial precedent regarding the rights of shareholders is more limited under Cayman Islands law than under U.S. law, you may have less protection of your shareholder rights than you would under U.S. law.***

Our corporate affairs are governed by our memorandum and articles of association and by the Companies Law (2012 Revision) and common law of the Cayman Islands. The rights of shareholders to take legal action against our directors and us, actions by minority shareholders and the fiduciary responsibilities of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law of the Cayman Islands is derived in part from comparatively limited judicial precedents in the Cayman Islands as well as from English common law, which has persuasive, but not binding, authority on a court in the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands has a less developed body of securities laws as compared to the United States, and provides significantly less protection to investors. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States.

As a result of all of the above, holders and beneficial owners of our ADSs may have more difficulties in protecting their interests through actions against our management, directors or major shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States.

***Our articles of association contain anti-takeover provisions that could have a material adverse effect on the rights of holders of our common shares and ADSs.***

Our articles of association contain provisions that limit the ability of others to acquire control of our company or cause us to engage in change-of-control transactions. These provisions could have the effect of depriving our shareholders of an opportunity to sell their shares at a premium over prevailing market prices by discouraging third parties from seeking to obtain control of our company in a tender offer or similar transaction. For example, our board of directors has the authority, without further action by our shareholders, to issue preferred shares in one or more series and to fix their designations, powers, preferences, privileges, and relative participating, optional or special rights and the qualifications, limitations or restrictions, including dividend rights, conversion rights, voting rights, terms of redemption and liquidation preferences, any or all of which may be greater than the rights associated with our common shares, in the form of ADS or otherwise. Preferred shares could be issued quickly with terms calculated to delay or prevent a change in control of our company or make removal of management more difficult. If our board of directors decides to issue preferred shares, the price of our ADSs may fall and the voting and other rights of the holders of our common shares and ADSs may be materially and adversely affected.

***We may be classified as a passive foreign investment company, which could result in adverse U.S. federal income tax consequences to U.S. holders of our ADSs or common shares.***

A non-U.S. corporation, such as our company, will be a passive foreign investment company, or PFIC, for U.S. federal income tax purposes for any taxable year if either, (1) 75% or more of its gross income for such year consists of certain types of passive income or (2) 50% or more of its average quarterly assets as determined on the basis of fair market value during such year produce or are held for the production of passive income.

Although the law in this regard is unclear, we treat New Oriental China as being owned by us for U.S. federal income tax purposes, not only because we control its management decisions but also because we are entitled to substantially all of the economic benefits associated with this entity, and, as a result, we consolidate this entity's operating results in our combined financial statements. If it were determined, however, that we are not the owner of New Oriental China for U.S. federal income tax purposes, we may be or become a PFIC. Assuming that we are the owner of New Oriental China for U.S. federal income tax purposes, and based upon an analysis of our company's income and assets in respect of the 2013 taxable year, we do not believe that we were a PFIC, for U.S. federal income tax purposes, for the taxable year ended May 31, 2013. In light of the amount of our cash balances and because the value of our assets for purposes of the PFIC test will generally be determined by reference to the market value of our ADSs and common shares, the determination of whether we will be or become a PFIC will depend in large part upon the market value of our ADSs and common shares, of which we cannot control. Accordingly, fluctuations in the market price of our ADSs and common shares may cause us to become a PFIC for the current taxable year or future taxable years. The determination of whether we will be or become a PFIC will also depend, in part, upon the nature of our income and assets over time, which are subject to change from year to year. There can be no assurance that our business plans will not change in a manner that will affect the composition of our income and assets and our PFIC status. Because there are uncertainties in the application of the relevant rules and PFIC status is a fact-intensive determination made on an annual basis, no assurance can be given that we are not or will not become classified as a PFIC.

---

**Table of Contents**

If we were to be classified as a PFIC in any taxable year, a U.S. Holder (as defined in Item 10. Additional Information E. Taxation U.S. Federal Income Taxation ) may incur significantly increased U.S. income tax on gain recognized on the sale or other disposition of the ADSs or common shares and on the receipt of distributions on the ADSs or common shares to the extent such gain or distribution is treated as an excess distribution under U.S. federal income tax rules. Further, if we are classified as a PFIC for any year during which a U.S. Holder holds our ADSs or common shares, we generally will continue to be treated as a PFIC for all succeeding years during which such U.S. Holder holds our ADSs or common shares. See Item 10. Additional Information E. Taxation U.S. Federal Income Taxation Passive Foreign Investment Company Rules.

**ITEM 4. INFORMATION ON THE COMPANY**

**A. History and Development of the Company**

Our first school was established by Michael Minhong Yu, our chairman and chief executive officer, in Beijing, China in 1993 to offer TOEFL test preparation courses to college students. We established New Oriental China in 2001 as a domestic holding company to act as the sponsor of our schools and hold some operating subsidiaries. Since our inception, we have grown rapidly and transformed ourselves from primarily a language training and test preparation company to the largest provider of private educational services in China offering a wide range of educational programs, services and products to a varied student population throughout China.

In order to facilitate foreign investment in our company, we established our offshore holding company, New Oriental Education & Technology Group Inc., in the British Virgin Islands in August 2004. On January 25, 2006, our shareholders approved the change of our offshore holding company's corporate domicile to the Cayman Islands, and we are now a Cayman Islands company. Since December 2007, we have established three wholly-owned subsidiaries in Hong Kong, which now directly own our wholly-owned subsidiaries in China.

We and certain selling shareholders of our company completed an initial public offering and listed our ADSs on the NYSE under the symbol EDU in September 2006. In February 2007, we and certain selling shareholders of our company completed an additional public offering of ADSs. On August 18, 2011, we effected a change in the ratio of our ADSs to common shares from one ADS representing four common shares to one ADS representing one common share.

Our principal executive offices are located at No. 6 Hai Dian Zhong Street, Haidian District, Beijing 100080, People's Republic of China. Our telephone number at this address is +(8610) 6090-8000. Our registered office in the Cayman Islands is located at Codan Trust Company (Cayman) Limited, Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands. We have branch offices in 50 cities in China.

**B. Business Overview**

We are the largest provider of private educational services in China based on the number of program offerings, total student enrollments and geographic presence. We offer a wide range of educational programs, services and products, consisting primarily of English and other foreign language training, test preparation courses for admissions and assessment tests in the United States, the PRC and Commonwealth countries, primary and secondary school education, development and distribution of educational content, software and other technology, and online education. We provide educational services primarily under our New Oriental brand, which we believe is the leading consumer brand in China's private education sector.

Since our inception in 1993, we have had approximately 16.1 million cumulative student enrollments. In the fiscal year ended May 31, 2013, we had approximately 2.5 million student enrollments, including approximately 1.8 million student enrollments in our language training programs and approximately 0.7 million student enrollments in our test preparation courses. We deliver our educational programs, services and products to students through an extensive physical network of schools, learning centers and bookstores, as well as through our virtual online network.

**Table of Contents**

Our total net revenues increased from US\$539.9 million for the fiscal year ended May 31, 2011 to US\$959.9 million for the fiscal year ended May 31, 2013, representing a compound annual growth rate, or CAGR, of 33.3%. Net revenues from our language training and test preparation courses accounted for 86.6%, 85.6% and 85.3%, respectively, of our total net revenues in the fiscal years ended May 31, 2011, 2012 and 2013. Net income attributable to New Oriental Education & Technology Group Inc. increased from US\$101.8 million in the fiscal year ended May 31, 2011 to US\$136.3 million in the fiscal year ended May 31, 2013, representing a CAGR of 15.7%.

**Our Network**

We deliver our educational programs, services and products to students through an extensive physical network of 57 schools, 669 learning centers and 32 bookstores operated by us, over 5,000 third-party bookstores and approximately 17,000 teachers in 50 cities as of May 31, 2013, as well as through our online network, which had approximately 8.5 million registered users as of May 31, 2013. In addition, we have an extensive network of students and alumni, which has been essential in helping us promote our brand and our programs, services and products by word-of-mouth referrals and through our students' and alumni's academic and career achievements. We plan to continue to open new schools and learning centers in cities that exhibit strong enrollment potential.

All of our schools, learning centers and bookstores operate under our New Oriental brand. Our hub schools in major cities consist of classrooms and administrative facilities with full student and administrative services, while our schools in satellite cities and our learning centers consist primarily of classroom facilities and limited course registration and management capabilities. We select new locations based on various factors, including demographics and the number of colleges in, and the economic condition of, the particular region. We have opened bookstores in our established schools to primarily sell educational materials relating to our courses and also sell self-help, know-how, inspirational and other books.

We lease all of our facilities except for our Yangzhou school, part of the premises for our headquarters in Beijing and our schools in Xi'an, Tianjin, Kunming, Wuhan, Guangzhou and Changsha. The following table sets forth information concerning the locations of our schools, learning centers and bookstores as of May 31, 2013.

City	Number of schools	Number of learning centers	Number of bookstores
Beijing	5	64	1
Shanghai	1	54	1
Guangzhou	1	29	1
Wuhan	1	44	1
Yangzhou	1		
Tianjin	1	34	1
Xi'an	1	19	1
Nanjing	2	15	1
Shenyang	1	26	1
Chongqing	1	11	1
Chengdu	1	16	1
Shenzhen	1	15	
Xiangyang	1	8	
Taiyuan	1	23	1
Haerbin	1	15	1
Changsha	1	18	1
Jinan	1	21	1
Zhengzhou	1	29	1
Hangzhou	1	22	1
Changchun	3	34	1
Shijiazhuang	1	9	1
Suzhou	1	11	1

**Table of Contents**

City	Number of schools	Number of learning centers	Number of bookstores
Zhuzhou	1	2	
Anshan	1	2	
Hefei	1	11	1
Kunming	1	26	1
Wuxi	1	6	
Foshan	1	3	
Fuzhou	1	11	1
Yichang	1		
Nanchang	1	18	1
Jingzhou	1	2	
Dalian	1	9	1
Lanzhou	1	8	1
Huangshi	1	2	
Ningbo	1	4	1
Xiamen	1	9	1
Qingdao	1	6	1
Nanning	1	5	
Xuzhou	1	6	1
Xiangtan	1		
Zhenjiang	1	1	
Luoyang	1	3	1
Nantong	1		
Jilin	1	2	
Guiyang	1	3	
Hohhot	1	4	1
Tangshan	1	3	
Urumqi	1	4	1
Shiyan	1	2	
Total	57	669	32

**Our Programs, Services and Products**

We provide a wide variety of educational programs, services and products. We deliver education to our students primarily in traditional classroom settings and also through online instruction. With the exception of the full-time primary and secondary school in Yangzhou and a full-time secondary school in Beijing, our classroom-based courses are generally designed to be completed in 2 to 16 weeks. Course fees are determined based on the length of the course, the size and the subject of the class, the area of study and the geographic location of the school. We update and expand our course offerings frequently in response to evolving market needs. We currently have a full-time staff of approximately 450 people involved in our centralized curriculum development process. Our program, service and product offerings are generally divided into seven areas: test preparation; K-12 after-school tutoring, language training; primary and secondary schools and kindergartens; educational content, software and other technology development and distribution; online education; and other services and products.

**Test Preparation Courses**

We offer test preparation courses to students taking language and entrance exams used by educational institutions in the United States, the PRC and Commonwealth countries. In our fiscal year ended May 31, 2013, we had approximately 738,000 student enrollments in our test preparation courses, of which approximately 326,000 were in overseas test preparation courses, 411,000 were in PRC test preparation courses.

We offer test preparation courses for the following major overseas exams: TOEFL, SAT, ACT, IELTS, GRE, GMAT, LSAT, BEC and TOEIC. In addition, we offer test preparation classes for the following major PRC admissions tests: CET 4, CET 6, National Tests for Entrance into Master's Degree Programs, Professional Title English Test and PETS. In November 2007, Educational Testing Service, the creator of TOEFL, and New Oriental reached an agreement making New Oriental's language schools the only language schools in China authorized by the Educational Testing Service to sell the TOEFL Practice Online, or the TPO, in their training classes. As part of the agreement, New Oriental has an exclusive right to provide the TPO as a component of its language training or test preparation courses and may also sell the TPO to the general public through its bookstores. Educational Testing Service will continue to sell the TPO on its own website and through its subsidiaries or other third-party resellers.





## **Table of Contents**

In our fiscal year ended May 31, 2013, approximately 39.0% and 15.6% of the total student enrollments in our overseas test preparation courses took place in Beijing and Shanghai, respectively, and approximately 18.4% of the total student enrollments in our PRC test preparation courses took place in Beijing. Our test preparation courses focus on quality instruction and test-taking techniques designed to help students achieve high scores on the admissions and assessment tests. Except for the customized small class program discussed above, our experienced teachers generally teach in large classes ranging from 50 to 500 students. Our students enroll in a 20- to 160-hour program with classes meeting one to four times per week for approximately 2.5 hours per class. We also offer intensive and condensed versions of our courses, which are compacted into shorter time periods. Course fees for our test preparation courses range from RMB150 to RMB25,000 per course.

### ***K-12 After-School Tutoring Courses***

*After-School Tutoring Courses for Middle School and High School Students.* Given the intense competition to gain admission into top high schools and higher education institutions in China, exam scores can be a deciding factor in gaining admission. Our after-school tutoring courses for middle school and high school students are designed to supplement students' regular school curricula and help students achieve better scores on entrance exams for admission into high schools or higher education institutions.

English proficiency is tested as a major subject of entrance exams for admission into China's high schools, colleges and universities. In 2002, we first established English after-school training program for middle and high school students. In March 2008, we launched our New Oriental U-Can All Subjects training program, which targets middle and high school Chinese students from ages 13 to 18 who are preparing for the high school entrance examination in China, known as the zhongkao and the college entrance examination, known as the gaokao. The gaokao is required for admission to bachelor degree programs and most associate degree programs at Chinese colleges and universities. To complement New Oriental U-Can All Subjects training program, we provide tutoring services to students who seek to retake the gaokao through Tongwen Gaokao School, a private school based in Changchun. In February 2009, we launched a customized learning program for students from ages 12 to 18, offering small class size tutoring ranging from one to five students per class, in all subjects required for the college and high school entrance examinations, respectively. With this strategy of offering affordable larger classes and higher priced individualized small classes for school aged children, we aim to capture more market share in the after-school training market in China.

Our typical U-Can All Subjects after-school tutoring courses for middle school and high school students last for 8 to 16 weeks with classroom instruction one to four times per week for 1.5 to 5 hours per visit. We also offer more intensive and condensed versions of our courses, in particular during the summer months when many academic institutions are on summer break. The sizes of these courses typically range from 1 to approximately 100 students per class.

In our fiscal year ended May 31, 2013, we had approximately 750,000 student enrollments in our after-school tutoring courses for middle school and high school students, and approximately 21.5%, 12.1%, and 5.4% of the enrollments took place in Beijing, Xi'an and Nanchang, respectively. Course fees for our English training courses for middle school and high school students range from approximately RMB200 to approximately RMB3,500 per course.

*After-School Tutoring Courses for Children.* English is a major subject in elementary schools. We established our English for children program in 2002 for children in kindergarten through grade six and it has achieved rapid growth since that time. We designed our English for children program based upon the following principles: (1) we use localized materials originally published by international education content providers and publishers while taking into account the local public schools' curricula and the skills and abilities of the individual child and adapting to his or her particular needs; (2) we assist students in mastering the basics of the language in various fun ways, including interactive games, activities and cultural studies; and (3) we help children develop a passion for learning the language and guide and inspire them to develop their self-learning abilities. In 2008, we launched our Pop Kids All Subjects training program, which offered after-school tutoring courses in English, Math, Chinese, writing, music and Arts for children in kindergarten and elementary schools.

## **Table of Contents**

Our after-school tutoring courses for children are typically divided into classes of 1 to approximately 25 students per class. Students attend class one to two times per week for 1.5 to 2 hours per class. We test our students to measure their progress and make sure they are progressing as needed to advance to the next book and class level without jeopardizing the fundamentals that will allow them to excel in the future.

To enhance our Pop Kids English program, we cooperate with the Sino-British Academic Exchange Center for Education Measurement (SBC), Cambridge ESOL's sole representative in China, for the administration of the Cambridge Young Learners English exam (YLE) to our students in the Pop Kids English program. Cambridge ESOL is a not-for-profit department of the University of Cambridge focusing on examinations for the English language. We currently administer the YLE exam for our POP Kids English students in 28 cities.

In our fiscal year ended May 31, 2013, we had approximately 729,000 student enrollments in our Pop Kids All Subjects after-school tutoring courses and approximately 12.7%, 8.8% and 7.2% of the enrollments took place in Wuhan, Guangzhou and Beijing, respectively. Course fees for these courses range from approximately RMB100 to approximately RMB2,000 per course.

### ***Language Training Courses for Adults***

Our language training courses primarily consist of various types of English language training courses. We also provide training courses for other foreign languages, including German, Japanese, French, Korean and Spanish.

English language training courses is a primary component of our language training courses. Many employers in China, including foreign-invested enterprises, multinational corporations' branch offices as well as domestic enterprises involved in international business transactions or the tourism industry, require their employees to have a high level of English proficiency. Our English for adults program offers courses designed to teach and improve students' English writing, reading, listening and speaking skills. Our schools and learning centers also have language labs at which our students can listen to and recite spoken passages on CDs and audio tapes to improve their listening and speaking skills. A typical course lasts for 6 to 12 weeks with classroom instruction one to four times per week for two to five hours per visit. We also offer more intensive and condensed versions of our courses, in particular during the summer months when many academic institutions are on summer break. The sizes of our English for adults courses typically range from 1 to approximately 150 students per class.

In our fiscal year ended May 31, 2013, we had approximately 174,000 student enrollments in our English for adults courses and approximately 28.2%, 15.2% and 7.2% of the total enrollments were for courses taught in Beijing, Shanghai and Wuhan, respectively. Course fees for our English for adults courses range from approximately RMB300 to approximately RMB3,000 per course.

### ***Primary and Secondary Schools***

We established the first full-time private primary and secondary school in Yangzhou in 2002. This is a private boarding school for students in grades 1 to 12 seeking a full curriculum taught in both Chinese and English, with a strong emphasis on English language training. We target parents who desire to provide their children with a global vision and an understanding and appreciation of both traditional Chinese culture and the modern world, a competitive advantage in academics and social development and English language proficiency. Our goal is to develop the Yangzhou school, and other new schools to be established in the future, into elite schools whose students consistently gain acceptance into the top universities in China and around the world.

We attempt to immerse our students in the English language at an early age through native English speaking teachers and activities designed to emphasize early and significant exposure to a bilingual environment. The Yangzhou private school has a capacity of up to 4,000 students. In our fiscal year ended May 31, 2013, we had over 3,700 students at the Yangzhou school, approximately 51% of whom came from Yangzhou, with the remainder from various parts of China. Our students must take an admission test and undergo an interview to gain acceptance into our school.

## **Table of Contents**

There are over 380 teachers and 280 supporting staff at the Yangzhou school. The school has been regarded as one of the best primary and secondary schools in the local market since shortly after its inception. In our fiscal year ended May 31, 2013, the school accepted 1,100 students out of over approximately 2,100 applicants from the local market as well as elsewhere in China.

The Yangzhou school has received various accreditations from local authorities. We work closely with the local educational authorities to make sure that our curriculum is compatible with public school curriculums and covers the full spectrum of required courses. We have also expanded our curriculum to include subjects, activities and techniques that teach the students to learn and think independently. There is less emphasis on memorization and recitation and greater emphasis on creative thinking and analytical activities. We use computers as a major part of our teaching and learning methods and encourage students to learn in an interactive format. In our fiscal year ended May 31, 2013, tuition at the Yangzhou school ranged from RMB17,000 to RMB21,000 per year.

In July 2006, we established an international high school program within the Yangzhou school. In July 2010, we opened an international high school in Beijing. Our international high school aims to provide students with a full curriculum of high school education in a bilingual environment while preparing them for admission into foreign universities. Each of the students of the class of 2013 of the international high school program at our Yangzhou school was admitted into at least one of the top 100 universities in the United States. In our fiscal year ended May 31, 2013, tuition at our international school ranges from RMB80,000 to RMB90,000 per year.

### ***Educational Content, Software and other Technology Development and Distribution***

We develop and edit educational materials for language training and test preparation, such as books, software, CD-ROMs, magazines and other periodicals. We distribute these materials through various distribution channels, consisting of our classrooms and bookstores as well as third-party distributors. In the fiscal year ended May 31, 2013, we developed and edited over 200 titles and distributed over 11.1 million books authored or licensed by us in China. Most of the materials distributed by us are education-related and include the materials that we use in our courses and titles that we market for use in English language area.

Our extensive distribution channels have attracted international education content providers to cooperate with us in distributing localized versions of their materials in China. We currently have arrangements with Pearson Education, The McGraw-Hill Companies, Cambridge University Press, Oxford University Press, McMillan, Harper Collins, Barron's or their respective authorized local publishers, to develop and distribute localized versions of selected educational materials in China, some of which bear both our logo and the original publisher's logo. We plan to establish additional strategic relationships with leading international education content providers to enrich our content offerings.

### ***Online Education***

We offer online education programs on our website [www.koolearn.com](http://www.koolearn.com). As of May 31, 2013, approximately 8.5 million users had registered accounts with us, with access to free informational content on our website. In the fiscal year ended May 31, 2013, we had approximately 176,000 users that paid for additional access to our specialized education programs. These users purchase pre-paid cards that give them the right to use our paid content for a specific period of time or for specific courses.

We currently offer approximately 2,000 online courses, including language training courses, test preparation courses, professional certification courses, and business knowledge and skills training courses in the areas of accounting, legal, management and others. We have live interactive online courses as well as courses that allow students to view replays of pre-recorded lectures. Our online courses are particularly attractive to students who need the flexibility to prepare at any time of the day or night and on short notice. As a supplement to our online courses, we also offer many online study services, including course planning, testing, composition correcting and one-on-one tutoring. Our online tools provide more flexibility by offering our students the ability to choose their best and most convenient way of learning as they experience our programs.

Partially through our Koolearn.com website, we also offer enterprise clients customized training services. By working closely with enterprise clients, we gain a good understanding of the clients' specific training needs and design training solutions to meet those needs. We also have the capability to develop customized e-learning management systems for enterprise clients.

## **Table of Contents**

### ***Other Services***

*Overseas Studies Consulting.* Our consultants help students through the application and admission process for overseas educational institutions and provide useful college, graduate and career counseling advice to help students make informed decisions. We also counsel students with the immigration process for overseas studies, such as obtaining visas and housing. We charge each student a fee based on the scope of consulting services requested by the student.

*Pre-school Education.* In September 2007, we established our pre-school business with the opening of our first kindergarten in Beijing, which currently has 140 students. In April 2009, we opened a kindergarten in Nanjing. As of May 31, 2013, our two kindergartens had a total of 380 students. In our fiscal year ended May 31, 2013, we also had approximately 380 student enrollments in two early childhood learning centers in Beijing.

*Brand Name Cooperation.* In January 2010, we established a small pilot program whereby we permit third parties in certain small cities to offer our Pop Kids English program and New Oriental Star kindergarten program under a brand name cooperation model. The cooperation schools operated by such third parties are not included in the counts of our schools and learning centers, and student enrollments from these schools are not included as our student enrollments. As of May 31, 2013, there were a total of 22 brand cooperation schools. For the fiscal years ended May 31, 2011, 2012 and 2013, we recognized revenues in an aggregate amount of US\$249,000, US\$811,000 and US\$1,577,000, respectively, from license and training fees received from these schools.

### **Marketing and Student Recruitment**

We employ a variety of marketing and recruiting methods to attract students. We have positioned ourselves as a provider of private educational services that inspires students to achieve their potential and build self-confidence and that boosts students' enthusiasm for learning. We believe prospective students are attracted to our schools due to our excellent brand name, the quality of our programs and our relatively long operating history in the private education sector.

We employ the following marketing methods to attract new and returning students:

*Speeches and Seminars.* Our management, most of whom are experienced teachers and were among our earliest teachers, and our top teachers frequently give speeches at colleges, universities, high schools and middle schools and to student groups, parent groups and educational organizations. They also participate in educational seminars and workshops. Their speeches include direct program promotion speeches during which they directly explain the merits and advantages of our programs or general English learning methods, as well as inspirational speeches designed to motivate students to reach their full potential and strive for success.

*Referrals.* Historically, our student enrollments have grown primarily through word-of-mouth referrals. Our student enrollments have benefited and will continue to benefit by referrals from our extensive network of students and alumni and the successful academic and professional careers that many of them have achieved.

*Distribution of Marketing Materials.* We use New Oriental booths and information tables to distribute free inspirational books authored by our chairman and chief executive officer Michael Minhong Yu and others, informational brochures, posters and flyers at various on-campus events, educational expos, conferences and college and employment fairs. We also conduct extensive free information sessions to introduce our programs to our target markets.

*Advertisements.* We advertise through our own websites and also on China's leading portals. We also have advertising arrangements with many Chinese national and regional newspapers and other media outlets, including school campus newspapers. In addition, we advertise through local radio stations and other advertisement platforms, including building lobby or elevator LCD displays and outdoor advertisement displays.

## **Table of Contents**

*Social Events and Activities.* We participate in and host community events designed to promote awareness of the virtues of education. We believe that these events enhance our public image and increase brand awareness. We also host English speech competitions, English drama performances and cultural events designed to raise enthusiasm for English language learning and to further promote awareness of our brand.

*Cross-Selling.* As we gain footholds in many different markets, we use our programs in one market as an opportunity to advertise our programs in other markets. With a variety of programs aimed at different age groups, our goal is to create a brand name that permeates every stage of our potential students' educational, career and life progression, from English for children to English for adults to test preparation to continuing professional education, and to encourage our students to introduce their children to the same system and courses. Outside of our organization, we have established cross-promotional relationships with a number of companies to promote our programs, services and products and awareness of our brand.

## **Competition**

The private education sector in China is rapidly evolving, highly fragmented and competitive, and we expect competition in this sector to persist and intensify. We face competition in each major program we offer and each geographic market in which we operate. For example, we face nationwide competition for our IELTS preparation courses from Global IELTS School, which offers IELTS preparation courses in many cities in China. We face regional competition for our English for children program from several competitors that focus on children's English language training in specific regions, including English First. We face limited competition from many competitors that focus on providing international and/or PRC test preparation courses in specific geographic markets in China. We also face competition from companies that focus on providing after-school tutoring services, including TAL Education Group and Xueda Education Group.

We believe that the principal competitive factors in our markets include the following:

brand recognition;

overall student experience;

ability to effectively market programs, services and products to a broad base of prospective students;

scope and quality of program, service and product offerings; and

alignment of programs, services and products catering to specific needs of students, parents, educators and employers.

We believe that our primary competitive advantages are our well-known New Oriental brand, our innovative and inspirational instruction methods and the breadth and quality of our programs, services and products. However, some of our existing and potential competitors may have more resources than we do. These competitors may be able to devote greater resources than we can to the development, promotion and sale of their programs, services and products and respond more quickly than we can to changes in student demands, testing materials, admissions standards, market needs or new technologies. In addition, we face competition from many different smaller sized organizations that focus on some of our targeted markets, which may be able to respond more promptly to changes in student preferences in these markets.

The increasing use of the internet and advances in internet- and computer-related technologies, such as web video conferencing and online testing simulators, are eliminating geographic and cost-entry barriers to providing private educational services. As a result, many of our international competitors that offer online test preparation and language training courses may be able to more effectively penetrate the China market. Many of these international competitors have strong education brands, and students and parents in China may be attracted to the offerings of our international competitors based in the country that the student wishes to study in or in which the selected language is widely spoken. In addition, many smaller companies are able to use the internet to quickly and cost-effectively offer their programs, services and products to a large number of students with less capital expenditure than previously required.



## **Table of Contents**

### **Regulation**

This section summarizes the principal PRC regulations relating to our businesses.

We operate our business in China under a legal regime consisting of the State Council, which is the highest authority of the executive branch of the PRC central government, and several ministries and agencies under its authority, including the Ministry of Education, or the MOE, the General Administration of Press and Publication, or GAPP, the Ministry of Industry and Information Technology, or the MIIT, the SAIC, the Ministry of Civil Affairs and their respective authorized local counterparts.

### ***Regulations on Private Education***

The principal regulations governing private education in China consist of the Education Law of the PRC, the Law for Promoting Private Education (2003) and the Implementation Rules for the Law for Promoting Private Education (2004), and the Regulations on Chinese-Foreign Cooperation in Operating Schools. Below is a summary of the relevant provisions of these regulations.

#### *Education Law of the PRC*

On March 18, 1995, the National People's Congress enacted the Education Law of the PRC, or the Education Law. The Education Law sets forth provisions relating to the fundamental education systems of the PRC, including a school system of pre-school education, primary education, secondary education and higher education, a system of nine-year compulsory education and a system of education certificates. The Education Law stipulates that the government should formulate plans for the development of education and establish and operate schools and other institutions of education, and that in principle, enterprises, social organizations and individuals are encouraged to operate schools and other types of educational organizations in accordance with PRC laws and regulations. However, no organization or individual may establish or operate a school or any other institution of education for profit-making purposes, though private schools may be operated for reasonable returns, as described in more detail below.

#### *The Law for Promoting Private Education (2003) and the Implementation Rules for the Law for Promoting Private Education (2004)*

The Law for Promoting Private Education became effective on September 1, 2003, and the Implementation Rules for the Law for Promoting Private Education became effective on April 1, 2004. Under these regulations, private schools are defined as schools established by social organizations or individuals using non-government funds. In addition, private schools providing certifications, pre-school education, education for self-study aid and other academic education shall be subject to approval by the education authorities, while private schools engaging in occupational qualification training and occupational skill training shall be subject to approvals from the authorities in charge of labor and social welfare. A duly approved private school will be granted a Permit for Operating a Private School, and shall be registered with the Ministry of Civil Affairs or its local counterparts as a privately run non-enterprise institution. Each of our schools has obtained the Permit for Operating a Private School and has been registered with the relevant local counterpart of the Ministry of Civil Affairs.

Under the above regulations, private schools have the same status as public schools, though private schools are prohibited from providing military, police, political and other kinds of education which are of a special nature. Government-run schools that provide compulsory education are not permitted to be converted into private schools. In addition, the operation of a private school is highly regulated. For example, the types and amounts of fees charged by a private school providing certifications shall be approved by the governmental pricing authority and be publicly disclosed. A private school that does not provide certifications shall file its pricing information with the governmental pricing authority and publicly disclose such information. Except for our primary and secondary school in Yangzhou and a private secondary school in Beijing, which provide graduation certifications to students, none of the schools operated by New Oriental China provides a diploma or certification to students.

Private education is treated as a public welfare undertaking under the regulations. Nonetheless, investors of a private school may choose to require reasonable returns from the annual net balance of the school after deduction of costs, donations received, government subsidies, if any, the reserved development fund and other expenses as required by the regulations. Private schools are divided into three categories: private schools established with donated funds; private schools that require reasonable returns and private schools that do not require reasonable returns.

## Table of Contents

The election to establish a private school requiring reasonable returns shall be provided in the articles of association of the school. The percentage of the school's annual net balance that can be distributed as reasonable return shall be determined by the school's board of directors, taking into consideration the following factors: (1) items and criteria for the school's fees, (2) the ratio of the school's expenses used for educational activities and improving the educational conditions to the total fees collected, and (3) the admission standards and educational quality. The relevant information relating to the above factors shall be publicly disclosed before the school's board determines the percentage of the school's annual net balance that can be distributed as reasonable returns. Such information and the decision to distribute reasonable returns shall also be filed with the approval authorities within 15 days from the decision made by the board. However, none of the current PRC laws and regulations provides a formula or guidelines for determining reasonable returns. In addition, none of the current PRC laws and regulations sets forth different requirements or restrictions on a private school's ability to operate its education business based on such school's status as a school that requires reasonable returns or a school that does not require reasonable returns.

At the end of each fiscal year, every private school is required to allocate a certain amount to its development fund for the construction or maintenance of the school or procurement or upgrade of educational equipment. In the case of a private school that requires reasonable returns, this amount shall be no less than 25% of the annual net income of the school, while in the case of a private school that does not require reasonable returns, this amount shall be equal to no less than 25% of the annual increase in the net assets of the school, if any. Private schools that do not require reasonable returns shall be entitled to the same preferential tax treatment as public schools, while the preferential tax treatment policies applicable to private schools requiring reasonable returns shall be formulated by the finance authority, taxation authority and other authorities under the State Council. To date, however, no regulations have been promulgated by the relevant authorities in this regard. As of May 31, 2013, 22 of our schools elected as schools not requiring reasonable returns, 30 of our schools elected as schools requiring reasonable returns, and the remaining schools are not classified. Preferential tax treatments granted to our schools by governmental authorities are subject to review and may be adjusted or revoked at any time in the future.

### *Sponsorship of Private Schools*

Under the Law for Promoting Private Education and the Implementation Rules for Promoting Private Education, entities and individuals that establish private schools are referred to as sponsors. As of May 31, 2013, New Oriental China was the sponsor of 55 schools and Beijing New Oriental Stars was the sponsor of two kindergartens.

The sponsorship interest that a sponsor holds in a private school is, for all practical purposes, substantially equivalent under PRC law and practice to the equity interest a shareholder holds in a company. Pursuant to the Implementation Rules for Promoting Private Education, a sponsor of a private school has the obligation to make capital contributions to the school in a timely manner. The contributed capital can be in the form of tangible or non-tangible assets such as materials in kind, land use rights or intellectual property rights. Pursuant to the Law for Promoting Private Education, the capital contributed by the sponsor becomes assets of the school and the school has independent legal person status. In addition, pursuant to the Law for Promoting Private Education and the Implementation Rules for Promoting Private Education, the sponsor of a private school has the right to exercise ultimate control over the school. Specifically, the sponsor has control over the private school's constitutional documents and has the right to elect and replace the private school's decision making bodies, such as the school's board of directors, and therefore controls the private school's business and affairs.

Before the Law for Promoting Private Education took effect in 2003, the Regulations on Schools Run by Different Sectors of Society had provided that upon liquidation, the residual assets of a private school after the original investment had been returned to the sponsor would be used by the relevant PRC government for the development of private education. However, this is no longer the case, as Article 68 of the Law for Promoting Private Education expressly abolished the Regulations on Schools Run by Different Sectors of Society. As advised by Tian Yuan Law Firm, our PRC counsel, since the Law for Promoting Private Education became effective on September 1, 2003, there has been no case in China where a private school became state property or was otherwise appropriated by a government authority upon liquidation.



## **Table of Contents**

Furthermore, we are not aware that PRC law provides that upon liquidation of a private school, the sponsor is legally restricted to receive only its invested capital and is not allowed to have other return. According to our PRC counsel, there is no national law that addresses this subject one way or the other. In the absence of a national law providing for the sponsor's rights upon liquidation of a private school, provincial regulations and interpretations are ambiguous and inconsistent on this subject. There are local regulations or interpretations that specifically provide that sponsors are entitled to private schools' residual assets pro rata based on their respective capital contribution. Nevertheless, there are also local regulations that are less clear in this regard.

Notwithstanding the legal uncertainties surrounding this issue, we believe that the potential risk that we will not receive all of the residual assets upon the liquidation of a school is immaterial. There were no capital contributions made by any PRC governmental authorities to our schools. Nor did any of our schools ever receive donations from any third parties, including PRC governmental authorities or any third party enterprises. Since the Law for Promoting Private Education became effective on September 1, 2003, we and our PRC counsel are not aware of any case in China where a private school became state property or was otherwise appropriated by a government authority upon liquidation without the prior consent of its sponsor. We historically have never liquidated any school that was profitable and we have no plan to do so in the future. If, for any reason, we would like to divest a profitable school, a commercially sensible way to do so is to sell the school, rather than to liquidate the school. In this situation, the sponsor is entitled to receive consideration for transferring sponsorship, which often exceeds its initial investment in the school.

### *Regulations on Chinese-Foreign Cooperation in Operating Schools*

Chinese-foreign cooperation in operating schools or training programs is specifically governed by the Regulations on Operating Chinese-Foreign Schools, promulgated by the State Council in 2003 in accordance with the Education Law, the Occupational Education Law and the Law for Promoting Private Education, and the Implementing Rules for the Regulations on Operating Chinese-Foreign Schools. The Regulations on Operating Chinese-foreign Schools and its implementing rules encourage substantive cooperation between overseas educational organizations with relevant qualifications and experience in providing high-quality education and Chinese educational organizations to jointly operate various types of schools in the PRC, with such cooperation in the areas of higher education and occupational education being encouraged. Chinese-foreign cooperative schools are not permitted, however, to engage in compulsory education and military, police, political and other kinds of education that are of a special nature in the PRC.

Permits for Chinese-Foreign Cooperation in Operating Schools shall be obtained from the relevant education authorities or the authorities that regulate labor and social welfare in the PRC. We have not applied for a Permit for Chinese-Foreign Cooperation in Operating Schools at this stage since we currently do not have Chinese-foreign Cooperation Schools.

### *Outline of China's National Plan for Medium- and Long-Term Education Reform and Development (2010-2020)*

On July 29, 2010, the PRC central government promulgated the Outline of China's National Plan for Medium- and Long-Term Education Reform and Development (2010-2020), which for the first time announced the policy that the government will implement a reform to divide private education entities into two categories: (1) for-profit private education entities and (2) not-for-profit private education entities. On October 24, 2010, the General Office of the State Council issued the Notices on the National Education System Innovation Pilot. Under this notice, the PRC government plans to implement a for-profit and non-profit classified management of the private schools in Shanghai, Zhejiang, Shenzhen and Jilin Huaqiao Foreign Language School. However, the above outline and the innovation pilot is still new and no further national law or regulation has been promulgated to implement them and, except in Shanghai, no other local government of the pilot areas has promulgated relevant regulations on differentiated management of the private schools and for-profit training institutions. On July 8, 2013, Shanghai promulgated the Interim Measures for the Registration of Operational Private Training Institutions, or Measure No. 5, which requires for-profit private training institutions to register with local administration of industry and commerce bureau. Measure No. 5 came into effect on August 8, 2013 and will remain effective for two years. Our school in Shanghai has been subject to 25% standard enterprise income tax, and is thus not affected by Measure No. 5. However, if similar regulations or policies are promulgated in other cities where we operate, and our schools choose to be or are required to be registered as for-profit private training institutions, they may be required to pay 25% standard enterprise income tax, which is higher than the tax rates they are currently subject to. In addition, if our schools choose to be not-for-profit private education entities, our contractual arrangements with New Oriental China and its schools and subsidiaries may be subject to more stringent scrutiny and the education authorities may not allow our schools to pay us services fees under the contractual arrangements as they currently do. As a result, the implementation of this reform may adversely affect our results of operations.

## **Table of Contents**

On June 18, 2012, the MOE issued the Implementation Opinions of the MOE on Encouraging and Guiding the Entry of Private Capital in the Fields of Education and Promoting the Healthy Development of Private Education to encourage private investment and foreign investment in the field of education. According to these opinions, the proportion of foreign capital in a Chinese-foreign education institute shall be less than 50%. These opinions currently do not apply to our schools because we currently do not have Chinese-foreign education institutes.

### *Regulations on Online and Distance Education*

Pursuant to the Administrative Regulations on Educational Websites and Online and Distance Education Schools issued by the MOE in 2000, educational websites and online education schools may provide educational services in relation to higher education, elementary education, pre-school education, teaching education, occupational education, adult education, other education and public educational information services.

Educational websites refer to organizations providing education or education-related information services to website visitors by means of a database or online education platform connected via the internet or an educational television station through an Internet Service Provider, or ISP.

Online education schools refer to education websites providing academic education services or training services with the issuance of various certificates.

Setting up education websites and online education schools is subject to approval from relevant education authorities, depending on the specific types of education. Any education website and online education school shall, upon the receipt of approval, indicate on its website such approval information as well as the approval date and file number.

According to the Administrative License Law promulgated by the Standing Committee of the National People's Congress on August 27, 2003 and effective as of July 1, 2004, only laws promulgated by the National People's Congress and regulations and decisions promulgated by the State Council may set down administrative license. On June 29, 2004, the State Council promulgated the Decision on Setting Down Administrative Licenses for the Administrative Examination and Approval Items Really Necessary to be Retained, in which the administrative license for online education schools was retained, while the administrative license for educational websites was not retained.

### *Regulations on Publishing and Distribution of Publications*

On December 25, 2001, the State Council promulgated the Administrative Regulations on Publication, or the Publication Regulations, which became effective on February 1, 2002 and was later amended on March 19, 2011. The Publication Regulations apply to publication activities, i.e., the publishing, printing, copying, importation or distribution of publications, including books, newspapers, periodicals, audio and video products and electronic publications, each of which requires approval from the relevant publication administrative authorities.

On April 13, 2005, the State Council announced a policy on private investments in China that relate to cultural matters, which affects private investments in businesses that involve publishing. The policy authorizes the Ministry of Culture and several other central government authorities to adopt detailed rules to implement the policy. In July 2005, the Ministry of Culture, together with other central government authorities, issued a regulation that prohibits private and foreign investors from engaging in the publishing business. Our subsidiaries and New Oriental China and its schools and subsidiaries are not permitted to engage in the publishing business under this regulation. Beijing New Oriental Dogwood Cultural Communications Co., Ltd., a subsidiary of New Oriental China, has been cooperating with qualified PRC publishing companies to publish our self-developed teaching materials and other content.

## **Table of Contents**

Subsequent to the implementation of the Publication Regulations, GAPP issued the Administrative Regulations on Publications Market, which became effective on September 1, 2003 and which were amended on June 16, 2004. According to the Administrative Regulations on Publications Market, any organization or individual engaged in general distribution, whole sale or retail of publications shall obtain a Permit for Operating Publications. Distribution of publications in the PRC is regulated on different administrative levels. An entity engaged in general distribution of publications shall obtain such permit from GAPP and may conduct general distribution of the publications in the PRC; an entity engaged in wholesaling of publications shall obtain such permit from the provincial counterpart of GAPP and may not engage in general distribution in the PRC; and an entity engaged in retail distribution of publications shall obtain such permit from the local counterpart of GAPP at the county level and may not conduct general distribution or wholesaling of publications in the PRC.

In addition, pursuant to the Administrative Regulations on Publishing Audio-Video Products promulgated by the State Council on December 25, 2001, which became effective as of February 1, 2002, any entity engaged in the wholesale or retail distribution of audio-video products shall secure a Permit for Operating Audio-Video Products from the relevant culture authorities.

The Administrative Regulations on Publishing Audio-Video Products was later amended on March 19, 2011, pursuant to which the Permit for Operating Audio-Video Products is replaced by the Permit for Operating Publications. In addition, GAPP and the Ministry of Commerce jointly issued the Administrative Regulations on Publications Market, which became effective on March 25, 2011, or the New Administrative Regulations on Publications Market. According to the New Administrative Regulations on Publication Market, the distribution of publications is still subject to the same license system provided in the Administrative Regulations on Publications Market, except that the scope of publications is widened to include audio and video products. Upon the effectiveness of the New Administrative Regulations on Publications Market, the Administrative Regulations on Publications Market ceased to be effective, and entities or individuals engaging in distribution of publications, including audio-video products, shall only need to hold a Permit for Operating Publications Business, while a Permit for Publishing Audio-Video Products shall no longer be needed.

The subsidiaries of New Oriental China engaged in the wholesale and retail distribution of books, periodicals, audio-visual products and electronic publications have obtained the relevant Permits for Operating Publications. During the term of the above-mentioned permits or licenses, GAPP or its local counterparts or other competent authorities may conduct annual or random examination or inspection from time to time to ascertain their compliance with applicable regulations and may require for change or renewal of such permits or licenses. If the subsidiaries of New Oriental China engaged in the wholesale and retail distribution of books, periodicals, audio-visual products and electronic publications are not able to pass the subsequent inspection or examination, they may not be able to maintain such permits or licenses necessary for their business.

### ***Regulations on Online Publications***

GAPP and the MIIT jointly promulgated the Tentative Internet Publishing Administrative Measures, or the Internet Publishing Measures, which took effect on August 1, 2002. The Internet Publishing Measures require Internet publishers to obtain approval from GAPP. The term "Internet Publishing" is defined as an act of online dissemination whereby internet information service providers select, edit and process works created by themselves or others (including content from books, newspapers, periodicals, audio and video products, electronic publications, and other sources that have already been formally published or works that have been made public in other media) and subsequently post the same on the internet or transmit the same to users via the internet for browsing, use or downloading by the public.

Xuncheng Network, a subsidiary of New Oriental China engaging in internet content services, received verbal confirmation from GAPP that the online content services that Xuncheng Network provides does not fall within the scope of "Internet Publishing" that requires approval or a license from GAPP. Obtaining an online publication license requires certain conditions, including having five or more qualified editors, which Xuncheng Network cannot satisfy. However, because there is no further official or publicly available interpretation of "Internet publishing," we cannot assure you that Xuncheng Network will not require an online publication license in the future.

## **Table of Contents**

### ***Regulations on Consulting Services for Overseas Studies or Other Overseas Visits for Private Matters***

The Ministry of Public Security and SAIC jointly issued the Administrative Measures on Intermediate Activities relating to Entry and Exit for Private Purpose on June 6, 2001, which requires that any entity engaged in intermediate and consulting services for Chinese citizens going abroad to visit families, relatives or friends, to reside abroad, to inherit properties, or to conduct other non-business matters other than studying, working or touring, shall obtain a license granted by the relevant provincial authority on public security. With respect to intermediate and consulting business activities relating to self-funded overseas studying, the MOE, the Ministry of Public Security and SAIC jointly issued the Administrative Regulations on Intermediate Services for Overseas Studies with Private Funds and their Implementing Rules in 1999, which require that any intermediate service organization engaged in such services procure from the MOE the Recognition on the Intermediate Service Organization for Self-funded Overseas Studies.

Beijing New Oriental Vision Overseas Consulting Co., Ltd., a subsidiary of New Oriental China engaging in overseas studies consulting and other consulting services, has obtained the relevant licenses from the MOE and the Beijing Municipal Public Security Bureau.

### ***Regulations on Internet Information Services***

Subsequent to the State Council's promulgation of the Telecom Regulations and the Internet Information Services Administrative Measures on September 25, 2000, or the Internet Information Measures, the MIIT and other regulatory authorities formulated and implemented a number of Internet-related regulations, including but not limited to the Internet Electronic Bulletin Board Service Administrative Measures, or the BBS Measures.

The Internet Information Measures require that commercial Internet content providers, or ICP providers, obtain a license for Internet information services, or ICP license, from the appropriate telecommunications authorities in order to carry on any commercial Internet information services in the PRC. ICP providers shall display their ICP license number in a conspicuous location on their home page. In addition, the Internet Information Measures also provide that ICP providers that operate in sensitive and strategic sectors, including news, publishing, education, health care, medicine and medical devices, must obtain additional approvals from the relevant authorities in charge of those sectors as well. The BBS Measures provide that any ICP provider engaged in providing online bulletin board services, or BBS, is subject to a filing process with the relevant telecommunications industry authorities. Xuncheng Network has obtained the ICP license and is in the process of completing such filing.

In July 2006, the MIIT posted a notice on its website entitled Notice on Strengthening Management of Foreign Investment in Operating Value-Added Telecom Services. The notice prohibits PRC Internet content providers from leasing, transferring or selling their ICP licenses or providing facilities or other resources to any illegal foreign investors. The notice states that PRC Internet content providers should directly own the trademarks and domain names for websites operated by them, as well as servers and other infrastructure used to support these websites. The notice also states that PRC Internet content providers had until November 1, 2006 to evaluate their compliance with the notice and correct any non-compliance. A PRC Internet content provider's failure to do so by November 1, 2006 may result in revocation of its ICP license.

### ***Regulations on Internet Culture Activities***

The Ministry of Culture of the PRC promulgated the Internet Culture Administration Tentative Measures, or the Internet Culture Measures, on May 10, 2003, which became effective on July 1, 2003, and which were amended on July 1, 2004. The Internet Culture Measures require ICP operators engaging in Internet culture activities to obtain an Internet culture business operations license from the Ministry of Culture in accordance with the Internet Culture Measures. The term Internet culture activities includes, among other things, acts of online dissemination of Internet cultural products, such as audio-visual products, games, performances of plays or programs, works of art and cartoons, and the production, reproduction, importation, sale (wholesale or retail), leasing and broadcasting of Internet cultural products.

Xuncheng Network, a subsidiary of New Oriental China engaging in the distribution of certain audio-visual products through the Internet, received verbal confirmation from the Ministry of Culture that the products of Xuncheng Network do not fall within the definition of Internet culture products and its operations do not fall within the definition of Internet culture activities as defined under the Internet Culture Measures. Accordingly, Xuncheng Network is not required to obtain an Internet culture business operations license. However, because there is no further official or publicly-available interpretation of these definitions, we cannot assure you that Xuncheng Network will not need an Internet culture business operations license in the future.

## **Table of Contents**

### ***Regulation on Broadcasting Audio-Video Programs through the Internet or Other Information Network***

The State Administration of Radio, Film and Television, or SARFT, promulgated the Rules for Administration of Broadcasting of Audio-Video Programs through the Internet and Other Information Networks, or the Broadcasting Rules, in 2004, which became effective on October 11, 2004. The Broadcasting Rules apply to the activities of broadcasting, integration, transmission, downloading of audio-video programs with computers, televisions or mobile phones as the main terminals and through various types of information networks. Pursuant to the Broadcasting Rules, a Permit for Broadcasting Audio-video Programs via Information Network is required to engage in these Internet broadcasting activities. On April 13, 2005, the State Council announced a policy on private investments in businesses in China that relate to cultural matters, which prohibits private investments in businesses relating to the dissemination of audio-video programs through information networks.

On December 20, 2007, SARFT and MIIT issued the Internet Audio-Video Program Measures, which became effective on January 31, 2008. Among other things, the Internet Audio-Video Program Measures stipulate that no entities or individuals may provide Internet audio-video program services without a License for Disseminating Audio-Video Programs through Information Network issued by SARFT or its local counterparts or completing the relevant registration with SARFT or its local counterparts and only entities wholly owned or controlled by the PRC government may engage in the production, editing, integration or consolidation, and transfer to the public through the Internet, of audio-video programs, and the provision of audio-video program uploading and transmission services. On February 3, 2008, SARFT and MIIT jointly held a press conference in response to inquiries related to the Internet Audio-Video Program Measures, during which SARFT and MIIT officials indicated that providers of audio-video program services established prior to the promulgation date of the Internet Audio-Video Program Measures that do not have any regulatory non-compliance records can re-register with the relevant government authorities to continue their current business operations. After the conference, the two authorities published a press release that confirms the above guidelines. On September 15, 2009, SARFT promulgated the Notice on Several Issues regarding the License for Disseminating Audio-Video Programs through Information Network. The Notice restates the necessity of applying for such license and sets forth the legal liabilities for those providing Internet audio-video program services without the license. Xuncheng Network, a subsidiary of New Oriental China engaging in online education services, obtained the License for Disseminating Audio-Video Programs through Information Network from SARFT on January 15, 2010.

### ***Regulations on Protection of the Right of Dissemination through Information Networks***

On May 18, 2006, the State Council promulgated the Regulations on Protection of the Right of Dissemination through Information Networks, which became effective on July 1, 2006. This regulation requires that every organization or individual who disseminates a third party's work, performance, audio or visual recording products to the public through information networks shall obtain permission from, and pay compensation to, the legitimate copyright owner of such products, unless otherwise provided under relevant laws and regulations. The legitimate copyright owner may take technical measures to protect his or her right of dissemination through information networks and any organization or individual shall not intentionally avoid, destroy or otherwise assist others in avoiding such protective measures unless permissible under law. This regulation also provides that permission from and compensation for the copyright owner are not required in the event of limited dissemination to teaching or research staff for the purpose of school teaching or scientific research only.

### ***Regulations on Copyright and Trademark Protection***

China has adopted legislation governing intellectual property rights, including copyrights and trademarks. China is a signatory to the main international conventions on intellectual property rights and became a member of the Agreement on Trade Related Aspects of Intellectual Property Rights upon its accession to the World Trade Organization in December 2001.

## **Table of Contents**

*Copyright.* The National People's Congress amended the Copyright Law in 2001 to widen the scope of works and rights that are eligible for copyright protection. The amended Copyright Law extends copyright protection to Internet activities, products disseminated over the Internet and software products. In addition, there is a voluntary registration system administered by the China Copyright Protection Center.

To address the problem of copyright infringement related to the content posted or transmitted over the Internet, the National Copyright Administration and the MIIT jointly promulgated the Administrative Measures for Copyright Protection Related to the Internet on April 30, 2005. These measures became effective on May 30, 2005.

*Trademark.* The PRC Trademark Law, adopted in 1982 and revised in 2001, protects the proprietary rights to registered trademarks. The Trademark Office under SAIC handles trademark registrations and grants a term of ten years to registered trademarks and another ten years to trademarks as requested upon expiry of the prior term. Trademark license agreements must be filed with the Trademark Office for record. We have registered certain trademarks and logos, including New Oriental and Pop Kids, with the Trademark Office and are in the process of registering additional marks. In addition, if a registered trademark is recognized as a well-known trademark in a specific case, the proprietary right of the trademark holder may be extended beyond the registered sphere of products and services of the trademark in such case. Our trademarks and New Oriental were recognized as well-known trademarks in a civil action adjudicated by the Intermediate People's Court of Jilin City, Jilin Province.

On November 5, 2004, the MIIT amended the Measures for Administration of Domain Names for the Chinese Internet, or the Domain Name Measures. The Domain Name Measures regulate the registration of domain names, such as the first tier domain name .cn. In February 2006, China Internet Network Information Center, or CNNIC, issued the Implementing Rules for Domain Name Registration and the Measures on Domain Name Disputes Resolution, pursuant to which CNNIC can authorize a domain name dispute resolution institution to decide disputes. We have registered many domain names with CNNIC.

## ***Foreign Currency Exchange***

Pursuant to the Foreign Currency Administration Rules promulgated in 1996 and amended in 2008 and various regulations issued by SAFE and other relevant PRC government authorities, RMB is freely convertible to current account items, such as trade-related receipts and payments, interest and dividend. Capital account items, such as direct equity investments, loans and repatriation of investment, require the prior approval from SAFE or its local counterpart for conversion of RMB into a foreign currency, such as U.S. dollars, and remittance of the foreign currency outside the PRC.

Payments for transactions that take place within the PRC must be made in RMB. Unless otherwise approved, PRC companies must repatriate foreign currency payments received from abroad. Domestic enterprises (including foreign-invested enterprises) may retain foreign exchange derived from current account items, but unless otherwise approved, they must convert all of their foreign currency receipts derived from capital account items into RMB.

SAFE promulgated the Circular on the Relevant Operating Issues Concerning the Improvement of the Administration of the Payment and Settlement of Foreign Currency Capital of Foreign Invested Enterprises, or SAFE Circular 142, on August 29, 2008, to regulate the conversion by a foreign-invested company of its capital contribution in foreign currency into RMB. The circular requires that the paid-in capital of a foreign-invested company settled in RMB converted from foreign currencies shall be used only for purposes within the business scope as approved by the authorities in charge of foreign investment or by other competent authorities and as registered with the Administration for Industries and Commerce and, unless set forth in the business scope or in PRC regulations, may not be used for equity investments within the PRC. In addition, SAFE has strengthened its oversight of the flow and use of the paid-in capital of a foreign-invested company settled in RMB converted from foreign currencies. The use of such RMB paid-in capital may not be changed without SAFE's approval. Violations of Circular 142 will result in severe monetary or other penalties. In strengthening Circular 142, SAFE promulgated the Circular on Further Clarifying and Regulating Relevant Issues Concerning the Administration of Foreign Exchange under Capital Account, or SAFE Circular 45, on November 9, 2011, which expressly prohibits a foreign invested company from converting registered capital in foreign exchange into RMB for the purpose of equity investment, granting certain loans, repayment of inter-company loans, or repayment of bank loans which have been transferred to a third party.

## **Table of Contents**

### ***Foreign Exchange Registration of Offshore Investment by PRC Residents***

Pursuant to the SAFE's Notice on Relevant Issues Concerning Foreign Exchange Administration for PRC Residents to Engage in Financing and Inbound Investment via Overseas Special Purpose Vehicles, or SAFE Circular No. 75, issued on October 21, 2005, and the Operating Instructions on SAFE Circular No. 75, or SAFE Circular No. 19, issued on May 27, 2011 and effective July 1, 2011, (1) a PRC citizen residing in the PRC, or PRC Resident, shall register with the local branch of SAFE before it establishes or controls an overseas special purpose vehicle, or SPV, for the purpose of overseas equity financing (including convertible debts financing); (2) when a PRC Resident contributes the assets of or its equity interests in a domestic enterprise into an SPV, or engages in overseas financing after contributing assets or equity interests into an SPV, such PRC Resident shall register his or her interest in the SPV and the change thereof with the local branch of SAFE; and (3) when the SPV undergoes a material event outside of China, such as change in share capital or merger and acquisition, the PRC resident shall, within 30 days from the occurrence of such event, register such change with the local branch of SAFE. PRC residents who are shareholders of SPVs established before November 1, 2005 were required to register with the local SAFE branch before March 31, 2006.

Under SAFE Circular No. 75 and Circular No. 19, failure to comply with the registration procedures set forth above may result in the penalties, including imposition of restrictions on a PRC subsidiary's foreign exchange activities and its ability to distribute dividends to the SPV.

Our beneficial owners immediately before our initial public offering who are PRC residents had registered with the local branch of SAFE prior to our initial public offering as required under SAFE Circular No. 75.

### ***Dividend Distribution***

The principal regulations governing dividend distributions by wholly foreign-owned enterprises and Sino-foreign equity joint ventures include:

Wholly Foreign-Owned Enterprise Law (1986), as amended;

Wholly Foreign-Owned Enterprise Law Implementing Rules (1990), as amended;

Sino-foreign Equity Joint Venture Enterprise Law (1979), as amended; and

Sino-foreign Equity Joint Venture Enterprise Law Implementing Rules (1983), as amended.

Under these regulations, wholly foreign-owned enterprises and Sino-foreign equity joint ventures in the PRC may pay dividends only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. Additionally, these foreign-invested enterprises are required to set aside certain amounts of their accumulated profits each year, if any, to fund certain reserve funds. These reserves are not distributable as cash dividends.

### ***Regulations on Offshore Lending***

On November 19, 2012, the SAFE promulgated the Circular regarding Further Improvement and Adjustment of Policies on Foreign Exchange Administration of Direct Investment, or Circular 59, which aims to simplify foreign exchange administration procedures concerning inbound and outbound direct investment. Pursuant to Circular 59, foreign invested enterprises are permitted to make loans to its offshore parent company provided that the amount of the lending is not greater than the sum of the distributed but unremitted profits and the proportionate undistributed profits.

---

**Table of Contents**

***Provisions Regarding Mergers and Acquisitions of Domestic Enterprises by Foreign Investors***

On August 8, 2006, six PRC regulatory agencies, including the CSRC, promulgated the M&A Rule to more effectively regulate foreign investment in PRC domestic enterprises. The M&A Rule, as amended on June 22, 2009, provides that the Ministry of Commerce must be notified in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise and any of the following situations exists: (1) the transaction involves an important industry in China, (2) the transaction may affect national economic security, or (3) the PRC domestic enterprise has a well-known trademark or historical Chinese trade name in China. The M&A Rule also contains a provision requiring offshore special purpose vehicles, or SPVs, formed for listing purposes through acquisitions of PRC domestic companies and controlled by PRC individuals to obtain the approval of the CSRC prior to publicly listing their securities on an overseas stock exchange.

The M&A Rule became effective on September 8, 2006 without retroactive effect. Based on the advice of Tian Yuan Law Firm, our PRC counsel, we do not believe that the CSRC approval was required for our listing on the NYSE because trading of our ADSs commenced prior to the effective date of the M&A Rule.

***Regulations on Taxation***

On March 16, 2007, the National People's Congress, the Chinese legislature, passed the EIT Law, which took effect on January 1, 2008. The EIT Law applies a uniform 25% enterprise income tax rate to both foreign-invested enterprises and domestic enterprises. There is a transition period for the enterprises, whether foreign-invested or domestic, which had received preferential tax treatments granted by relevant tax authorities prior to March 16, 2007. Enterprises that had been subject to an enterprise income tax rate lower than 25% prior to March 16, 2007 may continue to enjoy the lower rate and gradually transfer to the new tax rate within five years after the effective date of the EIT Law. Enterprises that had been entitled to exemptions or reductions from the standard income tax rate for a fixed term prior to March 16, 2007 may continue to enjoy such treatment until the fixed term expires. Preferential tax treatments will continue to be granted to industries and projects that are strongly supported and encouraged by the state, and enterprises otherwise classified as high and new technology enterprises strongly supported by the state upon re-examination will be entitled to a 15% enterprise income tax rate. The EIT Law empowers the State Council to enact appropriate implementing rules and regulations. The State Council promulgated the implementation rules of the EIT Law in December 2007 and the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation promulgated other supplemental rules in April 2008 and July 2008, respectively, regarding new criteria for the granting of high and new technology enterprises status. According to these rules, all enterprises which have been granted such status before the effectiveness of the EIT Law are required to be re-examined according to such rules before they can continue to be entitled to the preferential tax treatments. Any enterprises to be granted with high and new technology enterprises status shall meet certain requirements, including but not limited to the following: (1) in the latest three years, the enterprise itself owns the intellectual property right for the core technology of its product or service; (2) the enterprise's product or service falls into the ambit of high-tech fields heavily supported by the government; (3) technicians with a bachelor's degree account for more than 30% of all the staff, and the research and development personnel account for more than 10% of all the staff; (4) in the latest three financial years, the research and development expenses account for 3%-6% or more of the latest sales revenue and the research and development expenses incurred within China shall not be less than 60% of the total research and development expenses; and (5) the revenue derived from the high-tech product or service accounts for more than 60% of the total revenue. To apply for the high and new technology enterprises status, an enterprise shall file its corporate certificates and supporting documents evidencing the requirements to the relevant government authority. The government authority will examine the filed certificates and documents to determine whether the enterprise meets the high and new technology enterprises requirements. If the decision is positive, the authority will make a public announcement and grant the enterprise with a high and new technology enterprises certificate with a valid term of three years. Upon the expiration of the initial term, the enterprise shall file a new application to obtain such status. Loss of any preferential tax treatments previously granted to us could have a material and adverse effect on our financial condition and results of operations.



## Table of Contents

According to the Circular On Several Policies for Further Encouraging the Development of Software Industry and Integrated Circuit Industry promulgated by the State Council on January 28, 2011 and the Circular On Policies of Enterprises Income Tax for Further Encouraging the Development of Software Industry and Integrated Circuit Industry, jointly promulgated by the Ministry of Finance and the State Administration of Taxation on April 20, 2012 and effective from January 1, 2011, or Circular 27, an enterprise that qualifies as a software enterprise established after January 1, 2011, or a Software Enterprise, is exempted from enterprise income tax for two years beginning in the enterprise's first profitable year followed by a tax rate of 12.5% for the succeeding three years before December 31, 2017. The qualifications for a Software Enterprise provided in Circular 27 include the following:

the core business shall be software development;

the enterprise shall be a legal person established after January 1, 2011 and shall be granted the status of a Software Enterprise;

the enterprise's employees who have at least a junior college degree shall be more than 40% of the average monthly headcount of its total employees of that year, among whom the research and development staff shall be more than 20% of the average monthly headcount of its total employees of that year;

the enterprise shall own core technology and shall base its operation on such core technology, the annual total research and development expenses shall be more than 6% of its total revenue of that fiscal year, among which the research and development expenses incurred in China shall be more than 60% of the total research and development expenses;

the revenue generated from the sale of its software products shall normally be more than 50% of its total revenue (the revenue generated from the sale of embedded software products and integrated information system products shall be more than 40% of its total revenue), among which the revenue generated from the sale of software products developed by such enterprise shall normally be more than 40% of its total revenue (the revenue generated from the sale of embedded software products and integrated information system products shall be more than 30% of its total revenue);

the enterprise shall own intellectual property rights in the technologies used in its core business, among which its software products shall be certified with testing documents issued by a software testing institution recognized by provincial authority in charge of software industry and with Software Product Registration Certificates granted by the authority in charge of software industry;

the enterprise shall possess the means and ability to ensure the quality of the products it designs, and shall have established a quality control system which is fit for software engineering and shall provide the records for the valid operation of such system; and

the enterprise shall possess operation premises and maintain a working environment suitable for software development, and have technical support for the services it provides.

In order to be qualified as a Software Enterprise and be entitled to such preferential treatment, Software Enterprises are required to submit supporting materials to their respective competent tax authorities within four months from the end of each fiscal year.

The Administrative Provisions for Recognition of Software Enterprises shall be separately established by the Ministry of Industry and Information, the State Development and Reform Commission, the Ministry of Finance, the State Administration of Taxation and other relevant authorities.

Enterprises which have been entitled to similar tax preferential treatments according to previous tax regulations are allowed to continue enjoying the above preferential treatments until the tax holiday granted to them expires, even though they were established before January 1, 2011.

## Edgar Filing: New Oriental Education & Technology Group Inc. - Form 20-F

Three of our wholly owned subsidiaries in China, Beijing Pioneer, Shanghai Smart Words and Beijing Smart Wood, are qualified as Software Enterprises. Beijing Pioneer was exempt from income taxes from January 2010 through December 31, 2011 and have a tax rate of 12.5% through December 31, 2014. Shanghai Smart Words was exempt from income taxes from January 2011 through December 31, 2012 and have a tax rate of 12.5% through December 31, 2015. Beijing Smart Wood is exempt from income taxes from January 1, 2012 through December 31, 2013 followed by a 12.5% tax rate through December 31, 2016. Based on the criteria set out by Circular 27, we believe that another two of our wholly owned subsidiaries in China, Beijing Joy Tend Technology Co., Ltd., or Beijing Joy Tend and Beijing Right Time Technology Co., Ltd., or Beijing Right Time, satisfy the criteria of a Software Enterprise. However, this status is subject to the approval by respective tax authorities.

## **Table of Contents**

The EIT Law also provides that enterprises established outside of China whose de facto management bodies are located in China are considered resident enterprises and will generally be subject to the uniform 25% enterprise income tax rate on their global income. Although the term de facto management bodies is defined as management bodies which has substantial and overall management and control power on the operation, human resources, accounting and assets of the enterprise, the circumstances under which an enterprise's de facto management body would be considered to be located in China are currently unclear. A circular issued by the State Administration of Taxation on April 22, 2009 provides that a foreign enterprise controlled by a PRC company or a PRC company group will be classified as a resident enterprise with its de facto management bodies located within China if the following requirements are satisfied: (1) the senior management and core management departments in charge of its daily operations function mainly in the PRC; (2) its financial and human resources decisions are subject to determination or approval by persons or bodies in the PRC; (3) its major assets, accounting books, company seals, and minutes and files of its board and shareholders meetings are located or kept in the PRC; and (4) at least half of the enterprise's directors or senior management with voting rights reside in the PRC.

In addition, the State Administration of Taxation issued a bulletin on August 3, 2011, effective as of September 1, 2011, to provide more guidance on the implementation of the above circular. The bulletin clarified certain matters relating to resident status determination, post determination administration and competent tax authorities. It also specifies that when provided with a copy of a PRC tax resident determination certificate from a resident PRC-controlled offshore incorporated enterprise, the payer should not withhold 10% income tax when paying the PRC-sourced dividends, interest and royalties to the PRC-controlled offshore incorporated enterprise. Although both the circular and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those by PRC individuals, the determination criteria set forth in the circular and administration clarification made in the bulletin may reflect the SAT's general position on how the de facto management body test should be applied in determining the tax residency status of offshore enterprises and how the administration measures should be implemented, regardless of whether they are controlled by PRC enterprises or PRC individuals.

The EIT Law provides that a maximum income tax rate of 20% may apply to dividends payable to non-PRC investors that are non-resident enterprises, to the extent such dividends are derived from sources within the PRC. The State Council has reduced such rate to 10%, in the absence of any applicable tax treaties that may reduce such rate. We are a Cayman Islands holding company and substantially all of our income may be derived from dividends we receive from our operating subsidiaries located in the PRC. If we are required under the EIT Law to pay income tax for any dividends we receive from our PRC subsidiaries, the amount of dividends, if any, we may pay to our shareholders and ADS holders may be materially and adversely affected.

According to the Double Taxation Arrangement (Hong Kong), which became effective on January 1, 2007, The Notice of the State Administration of Taxation on Negotiated Reduction of Dividends and Interest Rates, which was issued on January 29, 2008, and The Notice of the State Administration of Taxation Regarding Interpretation and Recognition of Beneficial Owners under Tax Treaties, which became effective on October 27, 2009, dividends paid to enterprises incorporated in Hong Kong are subject to a withholding tax of 5% provided that a Hong Kong resident enterprise owns over 25% of the PRC enterprise distributing the dividend and can be considered as a beneficial owner and entitled to treaty benefits under the Double Taxation Arrangement (Hong Kong). Our wholly owned Hong Kong subsidiaries, Elite Concept Holdings Limited, Winner Park Limited and Smart Shine International Limited, own 100% of our PRC subsidiaries. Thus, dividends paid to us by our PRC subsidiaries through our Hong Kong wholly owned subsidiaries may be subject to the 5% withholding tax if we and our Hong Kong subsidiaries are considered as non-resident enterprises under the EIT Law and our Hong Kong subsidiaries are considered as beneficial owners and entitled to treaty benefits under the Double Taxation Arrangement (Hong Kong). If our Hong Kong subsidiaries are not regarded as the beneficial owners of any such dividends, it will not be entitled to the treaty benefits under the Double Taxation Arrangement (Hong Kong). As a result, such dividends would be subject to regular withholding tax of 10% as provided by the PRC domestic law rather than the favorable rate of 5% applicable under the Double Taxation Arrangement (Hong Kong).

## Table of Contents

On November 11, 2011, as approved by the State Council, the Ministry of Finance and the State Administration of Taxation, promulgated the Circular Regarding the Launch of Pilot Practice of Replacing Business Tax with Value-Added Tax in Transportation Industry and Some Modern Service Industries in Shanghai, or Circular No. 111, attached with three relevant annexes, namely (1) Annex 1-Measures for the Implementation of the Pilot Practice of Replacing Value Added Tax with Business Tax in the Transportation Industry and Some Modern Service Industries, (2) Annex 2- Provisions on Relevant Matters Concerning the Pilot Practice of Replacing Business Tax with Value-Added Tax in Transportation Industry and Some Modern Service Industries, and (3) Annex 3- Provisions on the Transitional Policies for the Pilot Practice of Replacing Business Tax with Value-Added Tax in Transportation Industry and Some Modern Service Industries. Circular No. 111 and its annexes stipulated that the launch of a pilot practice of replacing business tax with value-added tax ( Pilot Practice ) would commence in the transportation industry and some modern service industries, including software service and information system service, in Shanghai beginning in January 1, 2012. On July 31, 2012, upon approval by the State Council, the Ministry of Finance and the State Administration of Taxation promulgated the Circular Regarding the Launch of Pilot Practice of Replacing Business Tax with Value-Added Tax in Transportation Industry and Some Modern Service Industries in Beijing and other Seven Provinces and Municipalities, or Circular No. 71, which expanded the region for the Pilot Practice from Shanghai to Beijing and other regions. The Pilot Practice commenced in Beijing on August 1, 2012. On May 24, 2013, the Ministry of Finance and the State Administration of Taxation promulgated the Circular Regarding Nationwide Practice of Replacing Business Tax with Value-Added Tax in Transportation Industry and Some Modern Service Industries, or Circular No. 37, which started implementation from August 1, 2018 replacing Circular No. 11 and Circular No. 71.

### C. Organizational Structure

Substantially all of our operations are conducted in China through contractual arrangements between our wholly owned subsidiaries in China, New Oriental China (our variable interest entity) and New Oriental China's schools and subsidiaries and shareholder. The wholly owned subsidiaries that are parties to these contractual arrangements are Beijing Hewstone, Beijing Decision, Beijing Pioneer, Shanghai Smart Words, Beijing Smart Wood, Beijing Joy Tend and Beijing Right Time. Beijing Hewstone primarily engages in the educational software development business and also sub-licenses our trademarks to New Oriental China and its schools and subsidiaries. Beijing Decision primarily engages in the business of providing educational technology services and educational management services. Each of Beijing Pioneer, Shanghai Smart Words, Beijing Smart Wood, Beijing Joy Tend and Beijing Right Time primarily engages in the educational software development business.

In addition, we have a wholly-owned subsidiary in China, Beijing Judgment Education & Consulting Co., Ltd., or Beijing Judgment, which holds the real estate properties on which certain of our schools are located. Beijing Judgment in turn has two subsidiaries in China, Beijing Boost Caring Education & Consulting Co., Ltd., which primarily engages in the business of providing educational technology services and consulting services, and Beijing New Oriental Stars Education & Consulting Co., Ltd., or Beijing New Oriental Stars, which is a holding company for our two kindergartens.

In 2013, Beijing Hewstone established a wholly-owned subsidiary in China, Beijing Sincerity Technology Co., Ltd., or Beijing Sincerity, which holds our oversea study tour business.

**Table of Contents**

The following diagram sets out details of our significant subsidiaries and New Oriental China and its schools and subsidiaries as of the date of this annual report:

Equity interest for companies.

Sponsorship interest for schools and kindergartens.

Contractual arrangements including service agreements. See C. Organizational Structure Contractual Arrangements with New Oriental China, its Schools and Subsidiaries and its Shareholder.

Contractual arrangements including equity pledge agreements, option agreement and proxy agreement and power of attorney. See C. Organizational Structure Contractual Arrangements with New Oriental China, its Schools and Subsidiaries and its Shareholder.

---

**Table of Contents**

- (1) Beijing Century Friendship Education Investment Co., Ltd is 80% owned by Mr. Michael Minhong Yu, our company's founder, chairman and chief executive officer, and 20% owned by Ms. Bamei Li, Mr. Yu's mother.
- (2) Consisting of various PRC companies operating our educational content and other technology development and distributions business, online education business and overseas studies consulting business in China.

**Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Its Shareholder**

PRC laws and regulations currently require any foreign entity that invests in the education business in China to be an educational institution with relevant experience in providing educational services outside China. Our offshore holding companies are not educational institutions and do not provide educational services outside China. In addition, in the PRC, foreign ownership of high schools for students in grades ten to twelve is restricted and foreign ownership of primary and middle schools for students in grades one to nine is prohibited. As a result, our offshore holding companies are not allowed to directly own and operate schools in China. We conduct substantially all of our education business in China through contractual arrangements between our wholly owned subsidiaries in China, including Beijing Hewstone, Beijing Decision, Beijing Pioneer, Shanghai Smart Words, Beijing Smart Wood, Beijing Joy Tend and Beijing Right Time and New Oriental China, its schools and subsidiaries and its shareholder. In the fiscal years ended May 31, 2011, 2012 and 2013, New Oriental China and its schools and subsidiaries contributed in aggregate 97.2%, 97.2% and 99.0%, respectively, of our total net revenues. New Oriental China is our variable interest entity which is directly wholly owned by Century Friendship, a PRC domestic company controlled by Mr. Michael Minghong Yu, our founder, chairman and chief executive officer.

New Oriental China's schools and subsidiaries hold the requisite licenses and permits necessary to conduct our education business and have been directly conducting our education business. We have been and are expected to continue to be dependent on New Oriental China and its schools and subsidiaries to operate our education business until we qualify for direct ownership of our education business in China under PRC laws and regulations and acquire New Oriental China as our direct, wholly owned subsidiary. We have entered into contractual arrangements with New Oriental China, its schools and subsidiaries and its shareholder, which enable us to:

have power to direct the activities that most significantly affect the economic performance of New Oriental China and its schools and subsidiaries;

receive substantially all of the economic benefits from New Oriental China and its schools and subsidiaries in consideration for the services provided by our wholly owned subsidiaries in China; and

have an exclusive option to purchase all or part of the equity interests in New Oriental China, when and to the extent permitted by PRC law, or request any existing shareholder of New Oriental China to transfer all or part of the equity interest in New Oriental China to another PRC person or entity designated by us at any time in our discretion.

These contractual arrangements are summarized in the following paragraphs.

**Equity Pledge Agreements.** Pursuant to the equity pledge agreements dated as of May 25, 2006 among New Oriental China, all of the eleven shareholders of New Oriental China, Beijing Hewstone and Beijing Decision, each shareholder of New Oriental China agreed to pledge his or its equity interests in New Oriental China to Beijing Hewstone and Beijing Decision to secure the performance of obligations of New Oriental China and its schools and subsidiaries under the existing service agreements and any such agreements to be entered into in the future. The shareholders of New Oriental China agreed not to transfer, sell, pledge, dispose of or otherwise create any encumbrance on their equity interests in New Oriental China without the prior written consent of Beijing Decision and Beijing Hewstone. All parties to the equity pledge agreement have agreed that the equity pledge agreement is binding upon New Oriental China's shareholders and their successors.

## **Table of Contents**

In January 2012, the ten former shareholders of New Oriental China completed the transfer of all of their equity interests in New Oriental China to Century Friendship, a PRC domestic enterprise controlled by Mr. Michael Minhong Yu, our founder, chairman and chief executive officer, without consideration. Prior to the transfer, Century Friendship had held 53% of the equity interests in the New Oriental China while the ten former shareholders of New Oriental China held the remaining equity interests. The purpose of the transfers was to further strengthen our corporate structure by simplifying the shareholding structure of New Oriental China.

Pursuant to the five new equity pledge agreements dated April 23, 2012 among New Oriental China, Century Friendship and five of our wholly owned subsidiaries in China, namely Beijing Hewstone, Beijing Decision, Shanghai Smart Words, Beijing Pioneer and Beijing Smart Wood, Century Friendship agreed to pledge its equity interests in New Oriental China to these five subsidiaries to secure New Oriental China's and its schools and subsidiaries' performance of their obligations under the relevant principal agreements, including certain new enrollment system development service agreements, other operating service agreements, sale of educational software agreements and trademark license agreements, and Century Friendship has agreed not to transfer, sell, pledge, dispose of or otherwise create any encumbrance on its equity interests in New Oriental China without the prior written consents of our wholly owned subsidiaries in China. The equity pledge agreements are agreements which collateralize the security interest. The equity pledges of Century Friendship under these equity pledge agreements have been registered with the Haidian District, Beijing branch of the SAIC. The terms of the April 2012 equity pledge agreements are substantially the same as the 2006 agreements.

**Exclusive Option Agreement.** Exclusive option agreements were entered into by us and New Oriental China and the shareholders of New Oriental China on various dates, and amended on May 25, 2006. After the ten former shareholders of New Oriental China completed the transfer of all of their equity interests in New Oriental China to Century Friendship in early 2012, Century Friendship, as the sole shareholder of New Oriental China, executed a new option agreement with Shanghai Smart Words, which is one of our wholly owned subsidiaries in China, and New Oriental China on April 23, 2012, replacing previous exclusive option agreements. Pursuant to the current option agreement, Century Friendship is obligated to sell to Shanghai Smart Words, and Shanghai Smart Words has an exclusive, irrevocable and unconditional right to purchase from Century Friendship, in its sole discretion, part or of all of Century Friendship's equity interests in New Oriental China when and to the extent that applicable PRC law permits it to own part or all of the equity interest in New Oriental China. In addition, Shanghai Smart Words has an exclusive option to require Century Friendship to transfer all or part of Century Friendship's equity interest in New Oriental China to another PRC person or entity designated by Shanghai Smart Words at any time in its discretion. The purchase price to be paid by Shanghai Smart Words will be the minimum amount of consideration permitted by applicable PRC law at the time when such share transfer occurs.

**Power of Attorney.** On December 3, 2012, Century Friendship, in the capacity of the sole shareholder of New Oriental China, executed a proxy agreement and power of attorney with Beijing Pioneer, which is one of our wholly owned subsidiaries in China, and New Oriental China, whereby Century Friendship irrevocably appoints and constitutes Beijing Pioneer as its attorney-in-fact to exercise on Century Friendship's behalf any and all rights that Century Friendship has in respect of its equity interests in New Oriental China. This proxy agreement and power of attorney became effective on December 3, 2012 and replaces the powers of attorney executed by Century Friendship on April 23, 2012. The proxy agreement and power of attorney will remain effective as long as New Oriental China exists. Century Friendship does not have the right to terminate the proxy agreement and power of attorney or revoke the appointment of the attorney-in-fact without the prior written consent of Beijing Pioneer.

**Service Agreements.** Seven of our wholly owned subsidiaries in China have entered into a series of service agreements with New Oriental China and its schools and subsidiaries to enable them to receive substantially all of the economic benefits of New Oriental China and its schools and subsidiaries. In the fiscal years ended May 31, 2011, 2012 and 2013, the total amount of service fees that our PRC subsidiaries received from New Oriental China and its schools and subsidiaries under all the service agreements was US\$65.7 million, US\$118.6 million and US\$146.6 million, respectively.

There are four categories of service agreements, namely, new enrollment system development service agreements, other operating service agreements, sale of educational software agreements and trademark license agreements, each of which is summarized below.

---

## **Table of Contents**

*New Enrollment System Development Service Agreements.* Since 2005, Beijing Decision has entered into new enrollment system service agreements with certain schools of New Oriental China, under which Beijing Decision agreed to provide new enrollment system development and regular maintenance services to the schools of New Oriental China for a fee calculated based upon the number of enrollments. For the fiscal year ended May 31, 2013, there were 15 new enrollment system service agreements. Fourteen of these agreements may be renewed by both parties to the agreements, and one of these agreements provides automatic renew terms. The service fees are equal to the applicable fee rate multiplied by the number of student enrollments. The fees under the agreements are subject to the periodic review by our group financial department and are typically reviewed and adjusted each year. If no adjustment is made, the most recent fee rate will apply. For the fiscal year ended May 31, 2013, the fee rate was up to RMB30 per new student enrollment.

*Other Operating Service Agreements.* Pursuant to the operating service agreements between certain of our wholly owned subsidiaries in China and certain schools or subsidiaries of New Oriental China, our wholly owned subsidiaries in China have agreed to provide certain operating services to the schools or subsidiaries of New Oriental China for fees which are calculated based on a percentage of the respective revenues of New Oriental China's schools and subsidiaries. For the fiscal year ended May 31, 2013, there were 93 such service agreements between our wholly owned subsidiaries in China and New Oriental China's schools and subsidiaries. Of these agreements, 84 agreements provide automatic renewal terms and New Oriental China's schools and subsidiaries cannot terminate the agreements without the consent of our wholly owned subsidiaries in China. The remaining agreements may be renewed with mutual consent. The fees under these agreements were 1.0% to 6.0% of the monthly revenues of the applicable New Oriental China school or subsidiary for the fiscal year ended May 31, 2013. The fees under the agreements are subject to periodic review by our group financial department and typically are reviewed and adjusted each year. If no adjustment is made, the most recent fee rate will apply.

*Sale of Educational Software.* Beijing Hewstone, Beijing Pioneer, Beijing Smart Wood and Shanghai Smart Words sell various self-developed educational software to New Oriental China's schools and subsidiaries, which are in turn included as part of the course materials for students enrolled in relevant courses. For the fiscal year ended May 31, 2013, there were 182 such agreements between our wholly owned subsidiaries in China and New Oriental China's schools or subsidiaries. Except for four agreements that are silent on renewal, these agreements provide unlimited two-year automatic renewal terms and schools and subsidiaries of New Oriental China cannot terminate the agreements without the consent of our wholly owned subsidiaries in China. The price of the software is determined by our respective PRC subsidiaries.

*Trademark License Agreements.* Pursuant to the trademark license agreement dated May 13, 2006 between us as the licensor and New Oriental China as the licensee, we have licensed our trademarks to New Oriental China for their use in China. We have also allowed New Oriental China to enter into a sub-license agreement with each school and subsidiary of New Oriental China pursuant to which each of these schools and subsidiaries may use our trademarks in China by paying certain licensing fees. New Oriental China is authorized to collect the licensing fees from each sub-licensee and handle other related matters. The license is valid from May 14, 2006 to December 31, 2050, subject to the renewal on the expiry of the trademark registration every ten years. Pursuant to the second trademark license agreement entered into between Shanghai Smart Words as the licensor and a subsidiary of New Oriental China as the licensee, dated as of December 20, 2010, Shanghai Smart Words has granted a license to a subsidiary of New Oriental China to use certain trademarks for a license fee that equals 5% of the licensee's monthly revenues. The initial term of this license is two years, and can be automatically renewed and the subsidiary of New Oriental China cannot terminate the agreement without the consent of our wholly owned subsidiary in China.

In the opinion of Tian Yuan Law Firm, our PRC legal counsel:

the corporate structure of New Oriental China and its schools and subsidiaries and our wholly owned subsidiaries in China are in compliance with existing PRC laws and regulations; and

the contractual arrangements among our wholly owned subsidiaries in China, New Oriental China and its schools and subsidiaries and the shareholder of New Oriental China are valid, binding and enforceable under, and do not violate, PRC laws or regulations currently in effect.

We have been advised by our PRC legal counsel, however, that there are substantial uncertainties regarding the interpretation and application of current and future PRC laws and regulations. Accordingly, there can be no assurance that the PRC regulatory authorities will not in the future take a view that is contrary to the above opinion of our PRC legal counsel. We have been further advised by our PRC counsel that if the PRC government finds that the agreements that establish the structure for operating our education business in China do not comply with PRC regulatory restrictions on foreign investment in the education business, we could be subject to severe penalties. The imposition of any of these penalties could result in a material adverse effect on our ability to conduct our business. See Item 3. Key Information D. Risk Factors Risks Related to Our Corporate Structure If the PRC government finds that the agreements that establish the structure for operating our China business



## Edgar Filing: New Oriental Education & Technology Group Inc. - Form 20-F

do not comply with applicable PRC laws and regulations, we could be subject to severe penalties and Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China Uncertainties with respect to the PRC legal system could adversely affect us.

## **Table of Contents**

We are evaluating whether to make additional changes to the agreements with New Oriental China and its schools and subsidiaries to further strengthen our corporate structure. Century Friendship has informed us that it is willing to sign additional documents or amendments if and when we request it to do so in the best interests of our company.

### **D. Property, Plants and Equipment**

Our headquarters are located in Beijing, China, where we own approximately 19,000 square meters of office and classroom space. In addition, we own approximately 168,000 square meters of schools in Yangzhou and an aggregate of approximately 27,000 square meters of space for our schools, learning centers and bookstores in various cities in China, including Xi'an, Tianjin, Kunming, Wuhan, Guangzhou and Changsha.

## **ITEM 4A UNRESOLVED STAFF COMMENTS**

None

## **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our consolidated financial statements and the related notes included elsewhere in this annual report on Form 20-F. This discussion may contain forward-looking statements based upon current expectations that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under Item 3. Key Information D. Risk Factors or in other parts of this annual report on Form 20-F.

### **A. Operating Results**

#### ***General Factors Affecting Our Results of Operations***

We have benefited significantly from favorable demographic trends, the overall economic growth and the demand for high-quality private education and English language training in China. The overall economic growth and the increase in the GDP per capita in China have led to a significant increase in spending on education in China. At the same time, China's integration into the global economy has continued, resulting in more career opportunities for Chinese citizens who are able to communicate effectively in English. We anticipate that the demand for private education and English language training in China will continue to increase as China's economy continues to grow and as disposable income of urban households continues to rise. However, any adverse changes in the economic conditions or regulatory environment in China may have a material adverse effect on the private education industry in China, which in turn may harm our business and results of operations.

#### ***Specific Factors Affecting Our Results of Operations***

While our business is influenced by factors affecting the private education industry in China generally and by conditions in each of the geographic markets we serve, we believe our business is more directly affected by company-specific factors such as the number of student enrollments, the amount of course fees and our operating costs and expenses. The number of student enrollments is in turn largely driven by the demand for our courses, the effectiveness of our marketing and brand promotion efforts, the locations of our schools and learning centers, our ability to maintain the consistency and quality of our teaching, and our ability to respond to competitive pressure, as well as seasonal factors. We determine course fees primarily based on demand for our courses, the targeted market for our courses, the subject of the course, the geographic location of the school, cost of services, and the course fees charged by our competitors for the same or similar courses.

## Table of Contents

Our future results of operations will depend significantly upon our ability to increase student enrollments at existing schools and learning centers and further expand our school network throughout China, as well as offer a greater variety of courses, including smaller-size classes. Our planned expansion may result in substantial demands on our management, operational, technological, financial and other resources. To manage and support our growth, we must improve our existing operational, administrative and technological systems and our financial and management controls, and recruit, train and retain additional qualified teachers and school management personnel as well as other administrative and sales and marketing personnel, particularly as we grow outside of our existing markets. We will continue to implement additional systems and measures and recruit qualified personnel in order to effectively manage and support our growth. If we cannot achieve these improvements, our financial condition and results of operations may be materially adversely affected.

Due to certain restrictions and qualification requirements under PRC law that apply to foreign investment in China's education industry, we conduct substantially all of our education business in China through contractual arrangements between our wholly owned subsidiaries in China, New Oriental China, and the schools and subsidiaries and shareholder of New Oriental China. New Oriental China's schools and subsidiaries hold the requisite licenses and permits necessary to conduct our educational services business in China and operate our schools and learning centers and have been directly conducting our education business and operating our schools and learning centers.

Net Revenues. In the fiscal years ended May 31, 2011, 2012 and 2013, we generated total net revenues of US\$539.9 million, US\$753.2 million and US\$959.9 million, respectively. Our revenues are net of PRC business taxes and related surcharges, as well as scholarships and refunds.

We currently derive revenues from the following sources:

educational programs and services, which accounted for 90.8%, 89.6% and 89.4% of our total net revenues in the fiscal years ended May 31, 2011, 2012 and 2013, respectively; and

books and others, which accounted for 9.2%, 10.4% and 10.6% of our total net revenues in the fiscal years ended May 31, 2011, 2012 and 2013, respectively.

*Educational Programs and Services.* Our educational programs and services consist of language training and test preparation courses, primary and secondary school education and online education. Revenues from language training courses and test preparation courses accounted for 86.6%, 85.6% and 85.3%, respectively, of our total net revenues in the fiscal years ended May 31, 2011, 2012 and 2013.

We recognize revenues from course fees collected for enrollment in our language training and test preparation courses proportionally as we deliver the instruction over the period of the course. Course fees are generally paid in advance by students and are initially recorded as deferred revenues. Students are entitled to a short-term trial period which commences on the date the course begins. Tuition refunds are provided to students if they decide within the trial period that they no longer want to take the course. After the trial period, if a student withdraws from a class, usually no refunds will be provided and any collected but unearned portion of the fee is recognized at that time. We recognize revenues from school fees collected for enrollment in our primary and secondary schools ratably over the corresponding academic year. We sell pre-paid online education cards primarily to distributors, who in turn sell them to students. We recognize revenues from sales of pre-paid cards in proportion to the actual time that students spend on our online courses. Course fees and school fees collected and amounts received from sales of pre-paid cards are recorded as deferred revenues until they can be recognized as revenues upon their use or expiration. Upon expiration of a prepaid card, which is six months to one year from the date of the sale of the card, we recognize the remaining amount of deferred revenues as revenues.

The most significant factors that directly affect our revenues from educational programs and services are the number of student enrollments and the amount of course fees. We believe our students are attracted to us primarily because of our established brand and reputation in the private education sector, especially in the areas of English language training and overseas admissions and assessment test preparation, the quality of our instruction and the variety of our programs, services and products. For the past several years, our revenue growth has been driven primarily by increased enrollments in our English language training courses and test preparation courses and other programs and services. The number of student enrollments for our courses is affected by the demand for our courses, the effectiveness of our marketing and brand promotion, the demographic composition of the cities where we have schools and learning centers, our ability to respond to competitive pressure, as well as seasonal factors. To further penetrate the English language training markets for children and high-income individuals, we have offered and plan to continue offering an increasing number and a greater variety of smaller classes for children and adults, such as Pop Kids English classes for students in kindergarten through grade six with 1 to 25 students per class. In addition, we have expanded the scope of our test preparation course offerings to cover non-English subjects, including through our New Oriental U-Can (Non-English) all subjects training program for middle and high school students, and plan to further expand our course offerings in the future to capture a larger share of the huge after-school training

market in China.

**Table of Contents**

Our courses generally have the largest student enrollments in our first fiscal quarter, which runs from June 1 to August 31 of each year, primarily because many students enroll in our courses during the summer vacation to enhance their foreign language skills and/or prepare for admissions and assessment tests in subsequent school terms. In addition, we have generally experienced larger student enrollments in our third fiscal quarter, which runs from December 1 to February 28 of each year, primarily because many students enroll in our language training and other courses during the winter school holidays. We expect this seasonality in enrollment pattern to continue, especially for most of our language training courses for college and middle school students and test preparation courses.

We determine course fees primarily based on demand for our courses, the targeted market for our courses, the subject of the course, the geographic location of the school, cost of services, and the course fees charged by our competitors for the same or similar programs. Our test preparation courses are generally delivered in class settings ranging from 1 student to 500 students per class and our English language training courses are delivered in class settings generally ranging from 1 student to 300 students per class. We typically adjust course fees or school fees based on the market conditions of the city where the particular school is located, subject to the relevant local governmental authority's advance approval, if required. We expect to continue to derive a substantial majority of our revenues from educational programs and services.

A significant portion of our revenues has been derived from test preparation courses. The success of our test preparation courses depends on the continued use of admissions and assessment tests by educational institutions and governmental authorities both in China and abroad. If the use of admissions and assessment tests declines or falls out of favor with educational institutions, government authorities and other entities, the markets for our test preparation courses will shrink and our business may be materially and adversely affected.

*Books and Others.* We distribute and sell books and other educational materials developed or licensed by us through our own distribution channels, which consist of our bookstores and websites, and also through third-party distributors. We normally provide books and other educational materials that are required for our courses and do not separately charge students for these items. We recognize revenues from sales of books and other educational materials when the products are sold to end customers. As we believe successful content development is important to the success of our business in China, we intend to continuously enhance the quality and breadth of our education content offerings and distribute more books and other educational materials through our own bookstores, as well as third-party distributors, including over 5,000 bookstores. Accordingly, we expect revenues from sales of books and other educational materials to continue to increase in the future.

We also provide consulting services to students regarding overseas studies and related processes, such as visa applications. We charge each student a fee based on the scope of consulting services requested by the student and recognize revenues when our consulting services are delivered. We expect that revenues from these consulting services will continue to constitute a small portion of our total revenues in the future.

*Operating Costs and Expenses.* Our operating costs and expenses consist of cost of revenues, selling and marketing expenses and general and administrative expenses. The following table sets forth the components of our operating costs and expenses, both in absolute amount and as a percentage of total net revenues for the periods indicated.

<i>(in thousands, except percentages)</i>	For the Year Ended					
	2011		2012		2013	
	US\$	%	US\$	%	US\$	%
Net revenues	539,851	100	753,195	100	959,854	100
Operating costs and expenses:						
Cost of revenues	(213,779)	(39.6)	(293,063)	(38.9)	(384,177)	(40.0)
Selling and marketing	(81,954)	(15.2)	(113,568)	(15.1)	(142,098)	(14.8)
General and administrative	(148,409)	(27.5)	(226,404)	(30.1)	(311,014)	(32.4)
Loss on disposal of subsidiaries	(1,537)	(0.3)				
Total operating costs and expenses	(445,679)	(82.6)	(633,035)	(84.1)	(837,289)	(87.2)

## **Table of Contents**

We rely on our teachers to deliver educational services. Our teachers consist of both full-time teachers and contract teachers. Full-time teachers deliver instruction and may also be involved in management, administration and other functions at our schools. Full-time teachers' compensation and benefits primarily consist of teaching fees based on hourly rates, performance-linked bonuses based on student evaluations, as well as base salary, annual bonus and standard employee benefits in connection with their services other than teaching. Compensation of our contract teachers is comprised primarily of teaching fees based on hourly rates and performance-linked bonuses based on student evaluations and other factors. To attract and retain high-quality teachers, we have granted equity incentives, including restricted shares and share options, to some of our teachers. We account for teaching fees and performance-linked bonuses paid to our teachers as cost of revenues as they are directly associated with the provision of educational services, and account for the other compensation and benefits to our teachers as general and administrative expenses.

*Cost of Revenues.* Cost of revenues for educational programs and services primarily consists of teaching fees and performance-linked bonuses paid to our teachers and rental payments for our schools and learning centers and, to a lesser degree, depreciation and amortization of property and equipment used in the provision of educational services, as well as costs of course materials. Cost of books and other materials primarily consist of printing costs of books and other materials, and licenses fees, royalties and other fees paid to content licensors, publishing companies and third-party distributors. We anticipate that our total cost of revenues will continue to increase as we continue to open new schools and learning centers and hire additional teachers.

*Selling and Marketing Expenses.* Our selling and marketing expenses primarily consist of expenses relating to advertising, seminars, marketing and promotional trips and other community activities for brand promotion purpose. We expect that our selling and marketing expenses will continue to increase as we further expand into new geographic locations and enhance our brand recognition.

*General and Administrative Expenses.* Our general and administrative expenses primarily consist of compensation and benefits of administrative staff, compensation and benefits of full-time teachers excluding teaching fees and performance-linked bonuses and, to a lesser extent, costs to develop curriculum, costs of third-party professional services, rental and utilities payments relating to office and administrative functions, and depreciation and amortization of property and equipment used in our general and administrative activities. We expect that our general and administrative expenses will increase in the near term as we hire additional personnel and incur additional costs in connection with the expansion of our business.

*Share-based Compensation Expenses.* In January 2006, we adopted the 2006 Share Incentive Plan, under which we are authorized to, starting from 2006, issue up to 8,000,000 common shares pursuant to awards (including options) granted under the plan to our employees, directors and consultants in 2006, as well as additional shares in future periods. In the fiscal years ended May 31, 2006 and 2007, we granted options to purchase a total of 12,766,000 common shares, and in the fiscal year ended May 31, 2012, we granted options to purchase 3,060,000 common shares. Of those options, options to purchase 2,001,608 common shares had been forfeited as of May 31, 2013. During the past six fiscal years, we have granted a total of 7,208,841 non-vested equity shares, including 208,590 shares granted in the fiscal year ended May 31, 2013, of which 983,385 shares had been forfeited as of May 31, 2013. We account for share-based compensation expenses in accordance with an authoritative accounting pronouncement, which requires share-based compensation expense to be determined based on the fair value of our common shares as of their grant date.

**Table of Contents**

The following table sets forth the allocation of our share-based compensation expenses, both in absolute amount and as a percentage of total share-based compensation expenses, among our employees based on the nature of work which they were assigned to perform.

<i>(in thousands, except percentages)</i>	2011		For the Year Ended 2012		2013	
	US\$	%	US\$	%	US\$	%
Allocation of Share-based Compensation Expenses:						
Cost of revenues	900	6.0	216	0.9		
Selling and marketing						
General and administrative	14,145	94.0	23,909	99.1	27,242	100.0

For options granted to our employees and directors, we record share-based compensation expenses based on the fair value of our common shares underlying options as of the date of option grant and amortize the expenses over the vesting periods of the options. For non-vested equity shares granted to employees and directors, we record share-based compensation expenses based on the quoted market price of our ADSs on the grant date and amortize the expenses over the vesting periods of the non-vested equity shares.

*Loss on disposal of subsidiaries.* In April 2011, we sold a 60% equity interest in Mingshitang and a 100% equity interest in Tomorrow Oriental, resulting in disposal losses of US\$1.5 million.

**Taxation***Cayman Islands*

We are incorporated in the Cayman Islands. Under the current law of the Cayman Islands, we are not subject to income or capital gains tax. In addition, dividend payments are not subject to withholding tax in the Cayman Islands.

*PRC*

Other than our primary and secondary schools, our operating entities in China are subject to a 3% to 5% business tax on gross revenues generated from providing services and related surcharges, and a value-added tax at varying rates ranging from 3% to 17% on gross revenues from sales of books, educational software and other products. According to the then-in-effect Circular No. 111 and Circular No. 71 issued by the Ministry of Finance and the State Administration of Taxation on November 11, 2011 and July 31, 2012, respectively, the new enrollment system development services and other operating services provided by Beijing Hewstone, Beijing Decision, Shanghai Smart Words, Beijing Smart Wood and Beijing Pioneer which were previously subject to business tax before the implementation of Circular No. 111 and Circular No. 71, have since become subject to value-added tax following the implantation of these two circulars. Pursuant to the same, the operating services provided by Beijing Joy Tend and Beijing Right Time are also subject to value-added tax. On May 24, 2013, the Ministry of Finance and the State Administration of Taxation promulgated Circular No. 37, which replaces Circular No. 111 and Circular No. 71 and expands such practice of replacing business tax with value-added tax to nationwide starting August 1, 2013. Following the change from business tax to value-added tax, the applicable tax rate for such services shall increase by 1%, from 5% up to 6%, while the tax payable amount of value-added tax relating to such services shall be the output tax amount in a tax period minus input tax amount in the same period. Circular No. 37 and the relevant implementation measures and rules are relatively new and the interpretation and enforcement this circular involve uncertainties; however, to date, the practices instituted under the new circular have had no material adverse effect on the tax positions of our operating entities in China.

With regard to income tax, according to the Implementation Rules for the Law for Promoting Private Education (2004), private schools that do not require reasonable returns enjoy the same preferential tax treatment as public schools, while the preferential tax treatment policies applicable to private schools requiring reasonable returns shall be separately formulated by the relevant authorities under the State Council. As of May 31, 2013, 22 of our schools elected as schools not requiring reasonable returns, 30 of our schools elected as requiring reasonable returns and the remaining schools were not classified. The implementing rules of the EIT Law provide certain conditions under which not-for-profit entities may be exempted from enterprise income tax. According to such conditions, our schools may not be entitled to income tax exemption. To date, however, no separate specific regulations or policies have been promulgated by the relevant authorities in this regard and whether our schools can be entitled to any preferential income tax treatment remains unclear. In practice, tax treatments for private schools vary across different cities in China. For example, private schools in certain cities are subject to a 25% standard enterprise income tax starting from January 1, 2008, while in other cities, private schools are subject to a fixed amount of enterprise income tax each year as determined by the local tax authority in lieu of the 25% standard enterprise income tax or are not required to pay enterprise income tax. Among our schools in the four major cities from which we derived a significant portion of our revenues in the fiscal year ended May 31, 2013, three schools are subject to the standard 25% enterprise income tax rate and one school is not required by the governing tax bureau to pay any EIT since its establishment through May 31,

2013.



**Table of Contents**

Under PRC laws and regulations in effect before January 1, 2008, three wholly owned subsidiaries of our company in China, Beijing Judgment, Beijing Hewstone and Beijing Decision, and one subsidiary of New Oriental China, Xuncheng Network, were certified as high and new technology enterprises located in a high-tech zone in Beijing as their primary sources of revenues were educational software development and educational technology development and implementation. However, the implementation rules of the EIT Law promulgated by the State Council in December 2007 and other supplemental rules promulgated by the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation in April 2008 and July 2008, respectively, have provided new criteria for such high and new technology enterprises and all enterprises which had been granted such status before the effectiveness of the EIT Law are required to be re-examined according to such new rules before they can continue to be entitled to such preferential tax treatments. In December 2008, Beijing Hewstone and Beijing Decision and Xuncheng Network were recertified as high and new technology enterprise in Beijing. All of them are entitled to a 15% tax rate as long as they continue to qualify as a high and new technology enterprise. The deferred tax balance of Beijing Decision, Beijing Hewstone and Xucheng Network is calculated at a rate of 15%, as we expect Beijing Decision, Beijing Hewstone and Xucheng Network to continue to be qualified as high and new technology enterprise. As Beijing Judgment did not seek recertification, it became subject to the standard enterprise income tax rate of 25% from 2008. Enterprises that qualify as a newly established software enterprise are exempt from enterprise income tax for two years beginning in the enterprise's first profitable year followed by a tax rate of 12.5% for the succeeding three years. Three of our wholly owned subsidiaries in China, Beijing Pioneer, Shanghai Smart Words and Beijing Smart Wood, are qualified as Software Enterprises. Beijing Pioneer was exempt from income taxes from January 2010 through December 31, 2011 and have a tax rate of 12.5% through December 31, 2014. Shanghai Smart Words was exempt from income taxes from January 2011 through December 31, 2012 and have a tax rate of 12.5% through December 31, 2015. Beijing Smart Wood is exempt from income taxes from January 1, 2012 through December 31, 2013 followed by a 12.5% tax rate through December 31, 2016. Based on the criteria set out by Circular 27, we believe that other two of our wholly owned subsidiaries in China, Beijing Joy Tend Technology Co., Ltd., or Beijing Joy Tend and Beijing Right Time Technology Co., Ltd., or Beijing Right Time, satisfy the criteria of a Software Enterprise. However, the status of Beijing Joy Tend and Beijing Right Time is subject to the approval by respective tax authorities.

Preferential tax treatments granted to our schools by local governmental authorities are subject to review and may be adjusted or revoked at any time. In addition, if the government regulations or authorities were to phase out preferential tax benefits currently granted to high and new technology enterprises, New Oriental China and our wholly owned subsidiaries in China would be subject to the 25% uniform statutory tax rate. The discontinuation of any preferential tax treatments currently available to our schools, especially those schools in major cities, and to New Oriental China and our wholly owned subsidiaries, will cause our effective tax rate to increase, which could have a material adverse effect on our results of operations.

For additional information on PRC regulations on taxation, see Item 4. Information on the Company B. Business Overview Education Regulations on Taxation.

**Recent Acquisition**

In April 2012, our company signed an agreement with a third party to acquire a 100% equity interest in China Management Software Institute for US\$18.0 million. A deposit of US\$3.28 million has been paid. The acquisition closed in September 2012.

**Discontinued Operations**

In July 2012, our company transferred the ownership of Elite English, which provides high-end, personalized and advanced English language training, to Mr. Yunkai Weng, the head of Elite English, for US\$5,500,000 through three installments during the period from May 2014 to May 2016. As a result, the financial results associated with Elite English have been presented as discontinued operations in fiscal years ended May 31, 2011, 2012 and 2013.

**Table of Contents**

**Results of Operations**

The following table sets forth a summary of our consolidated results of operations for the periods indicated. This information should be read together with our consolidated financial statements and related notes included elsewhere in this annual report. The operating results in any period are not necessarily indicative of the results that may be expected for any future period.

**For the Year Ended May 31,**

pplement or free writing prospectus any other paying agents that we initially designate for the debt securities of a particular series. We

## **DESCRIPTION OF WARRANTS**

low. Specific warrant agreements will contain additional important terms and provisions and will be incorporated by reference as an ex

### **DESCRIPTION OF UNITS**

series of units offered will be described in the applicable prospectus supplement. If so described in a particular supplement, the specific







exchanges of the unsettled portion of any unit being partially settled. We may also block the transfer or exchange of any unit in this ma



**PLAN OF DISTRIBUTION**

supplement.



panies, pension funds, investment companies, educational and charitable institutions and other institutions, but shall in all cases be sub

syndicate of underwriters, the underwriting syndicate may reclaim selling concessions allowed to an underwriter or a dealer for distribu

close out any related open borrowings of stock, and may use securities received from us in settlement of those derivatives to close out any  
business days after the trade date for your securities, to make alternative settlement arrangements to prevent a failed settlement.

**LEGAL MATTERS**

**EXPERTS**

**WHERE YOU CAN FIND MORE INFORMATION**

m. These documents also may be accessed through the SEC's electronic data gathering, analysis and retrieval system, or EDGAR, via e  
Cambridge, Massachusetts 02139; telephone: (857) 285-6200 . Information contained on our website is not incorporated by reference into

**INCORPORATION BY REFERENCE**

ct, including all filings made after the date of the filing of this registration statement and prior to the effectiveness of this registration st



\$150,000,000

Common Stock

**Prospectus Supplement**

, 2017