

New Oriental Education & Technology Group Inc.

Form 20-F

September 27, 2018

[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, 2018.**

**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)

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Haidian District, Beijing 100080

People's Republic of China

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

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

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

\* Effective on 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. 158,319,910 common shares, par value US\$0.01 per share, as of May 31, 2018.

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 every Interactive Data File required to be submitted 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 such files). Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Emerging growth company

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If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

The term new or revised financial accounting standard refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

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>	2
<u>ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS</u>	2
<u>ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE</u>	2
<u>ITEM 3. KEY INFORMATION</u>	3
<u>ITEM 4. INFORMATION ON THE COMPANY</u>	37
<u>ITEM 4A. UNRESOLVED STAFF COMMENTS</u>	74
<u>ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS</u>	74
<u>ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</u>	95
<u>ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS</u>	102
<u>ITEM 8. FINANCIAL INFORMATION</u>	104
<u>ITEM 9. THE OFFER AND LISTING</u>	105
<u>ITEM 10. ADDITIONAL INFORMATION</u>	106
<u>ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	118
<u>ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u>	119
<u>PART II.</u>	120
<u>ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u>	120
<u>ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS</u>	121
<u>ITEM 15. CONTROLS AND PROCEDURES</u>	121
<u>ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT</u>	122
<u>ITEM 16B. CODE OF ETHICS</u>	122
<u>ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	123
<u>ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u>	123
<u>ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS</u>	123
<u>ITEM 16F. CHANGE IN REGISTRANT S CERTIFYING ACCOUNTANTS</u>	123
<u>ITEM 16G. CORPORATE GOVERNANCE</u>	123
<u>ITEM 16H. MINE SAFETY DISCLOSURE</u>	124
<u>ITEM 17. FINANCIAL STATEMENTS</u>	124

ITEM 18. FINANCIAL STATEMENTS

124

ITEM 19. EXHIBITS

125

**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 New Oriental Education & Technology Group Co., Ltd, formerly known as 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 depository 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 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. dollars, which is our reporting currency. Certain of our financial data in this annual report on Form 20-F is 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 RMB6.4096 to US\$1.00, the exchange rate set forth in the H.10 statistical release of the Federal Reserve Board on May 31, 2018. 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)
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 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.

## **PART I**

### **ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable.

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

Not applicable.

**Table of Contents****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, 2016, 2017 and 2018 and the consolidated balance sheet data as of May 31, 2017 and 2018 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, 2014 and 2015 and the selected consolidated balance sheet data as of May 31, 2014, 2015 and 2016 have been derived from our audited consolidated financial statements for the fiscal years ended May 31, 2014, 2015 and 2016, 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. Operating and Financial Review and Prospects A. Operating Results. Our audited consolidated financial statements are prepared and presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP.

	<b>For the Years Ended May 31,</b>				
<i>(in thousands of US\$ except share, per share and per ADS data)</i>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
<b>Selected Consolidated Statement of Operations Data:</b>					
Net revenues:					
Educational programs and services	1,006,198	1,102,974	1,309,339	1,608,954	2,165,152
Books and other services	132,689	143,792	169,009	190,555	282,278
<b>Total net revenues</b>	<b>1,138,887</b>	<b>1,246,766</b>	<b>1,478,348</b>	<b>1,799,509</b>	<b>2,447,430</b>
Operating costs and expenses: <sup>(1)</sup>					
Cost of revenues	(451,669)	(526,320)	(614,364)	(749,586)	(1,065,740)
Selling and marketing	(169,062)	(188,483)	(197,897)	(232,826)	(324,249)
General and administrative	(324,210)	(378,434)	(471,010)	(554,948)	(794,482)
<b>Total operating costs and expenses</b>	<b>(944,941)</b>	<b>(1,093,237)</b>	<b>(1,283,271)</b>	<b>(1,537,360)</b>	<b>(2,184,471)</b>
Gain on disposal of subsidiaries	3,621		3,760		
<b>Operating income</b>	<b>197,567</b>	<b>153,529</b>	<b>198,837</b>	<b>262,149</b>	<b>262,959</b>
Other income, net:					
Interest income	44,880	66,605	66,861	61,445	84,838
Realized gain from long-term investments				7,086	7,366
Impairment loss from long-term investments				(2,338)	(980)
Miscellaneous income, net	752	342	1,586	2,367	2,841

## Provision for income taxes:

Current	(28,235)	(31,552)	(39,467)	(51,142)	(73,193)
Deferred	2,193	5,331	1,936	518	13,785
Provision for income taxes	<b>(26,042)</b>	<b>(26,221)</b>	<b>(37,531)</b>	<b>(50,624)</b>	<b>(59,408)</b>
Loss from equity method investments	<b>(1,453)</b>	<b>(1,537)</b>	<b>(4,425)</b>	<b>(3,289)</b>	<b>(379)</b>
Net income	<b>215,704</b>	<b>192,718</b>	<b>225,328</b>	<b>276,796</b>	<b>297,237</b>
Add: Net loss (gain) attributable to noncontrolling interests		<b>295</b>	<b>(444)</b>	<b>(2,339)</b>	<b>(1,107)</b>
Net income attributable to New Oriental Education & Technology Group Inc.	215,704	193,013	224,884	274,457	296,130
Net income from continuing operation per ADS attributable to shareholders of New Oriental Education & Technology Group Inc. <sup>(2)</sup>					
-Basic	1.38	1.23	1.43	1.74	1.87
-Diluted	1.37	1.23	1.43	1.74	1.87
Shares used in calculating basic net income per share	156,033,992	156,438,606	156,782,439	157,551,320	158,168,794
Shares used in calculating diluted net income per share	157,903,464	157,302,174	157,391,686	157,986,394	158,556,500

**Table of Contents**

(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>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
General and administrative	20,079	15,689	16,810	20,287	57,443
Total	20,079	15,689	16,810	20,287	57,443

(2) Each ADS represents one common share.

The following table presents our selected consolidated balance sheet data as of May 31, 2014, 2015, 2016, 2017 and 2018:

<i>(in thousands of US\$)</i>	<b>As of May 31,</b>				
	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
<b>Selected Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	371,593	531,298	709,209	641,018	983,319
Total assets	1,603,545	1,951,537	2,354,834	2,924,979	3,977,712
Total current liabilities	576,065	725,232	918,190	1,202,681	1,750,884
Total liabilities	577,787	727,693	920,172	1,204,901	1,763,017
Total mezzanine equity					206,624
Total New Oriental Education & Technology Group Inc. shareholders equity	1,025,758	1,220,348	1,404,572	1,680,948	1,991,589
Noncontrolling interests		3,496	30,090	39,130	16,482
Total equity	1,025,758	1,223,844	1,434,662	1,720,078	2,008,071

**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. In addition, our teachers may not be able to apply for and obtain the teaching licenses on a timely basis, or at all, which may require us to rectify such noncompliance or subject us to penalties. 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, however, 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. More recently, in late 2016, there was negative media coverage referencing our small overseas study consulting division, New Oriental Vision Overseas Consultancy Co. 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, Ebola or other epidemics. For example, the influenza A (H1N1) outbreak from 2009 to 2010 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 87 as of May 31, 2018, and we increased the number of our learning centers in China from 86 as of May 31, 2006 to 994 as of May 31, 2018. 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 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 September 2010, we completed the acquisition of a 100% equity interest in Newave Education, a K-12 English language school in Shanghai. Due to the 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.

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' 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' 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' 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 over 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, other periodicals and Apps, 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. 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, such as TAL 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.

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**Table of Contents**

***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 took effect in the fall semester of 2012, and we finished adapting our tutoring programs and materials to these changes in curriculum standards in July 2013. In September 2014, the government announced plans to change policies relating to the gaokao, or college entrance exam, that will change the format of English exam in the coming years. In December 2014, the MOE issued the Implementation Opinions on Scholastic Standard Test of Senior Secondary Schools and the Opinions on Strengthening and Improving the Comprehensive Aptitude Assessment of High School Students, both of which reform the policies relating to the college entrance exam, including but not limited to the subject, format and content of the exam. These policies will be implemented on a province-by-province basis and some provinces such as Beijing, Shanghai, Zhejiang have promulgated relevant regulations on reformation of the college entrance exam. On September 18, 2016, the MOE promulgated the Guidance Opinions on Further Promoting the Reform of Exams and Entrance System for High Schools which promotes that the secondary school students shall participate the Secondary School Academic Proficiency Test, instead of participating in both the secondary school graduation exams and high school entrance exams, and the scores of students for certain subjects obtained in this Secondary School Academic Proficiency Test shall be taken into consideration for high school enrollment. In January 2017, MOE promulgated new curriculum standards for the subject of science in primary schools, which took effect in the fall semester of 2017. We will adapt our tutoring programs and materials to new curriculum requirements promulgated from time to time. 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.

***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. 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. 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.





## **Table of Contents**

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 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 5 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. The average class size for our short-term language training and test preparation courses started to decrease since the fiscal year ended May 31, 2009. In our fiscal year ended May 31, 2018, the average class size was approximately ten students per class, compared to approximately 30 students per class for fiscal year ended May 31, 2009. Although our smaller-sized classes are highly profitable, they are marginally less profitable on average than our large 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 these 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.

### ***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 school holidays 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.

**Table of Contents**

***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 new 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 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. In October 2013, we terminated the brand name cooperation for New Oriental Star kindergarten program. As another example, in October 2015, we launched Baixuehui non-academic training program, which offers after-school tutoring courses in STEM (science, technology, engineering, and mathematics), sports, dancing, painting, music and arts for students from age 3 to 18. We cooperated with third parties for teaching content and teachers in such non-academic training areas. We had five Baixuehui learning centers in Beijing as of May 31, 2018.

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 and executive chairman, 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.

## **Table of Contents**

***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 33.8% of our total net revenues for the fiscal year ended May 31, 2018 from our operations in Beijing, Shanghai, Hangzhou and Xi'an, 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.

***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, 2018, 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 liability or business disruption insurance in some of our teaching facilities, 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 liability insurance or business disruption insurance in some of our teaching facilities. 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.

## **Table of Contents**

***Capacity constraints or system disruptions to our computer systems or websites, any cybersecurity incidents, or a leak of student data 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. Although we use elastic cloud computing with an aim to timely expand our online program infrastructure to meet demand for such programs, we cannot assure you this will be sufficient to meet the increasing demands of our students as our business continues to grow. Our computer systems and operations could be vulnerable to interruption or malfunction due to events beyond our control, including natural disasters and telecommunications failures. We used an off-site computer center which is able to restore service within several minutes following significant damage to our on-site computer center.

Although we have built a backup system that runs on different servers for our operating data, we may still lose important student data or suffer disruption to our operations if there is a failure of the database system or the backup system. Our computer networks may also be vulnerable to unauthorized access, hacking, computer viruses and other security problems. Computer hackers may attempt to penetrate our network security and our website. We have in the past experienced several computer attacks, although they did not materially affect our operations. Unauthorized access to our proprietary business information or customer data may be obtained through break-ins, sabotage, breach of our secure network by an unauthorized party, computer viruses, computer denial-of-service attacks, employee theft or misuse, breach of the security of the networks of our third party providers, or other misconduct. Because the techniques used by computer programmers who may attempt to penetrate and sabotage our network security or our website change frequently and may not be recognized until launched against a target, we may be unable to anticipate these techniques. A user who circumvents security measures could misappropriate proprietary information or cause interruptions or malfunctions in operations. We could suffer economic and reputational damages and even bear legal liabilities if a technical failure of our systems or a security breach compromises student data, including identification or contact information, although there has not been any material compromise in the past. Any interruption to our computer systems or operations could have a material adverse effect on our ability to retain students and increase student enrollments.

We may be required to expend significant resources to protect against the threat of security breaches or to alleviate problems caused by these breaches, which would increase the cost of our business and eventually have adverse effect on our financial conditions and results of operations.

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

Terrorist attacks, geopolitical uncertainty, economic slowdown and international conflicts involving the United States, the United Kingdom and elsewhere, such as the attacks on September 11, 2001, the Boston marathon bombings on April 15, 2013, and the announcement of Brexit in June 2016, could have an adverse effect on our overseas test preparation courses and English language training courses. Such events 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.





## **Table of Contents**

### ***Failure to control rental costs, obtain leases at desired locations at reasonable prices or protect our leasehold interests could materially and adversely affect our business.***

Our office, schools and learning centers are mainly located on leased premises. The lease term generally ranges from one to ten years and the lease agreements are renewable upon mutual consent at the end of the applicable lease period. We may not be able to obtain new leases at desirable locations or renew our existing leases on acceptable terms or at all, which could adversely affect our business. We may have to relocate our operations for various other reasons, including increasing rentals, failure in passing the fire inspection in certain locations and the early termination of our lease agreements under applicable PRC laws and regulations, or otherwise subject to fines ranging from RMB1,000 to RMB10,000 for each lease agreement that has not been registered. However, failure to complete such registration would not affect the enforceability of the relevant lease agreements in practice.

In addition, a few of our lessors have not been able to provide us with copies of title certificates or other evidentiary documents to prove that they have authorization to lease the properties to us. As of the date of this annual report, we are not aware of any actions, claims or investigations threatened against us with respect to the defects in our leasehold interests. Our business and legal teams followed an internal guideline to identify and assess risks in connection with leasing the properties, and a final business decision was made after our analysis of the likely impact of the defects on the leasehold interests and the value of the properties to our expansion plan. However, there is no assurance that our decision would always lead to the favorable outcome we expected to achieve. If any of our leases are terminated as a result of challenges by third parties or government authorities for lack of title certificates or proof of authorization to lease, we do not expect to be subject to any fines or penalties but we may be forced to relocate the affected learning centers and incur additional expenses relating to such relocation. In addition, our teaching institutions are required to pass fire inspection and fire control assessment each year under applicable laws and regulations. If our use of the leased premise is challenged by relevant government authorities for lack of fire inspection, we may be further subject to fines, rectifications and we may need to relocate the affected learning centers and incur additional expenses. If we fail to find suitable replacement sites in a timely manner or on terms acceptable to us, our business and results of operations could be materially and adversely affected.

### **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.

In addition, our online education business is operated by our majority-owned subsidiary, Koolearn Technology Holding Limited, or Koolearn, through a series of contractual arrangements with Beijing New Oriental Xuncheng Network Technology Co., Ltd., or Beijing Xuncheng, and its subsidiaries and shareholders. These contractual arrangements enable Koolearn to (1) have power to direct the activities that most significantly affect the economic performance of Beijing Xuncheng and its subsidiaries; (2) receive substantially all of the economic benefits from Beijing Xuncheng and its subsidiaries in consideration for the services provided by Koolearn's wholly-owned subsidiaries in China; and (3) have an exclusive option to purchase all or part of the equity interests in Beijing Xuncheng, when and to the extent permitted by PRC law, or request any existing shareholder of Beijing Xuncheng to transfer all or part of the equity interest in Beijing Xuncheng 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 Beijing Xuncheng, Its Subsidiaries and Shareholders. In this annual report, we refer to New Oriental China and Beijing Xuncheng as our variable interest entities, and to New Oriental China and its schools and subsidiaries as well as Beijing Xuncheng and its subsidiaries as our consolidated affiliated entities.

**Table of Contents**

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, and (ii) the corporate structure of Beijing Xuncheng and its subsidiaries and the wholly-owned subsidiary of Koolearn 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, and (ii) the contractual arrangements among Koolearn's wholly-owned subsidiary in China, Beijing Xuncheng and its subsidiaries and shareholders 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.

It is uncertain whether any new PRC laws, rules or regulations relating to variable interest entity structures will be adopted or if adopted, what they would provide. In particular, in January 2015, the Ministry of Commerce published a discussion draft of the proposed Foreign Investment Law for public review and comments. Among other things, the draft Foreign Investment Law expands the definition of foreign investment and introduces the principle of actual control in determining whether a company is considered a foreign-invested enterprise. Under the draft Foreign Investment Law, variable interest entities would also be deemed as foreign-invested enterprises if they are ultimately controlled by foreign investors, and be subject to restrictions on foreign investments. However, the draft law has not taken a position on what actions will be taken with respect to the existing companies with the variable interest entity structure, whether or not these companies are controlled by Chinese parties. It is uncertain when the draft would be signed into law and whether the final version would have any substantial changes from the draft. See Risks Related to Doing Business in China Substantial uncertainties exist with respect to the enactment timetable, final content, interpretation and implementation of draft PRC Foreign Investment Law published for public comments and how it may impact the viability of our current corporate structure, corporate governance and business operations.

We have been further advised by our PRC counsel that if we, any of our PRC subsidiaries or consolidated affiliated entities 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 or consolidated affiliated entities;

discontinuing or restricting the operations of any related-party transactions among our PRC subsidiaries and our consolidated affiliated entities;

restricting our right to collect revenues or 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 our consolidated affiliated entities that most significantly impact their economic performance, and/or our failure to receive the economic benefits from our consolidated affiliated entities, we may not be able to consolidate our consolidated affiliated entities 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 subsidiaries in China or our consolidated affiliated entities.

### ***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 our variable interest entities, their respective schools and/or subsidiaries and their respective shareholders to operate substantially all of our education business. These contractual arrangements may not be as effective in providing us with control over our variable interest entities as direct ownership. From the legal perspective, if our variable interest entities, any of their schools and/or subsidiaries or their shareholders 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, 2016, 2017 and 2018, our consolidated affiliated entities contributed in aggregate 97.7%, 98.8% and 98.8%, 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 our consolidated affiliated entities, and our ability to conduct our business may be negatively affected, and we may not be able to consolidate the financial results of our consolidated affiliated entities into our consolidated financial statements in accordance with U.S. GAAP.

### ***Our ability to enforce the equity pledge agreements between us and the shareholders our variable interest entities may be subject to limitations based on PRC laws and regulations.***

Pursuant to the equity pledge agreements among our subsidiaries in China, each of our variable interest entities and their respective shareholders, each shareholder of our variable interest entities agrees to pledge its equity interests in the variable interest entity to our subsidiaries to secure the performance by themselves and by our consolidated affiliated entities of their obligations under the relevant contractual arrangements. The equity pledges of shareholders

of our variable interest entities 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 any of our consolidated affiliated entities or any of the shareholders of our variable interest entities 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 our variable interest entity in an auction or private sale and remit the proceeds to our 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 the variable interest entity. 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 our PRC subsidiary, a party to the option agreement with the shareholder of our variable interest entities, to designate another PRC person or entity to replace the shareholder pursuant to the direct transfer option we have under the option agreement.

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**Table of Contents**

In addition, for New Oriental China, the amount of registered equity interests pledged to our wholly-owned subsidiaries in the registration forms of the local branch of SAIC 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 the majority shareholder of Beijing Xuncheng, holding 74.4945% of Beijing Xuncheng. New Oriental China is wholly owned by Century Friendship, a PRC domestic company which is controlled by Mr. Michael Minhong Yu, our founder and executive chairman. 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 13.0% of our total common shares issued and outstanding as of September 21, 2018. 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 cause Beijing Xuncheng and its 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 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 our consolidated affiliated entities 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 and our consolidated affiliated entities have the apparent authority to enter into contracts on behalf of such entities without chops. All designated legal representatives of our PRC subsidiaries and our consolidated affiliated entities 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 our consolidated affiliated entities, 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 consolidated affiliated entity 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.

***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 (as amended on November 7, 2016 by the Standing Committee of the National People's Congress and became effective on September 1, 2017), or the Amended Private Education Law, which replaced the Law for Promoting Private Education (2003), and the Implementation Rules for the Law for Promoting Private Education (2004), or the Implementation Rules (2004), the amendment to which is currently under review by the State Council. The implementation of the Amended Private Education Law is still in a transition period pending for the promulgation of



amendment to the Implementation Rules (2004) and the adoption of local regulations of by each province in China. Thus the private schools in China, including our schools, are now in a transition period for re-registration according to the Amended Private Education Law and its Implementation Rules and other relevant regulations.

Under the Law for Promoting Private Education (2003), which was replaced and abolished on September 1, 2017, and its Implementation Rules (2004), a private school may elect to be a school that does not require reasonable returns or a school that requires 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 annual net income of the school, while in the case of a private school that does not require reasonable returns, this amount shall be no less than 25% of the annual increase in the net assets of the school, if any. As of May 31, 2018, 26 of our schools elected as schools not requiring reasonable returns, 37 of our schools elected as schools requiring reasonable returns, and the remaining schools are not classified or registered as companies.

## **Table of Contents**

Under the Amended Private Education Law, the term reasonable return is no longer used, and sponsors of private schools may choose to establish non-profit or for-profit private schools at their own discretion, except that private schools in compulsory education area can only be registered as non-profit private schools. Sponsors of for-profit private schools are entitled to retain the profits from their schools and the operating surplus may be allocated to the sponsors pursuant to the PRC Company Law and other relevant laws and regulations. Sponsors of non-profit private schools are not entitled to any distribution of profits from their schools and the entire income must be used for the operations of the schools. See Item 4. Information on the Company B. Business Overview Regulation. Under such requirements by the Amended Private Education Law, our schools have yet to be re-registered as non-profit or for-profit private schools during the transition period.

If our schools choose to be for-profit private education entities, they may be subject to PRC enterprise income tax at the rate of 25% and other taxes as if they were enterprises. For the year ended May 31, 2018, schools that accounted for approximately 64.1% of our consolidated net revenues were subject to a 25% income tax rate. Historically, the effective income tax rates for all our schools were 11.05%, 12.17% and 15.35% in the fiscal years ended May 31, 2016, 2017 and 2018, respectively. On the other hand, if our schools choose to be non-profit private education entities, our contractual arrangements with New Oriental China and its schools and subsidiaries may be subject to more stringent scrutiny.

On August 10, 2018, the Ministry of Justice published for public comments a draft of the amended Implementation Rules for the Law for Promoting Private Education, or the Draft Amended Implementation Rules, which has been submitted by the Ministry of Education to the State Council for approval. As of the date of this annual report, the Draft Amended Implementation Rules are still pending for approval. If these rules are signed into law, they would have several impacts on our existing business. For example:

Pursuant to the Draft Amended Implementation Rules, private schools that provide pre-school education and degree education, like our kindergartens, private primary and secondary school in Yangzhou and our private secondary school in Beijing, are subject to approval by the government's education department at or above county level using standards applicable to public schools of the same grade and category. Private training and education entities that provide after-school tutoring services for kindergarten kids or primary, middle and high school students are subject to approval and strict supervision by the government's education department at or above county level. Private training and education entities that offer courses of languages, art, sports, science and technology, research and other subjects that focus on character education and personality development, as well as private training and education entities that provide non-degree educational services for adults may directly apply to register as a legal person without obtaining prior approval from the relevant education authorities. Pursuant to the foregoing, except for our kindergartens, private primary and secondary school in Yangzhou, our private secondary school in Beijing and our private training and education entities that provide after-school tutoring services, all of our other existing schools would not be required to obtain approval from the government's education department.

The Draft Amended Implementation Rules require private schools providing online diploma-awarding education to hold both a private school operating permit and relevant internet operating permits. Private schools providing any online training and education services, or technology companies providing any online platform or system supporting such online training and educations, shall obtain relevant internet operation permits and file with the government's education department or the government's human resources and social security department at provincial level, and shall review and record the identities of entities or individuals

who apply for access to their online platforms. None of our schools provides online diploma-awarding education. The operating entity of our online education holds a license for Internet information services, or ICP license. It is unclear at the current stage whether further licenses would be required if the Draft Amended Implementation Rules are signed into law.

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**Table of Contents**

In addition, the Draft Amended Implementation Rules prohibit any entities that implement collectivization education from gaining control over non-profit schools through mergers and acquisitions, franchise chains, and control agreements. Any agreements between a non-profit private school and its connected party that involve major interests or will be repeatedly performed in a long-term shall be reviewed and audited by relevant government authorities in the aspect of necessity, legitimacy and compliance and shall be arm s-length transactions. These and other provisions on non-profit private schools, if signed into law, may force all of our training schools to elect to be for-profit schools and may substantially restrict our ability to acquire and control non-profit schools, which may in turn subject our schools to a 25% income tax rate discussed above and adversely affect our financial condition and results of operations.

Recently, several regulations on after-school tutoring activities have been promulgated. For instance, in February 2018, the Ministry of Education, the Ministry of Civil Affairs, the Ministry of Human Resources and Social Security and the SAIC jointly issued the Notice on Effectively Reducing the Extracurricular Burden of Primary and Secondary School Students and Launching Special Governance Actions of After-School Tutoring Institutions. The notice prohibits after-school tutoring institutions from providing courses more advanced than the syllabus and curricula applicable to the respective primary and secondary school students or courses focusing on enhancing students exam-taking skills or organizing grade examinations and competitions for primary and secondary school students. It is also forbidden to link the tutoring results at after-school tutoring institutions with the enrollment of primary and secondary schools. The Notice requires that rectification measures shall be taken by after-school tutoring institutions before the end of 2018 for authorities inspection, which is scheduled to be completed before June 2019.

On August 22, 2018, the State Council issued an Opinion on Supervising After-School Tutoring Institutions, or the State Council Circular 80, which provides guidance on regulating after-school tutoring institutions that target primary and secondary school students and specifies operating requirements that after-school tutoring institutions must meet. The State Council Circular 80 provides, among other things, that (i) the average available-for-use area per student must be no less than three square meters within the same training hours; (ii) private school shall purchase safety insurance for training participants; (iii) no in-service school teachers shall be hired by after-school tutoring institutions and all the teachers for Chinese, math, English, physics, chemistry and biology courses in after-school tutoring institutions shall obtain relevant teaching qualifications; (iv) the content, classes, enrollment targets, progress and school hours of courses like Chinese, mathematics, English, physics, chemistry, and biology shall be filed with the local education authorities and be made public; (v) the training courses offered to primary and secondary school students shall not be more advanced than the syllabus and curricula applicable to them; (vi) no tutoring courses shall be given after 8:30 p.m., and no homework from after-school institutions shall be allowed; (vii) no grade examination, competition or ranking in connection with the subjects of primary schools or middles schools shall be organized, and no class shall be arranged in conflict with the hours of regular schools, and (viii) no advance tuition fees of more than three months may be collected. See Item 4. Information on the Company B. Business Overview Regulation for more information. Such requirements in Circular 80 were further emphasized and interpreted in the Circular on Implementing Inspections and Rectification on After-school Training Institutions, promulgated by MOE on September 13, 2018, which requires that (i) the name, content, enrollment target, schedule and time of the classes arranged by the after-school tutoring institutions should be filed with the government s education department at county level and the after-school tutoring institutions should not recruit any students without such filing; and that (ii) teachers without teaching qualifications should attend the Teaching Qualification Examinations in the second half of 2018 and the after-school tutoring institutions should not hire the teachers who fail to pass such examinations. To comply with these and other requirements, we need to make necessary adjustments to our business and operations, which could be costly and time-consuming. We cannot assure you that we will be in full compliance with such requirements in time or at all. Any failure by us to comply with these and other requirements may subject us to administrative fines or penalties or order to suspend operations, which would materially and adversely affect our reputation, business, financial condition and results of operations.

In addition, under PRC laws and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. The contractual arrangements with our consolidated affiliated entities 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. We could face material and adverse tax consequences if the PRC tax authorities determine that the contractual arrangements among our subsidiaries in China and our consolidated affiliated entities, do not represent an arm's-length price and adjust our consolidated affiliated entities' 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 our consolidated affiliated entities, which could in turn increase their tax liabilities. In addition, the PRC tax authorities may impose late payment fees and other penalties to our consolidated affiliated entities 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.

**Table of Contents**

***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 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. We expect that if we convert the net proceeds from offshore offerings into RMB pursuant to SAFE Circular 142, our use of RMB funds will be for purposes within the approved business scope of our PRC subsidiaries. However, we may not be able to use such RMB funds to make equity investments in China through our PRC subsidiaries. SAFE promulgated the Notice on Reforming the Management Method relating to Conversion of the Capital Contribution of Foreign Invested Company from Foreign Exchange to Renminbi, or SAFE Circular 19, effective June 2015, which abolished SAFE Circular 142, but the foregoing rules have been retained in SAFE Circular 19. SAFE promulgated the Notice on Further Simplifying and Improving the Policies of Foreign Exchange Administration Applicable to Direct Investment, or SAFE Circular 13, effective in June 2015. Pursuant to SAFE Circular 13, annual foreign exchange inspection of direct investment is not required anymore and the registration of existing equity is required. SAFE Circular 13 also grants the authority to banks to examine and process foreign exchange registration with respect to both domestic and offshore direct investment. SAFE issued the Circular on Reforming and Regulating Policies on the Control over Foreign Exchange Settlement of Capital Accounts, or SAFE Circular 16, effective in June 2016. Pursuant to SAFE Circular 16, enterprises registered in China may also convert their foreign debts from foreign currency to RMB on a self-discretionary basis. SAFE Circular 16 provides an integrated standard for conversion of foreign exchange under capital account items (including but not limited to foreign currency capital and foreign debts) on a self-discretionary basis which applies to all enterprises registered in China. SAFE Circular 16 reiterates the principle that RMB converted from foreign currency-denominated capital of a

company may not be directly or indirectly used for purposes beyond its business scope or prohibited by PRC laws or regulations, while such converted RMB shall not be provided as loans to its non-affiliated entities. See also Item 4. Information on the Company B. Business Overview Regulation.

We expect that PRC laws and regulations may continue to limit our use of proceeds from offshore offerings. There are no costs associated with registering loans or capital contributions with relevant PRC government authorities, other than nominal processing charges. Under PRC laws and regulations, the PRC government authorities are required to process such approvals or registrations or deny our application within a prescribed period which is usually less than 90 days, but may be longer due to administrative delay. 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.



## **Table of Contents**

***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.

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.

## **Table of Contents**

In addition, the changes in the policies regarding the control of foreign exchange could adversely affect our business. In 2016, PRC government implemented various measures and policies regarding strengthening the management and supervision control of foreign control in both capital item and current item, which resulted in extension of time in the filing, registration and approval procedures of local branches and authorized banks in foreign control activities, and could result in delayed payment of salary to foreign employees by our subsidiaries and subsidiaries of our variable interest entity. The evolving policies regarding strengthening the management and supervision control of foreign control could adversely affect 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 since 2012. 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.

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.

***Substantial uncertainties exist with respect to the enactment timetable, final content, interpretation and implementation of draft PRC Foreign Investment Law published for public comments and how it may impact the viability of our current corporate structure, corporate governance and business operations.***

The Ministry of Commerce published a discussion draft of the proposed Foreign Investment Law in January 2015 aiming to, upon its enactment, replace the trio of existing laws regulating foreign investment in China, namely, the

Sino-foreign Equity Joint Venture Enterprise Law, the Sino-foreign Cooperative Joint Venture Enterprise Law and the Wholly Foreign-invested Enterprise Law, together with their implementation rules and ancillary regulations. The draft Foreign Investment Law embodies an expected PRC regulatory trend to rationalize its foreign investment regulatory regime in line with prevailing international practice and the legislative efforts to unify the corporate legal requirements for both foreign and domestic investments. The Ministry of Commerce has solicited comments on this draft and substantial uncertainties exist with respect to its enactment timetable, final content, interpretation and implementation.

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**Table of Contents**

Among other things, the draft Foreign Investment Law expands the definition of foreign investment and introduces the principle of actual control in determining whether a company is considered a foreign-invested enterprise. The draft Foreign Investment Law specifically provides that entities established in China but controlled by foreign investors will be treated as foreign-invested enterprises, whereas an entity established in China by an investor from a foreign jurisdiction would nonetheless be, upon market entry clearance by the Ministry of Commerce, treated as a PRC domestic investor in a restricted industry as indicated in the negative list, provided that the entity is controlled by PRC entities and/or citizens. In this connection, control is broadly defined in the draft law to cover the following summarized categories: (i) holding 50% or more of the shares, voting rights or other similar rights of the subject entity; (ii) holding less than 50% of the shares, voting rights or other similar rights of the subject entity but having the power to secure at least 50% of the seats on the board or other equivalent decision making bodies, or having the voting power to exert material influence on the board, the shareholders meeting or other equivalent decision making bodies; or (iii) having the power to exert decisive influence, via contractual or trust arrangements, over the subject entity's operations, financial matters or other key aspects of business operations. Once an entity is determined to be a foreign-invested enterprise, it will be subject to the foreign investment restrictions or prohibitions set forth in the Negative List issued on June 28, 2018 and became effective on July 28, 2018. Unless the underlying business of the foreign-invested enterprise falls within the Negative List, which calls for market entry clearance by the Ministry of Commerce, prior approval from the government authorities as mandated by the existing foreign investment legal regime would no longer be required for establishment of the foreign-invested enterprise.

The variable interest entity structure, or VIE structure, has been adopted by many PRC-based companies, including us, to obtain necessary licenses and permits in the industries that are currently subject to foreign investment restrictions in China. See Item 3 Key Information D. Risk Factors Risks Related to Our Corporate Structure and Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Its Shareholder. Under the draft Foreign Investment Law, variable interest entities that are controlled via contractual arrangement would also be deemed as foreign-invested enterprises, if they are ultimately controlled by foreign investors. Therefore, for any companies with a VIE structure in an industry category that is included in the Negative List as restricted industry, the VIE structure may be deemed legitimate if the ultimate controlling person(s) is/are of PRC nationality (either PRC companies or PRC citizens) or the foreign investment obtains market entry clearance from the Ministry of Commerce. Conversely, if the actual controlling person(s) is/are of foreign nationalities, then the variable interest entities will be treated as foreign-invested enterprises and any operation in the industry category on the Negative List without market entry clearance may be considered as illegal. There are uncertainties as to whether the Foreign Investment Law, once it is enacted, will have retrospective effect on existing VIE structures such as ours, or will grant real and full grandfathering and grace periods for such existing VIE structures.

It is likely that we would not be considered as ultimately controlled by Chinese parties, as our record shareholders in the U.S. hold a substantial majority of our total voting power. The draft Foreign Investment Law has not taken a position on what actions will be taken with respect to the existing companies with a VIE structure, whether or not these companies are controlled by Chinese parties, while it has solicited comments from the public on this point. If the enacted version of the Foreign Investment Law mandate further actions, such as market entry clearance or certain restructuring of our corporate structure and operations, to be completed by companies with existing VIE structure like us, there may be substantial uncertainties as to whether we can complete these actions in a timely manner, or at all, and our business and financial condition may be materially and adversely affected.

The draft Foreign Investment Law, if enacted as proposed, may also materially impact our corporate governance practice and increase our compliance costs. For instance, the draft Foreign Investment Law imposes stringent ad hoc and periodic information reporting requirements on foreign investors and the applicable foreign-invested enterprises. Aside from an investment implementation report and an investment amendment report that are required for each

investment and alteration of investment specifics, an annual report is mandatory, and large foreign-invested enterprises meeting certain criteria are required to report on a quarterly basis. Also, the Ministry of Commerce may supervise and examine the foreign investors and the FIEs regularly or irregularly on their compliance with the Foreign Investment Law. Any company found to be non-compliant with these information reporting obligations may potentially be subject to fines and/or administrative or criminal liabilities, and the persons directly responsible may be subject to criminal liabilities.

**Table of Contents**

***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 relevant 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. According to the Draft Amended Implementation Rules, we may need to obtain a private school operating permit from relevant local education authorities for our kindergartens, private primary and secondary school in Yangzhou, our private secondary school in Beijing, and our private training and education entities which offer after-school tutoring services for kindergarten kids or primary, middle and high school students. In addition, as we provide online tutoring and education services through our websites and mobile applications, we may also need to make a filing with the local education department or the department of human resources and social security under the Draft Amended Implementation Rules. As of the date of this annual report, the Draft Amended Implementation Rules are still pending for approval.

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.

***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 notice in July 2014, which replaced the previous notice issued in October 2005. The 2014 SAFE notice requires PRC domestic residents, including both PRC domestic institutions and PRC domestic individual residents, to register with the local SAFE branch, currently with local bank according to Notice of the State Administration of Foreign Exchange on Further Simplifying and Improving Policies for the Foreign Exchange Administration of Direct Investment issued by SAFE on 13 February 2015, before establishing or controlling any company outside of China

with the domestic or overseas assets or equity they legally hold for the purpose of investment, financing or conducting roundtrip investment. Such a company located outside of China is referred to in the notice as an offshore special purpose company. 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 in 2006. 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.



**Table of Contents**

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

In February 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 7. According to Circular 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.

According to Circular 7, from time to time, we need to make applications or update our registration with SAFE or its local branches on behalf of our employees who are affected by our new share incentive plan or material changes in our current share incentive plan. We are in the process of making an application on behalf of the PRC individuals who participate in our company's share incentive plans with SAFE in compliance with Circular 7; however, we cannot assure you that such application will be successful. If we or the participants of our share incentive plans who are PRC citizens fail to comply with Circular 7, we and/or such participants of our share incentive plans may be subject to fines and legal sanctions. In addition, there may be additional restrictions on the ability of such participants to exercise their stock options or remit proceeds gained from sale of their stock into China, and we may be prevented from further granting share incentive awards under our share incentive plans to our employees who are PRC citizens. 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, and the NDRC Circular 11 establish certain procedures for our offshore investing activities, which could make it more difficult for us to pursue growth through acquisitions in and outside China.***

In August 2006, 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. 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.

Further, pursuant to the Circular 11 issued by the NDRC, outbound investment via the overseas enterprises controlled by PRC residents are subject to verification and approval, record-filing and reporting requirements to the NDRC. According to Circular 11, sensitive projects, such as outbound investment in real estate, hotels, news media, cinemas or sports club, carried out by overseas enterprises controlled by PRC residents shall obtain verification and approval from the NDRC prior to the implementation of the project. The non-sensitive projects carried out by the overseas

enterprise directly controlled by PRC residents, including by means of making asset or equity investment by companies established for financing and investing, such as fund institutions, or providing financing or guarantee, shall complete record-filing with the competent authority prior to the implementation of such project. The non-sensitive projects carried out by the overseas enterprise indirectly controlled by PRC residents with the investment amount over RMB300 million shall be reported to the NDRC of relevant information by submitting an information reporting form for large-amount non-sensitive projects. See Item 4. Information on the Company B. Business Overview Regulation Regulation Administrative Measures for Outbound Investment by Enterprises for more detail of Circular 11. If we fail to comply with rules in Circular 11, we may be subject to warnings, project to be suspended for implementation or rectification within a specified time limit.

**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 1.8% for May 2018. 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 RMB 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 RMB 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 RMB and the U.S. dollar remained within a narrow band. Since June 2010, the RMB has fluctuated against the U.S. dollar, at times significantly and unpredictably. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the RMB 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.

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**Table of Contents**

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

In March 2007, the National People's Congress passed the Enterprise Income Tax Law, or the EIT Law, which took effect in January 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 which were amended in January 2016 and June 2016, 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.

A high and new technology enterprise is entitled to a favorable enterprise income tax rate of 15% and such qualification is reassessed by relevant governmental authorities every three years. Five of our wholly-owned subsidiaries in China, including Beijing Hewstone Technology Co., Ltd., or Beijing Hewstone, Beijing Decision Education & Consulting Co., Ltd., or Beijing Decision, Beijing Smart Wood Software Technology Co., Ltd., or Beijing Smart Wood, and two other subsidiaries, are qualified as high and new technology enterprises. Beijing Pioneer Technology Co., Ltd., or Beijing Pioneer, one of our wholly-owned subsidiaries in China, is in the process of renewing its qualification of high and new technology enterprises. Once the renewal is completed, Beijing Pioneer will be eligible for a the favorable enterprise income tax rate of 15% starting January 1, 2018. Beijing Xuncheng, one of our variable interest entities, is also qualified as high and new technology enterprises. An enterprise that qualifies as a software enterprise is exempt from enterprise income tax for the two years beginning in the enterprise's first profitable year and then is entitled to a reduced tax rate of 12.5% for the succeeding three years. Seven of our wholly-owned subsidiaries in China, including Beijing Smart Wood and six of our other wholly-owned subsidiaries in China are qualified as software enterprises. See Item 5. Operating and Financial Review and Prospects A. Operating Results Taxation PRC.

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. To date, no regulations have been promulgated by the relevant authorities with regard to the preferential income tax treatment applicable to private schools requiring reasonable returns. As of May 31, 2018, 26 of our schools elected as schools not requiring reasonable returns, 37 of our schools elected as requiring reasonable returns and the remaining schools were not classified or registered as companies.

The Amended Private Education Law, which became effective on September 1, 2017, no longer uses the term reasonable return. Instead, under the Amended Private Education Law, sponsors of private schools may choose to establish non-profit or for-profit private schools at their own discretion, except that private schools in compulsory education area can only be registered as non-profit private schools. Pursuant to the Amended Private Education Law, non-profit private schools will be entitled to the same tax benefits as public schools while taxation policies for for-profit private schools are still unclear. Other than our primary and secondary schools, which are required to be non-profit schools under the Amended Private Education law, we intend to register all of our schools as for-profit private schools to the extent practicable under the relevant local rules and regulations.

In practice, tax treatments for private schools vary across different cities in China. Private schools in certain cities are subject to a 25% standard enterprise income tax, 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 at all. For example, Beijing Haidian School was not required by the governing tax bureau to pay any EIT from its establishment through May 31, 2018. However, it is unclear what impact the Amended Private Education Law and any of its potential implementation rules would have on the tax treatment applicable to Beijing Haidian School, and whether Beijing Haidian School would continue to enjoy the preferential tax treatment in the future.

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**Table of Contents**

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.

***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. The State Administration of Taxation has issued a circular providing 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 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. Moreover, the State Administration of Taxation issued a bulletin in January 2014, to provide more guidance on the implementation of the above circular. This bulletin further provided that, among other things, an entity that is classified as a resident enterprise in accordance with the circular shall file the application for classifying its status of residential enterprise with the local tax authorities where its main domestic investors registered. From the year in which the entity is determined as a resident enterprise, any dividend, profit and other equity investment gain shall be taxed in accordance with the Article 26 of EIT law and the Article 17 and Article 83 of its implementation rules. 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 State Administration of Taxation'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.

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, 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. This could increase our and our shareholders' effective income tax rates and may require us to deduct withholding tax from any dividends we pay to our non-PRC shareholders.



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**Table of Contents*****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.

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 in January 2007, the Notice of the State Administration of Taxation on Negotiated Reduction of Dividends and Interest Rates, which was issued in 2008, and the Notice of the State Administration of Taxation Regarding Interpretation and Recognition of Beneficial Owners under Tax Treaties, which became effective in October 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 in December 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 was partially terminated by the Announcement of the State Administration of Taxation on Several Issues Concerning the Enterprise Income Tax on Indirect Property Transfer by Non-Resident Enterprises, or Bulletin 7, pursuant to which where a non-resident enterprise indirectly transfers properties such as equity in PRC resident enterprises without any justifiable business purposes with the aim of avoiding to pay enterprise income tax, such indirect transfer shall be reclassified as a direct transfer of equity in PRC resident enterprise. To determine whether there are reasonable commercial purposes, all arrangements related to the indirect transfer of PRC taxable properties shall be considered comprehensively and factors set out in the Announcement shall be comprehensively analyzed in light of the actual situation.

According to Bulletin 7, 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. On October 17, 2017, the SAT issued the Announcement of the State Administration of Taxation on Issues Concerning the Withholding of Non-resident Enterprise Income Tax at Source, or SAT Bulletin 37, which came into effect and superseded Circular 698 on December 1, 2017. The SAT Bulletin 37 further clarifies the practice and procedure of the withholding of nonresident enterprise income tax.

## **Table of Contents**

There is uncertainty as to the application of Bulletin 7 and Bulletin 37. As a result, we and our non-resident investors may have the risk of being taxed under Bulletin 7 and Bulletin 37 and may be required to spend valuable resources to comply with Bulletin 7 and Bulletin 37 or to establish that we or our non-resident investors should not be taxed under Bulletin 7 and Bulletin 37, which may have a material adverse effect on our financial condition and results of operations or such non-resident investors' investments in us.

***If we fail to obtain and maintain the licenses and approvals required under the ambiguous regulatory environment for online education in China, our business, financial condition and results of operations may be materially and adversely affected.***

The online education industry in China is still in its nascent stage. The relevant laws and regulations are relatively new and still evolving, and their interpretation and enforcement involve significant uncertainty and ambiguity. As a result, in certain circumstances it may be difficult to determine what actions or omissions may be deemed to be in violation of applicable laws and regulations. Issues, risks and uncertainties relating to PRC governmental regulation of the internet industry include, but are not limited to, the following.

The production, editing, transmission to the public through our online platform or mobile applications of our course materials and audio-visual content, may be deemed as providing audio-video programs or internet culture services under relevant PRC Laws. Thus, we may be required to obtain the License for Radio and TV Program Production and Operation License, License for Online Transmission of Audio-Visual Programs or Internet Culture Operation License as currently there is no further official or publicly available interpretation of whether such content would be deemed Radio and TV Program Production, Audio-Visual Programs or Internet cultural products. In light of the confirmation of the competent PRC government authorities, as of the date of this annual report, we are not explicitly required to obtain those licenses under current regulations and regulatory policies. However, we cannot assure that the competent PRC government authorities will not subsequently take a contrary view, especially in light of new regulatory developments. If the government authorities determine that our online tutoring services fall within the scope of business operations that require the above-mentioned licenses or other licenses or permits, we may not be able to obtain such licenses or permits on reasonable terms or in a timely manner or at all, and failure to obtain such licenses or permits may subject us to fines, legal sanctions or an order to suspend our online tutoring services.

***The audit report included in this annual report is prepared by auditors who are not inspected by the Public Company Accounting Oversight Board and, as such, you are 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 (the "SEC"), as auditors of companies that are traded publicly in the United States and a firm registered with the U.S. Public Company Accounting Oversight Board (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 PRC government authorities, our auditors are not currently inspected by the PCAOB.

Inspections of other accounting 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.

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**Table of Contents**

*If additional remedial measures are imposed on the big four PRC-based accounting firms, including our independent registered public accounting firm, in administrative proceedings brought by the SEC alleging such firms' failure to meet specific criteria set by the SEC with respect to requests for the production of documents, we could be unable to timely file future financial statements in compliance with the requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act.*

Starting in 2011 the Chinese affiliates of the big four accounting firms, including our independent registered public accounting firm, were affected by a conflict between U.S. and PRC law. Specifically, for certain U.S. listed companies operating and being audited in mainland China, the SEC and the PCAOB sought to obtain from the Chinese accounting firms access to their audit work papers and related documents. The accounting firms were, however, advised and directed that under PRC law they could not respond directly to the U.S. regulators on those requests, and that requests by foreign regulators for access to such papers in China had to be channeled through the China Securities Regulatory Commission, or the CSRC.

In late 2012 this impasse led the SEC to commence administrative proceedings under Rule 102(e) of its Rules of Practice and also under the Sarbanes-Oxley Act of 2002 against the Chinese accounting firms, including our independent registered public accounting firm. A first instance trial of the proceedings in July 2013 in the SEC's internal administrative court resulted in an adverse judgment against the accounting firms. The administrative law judge proposed penalties on the firms including a temporary suspension of their right to practice before the SEC, although that proposed penalty did not take effect pending review by the commissioners of the SEC. On February 6, 2015, before a review by the commissioners of the SEC had taken place, the firms reached a settlement with the SEC. Under the settlement, the SEC accepted that future requests by the SEC for the production of documents will normally be made to the CSRC. The firms will receive matching Section 106 requests, and are required to abide by a detailed set of procedures with respect to such requests, which in substance require them to facilitate production via the CSRC. If they fail to meet specified criteria, the SEC retains authority to impose a variety of additional remedial measures on the firms depending on the nature of the failure. Remedies for any future noncompliance could include, as appropriate, an automatic six-month bar on a single firm's performance of certain audit work, commencement of a new proceeding against a firm, or in extreme cases the resumption of the current proceeding against all four firms.

In the event that the SEC restarts the administrative proceedings, depending upon the final outcome, listed companies in the United States with major PRC operations may find it difficult or impossible to retain auditors in respect of their operations in the PRC, which could result in financial statements being determined to not be in compliance with the requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act, including possible delisting. Moreover, any negative news about any such future proceedings against these accounting firms may cause investor uncertainty regarding China-based, United States-listed companies and the market price of our ADSs may be adversely affected.

If our independent registered public accounting firm were denied, even temporarily, the ability to practice before the SEC and we were unable to timely find another registered public accounting firm to audit and issue an opinion on our financial statements, our financial statements could be determined not to be in compliance with the requirements of the Exchange Act. Such a determination could ultimately lead to the delisting of our ADSs from the NYSE or the deregistration of our ADSs from the SEC, or both, which would substantially reduce or effectively terminate the trading of our ADSs in the United States.

**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:

**Table of Contents**

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.

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 plans.

***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.



## **Table of Contents**

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.

***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 depositary may refuse to deliver, transfer or register transfers of ADSs generally when our books or the books of the depositary are closed, or at any time if we or the depositary 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.

## **Table of Contents**

***We have been named as a defendant in a putative shareholder class action lawsuit 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 lawsuit described in Item 8, Financial Information A. Consolidated Statements and Other Financial Information Legal Proceedings, including any appeals of such lawsuit should our initial defense be unsuccessful. We are currently unable to estimate the possible outcome or loss or possible range of loss, if any, associated with the resolution of the lawsuit. In the event that our initial defense of the lawsuit is unsuccessful, there can be no assurance that we will prevail in any appeal. Any adverse outcome, including any plaintiff's appeal of a judgment in the lawsuit, 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 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.

***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.

***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 (2013 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.

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**Table of Contents*****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 2018 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, 2018. 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, the determination of whether we will be or become a PFIC will depend in large part upon the market value of our ADSs, of which we cannot control. Accordingly, fluctuations in the market price of our ADSs 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.

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. U.S. Holders of our ADSs or common shares are urged to consult their tax

advisors concerning the United States federal income tax consequences if we are or become classified as a PFIC. 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

37

## **Table of Contents**

Our first school was established by Michael Minhong Yu, our executive chairman, 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.

Beijing Xuncheng, a then majority-owned subsidiary of New Oriental China, which operates our several online education platforms together with its subsidiaries, one of which is koolearn.com, listed its shares on the National Equities Exchange and Quotations in China for trading from March 21, 2017 to February 14, 2018 whereby it completed a voluntary delisting from the National Equities Exchange and Quotations. Subsequent to its delisting, Beijing Xuncheng went through a series of restructuring transactions and became a variable interest entity controlled by Koolearn Technology Holding Limited, or Koolearn, a majority-owned subsidiary of our offshore holding company. In July 2018, Koolearn submitted an application for its initial public offering and the listing of its shares on the Stock Exchange of Hong Kong Limited.

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 Conyers Trust Company (Cayman) Limited, Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands. We have branch offices in 75 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 language training and test preparation, pre-school, primary and secondary school education, online education, content development and distribution, overseas study consulting services, and study tour. 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 36.5 million cumulative student enrollments. In the fiscal year ended May 31, 2018, we had over 6.3 million student enrollments, including approximately 5.5 million student enrollments in our K-12 after-school tutoring courses, approximately 0.6 million student enrollments in our test preparation courses and approximately 0.1 million student enrollments in our language training programs. 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.

Our total net revenues increased from US\$1,478.3 million for the fiscal year ended May 31, 2016 to US\$2,447.4 million for the fiscal year ended May 31, 2018, representing a compound annual growth rate, or CAGR, of 28.7%. Net revenues from our language training and test preparation courses accounted for 83.8%, 83.9% and 82.7%, respectively, of our total net revenues in the fiscal years ended May 31, 2016, 2017 and 2018. Net income attributable to New Oriental Education & Technology Group Inc. increased from US\$224.9 million in the fiscal year ended May 31, 2016 to US\$296.1 million in the fiscal year ended May 31, 2018, representing a CAGR of 14.7%.



**Table of Contents****Our Network**

As of May 31, 2018, we deliver our educational programs, services and products to students through our extensive network of 87 schools, 994 learning centers and 18 bookstores operated by us, approximately 28,100 teachers in 75 cities and websites, as well as through 158 third-party distributors, who provided us with access to a nationwide network of online and offline bookstores. 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, Xiamen, Changsha, Hangzhou and Zhengzhou. The following table sets forth information concerning the locations of our schools, learning centers and bookstores as of May 31, 2018.

<b>City</b>	<b>Number of schools</b>	<b>Number of learning centers</b>	<b>Number of bookstores</b>
Beijing	5	105	1
Shanghai	1	57	1
Guangzhou	1	36	1
Wuhan	1	57	1
Yangzhou	3		
Tianjin	1	32	
Xi'an	1	34	1
Nanjing	2	20	
Shenyang	1	31	
Chongqing	1	16	1
Chengdu	1	29	1
Shenzhen	1	21	
Xiangyang	1	12	
Taiyuan	1	30	
Haerbin	1	12	1
Changsha	1	33	
Jinan	1	16	
Zhengzhou	1	37	
Hangzhou	1	44	1
Changchun	3	20	1
Shijiazhuang	1	15	
Suzhou	1	34	1

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Zhuzhou	1	1	
Anshan	1	1	
Hefei	1	29	
Kunming	1	20	
Wuxi	1	13	
Foshan	1	5	
Fuzhou	1	18	
Yichang	1	4	
Nanchang	1	29	1

**Table of Contents**

<b>City</b>	<b>Number of schools</b>	<b>Number of learning centers</b>	<b>Number of bookstores</b>
Jingzhou	1	5	
Dalian	1	7	1
Lanzhou	1	14	1
Huangshi	1	2	
Ningbo	1	8	
Xiamen	1	26	
Qingdao	4	20	
Nanning	1	8	
Xuzhou	1	4	1
Xiangtan	1	2	
Zhenjiang	1	3	
Luoyang	1	10	
Nantong	1	3	
Jilin	1	6	
Guiyang	1	10	
Hohhot	1	5	1
Tangshan	1	9	
Urumqi	1	6	1
Shiyan	1	4	
Quanzhou	1		
Wenzhou	1	3	
Weifang	1	2	
Zhuhai	1	2	1
Jinzhou	1	2	
Baoding	1	2	
Yantai	1	3	
Taian	1		
Kaifeng	1		
Cangzhou	1		
Qinhuangdao	1		
Anyang	1		
Handan	1		
Zhangzhou	1		
Nanyang	1	1	
Zhongshan	1		
Yinchuan	1		
Shaoxing	1	7	
Huzhou	1	1	
Hong Kong	1		
Yancheng	1	1	
Lianyungang	1		
Jiaozuo	1	7	
Dongguan	1		
Haikou	1		
<b>Total</b>	<b>87</b>	<b>994</b>	<b>18</b>
<b>Our Programs, Services and Products</b>			

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 900 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; pre-school, primary and secondary schools; educational content, software and other technology development and distribution; online education; and other services and products.

## **Table of Contents**

### ***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, 2018, we had approximately 576,000 student enrollments in our test preparation courses, of which approximately 280,000 were in overseas test preparation courses, 296,000 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, and PETS.

In our fiscal year ended May 31, 2018, approximately 29.7% and 9.5% of the total student enrollments in our overseas test preparation courses took place in Beijing and Shanghai, respectively, and approximately 9.7% and 9.5% of the total student enrollments in our PRC test preparation courses took place in Wuhan and Haerbin, respectively. 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 VIP class, our experienced teachers generally teach in classes ranging from 6 to 50 students. Our students enroll in a 50 to 280 hour program with classes meeting one to six times per week for approximately 1 to 3 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 RMB1,500 to RMB37,000 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 4 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 12 to approximately 50 students per class.

In our fiscal year ended May 31, 2018, we had approximately 3,032,000 student enrollments in our after-school tutoring courses for middle school and high school students, and approximately 15.9% and 8.5% of the enrollments took place in Beijing and Xi'an, respectively. Course fees for our all subject after-school tutoring courses for middle school and high school students range from approximately RMB500 to approximately RMB4,000 per course.

## **Table of Contents**

*After-School Tutoring Courses for Children.* English is a major subject in primary 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, Chinese, math, writing, music and arts for children in kindergarten and primary schools.

Our after-school tutoring courses for children are typically divided into classes of 8 to approximately 24 students per class. Students attend class approximately two times per week for 2 to 3 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.

In our fiscal year ended May 31, 2018, we had approximately 2,424,000 student enrollments in our Pop Kids All Subjects after-school tutoring courses and approximately 8.0% and 8.0% of the enrollments took place in Beijing and Wuhan, respectively. Course fees for these courses range from approximately RMB300 to approximately RMB4,000 per course.

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

We provide various types of English language training courses as well as training courses for other foreign languages, including German, Japanese, French, Korean, Italian 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 1 to 5 times per week for 1.5 to 2.5 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 our English courses for adults typically range from 6 to approximately 60 students per class.

In our fiscal year ended May 31, 2018, we had approximately 72,000 student enrollments in our English courses for adults and approximately 42.1% and 15.2% of the total enrollments were for courses taught in Beijing and Shanghai, respectively. Course fees for our English courses for adults range from approximately RMB400 to approximately RMB5,700 per course.

## ***Pre-school, 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. As of May 31, 2018, there were over 3,700 students at the Yangzhou school, approximately 40% to 50% 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 370 teachers and 360 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, 2018, the school accepted 1,211 students out of over approximately 1,900 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, 2018, tuition at the Yangzhou school ranged from RMB17,600 to RMB95,000 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. Of the students of the class of 2018 of the international high school program at our Yangzhou school, 98% was admitted into at least one of the top 100 universities in the United States. In our fiscal year ended May 31, 2018, tuition at our international school ranges from RMB95,000 to RMB120,000 per year.

In September 2007, we established our pre-school business with the opening of our first kindergarten in Beijing. We opened our second kindergarten in Nanjing in April 2009, the third one in Yangzhou in August 2014, the fourth one in Beijing in January 2017, and the fifth one in Hong Kong in September 2017. As of May 31, 2018, there were approximately 920 students at these kindergartens. In December 2014, we acquired a kindergarten chain in the city of Qingdao with three schools, which had approximately 790 students as of May 31, 2018.

### ***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, 2018, we developed and edited about 205 titles and distributed approximately 21.6 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 British Council, Cengage Learning, Monash College Pty Ltd, NCUK, International Baccalaureate, Bell Education, ETS, Cambridge University Press, Cambridge English Language Assessment, The McGraw-Hill Companies, Oxford University Press, Harper Collins, ACT, Stanford University, Carnegie Mellon University, 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 primarily offer online education courses to students covering a full spectrum of ages in three core categories—college education, K-12 education and pre-school education. We provide our courses and products through

different online platforms and mobile applications in multiple formats, including live and pre-recorded courses for different class sizes.

*College education.* Our college education services primarily include college test preparation, overseas test preparation, and English language learning. Our courses target college students and working professionals preparing for standardized tests or seeking to improve their English language proficiency. Our services in the college category were launched in 2005 and are provided through Koolearn and Koo platforms.

*K-12 education.* Our K-12 education services comprise after-school tutoring courses which cover the majority of standard school subjects from primary to high school in China, and we offer preparation courses designed for standardized college and high school entrance exams. We launched our K-12 course offerings in 2015. Leveraging our expertise in K-12, in 2017, we also launched our innovative DFUB courses, a location-based live interactive tutoring service targeting students in lower-tier cities where offline infrastructure may not be as convenient and there is growing demand for an effective online platform accessible anytime, anywhere.

## **Table of Contents**

*Pre-school education.* Our pre-school education category offers child-friendly online educational content delivered through our Donut English-learning and child education apps and Donut live online English classroom courses. We launched our Donut app series in 2012 and Donut live online classroom in 2017.

In addition, using our online education modules, we also provide educational content packages to schools and institutional customers such as universities, public libraries, telecom operators and online video streaming providers.

## ***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.

*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. In October 2013, we terminated the brand name cooperation for New Oriental Star kindergarten program. As of May 31, 2018, there were a total of 12 brand cooperation schools offering our Pop Kids English program. For the fiscal years ended May 31, 2016, 2017 and 2018, we recognized revenues in an aggregate amount of US\$265 thousand, US\$311 thousand and US\$591 thousand, respectively, from license and training fees received from these schools.

*Overseas Study Tour.* In May 2012, we started our overseas study tour business, organizing primary and middle school students to go overseas to learn foreign languages and other short-term curriculum, attend summer/winter school programs, or take part in other educational activities. For the fiscal year ended May 31, 2018, we recognized revenues of US\$19.4 million from organizing overseas study tour.

## **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.



## **Table of Contents**

*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 executive chairman 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 mainstream online media, such as social media, search engines, news and vertical websites. We also have advertising arrangements with traditional media, such as national and regional newspapers, outdoors, building lobby or elevator LCD displays. In addition, we have established a large number of communities where we interact with customers directly through the provision of content and services.

*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, such as TAL 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; and

scope and quality of program, service and product offerings.

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.

## **Table of Contents**

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.

## **Seasonality**

We have experienced, and expect to continue to experience, seasonal fluctuations in our 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. We expect quarterly fluctuations in our revenues and results of operations to continue.

## **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, as most recently amended in November 2016, and the Implementation Rules for the Law for Promoting Private Education, 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***

The National People's Congress enacted the Education Law of the PRC, or the Education Law, most recent amendment effective on June 1, 2016. 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.

On December 27, 2015, the National People's Congress amended the Education Law of the PRC, which became effective on June 1, 2016. The amended Education Law of the PRC, among other things, abolished the provision that prohibits any organization or individual from establishing or operating a school or any other education institution for profit-making purposes. Nevertheless, schools and other education institutions sponsored wholly or partially by government financial funds and donated assets remain prohibited from being established as for-profit organizations



## **Table of Contents**

### *The Law for Promoting Private Education and the Implementation Rules for the Law for Promoting Private Education*

Under the Law for Promoting Private Education and the Implementation Rules for the Law for Promoting Private Education, 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.

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, under the above regulations, 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.

Before September 1, 2017, the date the Amended Private Education Law became effective, private education is treated as a public welfare undertaking in all aspects under the Law for Promoting Private Education and its Implementation Rules. 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 were 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.

The election to establish a private school requiring reasonable returns was required to 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 was required to 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 was required to 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 was also required to 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 provided a formula or guidelines for determining reasonable returns. In addition, none of the current PRC laws and regulations set 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.

Every private school was required to allocate a certain amount to its development fund for the construction or maintenance of school facilities or procurement or upgrade of educational equipment. In the case of a private school that required 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 did 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.

## **Table of Contents**

On November 7, 2016, the Standing Committee of the National People's Congress promulgated the Amended Private Education Law, which became effective on September 1, 2017.

Under the Amended Private Education Law, the term "reasonable return" is no longer used, and sponsors of private school may choose to establish non-profit or for-profit private schools at their own discretion. Nevertheless, school sponsors are not allowed to establish for-profit private schools that are engaged in mandatory education according to the Amended Private Education Law. Therefore, schools engaged in mandatory education must retain their non-profit status after the effectiveness of the Amended Private Education Law.

The Amended Private Education Law further establishes a new classification system for private schools on whether they are established and operated for profit-making purposes. Key features of this system include the following:

sponsors of for-profit private schools are entitled to retain the profits and proceeds from the schools and the operation surplus may be allocated to the sponsors pursuant to the PRC Company Law and other relevant laws and regulations, whereas sponsors of non-profit private schools are not entitled to the distribution of profits or proceed from the non-profit schools and all operation surplus of non-profit schools shall be used for the operation of the schools;

for-profit private schools are entitled to set their own tuition and other miscellaneous fees without seeking prior approval from or reporting to the relevant government authorities, whereas the collection of fees by non-profit private schools shall be regulated by the provincial, autonomous regional or municipal governments;

private schools (for-profit and non-profit alike) may enjoy preferential tax treatments; non-profit private schools will be entitled to the same tax benefits as public schools whereas taxation policies for for-profit private schools are still unclear as more specific provisions are yet to be introduced;

for construction or expansion of the school, non-profit schools may acquire the required land use rights in the form of allocation by the government as a preferential treatment, whereas for-profit private schools shall acquire the required land use rights by purchasing them from the government;

the remaining assets of non-profit private schools after liquidation shall continue to be used for the operation of non-profit schools, whereas the remaining assets of for-profit private schools shall be distributed to the sponsors in accordance with the PRC Company Law; and

governments at or above the prefecture level may support private schools (for-private and non-private alike) by subscribing to their services, providing student loans and scholarships, and leasing or transferring unused state assets to the schools, and the governments may further support non-profit private schools in the form of government subsidies, bonus funds and incentives for donation.

On December 29, 2016, the State Council issued the Several Opinions of the State Council on Encouraging the Operation of Education by Social Forces and Promoting the Healthy Development of Private Education, which require

to ease the access to the operation of private schools and encourage social forces to enter into the education industry. The opinions also provide that each level of the government shall increase their support to the private schools in terms of financial investment, financial support, autonomy policies, preferential tax treatments, land policies, fee policies, autonomy operation, protection of the rights of teachers and students etc. Further, the opinions require each level of the government to improve local policies on government support to for-profit and non-profit private schools by such means as preferential tax treatments.

## **Table of Contents**

On December 30, 2016, the MOE, Ministry of Civil Affairs, the SAIC, the Ministry of Human Resources and Social Welfare and the State Commission Office of Public Sectors Reform jointly issued the Implementation Rules on the Classification Registration of Private Schools to reflect the new classification system for private schools as set out in the Amended Private Education Law. Generally, if a private school established before promulgation of the Amended Private Education Law chooses to register as a non-profit school, it shall amend its articles of association, continue its operation and complete the new registration process. If such private school chooses to register as a for-profit school, it shall conduct financial liquidation process, have the property rights of its assets such as lands, school buildings and net balance being authenticated by relevant government authorities, pay up relevant taxes, apply for a new Permit for Operating a Private School, re-register as for-profit schools and continue its operation. Specific provisions regarding the above registration process are yet to be introduced by governments at the provincial level.

On December 30, 2016, the MOE, the SAIC and the Ministry of Human Resources and Social Welfare jointly issued the Implementation Rules on the Supervision and Administration of For-profit Private Schools, pursuant to which the establishment, division, merger and other material changes of a for-profit private school shall first be approved by the education authorities or the authorities in charge of labor and social welfare, and then be registered with the competent branch of the SAIC.

On September 1, 2017, SAIC and MOE jointly issued the Notice of Relevant Work on the Registration and Management of the Name of For-Profit Private Schools, which specifies the requirements on the names of for-profit private schools.

Besides the Amended Private Education Law and the above regulations, other details of the requirements on the operation of non-profit schools and for-profit schools will be provided in implementation regulations that are yet to be introduced, such as

an amendment to the Implementation Rules for the Law for Promoting Private Education;

local regulations relating to legal person registration of for-profit and non-profit private schools; and

specific measures to be formulated and promulgated by the competent authorities responsible for the administration of private schools in the province(s) in which our schools are located, including specific measures for registration of pre-existing private schools and the collection of non-profit private schools fees, specific requirements for authenticating various parties' property rights of for-profit private schools, taxation policies for for-profit private schools.

As of the date of this annual report, certain local governments, for example, Shanghai, Jiangsu province, Hebei province, Shaanxi province and Hainan Province, have promulgated their local regulations relating to legal person registration and administration for private schools and certain local governments, for example, Shanghai, Jiangsu, Hubei, Hebei, Zhejiang, Yunnan, Gansu, Anhui and Liaoning, have promulgated general guidance to encourage the development of private schools. Among these local regulations and guidance, some local governments, such as Shanghai, Hubei, Hebei, Anhui, Yunnan and Zhejiang require the existing private schools to register either as for-profit or non-profit schools within a specific time period. 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, 2018, New Oriental China was the sponsor of 87 schools.

Before September 1, 2017, the date the Amended Private Education Law became effective, 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.

As of September 1, 2017, we were 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. As of September 1, 2017, there was 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 were 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 were also local regulations that are less clear in this regard.

## **Table of Contents**

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. Neither we nor our PRC counsel is aware of any case in China where a private school which has been solely funded by private sponsors without any government or donated funds 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 unless required by the laws and regulations. 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.

Upon the effectiveness of the Amended Private Education Law in September 2017, sponsors of for-profit private schools are entitled to retain the profits and proceeds from the schools and the operation surplus may be allocated to the sponsors pursuant to the PRC Company Law and other relevant laws and regulations, whereas sponsors of non-profit private schools are not entitled to the distribution of profits or proceed from the non-profit schools and all operation surplus of non-profit schools shall be used for the operation of the schools. The remaining assets of non-profit private schools after liquidation shall continue to be used for the operation of non-profit schools, whereas the remaining assets of for-profit private schools shall be distributed to the sponsors in accordance with the PRC Company Law.

### ***Regulations on After-School Tutoring***

The State Council issued an Opinion on Supervising After-School Tutoring Institutions on August 22, 2018, which provided various guidance on regulating after-school tutoring institutions that target primary and secondary school students (the State Council Circular 80 ). The State Council Circular 80 provides for the standardization of approval and registration of after-school tutoring institutions, and requires relevant governmental authorities to conduct special administration strengthening regulations on after-school tutoring institutions. The State Council Circular 80 specifies operating requirements that after-school tutoring institutions must meet. Such requirements include, among other things, that (i) the average available-for-use area per student within the same training hours shall be no less than three square meters, (ii) private school shall purchase safety insurance for training participants, and (iii) no in-service school teachers shall be hired by after-school tutoring institutions and all the teachers for Chinese, math, English, physics, chemistry and biology courses in after-school tutoring institutions shall obtain relevant teaching qualifications.

With respect to the examination and approval of after-school tutoring institutions, the State Council Circular 80 requires that no tutoring activities shall be conducted under the names of home schooling, consultation, culture transmission, etc., and that the operating permit for running a school must be obtained and the registration of business license or other lawful license shall be completed in compliance with the setting standard, failure of which shall cause suspension of licenses or termination of school operations unless rectification is timely made. The State Council Circular 80 further requires that setting up branches or learning centers by any after-school tutoring institutions within the same county shall be subject to approval by the local administrative departments for education of the same county, while setting-up cross-county branches or learning centers shall be subject to approval by the local administration of education where the branches are located.

In addition, the State Council Circular 80 provides detailed guidance on tutoring activities, which include, among other things, (i) the contents, classes, enrollment targets, progress, and school hours of courses like Chinese, mathematics, English, physics, chemistry, and biology shall be filed with the local administration of education and be made public; (ii) the training courses offered to the primary and secondary school students shall not be more advanced

than the syllabus and curricula applicable to them; (iii) no tutoring courses shall be given after 8:30 p.m., and no homework from after-school institutions shall be allowed; (iv) no grade examination, competition or ranking in connection with the subjects of primary schools or middle schools shall be organized, and no class shall be arranged in conflict with the time of regular schools, and (v) no advance tuition fees of more than three months may be collected, and the tutoring institutions shall set up a special account for the tuition and incidental fees and strictly control the minimum balance of the account and the flow of large-value funds. Furthermore, no fees or mandatory fundraising may be imposed.



## **Table of Contents**

The State Council Circular 80 strengthens the supervision and management of routine operations of after-school tutoring institutions requiring, among others, that the administrations of education shall (i) lead organization in comprehensive legal implementation over the after-school tutoring market, inspect and implement jointly with the administrations in human resources and social security, civil affairs, public security, emergency management, health and food supervision, (ii) implement the annual inspection and annual reporting policy including requiring the periodical reports, interim reports of significantly adverse impacts upon the corporate operations, and (iii) carry out the black-name list and white-name list policy to timely publicize at the official websites of the governments regarding any institution who fails in meeting legal requirements.

The State Council Circular 80 emphasizes the improvement of educating capabilities of primary schools and secondary schools. It puts an end to the phenomena of no teaching in class but teaching in after-school tutoring institutions after class, sets up a flexible school-leaving policy and encourages schools to help students to cultivate interests and broaden visions, to explore the potentials of school teachers and pro-actively utilize after-school resources, to give the choices of accepting after-school services to the students and parents.

In connection to the online education service providers, the State Council Circular 80 provides that the administrative departments of networking, culture, industry and information technology, radio and television shall cooperate with the education department to supervise online education within their respective responsibilities.

### ***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 accordance with the Education Law of the PRC, the Occupational Education Law and the Law for Promoting Private Education, and the Implementation Rules for the Regulations on Operating Chinese-Foreign Schools. The Regulations on Operating Chinese-foreign Schools and its implementation 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.

### ***Foreign Investment Access Special Management Measures (Negative List) (2018 Version)***

According to applicable PRC regulations on foreign-invested enterprises, capital contributions from a foreign holding company to its PRC subsidiaries, which are considered foreign-invested enterprises, may only be made when approved by or filed with the Ministry of Commerce or its local branch. In approving such capital contributions, the Ministry of Commerce or its local branch examines the business scope of each foreign invested enterprise under review to ensure it complies with the Foreign Investment Industrial Guidance Catalog (2017) issued in June, 2017, or Catalog 2017, for the catalogs of encourage and Foreign Investment Access Special Management Measures (Negative List) (2018 Version), or the Negative List, for the catalogs of restricted and prohibited. Industries not listed in the Negative List and Catalog 2017 are generally open to foreign investment unless specifically restricted by other PRC regulations. The Negative List was issued on June 28, 2018 and became effective on July 28, 2018.



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**Table of Contents**

Under such Negative List, pre-school education, senior high school education in grades 10 to 12, and higher education are in a restricted industry, meaning foreign educational organizations with relevant qualifications and experience and Chinese educational organizations are only allow to operate pre-school education, senior high schools and higher education in cooperative ways by the form of a cooperative joint venture in the PRC. Foreign investment is banned from compulsory education, which means grades 1 to 9. Foreign investment is allowed in after-school tutoring services and training services which do not grant certificates or diplomas and non-academic vocational training institutions.

*The Draft PRC Foreign Investment Law*

In January 2015, the Ministry of Commerce published a discussion draft of the proposed Foreign Investment Law aiming to, upon its enactment, replace the trio of existing laws regulating foreign investment in China, namely, the Sino-foreign Equity Joint Venture Enterprise Law, the Sino-foreign Cooperative Joint Venture Enterprise Law and the Wholly Foreign-invested Enterprise Law, together with their implementation rules and ancillary regulations.

Among other things, the draft Foreign Investment Law expands the definition of foreign investment and introduces the standard of actual control in determining whether a company is considered a foreign-invested enterprise, or an FIE. The draft Foreign Investment Law specifically provides that entities established in China but controlled by foreign investors must be deemed as FIEs, whereas an entity set up in a foreign jurisdiction would nonetheless be, upon market entry clearance by the Ministry of Commerce, treated as a PRC domestic investor provided that the entity is controlled by PRC entities and/or citizens. In this connection, control is broadly defined in the draft law to cover the following summarized categories: (i) holding 50% or more of the voting rights or similar equity interest of the subject entity; (ii) holding less than 50% of the voting rights or similar equity interest of the subject entity but having the power to secure at least 50% of the seats on the board or other equivalent decision making bodies, or having the voting power to exert material influence on the board, the shareholders meeting or other equivalent decision making bodies; or (iii) having the power to exert decisive influence, via contractual or trust arrangements, over the subject entity's operations, financial matters or other key aspects of business operations. Once an entity is determined to be an FIE, and its investment amount exceeds certain thresholds or its business operation falls within a negative list, to be separately issued by the State Council in the future and to replace the Foreign-Investment Industrial Guidance Catalog, market entry clearance by the Ministry of Commerce or its local counterparts will be required. Otherwise, all foreign investors may make investments on the same terms as domestic investors without being subject to additional approval from the government authorities as mandated by the existing foreign investment legal regime.

Under the draft Foreign Investment Law, variable interest entities that are controlled via contractual arrangement would also be deemed as FIEs, if they are ultimately controlled by foreign investors. Therefore, for any companies with a VIE structure in an industry category that is on the negative list, the VIE structure may be deemed legitimate only if the ultimate controlling person(s) is/are of PRC nationality (either PRC state-owned enterprises or agencies or PRC citizens). Conversely, if the actual controlling person(s) is/are of foreign nationalities, then the variable interest entities will be treated as FIEs and any operation in the industry category on the negative list without market entry clearance may be considered as illegal. However, the draft Foreign Investment Law has not taken a position on what actions shall be taken with respect to the existing companies with a VIE structure, whether or not these companies are controlled by PRC parties, while it has solicited comments from the public on this point.

The draft Foreign Investment Law also imposes stringent ad hoc and periodic information reporting requirements on foreign investors and the applicable FIEs. Aside from investment implementation report and investment amendment report that are required at each investment and alteration of investment specifics, an annual report is mandatory, and large foreign investors meeting certain criteria are required to report on a quarterly basis. Some of the information requested may be sensitive to foreign investors, such as the identity of the actual controller and the source of

investment. Any company found to be non-compliant with these information reporting obligations may potentially be subject to fines and/or administrative or criminal liabilities, and the persons directly responsible may be subject to criminal liabilities.

***Regulations on Online and Distance Education***

Pursuant to the Administrative Regulations on Educational Websites and Online and Distance Education Schools issued by the MOE, 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 within the issuance of various certificates.

## **Table of Contents**

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

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, pursuant to which the administrative license for online education schools was retained, while the administrative license for educational websites was not retained. On January 28, 2014, the State Council promulgated the Decision on Abolishing and Delegating Certain Administration Examination and Approval Items, pursuant to which the administrative approval for online education schools of higher education was abolished.

Notwithstanding these decisions formulated by the State Council, as the Administrative Regulations on Educational Websites and Online Education Schools were not explicitly abolished, in practice, certain local authorities continue to implement the approval requirement for setting up education websites and online education schools until February 3, 2016, when the State Council promulgated the Decision on Cancelling the Second Batch of 152 Items Subject to Administrative Examination and Approval by Local Governments Designated by the Central Government, explicitly withdrew the approval requirements for operating educational websites and online education schools as provided by the Administrative Regulations on Educational Websites and Online Education Schools, and reiterated the principle that administrative approval requirements may only be imposed in accordance with the PRC Administrative Licensing Law.

In December 2017, Shanghai Municipal Government promulgated the Management Methods of Classified Registration of Private Schools, the Setting Standards for Private Training Institutions of Shanghai, the Management Measures for the For-profit Private Training Institutions of Shanghai, and the Management Methods for the Non-Profit Private Training Institutions of Shanghai, or the Shanghai Implementation Regulations, collectively. Pursuant to the Shanghai Implementation Regulations, any management measures and regulations applied to institutions that provide training services only through the Internet will be further promulgated separately. These management measures and regulations have not yet been introduced as of the date hereof.

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

The State Council promulgated the Administrative Regulations on Publication, or the Publication Regulations, which was most recently amended on February 6, 2016. 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. According to the Publication Regulations, any entity engaging in the activities of publishing, printing, copying, importation or distribution of publications, shall obtain relevant permits of publishing, printing, copying, importation or distribution of publications. In addition, according to the effective Negative List, foreign investors are prohibited from engaging in the publishing business. Therefore, 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, to comply with the Publication Regulations.

According to the prior Measures for the Administration of Internal Informative Publications, entities engaging in printing internal informative publications may obtain an internal informative publications printing permit instead of the permit of publishing. Such internal informative publications are defined as publications used for internal

information communication and work guidance purpose and are not for sale. In April 2015, the current Measures for the Administration of Internal Informative Publications took effect and abolished the prior measures. Under the new regulation, the internal informative publications printing permit is not available for printing and publishing of textbooks and teaching materials for primary and secondary school students. In addition, the new regulation prohibits entities which have obtained the internal permit from offering the internal informative publications to its client or to the public. New Oriental China and its schools and subsidiaries engage in printing and providing teaching handouts and other materials to our students. Under the new regulation, it is uncertain whether printing and providing teaching handouts and other materials to our students would be deemed publishing activities. If the GAPP or its local branches or other competent authorities deem such activities as publishing, we may become subject to significant penalties, fines, legal sanctions or an order suspending our printing and providing of teaching handouts and other materials to our students.

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**Table of Contents**

GAPP issued new Administrative Regulations on Publications Market, effective on June 1, 2016, abolished the old regulation. According to the new regulation, any organization or individual engaged in 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 wholesaling of publications shall obtain such permit from the provincial counterpart of GAPP; and an entity engaged in retail distribution of publications shall obtain such permit from the local counterpart of GAPP at the county level. According to the new regulation, foreign-invested enterprises are allowed to engage in the business of distribution of publications. Foreign investors who intends to establish an enterprise engaging in the business of distribution of publications and foreign-invested enterprise which intends to engage in the business of distribution of publications shall firstly obtain the approval from local branch of the Ministry of Commerce. If and upon approval, the Ministry of Commerce will issue the Approval Certificate for Foreign-Invested Enterprises, on which the business scope of distribution of publications is specified along with the word subject to the permission in this industry. Afterwards, the foreign-invested enterprise shall file with its business scope of distribution of publications local office of the SAIC and shall obtain the Permit for Operating Publications Business from relevant offices of the GAPP before engaging in the business of distribution of publications.

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 was required to secure a Business Certificate for Audio-Video Products from the relevant culture authorities. The Administrative Regulations on Publishing Audio-Video Products was later amended in 2011, 2013 and was most recently amended on January 2, 2016, pursuant to which the Business Certificate for Audio-Video Products was replaced by the Permit for Operating Publications Business and entities or individuals engaging in distribution of audio-video products shall only need to hold a Permit for Operating Publications Business, while a Business Certificate for 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 Business. 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 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 studies, the Education Commission of Beijing and Beijing Administration for Industry and Commerce jointly issued the Beijing Measures of Supervisions and Recognition of Intermediate Services for Self-Funded Overseas Studies (Trial) in September 2015, which require that any intermediate service organization engaged in such services in Beijing shall satisfy certain requirements set up therein, including having employees with experience in educational services, having established stable and cooperative relations with an overseas educational institution, and having sufficient funds to protect the rights and interests of customers. The intermediate service organizations which satisfy such requirements may apply

with the Education Commission of for the Recognition on the Intermediate Service Organization for Self-funded Overseas Studies. Organizations or individuals without such Recognition from the Education Commission of Beijing are not allowed to engage in any intermediate and consulting business activities relating to self-funded overseas studies.



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**Table of Contents**

On January 12, 2017, the State Council promulgated the Decision of the State Council on the Third Installment of the Cancellation of the Administrative Licensing Matters Delegated to Local Governments, which, among other things, cancelled the Recognition on the Intermediate Service Organization for Self-funded Overseas Studies, which means that the requirement for intermediate service organizations to obtain Recognition on the Intermediate Service Organization for Self-funded Overseas Studies from the provincial government for their engaging in intermediate and consulting business activities relating to self-funded overseas studies is cancelled. This Decision provided that after the cancellation of such requirements, the MOE and the SAIC shall study and develop contract template for reference and strengthen their guidance, regulating and service to intermediate service organizations and that the relevant industrial association shall play their role in self-discipline.

***Guidelines for Overseas Study Tour participated by Primary and Middle School Students (Trial)***

The MOE promulgated the Guidelines for Overseas Study Tour participated by Primary and Middle School Students (Trial) (the Guidelines) in July 2014. Under the Guidelines, overseas study tours participated in by primary and middle school students (the Overseas Study Tour) means, by adapting to the characteristics of primary and middle school students and the educational needs, programs that organize primary and middle school students to go overseas to learn foreign languages and other short-term curriculum, perform art shows, compete in contests, visit schools, attend summer/winter school programs, or take part in other activities that help students expand their horizon and promote enrichment and enhancement, in the manner of group travel and group accommodation during the academic semesters or vacations. Overseas Study Tours attended by primary and middle school students shall follow the principles of safety, civility and efficiency. The schedule for study, from the perspective of both the content and the duration, shall be no less than 1/2 of the total schedule. The organizer shall choose legitimate and qualified cooperation institutions, and stress the importance of safe education, and shall appoint a guiding teacher for each group. The organizer shall apply the rules of cost accounting, notify the students and their supervisors of the composition of the fees and expenses, and enter into an agreement as required by law. The school and its staff shall not seek any economic benefit from organizing its own students to attend an Overseas Study Tour.

***Regulations on Tourism***

Tourism Law of the PRC, which was promulgated by the Standing Committee of the NPC and most recently amended on November 11, 2016, provides that, among other things, to engage in the businesses of outbound tourism, a travel agency shall obtain corresponding business permit, and the specific conditions shall be provided for by the State Council and that when organizing an outbound touring group, or organizing or receiving an inbound touring group, a travel agency shall, in accordance with the relevant provisions, arrange for a tour leader or tour guide to accompany the touring group in the whole tour. Regulations on Travel Agencies promulgated by the State Council, revised on February 6, 2016, and the implementation rules of Regulations on Travel Agencies, provide that, among other things, travel agent shall mean any entity that engages in the business of attracting, organizing, and receiving tourists, providing tourism services for tourists and operating domestic, outbound or border tourism; the aforementioned business shall include but not limit to arranging for transport services, arranging for accommodation services, providing services for tour guides or team leaders, providing services of tourism consultation and tourism activities design. According to the Regulations on Travel Agencies and its implementation rules, any tourism agent engages in the outbound tourism shall apply for a permit to engage in the outbound tourism from the administrative department of tourism under the State Council, the governments of provinces, autonomous regions, or municipalities.

The touring group for the Overseas Study Tour shall be organized by a qualified travel agent. Beijing New Oriental Walkite International Travel Co., Ltd, a subsidiary of the Company engaging the businesses of outbound tourism has obtained the aforementioned permit.



## **Table of Contents**

### ***Regulations on Value-added Telecommunications Services***

Under the PRC Telecommunications Regulations, promulgated by the State Council and most recently amended in February 2016, a telecommunication services provider in China must obtain an operating license from the MIIT, or its provincial authorities. The PRC Telecommunications Regulations categorize all telecommunication services in China as either basic telecommunications business or value-added telecommunications business. Internet information services and the business of online data transaction processing are two of the subsectors of the value-added telecommunications business.

As a subsector of the value-added telecommunications business, business of online data transaction processing refers to the business to provide online data processing and transaction processing services through public communication network or Internet for users through various data/transaction application platform connected to the public communication network or Internet, including transaction processing services, electronic data exchange services and network or electronic equipment data processing services. Under the PRC Telecommunications Regulations, any entity engages in the business of transaction processing services as an online marketplace platform is required to obtain a license from the MIIT or its provincial authorities in providing transaction processing services.

As a subsector of the value-added telecommunications business, Internet information services are also regulated by the Administrative Measures on Internet Information Services promulgated by the State Council, or the Internet Information 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. Beijing Xuncheng has obtained the ICP license.

The Notice on Strengthening Management of Foreign Investment in Operating Value-Added Telecom Services issued by the MIIT 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.

### ***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 and February 17, 2011. 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.

According to an answer published on the official website of the local counterpart of MOC in Beijing on August 2, 2017, educational products are not deemed as "internet cultural products" defined under the Internet Culture Provisions. Currently, Beijing Xuncheng and its subsidiaries are all located in Beijing and are therefore not required to obtain the Internet Culture Operation License.

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

The Rules for Administration of Broadcasting of Audio-Video Programs through the Internet and Other Information Networks, or the Broadcasting Rules, promulgated by the State Administration of Radio, Film and Television, or SARFT, 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. 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.

## **Table of Contents**

The SARFT and MIIT issued the Internet Audio-Video Program Measures, revised in August 2015. 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. The SARFT promulgated the Notice on Several Issues regarding the license for disseminating audio-video programs through information network in 2009. 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.

On April 25, 2016, the SAPPRFT promulgated the Private Network and Directional Broadcasting Audio-Video Programs Regulations, which came into effect on June 1, 2016 and replaced the Broadcasting Rules. The Broadcasting Audio-Video Programs Regulations provides, among other things, that a Permit for Broadcasting Audio-Video Programs via Information Network is required for engaging in broadcasting services through private network and directional communication. According to such Regulations, the Broadcasting Services through Private Network and Directional Communication shall mean the services and activities provided to the public through the private transmission channels that include internet, LAN and VPN based on Internet and through the receiving terminals of televisions, and other handheld electronic equipment, and such services and activities include the activities of content supply, integrated broadcast control, transmission and distribution with IPTVs, private-network mobile televisions, internet televisions. According to such Regulations, only the entities wholly or substantially owned by the State could apply for such Permit.

According to the confirmation from the local counterpart of SAFT in Beijing, provision of online educational courses do not fall within the definition of online audio-visual program services under the Audio-Visual Program Provisions and as a result, the License for Online Transmission of Audio-Visual Programs is not required for the operation of Beijing Xuncheng and its subsidiaries.

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

The Regulations on Protection of the Right of Dissemination through Information Networks, promulgated by the State Council, require 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, trademarks and domain names. 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 2001.

*Copyright.* The National People's Congress amended the Copyright Law 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.

## **Table of Contents**

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.

*Trademark.* The PRC Trademark Law, most recently revised in May 2014, 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. In July 2014, the State Administration for Industry and Commerce released Provisions on the Recognition and Protection of Well-Known Trademarks. According to these provisions, well-known trademarks shall be recognized on a case-by-case basis, and be subject to the principle of passive protection. 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 and an adjudication on disputed registered trademark issued by trademark appraisal committee.

*Domain names.* Pursuant to the Measures for the Administration of Internet Domain Names, which was promulgated by the Ministry of Industry and Information Technology of the PRC on August 24, 2017 with effect from November 1, 2017, domain name shall refer to the character mark of hierarchical structure, which identifies and locates a computer on the internet and corresponds to the Internet protocol (IP) address of that computer and the principle of first come, first serve is followed for the domain name registration service. Domain name applicants shall provide true, accurate and complete identification of the domain name holder as requested by the domain name registration service provider.

## ***Foreign Currency Exchange***

Pursuant to applicable PRC regulations on foreign currency exchange, 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 or prior registration with banks for conversion of RMB into a foreign currency.

Domestic companies or individuals can repatriate payments received from abroad in foreign currencies or deposit those payments abroad. Foreign-invested enterprises may retain foreign exchange in accounts with designated foreign exchange banks. Foreign exchange on the current account and capital account can be either retained or sold to financial institutions that have foreign exchange settlement or sales business based on the need of the enterprise without prior approval from SAFE, subject to certain restrictions.

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, 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 local branch of 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.

SAFE promulgated the Notice on Reforming the Management Method relating to Conversion of the Capital Contribution of Foreign Invested Company from Foreign Exchange to Renminbi, or SAFE Circular 19, effective in June 2015 to abolish SAFE Circular 142, but the foregoing rules have been retained in SAFE Circular 19. SAFE promulgated the Notice on Further Simplifying and Improving the Policies of Foreign Exchange Administration Applicable to Direct Investment, or SAFE Circular 13, effective in June 2015, pursuant to which annual foreign exchange inspection of direct investment is not required anymore and the registration of existing equity is required. SAFE Circular 13 also grants the authority to banks to directly examine and process foreign exchange registration with respect to both domestic and overseas direct investment. SAFE issued Notice on reform and regulations of the Administration Policy of Foreign Exchange under Capital Account, or SAFE Circular 16, effective June 9, 2016. Pursuant to SAFE Circular 16, enterprises registered in China may also convert their foreign debts from foreign currency to Renminbi on a self-discretionary basis. SAFE Circular 16 provides an integrated standard for conversion of foreign exchange under capital account items (including but not limited to foreign currency capital and foreign debts) on a self-discretionary basis which applies to all enterprises registered in China. SAFE Circular 16 reiterates the principle that Renminbi converted from foreign currency-denominated capital of a company may not be directly or indirectly used for purposes beyond its business scope or prohibited by PRC laws or regulations, while such converted Renminbi shall not be provided as loans to its non-affiliated entities. As SAFE Circular 16 is newly issued and SAFE has not provided detailed guidelines with respect to its interpretation or implementations, it is uncertain how these rules will be interpreted and implemented.



## **Table of Contents**

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

Pursuant to the Notice of the State Administration of Foreign Exchange on the Administration of Foreign Exchange Involved in Overseas Investment, Financing and Round-Trip Investment Conducted by Domestic Residents through Special-Purpose Companies, or SAFE Circular 37, effective in July 2014 and repealed the previous 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 75 on the same date, a PRC Resident, including both PRC domestic institutions and PRC domestic individual residents, shall register with the local branch of SAFE before it establishes or controls a company outside of China with the domestic or overseas assets or equity they legally hold for the purpose of investment and financing and conducting roundtrip investment in China. Such a company located outside of China is referred to as an offshore special purpose vehicle.

Under SAFE Circular 37, 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.

In June 2015, SAFE promulgated SAFE Circular 13, according to which, in order to simplify the procedures of performing the foreign exchange control policy of direct investment, the registration authorities under the SAFE foreign exchange control policies, including the registration of PRC residents under SAFE Circular 37 change from local SAFE branches to local banks authorized by SAFE and SAFE will strengthen the training and supervision for banks in performing the foreign exchange control policy of direct investment. Thus, according to SAFE Circular 13, the registration of PRC residents under SAFE Circular 37 shall be conducted with local banks authorized by SAFE.

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 in 2006.

### ***Regulations on 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.



## **Table of Contents**

### ***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.

### ***Regulations on Labor***

Pursuant to the PRC Labor Law, the PRC Labor Contract Law and its Implementing Regulations of the Employment Contracts Law, labor contracts in written form shall be executed to establish labor relationships between employers and employees. Wages cannot be lower than local minimum wage. The employer must establish a system for labor safety and sanitation, strictly abide by state standards, and provide relevant education to its employees. Employees are also required to work in safe and sanitary conditions meeting State rules and standards, and carry out regular health examinations of employees engaged in hazardous occupations.

In the respect of the employment of foreigner in PRC, Provision on the Employment of Foreigners in China provides that, among other things, to employ a foreigner who does not have Chinese nationality, an employer shall apply for an employment license for such foreigner, and may only employ him or her after such foreigner obtains a Foreigners Employment License of the People's Republic of China, or Employment License; prior to obtaining employment in China, a foreigner shall enter China with an employment visa (or in accordance with an agreement on mutual exemption of visas if there is such an agreement); and after entering China, such foreigner shall obtain an Employment Permit for Foreigners, or Employment Permit, and a residence permit for foreigners, save that the foreigners holding the Foreign Expert Permit issued by the State Administration of Foreign Experts Affairs are not required to hold Employment Licenses and Employment Permit. Provision on the Employment of Foreigners in China also provides that the Employment License is valid only in the area defined by the authority which issued such license; the actual employer of a foreigner shall be consistent with the employer recorded on the Employment License; if the actual employer changed but the foreigner is employed in a similar job by another employer within the same area defined by the authority which issued such license, the foreigner shall file with such authority to change information on the Employment License.

The Notice of Issues Related to the Management of Employment of Foreigners in China provides that, among other things, the Ministry of Labor and Social Security should cooperate with Ministry of Public Security to carry out regular and irregular investigation on the entities that employ relatively large number of foreigners about their employment of foreigners.

In the respect of hiring foreigners as teachers in schools, State Administration of Foreign Experts Affairs, promulgated a Notice of Issuing Regulations for Foreign Experts to Apply Permit to Work in China and Other Regulations, or SAFEA Circular 139. SAFEA Circular 139 provides that foreign experts shall obtain Foreign Expert Permit. Any foreign expert that apply the Foreign Expert Permit shall obey the laws and regulations of PRC, shall be healthy, shall have no criminal record, and shall meet one of the following requirement: (i) such foreign expert is employed to work in China in order to perform agreements between governments or international organizations, or to perform economic or trade agreements between Chinese party(s) and foreign party(s) as a professional person with foreign nationality who has technology or management skills; (ii) such foreign expert is employed to perform the work in the fields of education, scientific research, press, publication, culture, arts, health, or sport as a professional person with foreign nationality; (iii) such foreign expert is employed to perform a position higher than vice president of a domestic

enterprise or equivalent position as a professional person with foreign nationality who has technology or management skills; (iv) such foreign expert is a representative with foreign nationality, who is a PRC representative officer of a experts association or recruitment agent approved by State Administration of Foreign Experts Affairs; or (v) such foreign expert is employed to perform the work in the fields of economy, technology, engineering, trade, finance, accounting, tax, tourism who possesses specialty as a professional person with foreign nationality in urgent need with technology or management skills. According to SAFEA Circular 139, to apply a Foreign Expert Permit as a foreign expert to perform the work in the field of education, the applicant shall submit the application together with a copy of the employer's Certificate of Employing Foreign Experts and the agreement entered by such applicant and its employer to the provincial Administration of Foreign Experts Affairs where the employer located, provided that if the employer is the ministry, commission directly under the State Council, the authority directly under the State Council, the public institution or the professional corporation, the applicant shall submit the application to the State Administration of Foreign Experts Affairs. SAFEA Circular 139 also provides that entity shall obtain Certificate of Employing Foreign Experts to employ foreign experts and the application of Certificate of Employing Foreign Experts shall submit to the provincial Administration of Foreign Experts Affairs where the employer located, provided that the non-educational public institution located in Beijing that is directly under the ministry, commission of the State Council, the authority directly under the state council, the application shall submit to the State Administration of Foreign Experts Affairs. According to SAFEA Circular 139, the Administration of Foreign Experts Affairs will carry out annual inspection on the entity that has obtained Certificate of Employing Foreign Experts in January of each year.

## **Table of Contents**

In addition, State Administration of Foreign Experts Affairs promulgated an Opinion on Further Regulating the Employment of Foreign Experts in Education and Culture, which provides that, among other things, any entity that dispatches and introduce foreign experts in education and culture to work in China shall obtain Certificate of Employing Foreign Experts; the entity that dispatches the foreign experts, the dispatched foreign expert and the entity that employs the dispatched expert shall enter into an agreement to confirm each party's obligations and rights related to the employment of such foreign expert, and the entity that dispatches the foreign expert and the entity that employs the foreigner expert shall have the joint liability in the management of such foreign expert. Such Opinion on Further Regulating the Employment of Foreign Experts in Education and Culture also provides that any entity that engages in dispatching foreign expert in education and culture with Certificate of Employing Foreign Experts shall not introduce foreign experts working in the entity that without Certificate of Employing Foreign Experts, the provincial and regional Administration of Foreign Experts Affairs shall cooperate with the public security authorities and their exit-entry administration divisions to investigate and handle the illegal employment of foreign experts under applicable laws.

On February 19, 2016, the State Council promulgated the Decision of the State Council on the Second Installment of the Cancellation of the Administrative Licensing Matters Delegated to Local Governments, which among other things, cancelled Certificate of Employing Foreign Experts, which means that the requirements for the entity to obtain Certificate of Employing Foreign Experts for employing foreign experts from the provincial Administration of Foreign Experts Affairs is cancelled. According to a Q&A in relation to the cancellation of the requirement to obtain Certificate of Employing Foreign Experts in employing foreign experts publicized by the Education, Culture, Health Experts Department of State Administration of Foreign Experts Affairs on March 31, 2016, the provincial education authorities shall pay close attention to the study the necessity of setting up the requirements for qualification in employing foreign experts in their area, and set up the requirements through the development of local laws and temporary regulations if necessary. As of the date of this annual report, we are not aware of any local laws and temporary regulations was set up regarding the requirements to obtaining Certificate of Employing Foreign Experts for employing foreign experts.

According to the Circular on the Comprehensive Implementation of the Permit System for Foreigners to Work in China promulgated by the State Administration of Foreign Experts Affairs, the Ministry of Human Resources and Social Welfare, the Ministry of Foreign Affairs, and the Ministry of Public Security on March 28, 2017, from April 1, 2017, a foreigner who is approved to work in China will be issued a Permit to Working in China, which supersedes the Employment License or Foreign Expert Permit. The Employment License or Foreign Expert Permit issued before April 1, 2017 remain valid subject to its expiration date. According to the circular, the process of application and approval of the Permit to Working in China will be further simplified and standardized, with new and detailed regulation of the application and approval process of Permit to Working in China to be promulgated shortly. As of the date of this annual report, we are not aware of any new and detailed regulation set up regarding application and approval of the Permit to Working in China.

If the employment of foreigners is not in compliance with the above relevant regulations, the employer may become subject to penalties, fines or an order to terminate such employment and to bear all the expenses and costs arising from the repatriation of such foreigner.

## **Table of Contents**

### ***Regulations on Employee Share Incentive Awards Granted by Listed Companies***

According to a series of notices concerning individual income tax on earnings from employee share incentive awards, issued by the Ministry of Finance and the SAT, companies that implement employee stock ownership programs shall file the employee stock ownership plans and other relevant documents with the local tax authorities having jurisdiction over such companies before implementing such plans, and shall file share option exercise notices and other relevant documents with local tax authorities before exercise by their employees of any share options, and clarify whether the shares issuable under the employee share options referenced in the notice are shares of publicly listed companies.

The 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 SAFE Circular 7, in February 2012, pursuant to which if domestic individuals (meaning both PRC residents and non-PRC residents who reside in China for a continuous period of not less than one year, excluding the foreign diplomatic personnel and representatives of international organizations) participate in any stock 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 stock incentive plan, and obtain approval for an annual allowance with respect to the purchase of foreign exchange in connection with the stock purchase or stock option exercise. Such PRC individuals' foreign exchange income received from the sale of stocks and dividends distributed by the overseas listed company and any other income shall be fully remitted into a collective foreign currency account in China opened and managed by the PRC domestic agent before distribution to such individuals. In addition, such domestic individuals must also retain an overseas entrusted institution to handle matters in connection with the exercise of their stock options and their purchase and sale of stock. The PRC domestic agent also needs to update registration with SAFE within three months after the overseas-listed company materially changes its stock incentive plan or make any new stock incentive plans.

According to SAFE Circular 7, from time to time, we need to make applications or update our registration with SAFE or its local branches on behalf of our employees who are affected by our new share incentive plan or material changes in our current share incentive plan. However, we may not always be able to make applications or update our registration on behalf of our employees who hold our restricted shares or other types of share incentive awards in compliance with SAFE Circular 7, nor can we ensure you that such applications or update of registration will be successful. If we or the participants of our share incentive plans who are PRC citizens fail to comply with SAFE Circular 7, we and/or such participants of our share incentive plans may be subject to fines and legal sanctions, there may be additional restrictions on the ability of such participants to exercise their stock options or remit proceeds gained from sale of their stock into China, and we may be prevented from further granting share incentive awards under our share incentive plans to our employees who are PRC citizens.

### ***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. Complying with the requirements of the M&A Rules to complete acquisitions of PRC companies by foreign investors could be time-consuming, and any required approval processes, including obtaining approval from the MOFCOM, may delay or inhibit the ability to complete such transactions.

***Regulations on Taxation***

*PRC Enterprise Income Tax.* The National People's Congress, the Chinese legislature, passed the EIT Law, effective in 2008. The EIT Law applies a uniform 25% enterprise income tax rate to both foreign-invested enterprises and domestic enterprises. Preferential tax treatments are 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 State Council promulgated the implementation rules of the EIT Law in 2007 and the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation promulgated other supplemental rules in 2008 which were amended in 2016, respectively, regarding new criteria for the granting of high and new technology enterprises status. 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 in January 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 in April 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 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.

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.

Pursuant to the Notice on Issues Related to the Enterprise Income Tax Preferential Policies of Software and Integrated Circuit Industry on May 4, 2016, the software enterprises which enjoy preferential tax treatments shall provide filing documents with respect to preferential tax treatments to the relevant tax authority when filing annual enterprise income tax returns for the settlement of tax payments. In addition, pursuant to the Measures for Handling Matters Relating to Preferential Enterprise Income Tax Policies promulgated by the State Administration of Taxation on April 25, 2018, or Circular 23, an enterprise shall independently judge whether it satisfies the conditions prescribed under preferential taxation policies. The enterprises which satisfy such conditions shall calculate the tax reduction amount and enjoy the preferential tax treatments by filling out and submitting the enterprise income tax returns to the competent tax authority, and properly collect and retain relevant materials for future reference. For software enterprises, materials listed in the follow-up management requirements, which are contained in the catalogue attached to Circular 23, shall be prepared and submitted to the competent tax authority after annual financial settlement completed every year.

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 in April 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 in August 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.

In addition, the State Administration of Taxation issued a bulletin in January 2014, to provide more guidance on the implementation of the above circular. This bulletin further provided that, among other things, an entity that is classified as a resident enterprise in accordance with the circular shall file the application for classifying its status of residential enterprise with the local tax authorities where its main domestic investors registered. From the year in which the entity is determined as a resident enterprise, any dividend, profit and other equity investment gain shall be taxed in accordance with the Article 26 of EIT law and the Article 17 and Article 83 of its implementation rules.

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**Table of Contents**

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.

*PRC Withholding Tax.* According to the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Prevention of Fiscal Evasion and the Notice of the State Administration of Taxation Regarding Interpretation and Recognition of Beneficial Owners under Tax Treaties, dividends paid to shareholders residing 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 DTA. In January 2018, the State Administration of Taxation promulgated Circular 9, to clarify the definition of beneficial owner under PRC tax treaties and tax arrangements. According to Circular 9, a beneficial owner refers to a party who holds ownership and control over incomes or the rights or assets from which the incomes are derived. In determining whether a resident of the other contracting party to a double taxation agreement, or a DTA, who is applying for enjoying preferential treatment under the DTA has the status as a beneficial owner, comprehensive analysis shall be conducted in light of the actual circumstances of the specific case and based on several factors, include among others, if (1) an applicant is under the obligation to pay 50% or more of the incomes received to any resident of any third country (region) within 12 months upon receipt of the incomes; and (2) if the business activities carried out by an applicant constitutes substantive business activities. Substantive business activities shall include substantive manufacturing, distribution, management and other activities. Whether an applicant's business activities are substantive shall be determined based on the functions actually performed by the applicant and the risks assumed thereby. The substantive investment and shareholding management activities carried out by the applicant may constitute substantive business activities. Where the applicant concurrently engages in investment and shareholding management activities that do not constitute substantive business activities and other business activities, if the other business activities are not significant enough, the applicant will not be considered as engaging in substantive business activities and hence more likely not a beneficial owner. In addition, if the incomes derived by any of the following applicants from China are dividends, the relevant applicant may be directly determined as having the status of a beneficial owner :

The government of the other contracting party to the relevant DTA;

A company that is a resident of, and is listed on the market of, the other contracting party to the relevant DTA;

A resident individual of the other contracting party to the relevant DTA; or

Where one or more parties referred to in Item (1) through Item (3) directly or indirectly hold 100% of the shares of the applicant, and the mid-tier in the case of indirect shareholding is a resident of China or a resident of the other contracting party to the relevant DTA.

Further, According to Circular 9, agents or designated payees are not beneficial owners. The fact that an applicant collects incomes via an agent or a designated payee does not affect the determination of whether the applicant has the status of a beneficial owner irrespective of whether an agent or a designated payee is a resident of the other contracting party to the relevant DTA.

According to such SAT Circular 9, if the business activities carried out by an applicant do not constitute substantive business activities, then such applicant is likely not to be regarded as a beneficial owner. 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 DTA. 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 DTA. 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 DTA.

## **Table of Contents**

In addition, in December 21, 2017, SAT promulgated Notice on Issues Concerning the Policy for Temporary Exemption of Withholding Income Tax on Direct Investment by Overseas Investors with Distributed Profits, or Circular 88. According to the Circular 88, where overseas investors use the profits obtained from resident enterprises within China to invest directly in the encouraged investment projects, the deferred tax payment policy shall apply thereto and withholding income tax thereon shall be exempted temporarily. An overseas investor that is entitled to but has not actually enjoyed the policy of temporary exemption of withholding income tax under this Notice may apply to retroactively enjoy such policy within three years from the date of actual payment of relevant tax and for refund of the tax already paid.

According to the Circular 88, for the temporary exemption of overseas investors from payment of withholding income tax, the following conditions must be satisfied at the same time:

(1) Direct investment made by overseas investors with the profits distributed thereto, includes their activities of equity investment with the distributed profits such as capital increase, new establishment and equity purchase and excludes the increase through purchase or distribution and purchase of the shares of listed companies (excluding the conforming strategic investment), specifically including: (i) Increasing through purchase or distribution of the paid-in capital or capital reserve of resident enterprises within PRC; (ii) Investing in new establishment of resident enterprises within PRC; (iii) Purchasing the shares of resident enterprises within China from nonaffiliated parties; and (iv) Other methods prescribed by the Ministry of Finance and the State Administration of Taxation. The enterprises in which overseas investors invest through above investment activities shall be collectively referred to the invested enterprises.

(2) The profits distributed to overseas investors fall under the dividends, bonus and other equity investment income formed from the actual distribution of the retained income already realized by resident enterprises within China to investors.

(3) Where the profits used by overseas investors for direct investment are paid in cash, relevant amounts shall be transferred directly from the accounts of the profits distributing enterprises to the accounts of the invested enterprises or equity transferors and shall not be circulated among other domestic and overseas accounts before direct investment; where the profits used by overseas investors for direct investment are paid in kind, negotiable securities and other non-cash form, the ownership to relevant assets shall be transferred directly from the profits distributing enterprises to the invested enterprises or equity transferors and shall not be held by other enterprises and individuals on behalf thereof or temporarily.

(4) Direct investment by overseas investors in encouraged investment projects means that the invested enterprises engage in the business activities within the following scope prescribed below during the term of investment by overseas investors: (i) Falling within the catalogue of the industries for encouraging foreign investment as listed in the Catalogue of Industries for Guiding Foreign Investment; and (ii) Falling within the Catalogue of the Advantageous Industries for Foreign Investment in Central and Western Regions.

In addition, pursuant to the Announcement of the State Administration of Taxation on Issues Concerning the Implementation of the Policy for Temporary Exemption of Withholding Income Tax on Direct Investment by Overseas Investors with Distributed Profits promulgated by SAT on January 2, 2018 and retroactively effective on January 1, 2017, the business activities prescribed in Item (4) of Circular 88 shall include one or more of the following economic activities relating to encouraged investment projects: (i) manufacturing products or providing services; (ii) research and development activities; (iii) investment in construction projects or purchase of machines and equipment; and (iv) other business activities.



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**Table of Contents**

*PRC Value-Added Tax (VAT).* The VAT reform program change the charge of sales tax from business tax to VAT for certain pilot industries, and was initially applied only to certain pilot industries in Shanghai and was extended to apply nationwide and to cover more additional industry sectors. On March 24, 2016, the Ministry of Finance and the State Administration promulgated the Circular Regarding Overall Promotion of Pilot Practice of Replacing Business Tax with Value-Added Tax, effective on May 1, 2016. On June 18, 2016, the Ministry of Finance and the State Administration of Taxation promulgated the Circular Regarding Overall Promotion of Pilot Practice of Replacing Business Tax with Value-Added Tax in the Policy of Reinsurance, Real Estate Leasehold and Non-degree Education, in which the general taxpayers providing non-academic education services may apply a simple method for calculating the tax payable amount in accordance with the tax rate of 3%.

***Laws of Protection of Personal Information of Citizen***

According to the Law on the Protection of Consumer Rights and Interests, business operators must collect and use personal information of consumers in a lawful and proper manner by following the principle that information collection or use is genuinely necessary. They must expressly state the purposes, methods and scope of information collection or use, and obtain the consent of the consumers whose information is to be collected. To collect or use the personal information of consumers, business operators must disclose their information collection or use rules, and may not collect or use information in violation of laws or regulations, or in breach of any agreements between the parties concerned. Business operators and their staff members must strictly keep confidential the personal information of consumers collected, and may not divulge, sell or illegally provide others with such information.

According to the Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning the Application of Law in Handling Criminal Cases of Infringing Personal Information of Citizens, if a business operator collects personal information of citizens by purchasing, accepting or exchanging, or collects personal information of citizens in the course of performing their duties and providing services in violation of relevant laws and regulations of the State and meet one of the following standards, such operator will be considered in breach of criminal law and such operator and its responsible personnel must undertake criminal liabilities: (i) illegal acquisition, sale or provision of more than 50 pieces of track information, communication content, credit information or property information; (ii) illegal acquisition, sale, or provision of more than 500 pieces of accommodation information, communication records, health and physiological information, trading information, and other personal information which may affect the safety of personal and property; (iii) illegal acquisition, sale, or provision of more than 5000 pieces of personal information other than the information mentioned in the preceding (i) and (ii); (iv) the profits generated from using the illegally collected and acquired personal information is more than RMB50,000; and (v) resale the personal information collected during the course of performing their duties and providing service and the amount of resold personal information reaches 50% of the prescribed standard mentioned in (i) (ii), (iii) or (iv), as applicable.

***Laws of Network Security***

According to the Law of Network Security promulgated in November 7, 2016 and effective on June 1, 2017, in construction or operation of networks or supply of services through networks, technical measures and other necessary measures must be implemented in accordance with laws and regulations as well as the compulsory requirements of the national and industrial standards to safeguard the safe and stable operation of the networks, effectively respond to network security incidents, prevent illegal and criminal activities, and maintain the integrity, confidentiality and availability of network data. Law of Network Security provides that, among other things, the network operators must perform the following obligations:

protect networks from disturbance, damage or unauthorized access and prevent network data from being divulged, stolen or tampered with in accordance with the requirements of security graded protection system;

comply with the compulsory requirements of relevant national standards and take remedial measures to promptly notify users in accordance with relevant provisions and report the same to relevant competent authorities in a timely manner if they find that their network products or services have security defects, loopholes or other risks;

provide security maintenance for their products and services on a continuous basis;

**Table of Contents**

comply with relevant laws and administrative regulations on protection of personal information;

require users to provide authentic identity information when they enter into agreements with the users or when they confirm the supply of services where the network operators handle the network access or domain name registration services, the access formalities for fixed-line telephone or mobile phone for users, or provide users with the services of information release or instant messaging;

formulate emergency response plans for network security incidents and dispose of system loopholes, computer virus, network attack, network intrusion and any other security risks in a timely manner and initiate the emergency response plans, take appropriate remedial measures, and report the same to relevant competent authorities in accordance with relevant provisions in the event of any incidents endangering network security;

strengthen the management of the information published by their users; if they find any information that is prohibited from publication or transmission by laws or administrative regulations, they must immediately stop the transmission of such information, take disposal measures such as removal to prevent the spread of such information, keep relevant records, and report the same to relevant competent authorities; and

set up complaint and reporting platform for network information security, make public the complaint or reporting methods and other relevant information, accept and handle the complaints and reports on network information security in a timely manner, and cooperate with supervision and inspections conducted by Internet information department and other relevant departments in accordance with the applicable laws and regulations.

***Administrative Measures for Outbound Investment by Enterprises***

Administrative Measures for Outbound Investment by Enterprises, or Circular 11, is promulgated by NDRC, on December 26, 2017 and became effective on March 1, 2018. According to Circular 11, to make Outbound Investment, the investor shall go through verification and approval, record-filing and other procedures applicable to outbound investment projects, report relevant information, and cooperate with supervision and inspection. Outbound investments for purpose of Circular 11 are the investment activities whereby an enterprise within PRC, directly or via overseas enterprises under its control, acquires ownership, controlling power, rights of operation and management and other relevant rights and interests overseas by making asset or equity investment, providing financing or guarantee, etc., and the aforementioned investment activities shall include but not limited to (1) acquiring land ownership, land-use rights and other rights and interests overseas; (2) acquiring concession rights to explore or exploit natural resources and other rights and interests overseas; (3) acquiring ownership, rights of operation and management and other rights and interests of infrastructure overseas; (4) acquiring ownership, rights of operation and management and other rights and interests of enterprises or assets overseas; (5) constructing new fixed assets overseas, or renovating or expanding existing fixed assets overseas; (6) establishing a new enterprise overseas or increasing investment in an existing enterprise overseas; (7) setting up a new overseas equity investment fund or purchasing units in an existing overseas equity investment fund; and (8) controlling enterprises or assets overseas by agreements or trusts. Individual resident of PRC who invest overseas via overseas enterprises or enterprises in Hong Kong, Macao and Taiwan regions which are under their control shall also be subject to this Circular 11.



According to Circular 11, sensitive outbound investment projects carried out by an enterprise within PRC directly or via the overseas enterprises under their control should obtain verification and prior approval from NDRC. For the purpose of the Circular 11, sensitive outbound investment projects include: (1) Projects involving sensitive countries and regions, including (i) countries and regions that have not established diplomatic relations with China; (ii) countries and regions where war or civil unrest has broken out; (iii) countries and regions in which investment by enterprises shall be restricted pursuant to the international treaties, agreements, etc. concluded or acceded to by China; and (iv) other sensitive countries and regions, and (2) Projects involving sensitive industries, including (i) research, production and maintenance of weaponry and equipment; (ii) development and utilization of cross-border water resources; (iii) news media; and (iv) other industries in which outbound investment needs to be restricted pursuant to China's laws and regulations as well as related control policies.

## **Table of Contents**

Further according to Circular 11, the non-sensitive projects carried out by the overseas enterprise directly controlled by PRC residents, including by means of making asset or equity investment by companies established for financing and investing, such as fund institutions, or providing financing or guarantee, shall complete record-filing with the competent authority prior to the implementation of such project. The non-sensitive projects carried out by the overseas enterprise indirectly controlled by PRC residents with the investment amount over RMB300 million shall be reported to the NDRC of relevant information by submitting an information reporting form for large-amount non-sensitive projects.

Where an outbound investment project falls within the scope of administration by verification and approval or record-filing but its investor within the PRC fails to obtain a valid verification and approval document or notice of record-filing, departments in charge of foreign exchange administration and customs, should, pursuant to the law, not process its application, and no financial enterprises should, pursuant to the law, provide relevant fund settlement and financing services.

### **C. Organizational Structure**

Except our online education business that is operated by our majority-owned subsidiary, Koolearn, and its subsidiaries and consolidated variable interest entities, 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 currently parties to these contractual arrangements are Beijing Hewstone, Beijing Decision and Beijing Pioneer. 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. Beijing Pioneer primarily engages in the educational software development business.

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:

**Table of Contents**

Equity interest for companies.

Sponsorship interest for schools and kindergartens.

Contractual arrangements including equity pledge agreements, option agreement and proxy agreement, power of attorney, master exclusive service agreement and related 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, power of attorney, master exclusive service agreement and related service agreements. See C. Organizational Structure Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders.

- (1) Beijing Century Friendship Education Investment Co., Ltd is 80% owned by Mr. Michael Minhong Yu, our company's founder and executive chairman, and 20% owned by Ms. Bamei Li, Mr. Yu's mother.
- (2) Excluding Guangzhou Panyu Privately-Funded New Oriental Training Center, Guangzhou New Oriental School and Fuyang New Oriental Training School, which are separate legal entities but have been counted to our learning centers from the perspective of our internal management.
- (3) Consisting of various PRC companies operating our educational content and other technology development and distribution business, and overseas studies consulting business in China.

## **Table of Contents**

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, and our variable interest entities, their schools and subsidiaries and their shareholders. In the fiscal years ended May 31, 2016, 2017 and 2018, our variable interest entities contributed in aggregate 97.7%, 98.8% and 98.8%, respectively, of our total net revenues.

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

New Oriental China is our variable interest entity which is directly wholly owned by Century Friendship, a PRC domestic company controlled by Mr. Michael Minhong Yu, our founder and executive chairman. 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 the 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.

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 and executive chairman, 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 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, 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. Upon the conclusion of the master exclusive service agreement on September 19, 2014 between Beijing Pioneer and New Oriental China, the list of principal agreements has been updated to include the master exclusive service agreement and the relevant service agreements. 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 equity pledge agreements.

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**Table of Contents**

In February 2017, as part of our efforts to streamline the corporate structure, we removed Shanghai Smart Words as a party to the contractual arrangements with New Oriental China and its schools and subsidiaries and shareholder. The rights and obligations of Shanghai Smart Words under these contractual arrangements have been assumed by Beijing Decision. The April 2012 equity pledge agreements have been amended to reflect the foregoing change while the terms of these agreements remain unchanged. The equity pledges of Century Friendship under the amended agreements have been registered with the Haidian District, Beijing branch of the SAIC.

***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, one of our wholly-owned subsidiaries in China, and New Oriental China on April 23, 2012, replacing previous exclusive option agreements. On February 16, 2017, Beijing Decision entered into a new option agreement with Century Friendship and New Oriental China, replacing the previous option agreement dated April 23, 2012. Pursuant to the current option agreement, Century Friendship is obligated to sell to Beijing Decision, and Beijing Decision 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, Beijing Decision 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 Beijing Decision at any time in its discretion. The purchase price to be paid by Beijing Decision 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, 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.*** 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. On September 19, 2014, one of our wholly-owned subsidiaries, Beijing Pioneer, has entered into a master exclusive service agreement, as amended, with New Oriental China to enable our wholly-owned subsidiaries in China to receive substantially all of the economic benefits of New Oriental China and its schools and subsidiaries. After the conclusion of the master exclusive service agreement, the various existing service agreements between our wholly-owned subsidiaries will remain effective; however, if they have any conflict with the terms and conditions of the master exclusive service agreement, the master exclusive service agreement will prevail.

Under the master exclusive service agreement, Beijing Pioneer has the exclusive right to provide or designate any entities affiliated with it to provide New Oriental China and its schools and subsidiaries the technical and business support services set forth in schedule 2 of the agreement, including new enrollment system development service, sale of educational software and other operating services. Each service provider has the right to determine the fees associated with the services it provides based on the technical difficulty and complexity of the services and the actual

labor costs it incurs for providing the services during the relevant period. The term of this agreement is ten years and will be automatically extended upon the expiration. Beijing Pioneer may terminate the agreement at any time with a 30-day prior written notice to New Oriental China, whereas none of New Oriental China and its schools and subsidiaries can terminate this agreement. In the fiscal years ended May 31, 2016, 2017 and 2018, 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\$149.3 million, US\$269.2 million and US\$252.2 million, respectively.

**Table of Contents**

***Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders***

Subsequent to the voluntary delisting from the National Equities Exchange and Quotations in China in February 2018, Beijing Xuncheng went through a series of restructuring transactions and became a variable interest entity controlled by Koolearn, our majority-owned subsidiary which operates our online education business, through a series of contractual arrangements. Beijing Dexin Dongfang Network Technology Co., Ltd., or Dexin Dongfang, a wholly-owned PRC subsidiary of Koolearn, has entered into contractual arrangements with Beijing Xuncheng, its subsidiaries and shareholders, which enables us, through Koolearn, to:

have the power to direct the activities and most significantly affect the economic performance of Beijing Xuncheng and its subsidiary;

receive substantially all of the economic benefits from Beijing Xuncheng and its subsidiary; and

have an exclusive option to purchase all or part of the equity interest in Beijing Xuncheng, when and to the extent permitted by PRC law, or request any existing shareholder of Beijing Xuncheng to transfer all or part of the equity interest in Beijing Xuncheng 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 Agreement.*** Pursuant to share pledge agreements dated as of May 10, 2018 among Dexin Dongfang, Beijing Xuncheng and all of its shareholders, each shareholder of Beijing Xuncheng agreed to irrevocably and unconditionally pledge its equity interest in Beijing Xuncheng to Dexin Dongfang to secure the performance of obligations of Beijing Xuncheng, its shareholders, and relevant subsidiaries under the exclusive option agreement, the powers of attorney, the exclusive management consultancy and business cooperation agreement, and the letters of undertaking. Beijing Xuncheng's shareholders agreed not to transfer or dispose of the pledged equity interests or create or allow any third party to create any encumbrance on the pledged equity interests without prior written consent of Dexin Dongfang. The pledge takes effect upon registration with the relevant authorities and will remain in effect until the satisfaction of all contractual obligations of Beijing Xuncheng, its subsidiaries and its shareholders under the principal agreements or the termination of the principal agreements or 30 days after Dexin Dongfang provides a written termination notice to other parties, whichever is later.

***Exclusive Option Agreement.*** Exclusive Option Purchase Agreement dated as of May 10, 2018 was entered into by Dexin Dongfang, Beijing Xuncheng and all of its shareholders. Pursuant to this agreement, Beijing Xuncheng's shareholders unconditionally and irrevocably agreed to grant Dexin Dongfang an exclusive option to purchase all or part of the equity interests in Beijing Xuncheng for the minimum amount of consideration permitted by PRC law. Where the purchase price is required by PRC law to be an amount other than nil consideration, Beijing Xuncheng's shareholders undertake to return the amount of purchase price they shall have received to Dexin Dongfang or any of its designated third party. Dexin Dongfang has the sole discretion to decide whether to exercise the option in part, in full or at all. Without the prior written consent of Dexin Dongfang, none of the assets of Beijing Xuncheng may be sold, transferred or otherwise disposed of. In addition, without Dexin Dongfang's prior written consent, none of Beijing Xuncheng's shareholders may transfer or permit to create any encumbrance, guarantee or security over its equity interests in Beijing Xuncheng. Beijing Xuncheng's shareholders also undertook that if they receive any profit distribution or dividend from Beijing Xuncheng, they will immediately pay or transfer such amount, subject to the



relevant tax payment being made under the relevant laws and regulations, to Dexin Dongfang or its designated third party. This agreement will remain in effect until Dexin Dongfang or its designated third parties have acquired all the equity interests in Beijing Xuncheng. Dexin Dongfang may unilaterally terminate this agreement through a 30-day prior written notice.

***Powers of Attorney.*** On May 10, 2018, each of Beijing Xuncheng's shareholders executed a power of attorney whereby such shareholder irrevocably appoints Dexin Dongfang or any person designated by Dexin Dongfang as its attorney-in-fact to exercise on the shareholder's behalf any and all rights the shareholder has in respect of its equity interests in Beijing Xuncheng. The power of attorney will remain effective as long as the shareholder holds any equity interest in Beijing Xuncheng. On May 10, 2018, Beijing Xuncheng also executed a power of attorney whereby it irrevocably appoints Dexin Dongfang or any person designated by Dexin Dongfang as its attorney-in-fact to exercise on its behalf any and all rights it has in respect of its equity interest in its current or future majority-owned subsidiaries. The power of attorney will remain effective as long as Beijing Xuncheng continues to hold any equity interest in its subsidiaries.

**Table of Contents**

***Exclusive Management Consultancy and Cooperation Agreement.*** Exclusive Management Consultancy and Cooperation Agreement dated as of May 10, 2018 was entered into by and among Dexin Dongfang, Beijing Xuncheng and its subsidiaries, and all of its shareholders. Pursuant to the agreement, Dexin Dongfang has the exclusive right to provide, or designate any third party to provide Beijing Xuncheng and its subsidiaries with corporate management services, intellectual property licenses, technical and business supports, and other additional services as the parties may agree from time to time. Without Dexin Dongfang's prior written consent, neither Beijing Xuncheng nor any of its subsidiaries may accept foregoing services from a third party. Dexin Dongfang owns all intellectual property rights arising out of the performance of this agreement. In exchange for the services, Beijing Xuncheng and its subsidiaries agree to pay their entire income to Dexin Dongfang as the service fee. In addition, without Dexin Dongfang's prior written consent, Beijing Xuncheng and its subsidiaries shall not enter into any transactions that may affect its assets, obligations, rights or operations, other than those transactions entered into in the ordinary course of business. Dexin Dongfang has the right to appoint directors, general managers, financial controllers and other senior managers Beijing Xuncheng and its subsidiaries. Without Dexin Dongfang's prior written consent, Beijing Xuncheng shall not change or remove directors appointed by Dexin Dongfang or make any distribution to its shareholders. This agreement will remain effective until terminated upon the agreement of the parties.

***Letters of Undertaking.*** As of the date of this annual report, Century Friendship directly held the entire equity interest in New Oriental China, the largest shareholder of Beijing Xuncheng. To ensure stability and continued validity and enforceability of the foregoing agreements, Century Friendship and its shareholders, our founder Mr. Yu and Ms. Li Bamei, have executed a letter of undertaking dated May 10, 2018 whereby they undertake not to enter into any arrangement, including pledge, sale, disposal or creation of other third party rights, in relation to Century Friendship's equity interests in New Oriental China which may adversely affect the implementation of the foregoing agreements entered into by New Oriental China unless they have obtained consent from Koolearn or Dexin Dongfang, and the counterparties or beneficiaries of such arrangement have executed written undertaking(s) to the effect that they will not affect the performance of the foregoing agreements entered into by New Oriental China. In addition, Century Friendship and its shareholders undertake not to participate in, invest in, own or manage any businesses competing with that of Beijing Xuncheng and its subsidiaries as long as they continue to hold equity interest in Beijing Xuncheng. The general partner of each limited partnership that holds equity interest in Beijing Xuncheng executed a similar letter of undertaking as of May 10, 2018 to the same effect.

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

(i) the corporate structure of New Oriental China and its schools and subsidiaries, and our wholly-owned subsidiaries in China, and (ii) the corporate structure of Beijing Xuncheng and its subsidiaries and Dexin Dongfang are in compliance with existing PRC laws and regulations; and

(i) 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 and (ii) the contractual arrangements among Dexin Dongfang, Beijing Xuncheng and its subsidiaries and shareholders 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 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**

### **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 210,000 square meters of schools in Yangzhou and an aggregate of approximately 63,000 square meters of space for our schools, learning centers and bookstores in various cities in China, including Hangzhou, Xiamen, Zhengzhou, Xi'an, Tianjin, Kunming, Wuhan, Guangzhou, Changsha and Beijing.

## **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, our ability to optimize our comprehensive online and offline integrated education ecosystem on a constant basis, 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.

Our future results of operations will depend significantly upon our ability to increase paying users for our online courses, 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.

## Table of Contents

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, our variable interest entities and their schools and subsidiaries and their shareholders. Our variable interest entities' 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, 2016, 2017 and 2018, we generated total net revenues of US\$1,478.3 million, US\$1,799.5 million and US\$2,477.4 million, respectively. Our revenues are net of PRC business taxes and related surcharges as well as refunds.

We currently derive revenues from the following sources:

educational programs and services, which accounted for 88.6%, 89.4% and 88.5% of our total net revenues in the fiscal years ended May 31, 2016, 2017 and 2018, respectively; and

books and other services, which accounted for 11.4%, 10.6% and 11.5% of our total net revenues in the fiscal years ended May 31, 2016, 2017 and 2018, respectively.

*Educational Programs and Services.* Our educational programs and services consist of language training and test preparation courses, pre-school education, primary and secondary school education and online education. Revenues from language training courses and test preparation courses accounted for 83.8%, 83.9% and 82.7%, respectively, of our total net revenues in the fiscal years ended May 31, 2016, 2017 and 2018.

We recognize revenues from course fees collected for enrollment in our language training and test preparation courses and online education 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 revenue. 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 only those collected but unearned portion of the fee is available to be refunded. We recognize revenues from school fees collected for enrollment in our pre-school education and primary and secondary schools ratably over the corresponding academic year.

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, overseas admissions and assessment test preparation and K-12 after-school tutoring program, 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 K-12 after-school tutoring courses and overseas 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 K-12 after-school tutoring market, we have expanded the scope of our 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 Pop Kids (Non-English) all subjects training program for primary school students, and plan to further expand our course offerings and geographic coverage in the future to

capture a larger share of the huge after-school training market in China. In order to use new technology to reshape our traditional offline classroom-teaching offerings and enhance customers' learning experience, we developed our own O2O two-way interactive learning platform, or the O2O platform, by standardizing and digitalizing our education content and user data. We established a database of learning modules for internet-based self-learning practice and assessment. The O2O platform complements and supports students' offline learning activities by offering online learning components, such as pushing customized content to students, recommending additional courses based on their online study records and performance, facilitating interaction between students, teachers and parents across a variety of devices, including smartphones, tablets and PCs.

**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. 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 100 students per class. Our K-12 after-school tutoring courses and our English language training courses are delivered in class settings generally ranging from 1 student to 60 students per class. In November 2013, we launched an online test preparation program on our own online education website koolearn.com, which features live broadcasts of a series of our most popular offline test preparation classes. 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 Other Services.* 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, 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.

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 increase 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>	<b>For the Year Ended May 31,</b>					
	<b>2016</b>		<b>2017</b>		<b>2018</b>	
	<b>US\$</b>	<b>%</b>	<b>US\$</b>	<b>%</b>	<b>US\$</b>	<b>%</b>
Net revenues	1,478,348	100.0	1,799,509	100.00	2,447,430	100.00
Operating costs and expenses:						



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Cost of revenues	(614,364)	(41.5)	(749,586)	(41.7)	(1,065,740)	(43.5)
Selling and marketing	(197,897)	(13.4)	(232,826)	(12.9)	(324,249)	(13.2)
General and administrative	(471,010)	(31.9)	(554,948)	(30.8)	(794,482)	(32.5)
Total operating costs and expenses	(1,283,271)	(86.8)	(1,537,360)	(85.4)	(2,184,471)	(89.2)

## **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. 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.

*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 to our employees, directors and consultants. The number of common shares available for grant under the 2006 Share Incentive Plan may be increased by (i) an additional 5,000,000 shares on January 1, 2007, (ii) an additional 5,000,000 shares on January 1, 2008, and (iii) an annual increase in common shares to be added on the first business day of each calendar year beginning in 2009 equal to the lesser of (x) 3,000,000 shares, (y) two percent (2%) of total common shares outstanding as of such date, or (z) a lesser number of shares as determined by the plan administrator. Since the adoption of our 2006 Share Incentive Plan, we have granted options to purchase 15,826,000 common shares, of which 2,277,546 options to purchase common shares had been forfeited under our 2006 Share Incentive Plan. In addition, since the adoption of our 2006 Share Incentive Plan, we have granted a total of 8,608,671 non-vested equity shares under 2006 Share Incentive Plan. Our 2006 Share Incentive Plan expired in January 2016, but the expiration of our 2006 Share Incentive Plan does not affect the effectiveness of options granted prior to such expiration.

In January 2016, we adopted the 2016 Share Incentive Plan, under which we are authorized to issue up to 10,000,000 common shares pursuant to awards (including options) granted to our employees, directors and consultants. Since the adoption of our 2016 Share Incentive Plan, we have granted a total of 1,921,646 non-vested equity shares, among which, 436,016 and 1,485,630 were granted in the year ended May 31, 2017 and 2018, respectively. 4,050 and 47,006 shares were forfeited in the year ended May 31, 2017 and 2018, respectively.

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. 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>	<b>For the Year Ended May 31,</b>					
	<b>2016</b>		<b>2017</b>		<b>2018</b>	
	<b>US\$</b>	<b>%</b>	<b>US\$</b>	<b>%</b>	<b>US\$</b>	<b>%</b>
Allocation of Share-based Compensation Expenses:						
General and administrative	16,810	100.0	20,287	100.0	57,443	100.0

## **Table of Contents**

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.

In April 2016, we sold 51% equity interest in Beijing Dianshi Jingwei Technology Co., Ltd, or Dianshi Jingwei, one of our wholly-owned subsidiaries, to some members of Dianshijingwei's management, for a cash consideration of US\$2.3 million, of which US\$1.5 million had been collected as of May 31, 2016, and the remaining consideration was collected in June 2017. We recorded a gain of US\$3.8 million from this disposal. After the disposal, we stopped consolidating Dianshi Jingwei and started to recognize our remaining investment in Dianshijingwei using the equity method as we retained the ability to exercise significant influence over Dianshi Jingwei.

## **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.

### *Hong Kong*

Our subsidiaries incorporated in Hong Kong are subject to 16.5% Hong Kong profit tax on their taxable income generated from operations in Hong Kong. No Hong Kong profit tax has been levied as we did not have assessable profit that was earned in or derived from any Hong Kong subsidiary during the periods presented. Under the Hong Kong tax law, our Hong Kong subsidiaries are exempted from the Hong Kong income tax on its foreign-derived income. Hong Kong does not impose a withholding tax on dividends.

### *PRC*

Other than our primary and secondary schools, our operating entities in China are subject to a value-added tax ( VAT ) at varying rates ranging from 3% to 17% (or 16% starting May 1, 2018) on their respective net revenues. Our operating entities that provide education services are subject to a simple VAT collection method and apply for a 3% VAT rate since June 2016 according to the Notice of the Ministry of Finance and the State Administration of Taxation on Further Clarifying the Policies regarding Reinsurance, Immovable Property Leasing and Non-Academic Education in the Comprehensive Promotion of the Pilot Program of Replacing Business Tax with Value-Added Tax, or the Circular 68. VAT is reported as a deduction to revenue when incurred. Circular 68 and the subsequent relevant implementation measures and rules are relatively new, and the interpretation and enforcement of this circular and its implementation measures and rules involve uncertainties.

With regard to income tax, enterprises in China are generally subject to enterprise income tax at a rate of 25%. Enterprises that qualify as high and new technology enterprises are entitled to a favorable enterprise income tax rate of 15% rather than the 25% uniform statutory tax rate. Such qualification is reassessed by relevant governmental authorities every three years. Five of our wholly-owned subsidiaries in China, including Beijing Hewstone, Beijing Decision, Beijing Smart Wood, and two other subsidiaries, are qualified as high and new technology enterprises. Beijing Pioneer, one of our wholly-owned subsidiaries in China, is in the process of renewing its qualification of high and new technology enterprises. Once the renewal is completed, Beijing Pioneer will be eligible for a the favorable enterprise income tax rate of 15% starting January 1, 2018. Beijing Xuncheng, one of our variable interest entities, is

also qualified as high and new technology enterprises.

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**Table of Contents**

An enterprises that qualifies as a software enterprise is exempt from enterprise income tax for the two years beginning from such enterprise's first profitable year and then is entitled to a reduced tax rate of 12.5% for the succeeding three years. Seven of our wholly-owned subsidiaries in China, including Beijing Smart Wood and six other subsidiaries, are qualified as software enterprises. For those subsidiaries that are qualified as both high and new technology enterprises and software enterprises, they have elected to enjoy income tax exemption for the two years beginning from their first profitable year, then a reduced tax rate of 12.5% for the succeeding three years, and then a reduced tax rate of 15% so long as they continue to meet the qualification of high and new technology enterprises.

In addition, under the current regulatory regime, whether our schools are entitled to any preferential income tax treatment remains unclear, and practice varies across different cities in China. Pursuant 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. To date, no regulations have been promulgated by the relevant authorities with regard to the preferential income tax treatment applicable to private schools requiring reasonable returns. As of May 31, 2018, 26 of our schools elected as schools not requiring reasonable returns, and 37 of our schools elected as requiring reasonable returns and the remaining schools were not classified or registered as companies. The Amended Private Education Law, which became effective on September 1, 2017, no longer uses the term reasonable return. Instead, under the Amended Private Education Law, sponsors of private schools may choose to establish non-profit or for-profit private schools at their own discretion, except that private schools in compulsory education area can only be registered as non-profit private schools. Pursuant to the Amended Private Education Law, non-profit private schools will be entitled to the same tax benefits as public schools while taxation policies for for-profit private schools are still unclear. Due to a lack of implementation rules, 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, 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 at all. 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, 2018, three schools are subject to the standard 25% enterprise income tax rate and one school was not required by the governing tax bureau to pay any EIT from its establishment through May 31, 2018.

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, our wholly-owned subsidiaries and variable interest entities 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 our wholly-owned subsidiaries and variable interest entities, 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 Regulation Regulations on Taxation.

**Recent Acquisition**

In October 2017, we acquired the entire equity interest in Hangzhou Shengshen, a K-12 education group located in Zhejiang, for a total consideration of US\$11.0 million.

**Recent Disposal**

In April 2016, we disposed 51% equity interest in Dianshijingwei for a cash consideration of US\$2.3 million and recorded a gain of US\$3.8 million from this disposal.

**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.

<i>(in thousands of US\$)</i>	<b>For the Year Ended May 31,</b>		
	<b>2016</b>	<b>2017</b>	<b>2018</b>
Net revenues:			
Educational programs and services	1,309,339	1,608,954	2,165,152
Books and other services	169,009	190,555	282,278
Total net revenues	1,478,348	1,799,509	2,447,430
Operating costs and expenses <sup>(1)</sup> :			
Cost of revenues	(614,364)	(749,586)	(1,065,740)
Selling and marketing	(197,897)	(232,826)	(324,249)
General and administrative	(471,010)	(554,948)	(794,482)
Total operating costs and expenses	(1,283,271)	(1,537,360)	(2,184,471)
Gain on disposal of subsidiaries	3,760		
Operating income	198,837	262,149	262,959
Other income, net	68,447	68,560	94,065
Provision for income taxes	(37,531)	(50,624)	(59,408)
Loss from equity method investments	(4,425)	(3,289)	(379)
Net income	225,328	276,796	297,237
Net loss (gain) attributable to the noncontrolling interests	(444)	(2,339)	(1,107)
Net income attributable to New Oriental Education & Technology Group Inc.	224,884	274,457	296,130

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

<i>(in thousands of US\$)</i>	<b>For the Year Ended May 31,</b>		
	<b>2016</b>	<b>2017</b>	<b>2018</b>
General and administrative	16,810	20,287	57,443

***Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017***

**Net Revenues.** Our total net revenues increased by 36.0% from US\$1,799.5 million for the fiscal year ended May 31, 2017 to US\$2,447.4 million for the fiscal year ended May 31, 2018. This increase was due to the increased revenues from both educational programs and services as well as from books and other services.

**Educational Programs and Services.** Net revenues from our educational programs and services increased by 34.6% from US\$1,609.0 million for the fiscal year ended May 31, 2017 to US\$2,165.2 million for the fiscal



year ended May 31, 2018. This increase was primarily due to the growth in revenues from language training and test preparation courses from US\$1,510.5 million in the fiscal year ended May 31, 2017 to US\$2,023.0 million in the fiscal year ended May 31, 2018. The increase in revenues from language training and test preparation courses was mainly attributable to the increase in the number of student enrollments from approximately 4.8 million in the fiscal year ended May 31, 2017 to over 6.3 million in the fiscal year ended May 31, 2018, and in particular, the increased number of student enrollments in test preparation courses for middle and high school students and language training courses for children. Our total numbers of schools and learning centers were 87 and 994, respectively, as of May 31, 2018, compared to 77 and 778, respectively, as of May 31, 2017.

*Books and Other services.* Net revenues from sales of books and other educational materials and services increased by 48.1% from US\$190.6 million in the fiscal year ended May 31, 2017 to US\$282.3 million in the fiscal year ended May 31, 2018, primarily due to the increased revenue of US\$74.6 million from the overseas consulting business in the fiscal year ended May 31, 2018.

*Operating Costs and Expenses.* Our total operating costs and expenses increased by 42.1% from US\$1,537.4 million in the fiscal year ended May 31, 2017 to US\$2,184.5 million in the fiscal year ended May 31, 2018. This increase resulted from increases in our cost of revenues, selling and marketing expenses and general and administrative expenses line items.

## **Table of Contents**

*Cost of Revenues.* Our cost of revenues increased by 42.2% from US\$749.6 million in the fiscal year ended May 31, 2017 to US\$1,065.7 million in the fiscal year ended May 31, 2018. This increase was primarily due to an increase in teaching fees and performance-linked bonuses paid to our teachers during the fiscal year ended May 31, 2018.

*Selling and Marketing Expenses.* Our selling and marketing expenses increased by 39.3% from US\$232.8 million in the fiscal year ended May 31, 2017 to US\$324.2 million in the fiscal year ended May 31, 2018. This increase was primarily due to the addition of over 4,000 new sales and marketing personnel during the fiscal year ended May 31, 2018.

*General and Administrative Expenses.* Our general and administrative expenses increased by 43.2% from US\$554.9 million in the fiscal year ended May 31, 2017 to US\$794.5 million in the fiscal year ended May 31, 2018. This increase was primarily due to an increase of US\$141.8 million in human resources expenses and an increase of US\$22.7 million in general operational expenses during the fiscal year ended May 31, 2018.

*Other Income, Net.* Our other income, net which primarily includes interest income, increased from US\$68.6 million in the fiscal year ended May 31, 2017 to US\$94.1 million in the fiscal year ended May 31, 2018.

*Provision for Income Tax.* Our income tax expense increased by 17.4% from US\$50.6 million in the fiscal year ended May 31, 2017 to US\$59.4 million in the fiscal year ended May 31, 2018. The increase was primarily due to higher income tax rate incurred in the fiscal year ended May 31, 2018.

*Net Income.* As a result of the foregoing, our net income for the fiscal year ended May 31, 2018 was US\$297.2 million, compared to US\$276.8 million for the fiscal year ended May 31, 2017.

### ***Fiscal Year Ended May 31, 2017 Compared to Fiscal Year Ended May 31, 2016***

*Net Revenues.* Our total net revenues increased by 21.7% from US\$1,478.3 million for the fiscal year ended May 31, 2016 to US\$1,799.5 million for the fiscal year ended May 31, 2017. This increase was due to the increased revenues from both educational programs and services as well as from books and other services.

*Educational Programs and Services.* Net revenues from our educational programs and services increased by 22.9% from US\$1,309.3 million for the fiscal year ended May 31, 2016 to US\$1,608.9 million for the fiscal year ended May 31, 2017. This increase was primarily due to the growth in revenues from language training and test preparation courses from US\$1,238.6 million in the fiscal year ended May 31, 2016 to US\$1,510.5 million in the fiscal year ended May 31, 2017. The increase in revenues from language training and test preparation courses was mainly attributable to the increase in the number of student enrollments from approximately 3.6 million in the fiscal year ended May 31, 2016 to over 4.8 million in the fiscal year ended May 31, 2017, and in particular, the increased number of student enrollments in test preparation courses for middle and high school students and language training courses for children. Our total numbers of schools and learning centers were 77 and 778, respectively, as of May 31, 2017, compared to 66 and 682, respectively, as of May 31, 2016.

*Books and Other services.* Net revenues from sales of books and other educational materials and services increased by 12.7% from US\$169.0 million in the fiscal year ended May 31, 2016 to US\$190.6 million in the fiscal year ended May 31, 2017, primarily due to the increased revenue of US\$18.8 million from the overseas consulting business in the fiscal year ended May 31, 2017.

*Operating Costs and Expenses.* Our total operating costs and expenses increased by 19.8% from US\$1,283.3 million in the fiscal year ended May 31, 2016 to US\$1,537.4 million in the fiscal year ended May 31, 2017. This increase resulted from increases in our cost of revenues, selling and marketing expenses and general and administrative expenses line items.

*Cost of Revenues.* Our cost of revenues increased by 22.0% from US\$614.4 million in the fiscal year ended May 31, 2016 to US\$749.6 million in the fiscal year ended May 31, 2017. This increase was primarily due to an increase in teaching fees and performance-linked bonuses paid to our teachers during the fiscal year ended May 31, 2017.

## **Table of Contents**

*Selling and Marketing Expenses.* Our selling and marketing expenses increased by 17.7% from US\$197.9 million in the fiscal year ended May 31, 2016 to US\$232.8 million in the fiscal year ended May 31, 2017. This increase was primarily due to the addition of over 500 new sales and marketing personnel during the fiscal year ended May 31, 2017.

*General and Administrative Expenses.* Our general and administrative expenses increased by 17.8% from US\$471.0 million in the fiscal year ended May 31, 2016 to US\$554.9 million in the fiscal year ended May 31, 2017. This increase was primarily due to an increase of US\$56 million in human resources expenses and an increase of US\$13.2 million in general operational expenses during the fiscal year ended May 31, 2017.

*Other Income, Net.* Our other income, net which primarily includes interest income, increased from US\$68.4 million in the fiscal year ended May 31, 2016 to US\$68.6 million in the fiscal year ended May 31, 2017.

*Provision for Income Tax.* Our income tax expense increased by 34.9% from US\$37.5 million in the fiscal year ended May 31, 2016 to US\$50.6 million in the fiscal year ended May 31, 2017. The increase was primarily due to higher income tax rate incurred in the fiscal year ended May 31, 2017.

*Net Income.* As a result of the foregoing, our net income for the fiscal year ended May 31, 2017 was US\$276.8 million, compared to US\$225.3 million for the fiscal year ended May 31, 2016.

## **Discussion of Segment Operations**

For the years ended May 31, 2016, 2017 and 2018, we identified seven operating segments, including language training and test preparation, primary and secondary school education, online education, content development and distribution, pre-school education, overseas study consulting services, and study tour. In the year ended May 31, 2018, we identified language training and test preparation as a reportable segment. Primary and secondary school education, online education, content development and distribution, pre-school education, overseas study consulting services and study tour operating segments were aggregated as others because individually they do not exceed the 10% quantitative threshold.

Net revenues from our language training and test preparation courses accounted for 83.8%, 83.9% and 82.7%, respectively, of our total net revenues in the fiscal years ended May 31, 2016, 2017 and 2018. 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.

Cost of revenues for our language training and test preparation courses primarily consists of teaching fees and performance-linked bonuses paid to our teachers, 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.

Selling and marketing expenses for each of our language training and test preparation courses primarily consist of marketing and promotion expenses and other costs related to our selling and marketing activities for the corresponding reportable segment.

General and administrative expenses for our language training and test preparation courses primarily consist of compensation and benefits of administrative staff of our language training and test preparation courses segment, compensation and benefits, rental and utilities payments relating to office and administrative functions of our language training and test preparation courses segment, depreciation and amortization of property and equipment used

in the general and administrative activities of our language training and test preparation courses segment and, to a lesser extent, costs to develop our curriculum.

The following table lists our net revenues and operating costs and expenses by reportable segment for the periods indicated.

<i>(in thousands of US\$)</i>	<b>For the Year Ended May 31,</b>		
	<b>2016</b>	<b>2017</b>	<b>2018</b>
<b>Net revenues of reportable segments:</b>			
Language training and test preparation courses	1,238,572	1,510,497	2,022,978
<b>Total net revenues of reportable segments</b>	<b>1,238,572</b>	<b>1,510,497</b>	<b>2,022,978</b>
Total net revenues of our company	1,478,348	1,799,509	2,447,430
<b>Operating costs and expenses of reportable segments:</b>			
<b>Cost of revenues:</b>			
Language training and test preparation courses	(516,370)	(623,364)	(869,012)
<b>Selling and marketing:</b>			
Language training and test preparation courses	(125,815)	(146,544)	(193,851)
<b>General and administrative:</b>			
Language training and test preparation courses	(296,686)	(363,949)	(504,985)
<b>Total operating costs and expenses of reportable segments</b>	<b>(938,871)</b>	<b>(1,133,857)</b>	<b>(1,567,848)</b>
<b>Total operating costs and expenses of our company</b>	<b>(1,283,271)</b>	<b>(1,537,360)</b>	<b>(2,184,471)</b>

**Table of Contents**

***Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017***

*Net Revenues of Language Training and Test Preparation Courses*

Net revenues from our language training and test preparation courses increased by 33.9% from US\$1,510.5 million for the fiscal year ended May 31, 2017 to 2,023.0 million for the fiscal year ended May 31, 2018, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017 Net Revenues Educational Programs and Services.

*Operating Costs and Expenses of Language Training and Test Preparation Courses*

*Cost of Revenues.* Cost of revenues for our language training and test preparation courses increased by 39.4% from US\$623.4 million for the fiscal year ended May 31, 2017 to US\$869.0 million for the fiscal year ended May 31, 2018, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017 Operating Costs and Expenses Cost of Revenues.

*Selling and Marketing Expenses.* Selling and marketing expenses for our language training and test preparation courses increased by 32.3% from US\$146.5 million for the fiscal year ended May 31, 2017 to US\$193.9 million for the fiscal year ended May 31, 2018, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017 Operating Costs and Expenses Selling and Marketing Expenses.

*General and Administrative Expenses.* General and administrative expenses for our language training and test preparation courses increased by 38.8% from US\$363.9 million for the fiscal year ended May 31, 2017 to US\$505.0 million for the fiscal year ended May 31, 2018, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2018 Compared to Fiscal Year Ended May 31, 2017 Operating Costs and Expenses General and Administrative Expenses.

***Fiscal Year Ended May 31, 2017 Compared to Fiscal Year Ended May 31, 2016***

*Net Revenues of Language Training and Test Preparation Courses*

Net revenues from our language training and test preparation courses increased by 22.0% from US\$1,238.6 million for the fiscal year ended May 31, 2016 to US\$1,510.5 million for the fiscal year ended May 31, 2017, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2017 Compared to Fiscal Year Ended May 31, 2016 Net Revenues Educational Programs and Services.

*Operating Costs and Expenses of Language Training and Test Preparation Courses*

*Cost of Revenues.* Cost of revenues for our language training and test preparation courses increased by 20.7% from US\$516.4 million for the fiscal year ended May 31, 2016 to US\$623.4 million for the fiscal year ended May 31, 2017, primarily due to the factors discussed in Results of Operations Fiscal Year Ended

May 31, 2017 Compared to Fiscal Year Ended May 31, 2016 Operating Costs and Expenses Cost of Revenues.

## **Table of Contents**

*Selling and Marketing Expenses.* Language Training and Test Preparation Courses. Selling and marketing expenses for our language training and test preparation courses increased by 16.5% from US\$125.8 million for the fiscal year ended May 31, 2016 to US\$146.5 million for the fiscal year ended May 31, 2017, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2017 Compared to Fiscal Year Ended May 31, 2016 Operating Costs and Expenses Selling and Marketing Expenses.

*General and Administrative Expenses.* Language Training and Test Preparation Courses. General and administrative expenses for our language training and test preparation courses increased by 22.7% from US\$296.7 million for the fiscal year ended May 31, 2016 to US\$363.9 million for the fiscal year ended May 31, 2017, primarily due to the factors discussed in Results of Operations Fiscal Year Ended May 31, 2017 Compared to Fiscal Year Ended May 31, 2016 Operating Costs and Expenses General and Administrative Expenses.

## **Inflation**

According to the National Bureau of Statistics of China, the year-over-year percent changes in the consumer price index in China for May 2016, 2017 and 2018 were increases of 2.0%, 1.5% and 1.8%, respectively. Inflation has had some impact on our operations in recent years, in the form of higher salaries for our teachers and other staff and higher rental payments for certain of the properties we lease. Additionally, because a substantial portion of our assets consists of cash and cash equivalents and short-term investments in RMB, high inflation could significantly reduce the value and purchasing power of these assets. We are not able to hedge our exposure to higher inflation in China. We can provide no assurance that we will not be affected in the future should rates of inflation increase again in China.

## **Critical Accounting Policies**

We prepare our consolidated financial statements in accordance with U.S. GAAP, which requires us to make judgments, estimates and assumptions that affect the reported amounts of our assets and liabilities and the disclosure of our contingent assets and liabilities at the end of each fiscal period and the reported amounts of revenues and expenses during each fiscal period. We continually evaluate these judgments and estimates based on our own historical experience, knowledge and assessment of current business and other conditions, our expectations regarding the future based on available information and assumptions that we believe to be reasonable, which together form our basis for making judgments about matters that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, our actual results could differ from those estimates. Some of our accounting policies require a higher degree of judgment than others in their application.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors that should be considered when reviewing our financial statements. We believe the following accounting policy involves the most significant judgments and estimates used in the preparation of our consolidated financial statements.

## **Revenue recognition**

We recognize revenue when persuasive evidence that an arrangement exists, delivery of the product or service has occurred, the selling price is both fixed and determinable and collection is reasonably assured. The primary sources of our company's revenues are as follows:

*Educational programs and services*



The educational programs and services consist of language training and test preparation courses, pre-school education, primary and secondary school education and online education. Tuition is generally paid in advance and is initially recorded as deferred revenue. Revenue is recognized proportionately as the instruction is delivered over the period of the course for the course fees collected for enrollment in the language training and test preparation courses and online education or ratably over the corresponding academic year for the school fees collected for enrollment in the pre-school education and primary and secondary school education, and is reported net of business taxes, VAT and refunds. Students are entitled to a short term trial period which commences on the date the course begins. 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 only those collected but unearned portion of the fee is available to be refunded. Refunds have been insignificant for the years ended May 31, 2016, 2017 and 2018..

## **Table of Contents**

### *Other services*

Other service revenues are primarily derived from consulting services to students regarding overseas studies and study tours. Revenue is recognized after a contract is signed. The price is fixed or determinable, services are delivered and collection is reasonably assured.

### *Books*

Our company sells books or other educational materials developed or licensed by our own book stores or websites or through third party distributors. Revenue from sales of books and other educational materials is recognized when the products are sold to the end customers. Our company provides books and other educational materials that are required for its courses and does not separately charge students for these items.

### ***Consolidation of Variable Interest Entity***

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. To comply with the PRC laws and regulations, we conduct substantially all of our business through New Oriental China and Xuncheng, our variable interest entities, and their schools and subsidiaries. We have, through our wholly-owned subsidiaries in the PRC, entered into contractual arrangements with New Oriental China, its schools and subsidiaries, and their shareholders such that New Oriental China and its schools and subsidiaries (collectively the VIEs ) are considered variable interest entities for which we are considered their primary beneficiary. We believe we have substantive kick-out rights per the terms of the option agreement, which gives us the power to control the shareholder of New Oriental China. More specifically, we believe that the terms of the exclusive option agreement are currently exercisable and legally enforceable under PRC laws and regulations. We also believe that the minimum amount of consideration permitted by the applicable PRC law to exercise the option does not represent a financial barrier or disincentive for us to exercise our rights under the exclusive option agreement. A simple majority vote of our board of directors is required to pass a resolution to exercise our rights under the exclusive option agreement, for which consent of the shareholder of New Oriental China is not required. Therefore, we believe this gives us the power to direct the activities that most significantly impact the VIEs' economic performance. We believe that our ability to exercise effective control, together with the service agreements and the equity pledge agreements, give us the rights to receive substantially all of the economic benefits from the VIEs in consideration for the services provided by our wholly-owned subsidiaries in China. Accordingly, as the primary beneficiary of the VIEs and in accordance with U.S. GAAP, we consolidate their financial results and assets and liabilities in our consolidated financial statements. In September 2015, the contractual arrangements with Beijing Xuncheng were terminated, subsequent to which we continued to consolidate Beijing Xuncheng through voting interest held by New Oriental China.

On May 10, 2018, Dexin Dongfang, a wholly-owned PRC subsidiary of Koolearn, our controlled subsidiary, entered into contractual arrangements with Beijing Xuncheng, its subsidiaries, and its shareholders such that Beijing Xuncheng and its subsidiaries (collectively the Xuncheng VIEs ) are considered variable interest entities for which Koolearn is considered as their primary beneficiary. We believe Koolearn has substantive kick-out rights per the terms of the exclusive option agreement, which gives Koolearn the power to control the shareholders of Beijing Xuncheng. More specifically, we believe that the terms of the exclusive option agreement are currently exercisable and legally enforceable under PRC laws and regulations. We also believe that the minimum amount of consideration permitted by the applicable PRC law to exercise the option does not represent a financial barrier or disincentive for Koolearn to exercise its rights under the exclusive option agreement. A simple majority vote of Koolearn's board of directors is required to pass a resolution to exercise its rights under the exclusive option agreement, for which consent of the

shareholders of Beijing Xuncheng is not required. Therefore, we believe this gives Koolearn the power to direct the activities that most significantly impact the Xuncheng VIEs' economic performance. We believe that Koolearn's ability to exercise effective control, together with the exclusive management consultancy and business cooperation agreement and the equity pledge agreement, give Koolearn the rights to receive substantially all of the economic benefits from the Xuncheng VIEs in consideration for the services provided by Koolearn's wholly-owned subsidiaries in China. Accordingly, as the primary beneficiary of the Xuncheng VIEs and in accordance with U.S. GAAP, we consolidate their financial results and assets and liabilities in our consolidated financial statements.

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## **Table of Contents**

As advised by Tian Yuan Law Firm, our PRC counsel, our corporate structure in China complies with all existing PRC laws and regulations. However, our PRC legal counsel has also advised us that as there are substantial uncertainties regarding the interpretation and application of PRC laws and regulations, and we cannot assure you that the PRC government would agree that our corporate structure or any of the above contractual arrangements comply with current or future PRC laws or regulations. PRC laws and regulations governing the validity of these contractual arrangements are uncertain and the relevant government authorities may have broad discretion in interpreting these laws and regulations. See Item 3. Risk factors D. 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 and Risks Related to Our Corporate Structure We rely on contractual arrangements for our operations in China, which may not be as effective in providing operational control as direct ownership, Risks Related to Our Corporate Structure Our ability to enforce the equity pledge agreements between us and the shareholders our variable interest entities may be subject to limitations based on PRC laws and regulations and Risks Related to Our Corporate Structure 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.

We are a holding company with no material operations of our own. We conduct substantially all of our education business in China through contractual arrangements with the VIEs. See Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Its Shareholder and Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders for a summary of these contractual arrangements. In the fiscal years ended May 31, 2016, 2017 and 2018, the VIEs contributed in aggregate 97.7%, 98.8% and 98.8%, respectively, of our total net revenues. Our operations not conducted through contractual arrangements with the VIEs primarily consist of our kindergarten programs and the leasing of our commercial property. As of May 31, 2017 and 2018, the VIEs accounted for an aggregate of 71.1% and 71.2%, respectively, of our total assets, and 94.6% and 95.8%, respectively, of our total liabilities. The assets not associated with the VIEs primarily consist of cash, investments and commercial property.

### ***Business Combinations***

Business combinations are recorded using the acquisition method of accounting. The purchase price of the acquisition is allocated to the tangible assets, liabilities, identifiable intangible assets acquired and non-controlling interest, if any, based on their estimated fair values as of the acquisition date. The excess of the purchase price over those fair values is recorded as goodwill. Acquisition-related expenses and restructuring costs are expensed as incurred.

In a business combination achieved in stages, we remeasure the previously held equity interest in the acquire immediately before obtaining control at its acquisition-date fair value and the remeasurement gain or loss, if any, is recognized in the consolidated statements of operations.

### ***Share-based Compensation***

Share-based payments to employees and directors are measured based on the grant-date fair value of the equity instrument issued and recognized as compensation expense net of forfeitures on a straight-line basis over the requisite service period, with a corresponding addition to paid-in capital. We use the binomial option pricing model to measure the fair value of options granted and the quoted market price of our company's equity shares to measure the fair value of non-vested equity shares granted to employees at each measurement date. The binomial option pricing model is adopted because we believe that considering the possibility of exercise of an option over the life of the option, as affected by the reality of changing stock prices and non-constant risk free rates, would better reflect the measurement

objective of relevant accounting literature.

## **Table of Contents**

The amount of compensation expense recognized at any date is at least equal to the portion of the fair value of the awards that are vested as of that date. The forfeitures are recognized as they occur.

### ***Cost Method Investments***

For investee companies over which we do not have significant influence or control through investment in common shares or in-substance common shares and which do not have readily determinable fair value, we carry the investment at cost and recognize as income any dividend received from distribution of the investee's earnings.

We review our cost method investments for impairment whenever an event or circumstance indicates that an other-than-temporary impairment has occurred. We consider available quantitative and qualitative evidence in evaluating potential impairment of our cost method investments. An impairment charge is recorded if the cost of an investment exceeds its fair value and such excess is determined to be other-than-temporary.

We estimate the fair value of these investee companies based on the discounted cash flow approach. Factors we consider in making such a determination include general market conditions, the duration and the extent to which the fair value of an investment is less than its cost, and our intent and ability to hold such investment. We did not record any impairment loss on our cost method investments during the years ended May 31, 2016, 2017 and 2018.

### ***Equity Method Investments***

Investee companies over which we have the ability to exercise significant influence, but do not have a controlling interest through investment in common shares or in-substance common shares, are accounted for using the equity method. Significant influence is generally considered to exist when we have an ownership interest in the voting stock of the investee between 20% and 50%. Other factors, such as representation on the investee's board of directors, voting rights and the impact of commercial arrangements, are also considered in determining whether the equity method of accounting is appropriate. For certain investments, where we hold more than 50% equity interest, we may only have significant influence but not control over the investees. For certain investments, where we hold less than a 20% equity or voting interest, we may also have significant influence. Equity method is also used to account for these investments.

Under the equity method, we initially record investments at cost and subsequently recognize proportionate share of each equity investee's net income or loss after the date of investment into earnings and accordingly adjust the carrying amount of the investment.

An impairment charge is recorded if the carrying amount of the investment exceeds its fair value and this condition is determined to be other-than-temporary. We estimated the fair value of the investee company based on comparable quoted price for similar investment in active market, if applicable, or discounted cash flow approach which requires significant judgments, including the estimation of future cash flows, which is dependent on internal forecasts, the estimation of long term growth rate of a company's business, the estimation of the useful life over which cash flows will occur, and the determination of the weighted average cost of capital. We did not record any impairment losses on our equity method investment during the years ended May 31, 2016, 2017 and 2018, respectively.

### ***Available-for-sale Investments***

For investments in investees' preferred shares which are determined to be debt securities, we account for them as long-term available-for-sale investments when they are not classified as either trading or held-to-maturity investments.

Available-for-sale investments are carried at their fair values and the unrealized gains or losses from the changes in fair values are included in accumulated other comprehensive income. Realized gains or losses, and provision for decline in value judged to be other than temporary, if any, are recognized in the consolidated statements of operations.

## **Table of Contents**

We review our investments for other-than-temporary impairment based on the specific identification method. We consider available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds the investment's fair value, we consider, among other factors, general market conditions, government economic plans, the duration and the extent to which the fair value of the investment is less than the cost, our intent and ability to hold the investment, and the financial condition and near term prospects of the investees. We recorded nil, US\$2.3 million and US\$980 thousand impairment losses during the years ended May 31, 2016, 2017 and 2018, respectively.

### ***Non-controlling interests and redeemable non-controlling interests***

Our consolidated financial statements include entities in which we have a controlling financial interest. Earnings or losses attributable to minority shareholders of a consolidated affiliated company are classified separately as non-controlling interest in our consolidated statements of operations.

Non-controlling interests in subsidiaries that are redeemable outside of our control for cash or other assets are classified outside of permanent equity at redemption value. If the redemption event is probable to occur, we adjust the redeemable non-controlling interests to the redemption values on each balance sheet date with changes recognized as an adjustment to retained earnings, or in the absence of retained earnings, as an adjustment to additional paid-in capital.

### ***Income Taxes***

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. Significant judgment is required in determining our provision for income taxes and income tax assets and liabilities, including evaluating uncertainties in the application of accounting principles and complex tax laws.

We account for income taxes using the asset and liability approach. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax bases of assets and liabilities, net of operating loss carry forwards and credits, by applying enacted tax rates that will be in effect for the period in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in the consolidated statements of operations in the period of change. Deferred tax assets are reduced by a valuation allowance when it is considered more likely than not that some portion or all of the deferred tax assets will not be realized.

We account for uncertain tax positions by reporting a liability for unrecognized tax benefits resulting from uncertain tax positions taken or expected to be taken in a tax return. Tax benefits are recognized from uncertain tax positions when we believe that it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. We recognize interest and penalties, if any, related to unrecognized tax benefits in income tax expenses.

Uncertainties exist with respect to how the PRC's Enterprise Income Tax Law applies to our overall operations, and more specifically, with regard to our tax residency status. The Enterprise Income Tax Law includes a provision specifying that legal entities organized outside of the PRC will be considered residents for PRC income tax purposes if their place of effective management or control is within the PRC. The implementation rules to the Enterprise Income Tax Law provide that non-resident legal entities will be considered PRC residents if substantial and overall management and control over the manufacturing and business operations, personnel, accounting, properties, among others, occur within the PRC. Despite the present uncertainties resulting from the limited PRC tax guidance on the



issue, we do not believe that our legal entities organized outside of the PRC should be treated as residents for the Enterprise Income Tax Law's purposes. If one or more of our legal entities organized outside of the PRC were characterized as PRC tax residents, the impact would adversely affect our results of operation. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China 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.

**Table of Contents*****Economic lives and impairment of property and equipment***

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated on a straight line basis over the following estimated useful lives:

Buildings	20-50 years
Transportation equipment	10 years
Furniture and education equipment	5 years
Computer equipment and software	3 years
Leasehold improvements	Shorter of the lease term or estimated useful life

Judgment is required to determine the estimated useful lives of property and equipment, especially for the equipment, including determining how long existing equipment can function and when new technologies will be introduced at cost-effective price points to replace existing equipment. Changes in these estimates and assumptions could materially impact our financial position and results of operations.

We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may no longer be recoverable. When these events occur, we measure impairment by comparing the carrying value of the long-lived assets to the estimated undiscounted future cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flow is less than the carrying amount of the assets, we would recognize an impairment loss based on the fair value of the assets. We did not record any impairment loss on long-lived assets during the years ended May 31, 2016, 2017 and 2018.

***Impairment of goodwill***

Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired in business combinations. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

Goodwill is tested for impairment at the reporting unit level on an annual basis (May 31 of each year) and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in the stock prices, business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and determination of the fair value of each reporting unit. The estimation of fair value of each reporting unit using a discounted cash flow methodology also requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, estimation of the long-term rate of growth for our business, estimation of the useful life over which cash flows will occur, and determination of our weighted average cost of capital. The estimates used to calculate the fair value of a reporting unit change from year to year based on operating results and market conditions. Changes in these estimates and assumptions could materially affect the determination of fair value and goodwill impairment for the reporting unit.

In order to test goodwill for impairment, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If it is more likely than not that the fair value of a reporting unit is less than its carrying amount, goodwill is then tested following a two-step process. The first step compares the fair value of each reporting unit to its carrying amount, including goodwill. If the fair value of each reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step compares the implied fair value of goodwill to the carrying value of a reporting unit's goodwill.

The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill.

**Table of Contents**

We recorded nil, US\$1.7 million and nil impairment losses during the years ended May 31, 2016, 2017 and 2018, respectively.

***Recently Issued Accounting Pronouncements***

Refer to Note 2 to our consolidated financial statements regarding recent issued accounting pronouncements.

**B. Liquidity and Capital Resources**

Our principal source of liquidity has been cash generated from operating activities. As of May 31, 2018, we had US\$983.3 million in cash and cash equivalents. Our cash and cash equivalents consist of cash on hand and liquid investments that are unrestricted as to withdrawal or use, have maturities of three months or less and are placed with banks and other financial institutions. Although we consolidate the results of New Oriental China and its schools and subsidiaries, we do not have direct access to the cash and cash equivalents or future earnings of New Oriental China. However, a portion of the cash balances of New Oriental China and its schools and subsidiaries are paid to our wholly-owned subsidiaries in China pursuant to contractual arrangements for the services our subsidiaries provide to New Oriental China and its schools and subsidiaries.

We expect to require cash to fund our ongoing business needs, particularly the rent and other costs and expenses relating to opening new schools and learning centers. We opened 305 new learning centers and closed 79 existing centers in fiscal year 2018. We plan to continue to add schools and learning centers in the future with a focus on opening new learning centers in fast growing, high profit margin cities. We expect to incur capital expenditures ranging from approximately RMB1.0 million (US\$0.1 million) to RMB4.0 million (US\$0.6 million) per new school depending primarily on the size and geographic location of the school. Other cash needs include acquisitions of businesses and properties that complement our operations when suitable opportunities arise. We have not encountered any difficulties in meeting our cash obligations to date. 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 foreseeable future.

The following table sets forth a summary of our cash flows for the periods indicated:

<i>(in thousands of US\$)</i>	<b>For the Year Ended May 31,</b>		
	<b>2016</b>	<b>2017</b>	<b>2018</b>
Net cash provided by operating activities <sup>(1)</sup>	524,313	622,694	781,127
Net cash used in investing activities	(309,737)	(672,264)	(406,716)
Net cash (used in) provided by financing activities <sup>(1)</sup>	(916)	4,792	(74,881)
Effect of foreign exchange rate changes	(35,749)	(23,413)	42,771
Net change in cash and cash equivalents	177,911	(68,191)	342,301
Cash and cash equivalents at beginning of period	531,298	709,209	641,018
Cash and cash equivalents at end of the period	709,209	641,018	983,319

(1)

The reclassification of the cash flows in the years ended May 31, 2016 and 2017 is due to the adoption of ASU 2016-09 by using the retrospective application.

***Operating Activities***

Net cash provided by operating activities amounted to US\$781.1 million in the fiscal year ended May 31, 2018. Our net cash provided by operating activities in the fiscal year ended May 31, 2018 reflected net income of US\$297.2 million, as adjusted by the reconciliation of certain non-cash items, including US\$77.1 million in depreciation and US\$57.4 million in share-based compensation expense. Additional factors affecting operating cash flow included an increase in the deferred revenues in the amount of US\$334.4 million due to the increased amount of course fees received during the period, and an increase in the accrued expenses and other current liabilities account of US\$68.2 million, primarily due to an increase in accrued employee salary expenses and welfare benefits.

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**Table of Contents**

Net cash provided by operating activities amounted to US\$622.7 million in the fiscal year ended May 31, 2017. Our net cash provided by operating activities in the fiscal year ended May 31, 2017 reflected net income of US\$276.8 million, as adjusted by the reconciliation of certain non-cash items, including US\$53.9 million in depreciation and US\$20.3 million in share-based compensation expense. Additional factors affecting operating cash flow included an increase in deferred revenues in the amount of US\$237.6 million due to the increased amount of course fees received during the period, and an increase in the accrued expenses and other current liabilities account of US\$40.3 million, primarily due to an increase in accrued employee salary expenses and welfare benefits.

Net cash provided by operating activities amounted to US\$524.3 million in the fiscal year ended May 31, 2016. Our net cash provided by operating activities in the fiscal year ended May 31, 2016 reflected net income of US\$225.3 million, as adjusted by the reconciliation of certain non-cash items, including US\$47.3 million in depreciation and US\$16.8 million in share-based compensation expense. Additional factors affecting operating cash flow included an increase in deferred revenues in the amount of US\$179.6 million due to the increased amount of course fees received during the period, and an increase in the accrued expenses and other current liabilities account of US\$54.4 million, primarily due to an increase in accrued employee salary expenses and welfare benefits.

***Investing Activities***

We lease all of our facilities except for part of the premises for the Beijing, Xi'an, Tianjin, Kunming, Wuhan, Guangzhou, Changsha, Xiamen, Zhengzhou, Hangzhou and Yangzhou schools, which premises we own. Our cash used in investing activities is primarily related to our purchase of land use rights and the premises for the facilities we own and equipment used in our operations, our investment in term deposits and short term investments. Net cash used in investing activities amounted to US\$406.7 million in the fiscal year ended May 31, 2018, compared to US\$672.3 million in the fiscal year ended May 31, 2017 and US\$309.7 million in the fiscal year ended May 31, 2016.

Net cash used in investing activities in the fiscal year ended May 31, 2018 was primarily attributable to net purchase of short term held-to-maturity investments in the amount of US\$224.5 million, long term available-for-sale investments in the amount of US\$55.2 million and the purchase of property and equipment in the amount of US\$214.3 million in connection with the expansion of our school network.

Net cash used in investing activities in the fiscal year ended May 31, 2017 was primarily attributable to net purchase of short term held-to-maturity investments in the amount of US\$522.8 million, long term available for sale investments in the amount of US\$43.5 million and the purchase of property and equipment in the amount of US\$105.7 million in connection with the expansion of our school network.

Net cash used in investing activities in the fiscal year ended May 31, 2016 was primarily attributable to net purchase of short term held-to-maturity investments in the amount of US\$260.9 million, long term available for sale investments in the amount of US\$78.8 million and the purchase of property and equipment in the amount of US\$64.4 million in connection with the expansion of our school network.

***Financing Activities***

Net cash used in financing activities amounted to US\$74.8 million in the fiscal year ended May 31, 2018, compared to net cash provided by financing activities of US\$4.8 million in the fiscal year ended May 31, 2017 and net cash used in financing activities of US\$0.9 million in the fiscal year ended May 31, 2016.

Net cash used in financing activities in the fiscal year ended May 31, 2018 was primarily attributable to dividend paid to the shareholders in the amount of US\$71.2 million.

Net cash provided by financing activities in the fiscal year ended May 31, 2017 was primarily attributable to capital contribution from noncontrolling interests of US\$8.8 million.

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**Table of Contents**

Net cash used in financing activities in the fiscal year ended May 31, 2016 was primarily attributable to investment of RMB445.7 million (US\$68.3 million) by investors into Beijing Xuncheng, a subsidiary of New Oriental China and cash dividend in the amount of US\$62.7 million.

**Holding Company Structure***Overview*

We are a holding company with no material operations of our own. We conduct substantially all of our education business in China through contractual arrangements with our variable interest entities, and their schools and subsidiaries and shareholders. See Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Its Shareholder and Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders for a summary of these contractual arrangements. In the fiscal years ended May 31, 2016, 2017 and 2018, our variable interest entity(ies) contributed in aggregate 97.7%, 98.8% and 98.8%, respectively, of our total net revenues. Our operations not conducted through contractual arrangements with our variable interest entities primarily consist of our kindergarten programs and the leasing of our commercial property. As of May 31, 2017 and 2018, our variable interest entity(ies) accounted for an aggregate of 71.1% and 71.2%, respectively, of our total assets, and 94.6% and 95.8%, respectively, of our total liabilities. The assets not associated with our variable interest entity(ies) primarily consist of cash and cash equivalents, term deposits and short-term investments. As of May 31, 2017 and 2018, US\$75.9 million and US\$105.0 million, respectively, of these assets were denominated in U.S. dollars, and US\$441.2 million and US\$454.6 million, respectively, of these assets were denominated in RMB.

As a holding company, our ability to pay dividends and other cash distributions to our shareholders depends in part upon dividends and other distributions paid to us by our PRC subsidiaries. The amount of dividends paid by our PRC subsidiaries to us primarily depends on the service fees paid to our PRC subsidiaries from our variable interest entity(ies), and, to a lesser degree, our PRC subsidiaries' retained earnings. As of May 31, 2016, 2017 and 2018, the total amount of service fees payable to our PRC subsidiaries from our variable interest entity(ies) under the service agreements was US\$262.7 million, US\$267.5 million and US\$369.6 million, respectively. Conducting our operations through contractual arrangements with our variable interest entities entails a risk that we may lose the power to direct the activities that most significantly affect the economic performance of our variable interest entities, which may result in our being unable to consolidate their financial results with our results and may impair our access to their cash flow from operations and thereby reduce our liquidity. See Item 3. Risk Factors D. Risks Related to Our Corporate Structure for more information, including the risk factors titled 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 and We rely on contractual arrangements for our operations in China, which may not be as effective in providing operational control as direct ownership.

*Dividend Distributions*

Under PRC law, each of our PRC subsidiaries, variable interest entities and their respective subsidiaries which is not a for-profit private school is required to set aside at least 10% of its after-tax profits each year, if any, to fund a statutory surplus reserve until such reserve reaches 50% of its registered capital and to further set aside a portion of its after-tax profit to fund the reserve fund at the discretion of our board of directors. Although the statutory reserves can be used, among other ways, to increase the registered capital and eliminate future losses in excess of retained earnings of the respective companies, the reserve funds are not distributable as cash dividends except in the event of liquidation. In addition, each of our schools that requires or does not requires reasonable returns in China is required to allocate a certain amount out of its annual net income or annual increase in the net assets, if any, to its development fund for the



construction or maintenance of the school or procurement or upgrade of educational equipment. For our schools which have elected to require reasonable returns, this amount shall be no less than 25% of the annual net income of the school, and for our schools which have elected not to 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. Upon the effectiveness of the Amended Law for Promoting Private Education in September 2017, sponsors of for-profit private schools are entitled to retain the profits and proceeds from the schools and the operation surplus may be allocated to the sponsors pursuant to the PRC Company Law and other relevant laws and regulations. Our PRC subsidiaries are permitted to pay dividends to us only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations.

**Table of Contents**

Pursuant to contractual arrangements that our wholly-owned subsidiaries in China have with our variable interest entities, the earnings and cash of variable interest entities and their schools and subsidiaries are used to pay service fees in RMB to our PRC subsidiaries in the manner and amount set forth in these agreements. After paying the applicable withholding taxes and making appropriations for its statutory reserve requirement, the remaining net profits of our PRC subsidiaries would be available for distribution to three Hong Kong-incorporated intermediate holding companies wholly owned by our company, and from these three Hong Kong-incorporated intermediate holding companies to our company. See Item 4. Information on the Company C. Organizational Structure for a diagram of our corporate structure. As of May 31, 2018, the net assets of our PRC subsidiaries and variable interest entities and their schools and subsidiaries which were restricted due to statutory reserve requirements and other applicable laws and regulations, and thus not available for distribution, were in aggregate US\$542.5 million, and the net assets of our PRC subsidiaries and variable interest entities and their schools and subsidiaries which were unrestricted and thus available for distribution were in aggregate US\$1,440.2 million. We do not believe that these restrictions on the distribution of our net assets will have a significant impact on our ability to timely meet our financial obligations in the future. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China 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 for more information.

Furthermore, cash transfers from our PRC subsidiaries to our Hong Kong-incorporated intermediate holding companies are subject to PRC government control of currency conversion. Restrictions on the availability of foreign currency may affect 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. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China Governmental control of currency conversion may affect the value of your investment.

**Capital Expenditures**

The expansion of our network of schools, learning centers, O2O ecosystem and bookstores has required significant investment. Our capital expenditures were US\$64.4 million, US\$105.7 million and US\$214.3 million in the fiscal years ended May 31, 2016, 2017 and 2018, respectively. Our capital expenditures are incurred primarily in connection with facility acquisitions, leasehold improvements and investments in equipment, technology and operating systems. Our capital expenditures for the fiscal year ended May 31, 2018 were primarily due to our investments in facilities, equipment, technology and operating systems to meet the expected growth of our operations. We intend to cost-efficiently allocate our capital resources by leasing most of our new facilities in the foreseeable future. We may also make acquisitions of businesses and properties that complement our operations when suitable opportunities arise. We believe that we will be able to fund our capital needs in the foreseeable future through cash generated from our operating activities.

**C. Research and Development, Patents and Licenses, etc.****Technology**

Our technology platform is designed to provide systems that help distinguish us in the marketplace, operate cost-effectively and accommodate future growth. We currently use a combination of commercially available and custom developed software and hardware systems. Our technology platform is a combination of e-learning platforms, alumni platforms, content management systems, exam platforms, e-business promotion platforms and bookstore platforms, live Internet classrooms, as well as licensed speech recognition platforms. Our investment in system

infrastructure has several key benefits: simplification of the storage and processing of large amounts of data, facilitation of the deployment and operation of large-scale programs and services and automation of much of the administration of our business. It also provides us with the ability to scale both capacity and functionality and build large clusters seamlessly.

One of our ongoing primary objectives is to maintain reliable systems. We have implemented performance monitoring for all key web and business systems to enable us to respond quickly to potential problems. Based on cluster technology, our system can identify errors and isolate failed servers automatically so that our clients can access our services at any time. Our websites are hosted at third party facilities in Beijing. This facility provides redundant utility systems, a backup electric generator and 24-hour a day server support. All servers have redundant power supplies and file systems to maximize system and data availability. We regularly back up our database on a server hosted at an Internet data center to minimize the impact of data loss due to system failures. We do not capitalize any related costs.

## Table of Contents

### **Intellectual Property**

Our trademarks, copyrights, trade secrets and other intellectual property rights distinguish our services and products from those of our competitors and contribute to our competitive advantage in our target markets. To protect our brand and other intellectual property, we rely on a combination of trademark, copyright and trade secret laws as well as confidentiality agreements with our employees, contractors and others. , New Oriental, , and are registered trademarks in China and have been recognized as well-known trademarks ( ) in civil action adjudicated and/or administrative determination in China. We have also registered additional trademarks and logos, including Pop Kids, with the Trademark Office of the State Administration for Industry and Commerce in China. Our main websites are located at [www.xdf.cn](http://www.xdf.cn), [www.neworiental.org](http://www.neworiental.org), [english.neworiental.org](http://english.neworiental.org), and [www.koolearn.com](http://www.koolearn.com). In addition, we have registered other domain names, including [www.dogwood.com.cn](http://www.dogwood.com.cn), [www.popkids.com.cn](http://www.popkids.com.cn), [www.young.com](http://www.young.com), [www.ileci.com](http://www.ileci.com), [www.okayzhahui.com](http://www.okayzhahui.com), [www.51zhishang.com](http://www.51zhishang.com), [www.donut.cn](http://www.donut.cn), [www.maxen.com.cn](http://www.maxen.com.cn), [www.51pigai.com](http://www.51pigai.com) and [www.66xue.com](http://www.66xue.com).

In order to develop, improve, market and deliver new programs and services, we are required to obtain licenses from others from time to time. For example, we currently have arrangements with international education content providers and publishers such as British Council, Cengage Learning, Monash College Pty Ltd, NCUK, International Baccalaureate, Bell Education, ETS, Cambridge University Press, Cambridge English Language Assessment, The McGraw-Hill Companies, Oxford University Press, Harper Collins, ACT, Stanford University, Carnegie Mellon University, or their respective authorized local publishers, to develop and distribute localized versions of specified books in China. There can be no assurance that we will be able to continue to obtain licenses on commercially reasonable terms or at all or that rights granted under any licenses will be valid and enforceable

We cannot be sure that our efforts to protect our intellectual property rights will be adequate or that third parties will not infringe or misappropriate these rights. In addition, there can be no assurance that competitors will not independently develop similar intellectual property. If others are able to copy and use our programs and services, we may not be able to maintain our competitive position. 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 litigation is necessary to enforce our intellectual property rights or determine the scope of the proprietary rights of others, we may have to incur substantial costs or divert other resources, which could harm our business

In addition, competitors, content providers, publishers and others may claim that we have infringed their intellectual property rights. Defending any such lawsuit, whether with or without merit, could be time-consuming, result in costly litigation or prevent us from offering our programs and services, which could harm our business. If a lawsuit against us is successful, we may lose the rights to use our products or be required to modify them, or we may have to pay financial damages.

We have adopted guidelines, procedures and safeguards designed to educate our employees and contractors regarding the importance of respecting the intellectual property rights of third parties, and detect and prevent any conduct or activities by our employees or contractors that infringe or have the potential to infringe upon such third-party rights. The guidelines specify certain key principles and policies that we require all of our employees and contractors to uphold as a fundamental condition of their employment. The procedures and safeguards we have implemented to ensure compliance with these principles and policies include the assignment of dedicated staff to monitor and enforce compliance with these intellectual property guidelines, including in particular our content control group, which reviews the content of our course materials to ensure that no infringing materials are used in our classrooms. We have also made efforts to ensure that our marketing materials are reviewed and approved by appropriate management before being distributed to the public. We believe these guidelines, procedures and safeguards will further improve our ability to avoid infringing or potentially infringing activities, minimize our exposure to third party claims and

protect our reputation as a company that respects the intellectual property rights of third parties.

**Table of Contents****D. Trend Information**

Other than as disclosed elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events since the beginning of our fiscal year 2018 that are reasonably likely to have a material effect on our net revenues, income from operations, profitability, liquidity or capital resources, or that would cause the disclosed financial information to be not necessarily indicative of future operating results or financial condition.

**E. Off-balance Sheet Arrangements**

We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as shareholders' equity, or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

**F. Tabular Disclosure of Contractual Obligations**

The following table sets forth our contractual obligations as of May 31, 2018:

<i>(in thousands of US\$)</i>	<b>Total</b>	<b>Payment due by period</b>			
		<b>Less than 1 year</b>	<b>1-3 years</b>	<b>3-5 years</b>	<b>More than 5 years</b>
Operating Lease Obligations <sup>(1)</sup>	1,257,462	296,575	496,811	299,632	164,444
Purchase and Leasehold Improvements Obligations <sup>(2)</sup>	31,987	31,987			
<b>Total</b>	<b>1,289,450</b>	<b>328,562</b>	<b>496,811</b>	<b>299,632</b>	<b>164,444</b>

(1) Represents lease obligations under our facility leases.

(2) Represents leasehold improvement obligations in connection with renovations of the leased facilities.

**ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES****A. Directors and Senior Management**

The following table sets forth information regarding our executive officers and directors as of the date of this annual report.

<b>Name</b>	<b>Age</b>	<b>Position/Title</b>
Michael Minhong Yu	55	Executive Chairman
Chenggang Zhou	56	Director and Chief Executive Officer
Zhihui Yang	44	Chief Financial Officer

Louis T. Hsieh	54	Director
Robin Yanhong Li	49	Independent Director
Denny Lee	50	Independent Director
John Zhuang Yang	63	Independent Director

*Mr. Michael Minhong Yu* is the founder of our company and has served as the chairman of our board of directors since 2001. He was also our chief executive officer from 2001 to September 2016. Mr. Yu also serves as vice chairman of the Beijing Young Entrepreneurs Association and vice chairman of the Committee of Education of the Central Committee of the China Democratic League. Prior to founding our first school in 1993, Mr. Yu was an English instructor at Peking University from 1985 and 1991. Mr. Yu received his bachelor's degree in English from Peking University.

*Mr. Chenggang Zhou* has served as our director since November 2010 and chief executive officer since September 2016. Mr. Zhou joined New Oriental in 2000 and has held multiple positions in our company since then, including president, executive president for domestic business, executive vice president, vice president and president of Beijing and Shanghai New Oriental Schools. Prior to joining us, Mr. Zhou was a correspondent for the Asia Pacific region and a program host at BBC. Mr. Zhou received his bachelor's degree in English from Suzhou University in China and his master's degree in communications from Macquarie University, Australia.

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**Table of Contents**

*Mr. Zhihui Yang* has served as our chief financial officer since April 2015. Prior to that, Mr. Yang held multiple positions after he joined our company in April 2006, including vice president of finance, deputy director of president office and senior financial manager. Prior to joining us, Mr. Yang served as the financial director of Beijing Hua De Xin Investment Co., Ltd. from July 2002 to March 2006. From August 1997 and May 2002, Mr. Yang worked for PricewaterhouseCoopers as a senior auditor. Mr. Yang received his bachelor's degree in economics from Guanghua School of Management of Peking University.

*Mr. Louis Hsieh* has served as our director since March 2007 and senior advisor since January 2016. From May 2009 to January 2016, Mr. Hsieh served as our president, and from December 2005 to April 2015, he served as our chief financial officer. Mr. Hsieh currently serves as the chief financial officer of NIO Inc., a NYSE listed company and a pioneer in China's premium electric vehicle market. He is also an independent director and chairman of audit committee for each of JD.com, Inc., China's largest direct sales internet company, and YUM China Holdings, a NYSE-listed restaurant company operating KFC, Pizza Hut, Little Sheep Hot Pot, Taco Bell in China. Prior to joining us in 2005, Mr. Hsieh was the chief financial officer of ARIIO Data Networks, Inc. in San Jose, California from 2004 to 2005. Prior to that, Mr. Hsieh was a managing director for private equity firm of Darby Asia Investors (HK) Limited from 2002 to 2003. From 2000 to 2002, Mr. Hsieh was managing director and Asia-Pacific tech/media/telecoms head of UBS Capital Asia Pacific, the private equity division of UBS AG. From 1997 to 2000, Mr. Hsieh was a technology investment banker at JP Morgan in San Francisco, California, where he was a vice president, and Credit Suisse First Boston in Palo Alto, California, where he was an associate. From 1990 to 1996, Mr. Hsieh was a corporate and securities attorney at White & Case LLP in Los Angeles. Mr. Hsieh holds a bachelor's degree in Industrial Engineering and Engineering Management from Stanford University, an MBA degree from the Harvard Business School, and a J.D. degree from the University of California at Berkeley.

*Mr. Robin Yanhong Li* has served as our independent director since September 6, 2006. Mr. Li is a co-founder of Baidu, Inc., the leading Chinese language Internet search provider listed on the Nasdaq Global Select Market. Mr. Li has served as the chairman of the board of directors of Baidu since its inception in January 2000 and as its chief executive officer since January 2004. He served as the president of Baidu from February 2000 to December 2003. Prior to founding Baidu, Mr. Li worked as an engineer at Infoseek, a pioneer in the Internet search engine industry, from July 1997 to December 1999. Currently, Mr. Li acts as the vice chairman of the Internet Society of China (ISC). Mr. Li has also been a vice chairman of All-China Federation of Industry & Commerce since December 2012. Mr. Li received a bachelor's degree in information science from Peking University and a master's degree in computer science from the State University of New York at Buffalo.

*Mr. Denny Lee* has served as our independent director since September 6, 2006. Mr. Lee has served as a director of NetEase, Inc., formerly known as Netease.com, Inc., a leading internet technology company in China listed on the Nasdaq Global Select Market, since April 2002. He was the chief financial officer of NetEase, Inc. from April 2002 to June 2007 and its financial controller from November 2001 to April 2002. Prior to joining NetEase, Inc. in 2001, Mr. Lee worked in the Hong Kong office of KPMG for more than ten years. Mr. Lee currently serves as the chairman of the audit committees and an independent non-executive director on the boards of Concord Medical Services Holdings Limited, Jianpu Technology Inc. and NIO Inc., which are listed on the New York Stock Exchange, and as an independent non-executive director on the board of China Metal Resources Utilization Ltd., which is listed on the main board of Hong Kong Stock Exchange. Mr. Lee graduated from the Hong Kong Polytechnic University majoring in accounting and is a member of The Hong Kong Institute of Certified Public Accountants and The Chartered Association of Certified Accountants.

*Dr. John Zhuang Yang* has served as our independent director since September 3, 2007. Dr. Yang is currently the Dean of the Beijing International M.B.A. Program at Peking University. He also serves as a full-time professor at National School of Development of Peking University and holds a tenured professorship at Fordham University's



graduate school of business. Dr. Yang currently also serves as an independent director of Tristate Holdings Limited, a company listed on the Hong Kong Stock Exchange. Dr. Yang holds a Ph.D. degree in business administration from Columbia University, a master's degree in sociology from Columbia University, a master's degree in international and public affairs from the Woodrow Wilson School of Public and International Affairs at Princeton University, and a bachelor's degree from the English Language and Literature Department of Peking University.

## **Table of Contents**

### **Employment Agreements**

We have entered into employment agreements with each of our executive officers. We may terminate employment for cause, at any time, without notice or remuneration, for certain acts of the executive officer, such as a conviction of or plea of guilty to a felony, negligence or dishonesty to our detriment and failure to perform agreed duties after a reasonable opportunity to cure the failure, death, or physical or mental incapacitation. We may also terminate an executive officer's employment without cause. In such case we are required to provide severance compensations as expressly required by applicable law. An executive officer may terminate his employment with us at any time with a one-month prior notice if there is a material reduction in his or her authority, duties and responsibilities or if there is a material reduction in his or her annual salary before the next annual salary review. An executive officer may also resign prior to the expiry of the term of his or her employment agreement if our board approves his or her resignation or agrees to an alternative arrangement with such executive officer.

Each executive officer has agreed to hold, both during and after the termination or expiry of his or her employment agreement, in strict confidence and not to use, except as required in the performance of his or her duties in connection with the employment, any of our confidential information or trade secrets, any confidential information or trade secrets of our clients or prospective clients, or the confidential or proprietary information of any third party received by us and for which we have confidential obligations. Our executive officers have also agreed to disclose in confidence to us all inventions, designs and trade secrets which they conceive, develop or reduce to practice and to assign all right, title and interest in them to us, and assist us in obtaining patents, copyrights and other legal rights for these inventions, designs and trade secrets. In addition, each executive officer has agreed to be bound by non-competition and non-solicitation restrictions during the term of his or her employment and one year following the termination or expiry of such employment agreement. Specifically, each executive officer has agreed not to (1) approach our clients, customers or contacts or other persons or entities introduced to the executive officer for the purpose of doing business with such person or entities that will harm our business relationships with these persons or entities; (2) assume employment with or provide services as a director for any of our competitors, or engage, whether as principal, partner, licensor or otherwise, in any business which is in direct or indirect competition with our business or (3) seek directly or indirectly, to solicit the services of any of our employees who is employed by us on or after the date of the executive officer's termination, or in the year preceding such termination.

### **B. Compensation of Directors and Executive Officers**

For the fiscal year ended May 31, 2018, we paid an aggregate of approximately US\$2.7 million in cash to our executive officers and non-executive directors as a group. In addition, we made contributions to the pension insurance, medical insurance, housing fund, unemployment and other benefits for the benefits of our executive officers and non-executive directors in the aggregate amount of US\$108,000. See Share Incentives below for more information. No executive officer is entitled to any severance benefits upon termination of his employment with our company except as required under applicable PRC law.

### **Share Incentives**

#### ***2006 Share Incentive Plan***

Our 2006 Share Incentive Plan, as amended, or the 2006 plan, is designed to attract and retain the best available personnel, provide additional incentives to employees, directors and consultants and promote the success of our business. The maximum aggregate number of shares which may be issued pursuant to all awards (including options) granted under the 2006 plan is 8,000,000 shares, plus (1) 5,000,000 shares added on January 1, 2007, (2) 5,000,000

shares added on January 1, 2008 and (3) an annual increase on the first business day of each calendar year beginning in 2009 equal to the lesser of (x) 3,000,000 shares, (y) two percent (2%) of the number of shares outstanding as of such date, and (z) a lesser number of shares determined by the administrator of the 2006 plan. The 2006 plan expired in January 2016. No additional awards may be granted under the 2006 plan after its expiration, but the expiration of the plan would not impair any award previously granted under the plan.

## **Table of Contents**

The following paragraphs describe the principal terms of the 2006 plan.

*Types of Awards.* We may grant the following types of awards under our 2006 plan:

options to purchase our common shares;

restricted shares, which are common shares issued to the grantee that are subject to transfer restrictions, right of first refusal, repurchase, forfeiture, and other terms and conditions as established by our plan administrator; and restricted share units, which may be earned upon the passage of time or the attainment of performance criteria and which may be settled for cash, common shares or other securities, or a combination of cash, common shares or other securities as established by our plan administrator;

share appreciation rights, which entitle the grantee the right to common shares or cash compensation measured by the appreciation in the value of common shares; and

dividend equivalent rights, which entitle the grantee to compensation measured by dividends paid with respect to common shares.

*Plan Administration.* Our board of directors, or a committee designated by our board or directors, administers the 2006 plan. The committee or the full board of directors, as appropriate, determines the provisions and terms and conditions of each award grant.

*Award Agreement.* Awards granted under our 2006 plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each award. In addition, the award agreement also specifies whether the option constitutes an incentive share option, or ISO, or a non-qualifying stock option.

*Eligibility.* We may grant awards to our employees, directors and consultants, including those of our parent companies and subsidiaries. However, we may grant options that are intended to qualify as ISOs only to our employees and employees of our parent companies and subsidiaries.

*Acceleration of Awards upon Corporate Transactions.* The outstanding awards will terminate and accelerate upon occurrence of certain significant corporate transactions, including amalgamations, consolidations, liquidations or dissolutions, sales of substantially all or all of the assets, reverse takeovers or acquisitions resulting in a change of control. If the successor entity assumes or replaces our outstanding awards under the 2006 plan, such assumed or replaced awards will become fully vested and immediately exercisable and payable, and be released from repurchase or forfeiture rights immediately upon termination of the grantee's continuous service to us if such service is terminated by the successor entity without cause within 12 months after the effective date of the corporate transaction. Furthermore, if the successor entity does not assume or replace our outstanding awards, each outstanding award will become fully vested and immediately exercisable and payable, and will be released from any repurchase or forfeiture rights immediately before the effective date of the corporate transaction, as long as the grantee's continuous service with us has not been terminated before this date.

*Exercise Price and Term of Awards.* In general, the plan administrator determines the exercise price of an option and sets forth the price in the award agreement. The exercise price may be a fixed or variable price related to the fair

market value of our common shares. In September 2012, we amended the 2006 plan to clarify that the plan administrator has the power to reduce the exercise price of an outstanding option and also reduce the number of the underlying common shares without seeking shareholders' approval, if such modification would not result in significant additional share-based compensation expenses to be incurred by our company.

The term of each award under our 2006 plan will be specified in an award agreement, but the term of an ISO shall not exceed ten years from the date of grant thereof.

*Vesting Schedule.* In general, one-sixth of the common shares underlying the option will vest on each six-month anniversary of the vesting commencement date specified in the option award notice. The vesting will be suspended if the grantee's leave of absence exceeds 90 days and will resume upon the grantee's return to service to us. The vesting schedule of equity share awards is subject to the applicable award agreement.

### ***2016 Share Incentive Plan***

We adopted our 2016 Share Incentive Plan, or the 2016 plan, in January 2016 to continue to provide incentives to employees, directors and consultants after the expiration of our 2006 plan. The maximum aggregate number of shares which may be issued pursuant to all awards (including options) granted under the 2016 plan is 10,000,000 shares.

**Table of Contents**

The following paragraphs describe the principal terms of the 2016 plan.

*Amendment of the Plan.* Our board of director may at any time amend, suspend or terminate the 2016 plan. Unless we decide to follow home country practice, the following amendments to the 2016 plan require approval from our shareholders (i) increase of the number of shares available under the 2016 plan, (ii) extension of the term of the 2016 plan, (iii) extension of the exercise period of an option beyond ten years, and (iv) any other amendments about which shareholders' approval are necessary and desirable under applicable laws or stock exchange rules.

The remaining terms of the 2016 plan are substantially identical to the terms of the 2006 plan described above.

The following table summarizes, as of September 21, 2018, the outstanding non-vested equity shares granted under our 2006 plan and 2016 plan to several of our directors and executive officers.

Name	Common Shares		Date of Grant	Date of Expiration
	Underlying Outstanding NES	Exercise Price (US\$/Share)		
Chenggang Zhou	*		10/27/2017	12/31/2020
Zhihui Yang	*		10/27/2017	12/31/2020
Louis T. Hsieh	*		10/27/2017	12/31/2020

\* Less than 1% of our total outstanding voting securities.  
Non-vested equity share awards.

***Koolearn Share Incentive Plan***

On 13 July 2018, Koolearn adopted a share option plan, or the Koolearn Share Option Plan to provide incentives to directors and employees of Koolearn and its consolidated affiliated entities. The overall limit on the number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised in accordance with the Koolearn Share Option Plan must not exceed 47,836,985 ordinary shares of Koolearn. To date, options to obtain an aggregate of 27,904,930 ordinary shares of Koolearn have been conditionally granted under the plan and no options are granted to our directors or executive officers. The exercise price of all the options granted under the plan is HK\$8.88 (US\$1.13) per share.

**C. Board Practices**

Our board of directors currently consists of six directors, which consist of three independent directors and three directors who are, or have been within the past three years, also our executive officers. Section 303A.01 of the NYSE Listed Company Manual requires each listed company to have a majority of independent directors on the board of directors after the first anniversary of the company's listing on the NYSE. We are not required under the laws of the Cayman Islands to have a majority of independent directors on our board of directors. Pursuant to the exception granted to foreign private issuers under Section 303A.00 of the NYSE Listed Company Manual, we have elected to follow our home country practice with respect to our board of directors. A director is not required to hold any shares in the company by way of qualification. A director may vote with respect to any contract, proposed contract or arrangement in which he is materially interested. A director may exercise all the powers of the company to borrow money, mortgage its undertaking, property and uncalled capital, and issue debentures or other securities whenever

money is borrowed or as security for any obligation of the company or of any third party. Our independent directors hold executive sessions, during which only the independent directors are present, at least once a year. Depending on the nature of the discussion at an executive session, each of the three independent directors may preside at the executive sessions. In the fiscal year ended May 31, 2018, our board held meetings or passed resolutions by unanimous written consent 15 times.

### **Committees of the Board of Directors**

We have established three fully independent committees under the board of directors: the audit committee, the compensation committee and the nominating and corporate governance committee. We have adopted a charter for each of the three committees. The committee charters are available on our website at <http://investor.neworiental.org>. Each committee's members and functions are described below.

**Table of Contents**

*Audit Committee.* Our audit committee consists of Mr. Denny Lee, Mr. Robin Yanhong Li and Dr. John Zhuang Yang. Mr. Lee is the chairman of our audit committee. All of the members of our audit committee satisfy the independence requirements of Section 303A of the NYSE Listed Company Manual and Rule 10A-3 under the Exchange Act. Our board of directors has determined that Mr. Denny Lee's simultaneous service on the audit committee of two other public companies would not impair his ability to effectively serve on our audit committee. The audit committee oversees our accounting and financial reporting processes and the audits of the financial statements of our company. The audit committee is responsible for, among other things:

selecting the independent registered public accounting firm and pre-approving all auditing and non-auditing services permitted to be performed by the independent registered public accounting firm;

reviewing with the independent registered public accounting firm any audit problems or difficulties and management's response;

reviewing and approving all proposed related party transactions, as defined in Item 404 of Regulation S-K under the U.S. Securities Act of 1933, as amended;

discussing the annual audited financial statements with management and the independent registered public accounting firm;

reviewing major issues as to the adequacy of our internal controls and any special audit steps adopted in light of material control deficiencies; and

meeting separately and periodically with management and the independent registered public accounting firm.

In the fiscal year ended May 31, 2018, the audit committee held meetings or passed resolutions by unanimous written consent twice, and also approved certain other matters together with the rest of the board members four times, including the audit committee's approval of four quarterly earnings releases.

*Compensation Committee.* Our compensation committee consists of Mr. Robin Yanhong Li, Mr. Denny Lee and Dr. John Zhuang Yang. Mr. Li is the chairman of our compensation committee. All of the members of our compensation committee satisfy the independence requirements of Section 303A of the NYSE Listed Company Manual. The compensation committee assists the board in reviewing and approving the compensation structure, including all forms of compensation, relating to our directors and executive officers. Our chief executive officer may not be present at any committee meeting during which his compensation is deliberated. The compensation committee is responsible for, among other things:

reviewing and approving the total compensation package for our chief executive officer;



reviewing and recommending to the board with respect to the compensation of our directors; and

reviewing periodically and approving any long-term incentive compensation or equity plans, programs or similar arrangements, annual bonuses, and employee pension and welfare benefit plans.

In the fiscal year ended May 31, 2018, the compensation committee passed resolutions by unanimous written consent once, and also approved certain matters together with the rest of the board members once.

## **Table of Contents**

*Nominating and Corporate Governance Committee.* Our nominating and corporate governance committee consists of Dr. John Zhuang Yang, Mr. Robin Yanhong Li and Mr. Denny Lee. Dr. Yang is the chairman of our nominating and corporate governance committee. All of the members of our nominating and corporate governance committee satisfy the independence requirements of Section 303A of NYSE Listed Company Manual. The nominating and corporate governance committee assists the board of directors in selecting individuals qualified to become our directors and in determining the composition of the board and its committees. The nominating and corporate governance committee is responsible for, among other things:

selecting and recommending to the board nominees for election or re-election to the board, or for appointment to fill any vacancy;

reviewing annually with the board the current composition of the board with regards to characteristics such as independence, age, skills, experience and availability of service to us;

advising the board periodically with regards to significant developments in the law and practice of corporate governance as well as our compliance with applicable laws and regulations, and making recommendations to the board on all matters of corporate governance and on any remedial action to be taken; and

monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our procedures to ensure proper compliance.

In the fiscal year ended May 31, 2018, the nominating and corporate governance committee approved certain matters together with the rest of the board members once.

## **Duties of Directors**

Under Cayman Islands law, our directors have a duty of loyalty to act honestly in good faith with a view to our best interests. Our directors also have a duty to exercise the skill they actually possess and such care and diligence that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association. A shareholder has the right to seek damages if a duty owed by our directors is breached.

## **Terms of Directors and Officers**

Our officers are elected by and serve at the discretion of the board of directors. Our directors are not subject to a term of office and hold office until such time as they resign or are removed from office by ordinary resolution or the unanimous written resolution of all shareholders. A director will be removed from office automatically if, among other things, the director (1) becomes bankrupt or makes any arrangement or composition with his creditors; or (2) dies or is found by our company to be or becomes of unsound mind.

## **D. Employees**

We had 28,690, 34,217 and 44,531 full time employees and 7,993, 8,767 and 9,711 contract teachers and staff as of May 31, 2016, 2017 and 2018, respectively. Our employees are not covered by any collective bargaining agreement. We consider our relations with our employees to be generally good.

E. Share Ownership

The following table sets forth information with respect to the beneficial ownership of our common shares by:

each of our directors and executive officers; and

each person known to us who owns beneficially more than 5% of our common shares.

Except as specifically noted, the beneficial ownership is as of September 21, 2018.

**Table of Contents**

	Shares Beneficially Owned	
	Number <sup>(1)</sup>	% <sup>(2)</sup>
<b>Directors and Executive Officers:</b>		
Michael Minhong Yu <sup>(3)</sup>	20,664,600	13.0
Chenggang Zhou	*	*
Zhihui Yang	*	*
Louis T. Hsieh	*	*
Robin Yanhong Li	*	*
Denny Lee	*	*
John Zhuang Yang	*	*
All Directors and Executive Officers as a Group <sup>(4)</sup>	21,480,619	13.5
<b>Principal Shareholders:</b>		
Tigerstep Developments Limited <sup>(5)</sup>	20,664,600	13.0
UBS Group AG. <sup>(6)</sup>	18,950,228	11.9

\* Less than 1%

- (1) Beneficial ownership is determined in accordance with the rules of the SEC.
- (2) For each person and group included in this table, percentage ownership is calculated by dividing the number of shares beneficially owned by such person or group by the sum of (i) 158,690,714, being the number of common shares outstanding as of September 21, 2018 and (ii) the number of common shares underlying share options held by such person or group that are exercisable within 60 days after September 21, 2018 and the number of non-vested equity shares held by such person or group that will vest within 60 days after September 21, 2018.
- (3) Includes 20,664,600 common shares held by Tigerstep Developments Limited, a British Virgin Islands company wholly owned by Minhong Yu. Through a trust arrangement, Michael Minhong Yu, together with his family, holds beneficial interest in Tigerstep Development Limited. The business address of Mr. Yu is No. 6 Hai Dian Zhong Street, Haidian District, Beijing 100080, People's Republic of China.
- (4) Includes (i) common shares, (ii) common shares issuable upon exercise of all of the options that are exercisable within 60 days after September 21, 2018 and (iii) non-vested equity shares that will vest within 60 days after September 21, 2018 held by all of our directors and senior executive officers as a group.
- (5) Tigerstep Developments Limited, a company incorporated in the British Virgin Islands, is wholly owned by Minhong Yu. The registered address of Tigerstep Developments Limited is P.O. Box 957, Offshore Incorporation Centre, Road Town, Tortola, the British Virgin Islands.
- (6) The number of common shares beneficially owned is as of May 3, 2017, as reported in a Schedule 13G filed by UBS Group AG on May 3, 2017 on behalf of the UBS Asset Management division. As set forth in the Schedule 13G, Schroder Investment Management has sole power to vote 10,937,288 common shares and shared power to dispose of 18,950,228 common shares. The business address of UBS Group AG is Bahnhofstrasse 45, Zurich, Switzerland.

None of our existing shareholders have different voting rights from other shareholders. To our knowledge, we are not owned or controlled, directly or indirectly, by another corporation, by any foreign government or by any other natural or legal persons, severally or jointly. We are not aware of any arrangement that may, at a subsequent date, result in a change of control of our company. As of September 21, 2018, we had 158,690,714 common shares issued and outstanding, and Deutsche Bank Trust Company Americas, as the depository of our ADS facility, was the only record holder of our common shares in the United States, holding approximately 90% of our total outstanding common shares. The number of beneficial owners of our ADSs in the United States is likely much larger than the one record holder of our common shares in the United States.

**ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS**

A. Major Shareholders

Please refer to Item 6. Directors, Senior Management and Employees E. Share Ownership.

B. Related Party Transactions  
**Agreements with Koolearn**

*Deed of Non-Competition Undertakings*

As of the date of this annual report, Koolearn was in the process of applying for the listing of its securities on the Stock Exchange of Hong Kong Limited, or the HKEx. We expect to remain Koolearn's controlling shareholder after the completion of the listing. With respect to the ongoing relationship between us and Koolearn after the listing of Koolearn's securities on the HKEx, we issued a deed of non-competition undertakings on August 28, 2018 in favor of Koolearn. Pursuant to this deed, we undertake, among other things, not to, and procure our group entities not to, carry on engage or participate in online education services within China, except for (i) making minority investments in a business that provide online education services in China, or (ii) operating our existing Blingabc and Leci businesses with the restrictions set forth in the deed of non-competition undertakings, provided, however, if we propose to issue or transfer any equity interest in these businesses, Koolearn has the option to purchase all or any portion of the offered equity interest. The foregoing undertaking will end if Koolearn's securities cease to be listed on HKEx or 12 months after we cease to be the controlling shareholder of Koolearn, whichever is earlier.

## **Table of Contents**

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

See Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Its Shareholder for a summary of the contractual arrangements we have entered into with New Oriental China and its subsidiaries and shareholder.

### **Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders**

See Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with Beijing Xuncheng, Its Subsidiaries and Shareholders for a summary of the contractual arrangements we have entered into with Beijing Xuncheng, its subsidiaries and shareholders.

### **Employment Agreements**

See Item 6. Directors, Senior Management and Employees A. Directors and Senior Management for a description of the employment agreements we have entered into with our senior executive officers.

### **Share Incentives**

See Item 6. Directors, Senior Management and Employees B. Compensation of Directors and Executive Officers for a description of share-based compensation we have provided to our directors, officers and other individuals as a group.

### **Lease Arrangements with an Affiliate**

Since April 2010, we have been renting several floors of office space in a building in Beijing owned by Metropolis Holding (Tianjin) Co., Ltd., or Metropolis Holding. In February 2012, Fine Talent Holdings Limited, a British Virgin Islands company owned by Mr. Michael Minhong Yu, our executive chairman, purchased all of the equity interests in Metropolis Holding from its former owner which was and is unrelated to us. As a result, our lease agreements with Metropolis Holding became related parties transactions. As of May 31, 2018, twenty one of our operating entities rented office space from Metropolis Holding pursuant to a series of lease agreements. The terms and conditions, including rental rates, of these lease agreements are generally the same as other tenants in the same building. These lease agreements are typically three years and can be renewed upon mutual agreements upon expiration. The lease arrangements were approved by all of our directors, including all of the disinterested directors. During the fiscal year ended May 31, 2018, we accrued a total of US\$7.9 million rent to Metropolis Holding. As of May 31, 2018, amounts due from Metropolis Holding were US\$3.0 million, which represented prepaid rent and rental deposit.

### **New Oriental Education and Culture Industrial Investment Fund**

In July 2018, New Oriental Education Industry Fund, a 7-year growth equity fund with the total committed capital of RMB1.5 billion, was established. An entity controlled by Mr. Michael Minhong Yu and an unrelated third party act as the joint general partners of the fund. We participate in the fund as a limited partner and have committed to invest RMB500 million in the fund. The fund will focus on investment opportunities in the education industry and expects to invest in the whole industry chain of education with emphasis on six main themes, including pre-school education, K-12 education, non-disciplinary education, occupational education, international education and AI in education.

**Table of Contents**

**Transactions with Other Related Parties**

During the fiscal year ended May 31, 2018, we recorded revenue in the amount of US\$92 thousand from other related parties. As of May 31, 2018, we had US\$808 thousand in aggregate due from other related parties and US\$30 thousand in aggregate due to other related parties.

C. **Interests of Experts and Counsel**

Not applicable.

**ITEM 8. FINANCIAL INFORMATION**

A. **Consolidated Statements and Other Financial Information**

See Item 18 Financial Statements.

**Legal and Administrative Proceedings**

From time to time, we are subject to legal proceedings, investigations and claims incidental to the conduct of our business.

***Litigation***

Our Company and certain of our officers and directors have been named as defendants in a putative securities class action filed in the United States District Court for the District of New Jersey: Amy Chan v. New Oriental Education & Technology Group Inc., et al., Civil Action No. 16-cv-9279-KSH-CLW (filed on December 15, 2016). On March 30, 2017, the court entered an order appointing lead plaintiffs of this action. On May 30, 2017, the lead plaintiffs filed an amended complaint.

The pending action was purportedly brought on behalf of a class of persons who allegedly suffered damages as a result of their trading in our ADSs between September 28, 2016 and December 1, 2016. The amended complaint alleges that our Company's public filings contained material misstatements and omissions in violation of the federal securities laws. On July 31, 2017, our Company filed a motion to dismiss the amended complaint, which motion is currently pending before the court.

The action remains in its preliminary stages, with the court still to rule on New Oriental's motion to dismiss. We believe the case is without merit and intend to defend the action vigorously. For risks and uncertainties relating to the pending case against us, please see Item 3. Key Information D. Risk Factors Risks Related to Our ADSs We have been named as a defendant in a putative shareholder class action lawsuit that could have a material adverse impact on our business, financial condition, results of operation, cash flows and reputation.

We have been subject to copyright, trademark and trade name infringement claims and legal proceedings in the past which related to, among other things, 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 we may be subject to similar claims and legal proceedings from time to time in the future. See Item 3. Key Information D. Risk Factors Risks Related to Our Business 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.

### **Dividend Policy**

On April 17, 2012, our board of directors declared a special cash dividend in the amount of US\$0.30 per ADS. The cash dividend was paid on September 28, 2012 to shareholders of record at the close of business on August 31, 2012. The aggregate amount of cash dividends paid was US\$47.0 million, which was funded by surplus cash on our balance sheet. On July 23, 2013, our board of directors declared a special cash dividend in the amount of US\$0.35 per ADS. The cash dividend was paid on October 7, 2013 to shareholders of record at the close of business on September 6, 2013. The aggregate amount of cash dividends paid was US\$54.5 million, which was funded by surplus cash on our balance sheet. On July 21, 2015, our board of directors declared a special cash dividend in the amount of US\$0.4 per ADS. The cash dividend was paid in October 2015 to shareholders of record at the close of business on September 4, 2015. The aggregate amount of cash dividends paid was approximately US\$62.7 million. On July 25, 2017, our board of directors declared a special cash dividend in the amount of US\$0.45 per ADS. The cash dividend was paid in October 2017 to shareholders of record at the close of business on September 6, 2017. The aggregate amount of cash dividends paid was approximately US\$71.2 million.



## **Table of Contents**

Other than the declaration of the special cash dividend described in the preceding paragraph, we have not declared any dividend since the completion of our initial public offering and have no present intention to declare any additional dividends on our shares in the future. We currently intend to retain all of our available funds and any future earnings to operate and expand our business and we have no plan to repatriate the remaining undistributed earnings from our subsidiaries in China.

We are a holding company incorporated in the Cayman Islands. We rely on dividends from our subsidiaries in China and consulting, license and other fees paid to us by New Oriental China and its schools and subsidiaries. Current PRC regulations permit our subsidiaries to pay dividends to us only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, each of our PRC subsidiaries and New Oriental China and its subsidiaries are 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 to further set aside a portion of its after-tax profits to fund the employee welfare fund at the discretion of the board. These reserves may not be distributed as cash dividends. Further, if our PRC subsidiaries or New Oriental China and its schools and subsidiaries 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. Moreover, at the end of each fiscal year, every private school in China is required to allocate a certain amount out of its annual net income or annual increase in the net assets, if any, 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.

Our board of directors has complete discretion regarding whether to declare and distribute dividends. Even if our board of directors decides to pay dividends, the form, frequency and amount will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that the board of directors may deem relevant. If we pay any dividends, we will pay our ADS holders to the same extent as holders of our common shares, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder.

### **B. Significant Changes**

Except as disclosed elsewhere in this annual report, we have not experienced any significant changes since the date of our audited consolidated financial statements included in this annual report.

## **ITEM 9. THE OFFER AND LISTING**

### **A. Offering and Listing Details**

See C. Markets.

### **B. Plan of Distribution**

Not applicable.

C. Markets

Our ADSs have been listed on the NYSE since September 7, 2006 and trade under the symbol EDU. 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.

**Table of Contents**

The following table provides the high and low trading prices for our ADSs on the NYSE for the periods indicated. For ease of comparison, the ADS prices before August 18, 2011 have been retroactively adjusted to reflect the ADS to common share ratio change that took effect on August 18, 2011.

	<b>Trading Price</b>	
	<b>High</b>	<b>Low</b>
	<b>US\$</b>	<b>US\$</b>
<b>Annual High and Low</b>		
Fiscal Year 2014	34.50	20.06
Fiscal year 2015	27.42	18.10
Fiscal year 2016	43.58	18.09
Fiscal year 2017	76.18	38.11
Fiscal Year 2018	108.40	69.91
<b>Quarterly Highs and Lows</b>		
First Fiscal Quarter of 2017	45.37	38.11
Second Fiscal Quarter of 2017	53.38	39.31
Third Fiscal Quarter of 2017	52.37	37.16
Fourth Fiscal Quarter of 2017	76.18	48.95
First Fiscal Quarter of 2018	86.88	69.91
Second Fiscal Quarter of 2018	94.63	80.59
Third Fiscal Quarter of 2018	108.40	82.07
Fourth Fiscal Quarter of 2018	105.66	83.00
First Fiscal Quarter of 2019	108.24	73.51
<b>Monthly Highs and Lows</b>		
March 2018	97.35	84.27
April 2018	96.55	83.00
May 2018	105.66	88.20
June 2018	108.24	90.88
July 2018	99.47	85.34
August 2018	88.73	73.51
September 2018 (through September 21)	78.57	67.23

**D. Selling Shareholders**

Not applicable.

**E. Dilution**

Not applicable.

**F. Expenses of the Issue**

Not applicable.

**ITEM 10. ADDITIONAL INFORMATION**

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association

We are a Cayman Islands company and our affairs are governed by our memorandum and articles of association, the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, or the Companies Law, and the common law of the Cayman Islands. The following are summaries of material provisions of our amended and restated memorandum and articles of association in effect as of the date of this annual report insofar as they relate to the material terms of our common shares.

## **Table of Contents**

### **Registered Office and Objects**

Our registered office in the Cayman Islands is located at Conyers Trust Company (Cayman) Limited, Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands, or at such other place as our board of directors may from time to time decide. The objects for which our company is established are unrestricted and we have full power and authority to carry out any object not prohibited by the Companies Law, as amended from time to time, or any other law of the Cayman Islands.

### **Board of Directors**

A director is not required to hold any shares in our company by way of qualification. A director may vote with respect to any contract, proposed contract or arrangement in which he is materially interested. A director may exercise all the powers of our company to borrow money, mortgage its undertaking, property and uncalled capital, and issue debentures or other securities whenever money is borrowed or as security for any obligation of our company or of any third party. The directors may receive such remuneration as our board may from time to time determine. There is no age limit requirement with respect to the retirement or non-retirement of a director. See also Item 6. Directors, Senior Management and Employees C. Board Practices Duties of Directors and Item 6. Directors, Senior Management and Employees C. Board Practices Terms of Directors and Officers.

### **Common Shares**

*General.* All of our outstanding common shares are fully paid and non-assessable. Certificates representing the common shares are issued in registered form. Our shareholders who are non-residents of the Cayman Islands may freely hold and vote their shares.

*Dividends.* The holders of our common shares are entitled to such dividends as may be declared by our board of directors, subject to the Companies Law and our memorandum and articles of association.

*Voting Rights.* Each common share is entitled to one vote on all matters upon which the common shares are entitled to vote. Voting at any shareholders' meeting is by show of hands unless a poll is demanded. A poll may be demanded by our chairman or any shareholder holding at least 10% of the shares given a right to vote at the meeting, present in person or by proxy.

A quorum required for a meeting of shareholders consists of at least two shareholders present in person or by proxy or, if a corporation or other non-natural person, by its duly authorized representative, which hold in aggregate at least one-third of our voting share capital. Shareholders' meetings are held annually and may be convened by our board of directors on its own initiative or upon a request to the directors by shareholders holding in aggregate not less than 33% of our voting share capital. Advance notice of at least seven days is required for the convening of our annual general meeting and other shareholders' meetings.

An ordinary resolution to be passed by the shareholders requires the affirmative vote of a simple majority of the votes attaching to the common shares cast in a general meeting, while a special resolution requires the affirmative vote of not less than two-thirds of the votes cast attaching to the common shares. A special resolution is required for important matters such as a change of name. Holders of the common shares may affect certain changes by ordinary resolution, including increasing the amount of our authorized share capital, consolidating and dividing all or any of our share capital into shares of a larger amount than our existing share capital, and canceling any shares.

*Transfer of Shares.* Subject to the restrictions of our memorandum and articles of association, as applicable, any of our shareholders may transfer all or any of his or her common shares by an instrument of transfer in the usual or common form prescribed by the New York Stock Exchange or in any other form approved by our board.

Our board of directors may, in its sole discretion, decline to register any transfer of any common share which is not fully paid up or on which we have a lien. Our directors may also decline to register any transfer of any common share unless (1) the instrument of transfer is lodged with us, accompanied by the certificate for the common shares to which it relates and such other evidence as our board of directors may reasonably require to show the right of the transferor to make the transfer; (2) the instrument of transfer is in respect of only one class of common shares; (3) the instrument of transfer is duly and properly signed; (4) in the case of a transfer to joint holders, the number of joint holders to whom the common share is to be transferred does not exceed four; (5) the shares conceded are free of any lien in favor of us; or (6) a fee of such maximum sum as the New York Stock Exchange may determine to be payable, or such lesser sum as our board of directors may from time to time require, is paid to us in respect thereof.

## **Table of Contents**

If our directors refuse to register a transfer they shall, within two months after the date on which the instrument of transfer was lodged, send to each of the transferor and the transferee notice of such refusal. The registration of transfers may, on 14 days' notice being given by advertisement in such one or more newspapers or by electronic means, be suspended and the register closed at such times and for such periods as our board of directors may from time to time determine, provided, however, that the registration of transfers shall not be suspended nor the register closed for more than 30 days in any year.

*Liquidation.* On a return of capital on winding up or otherwise (other than on conversion, redemption or purchase of shares), assets available for distribution among the holders of common shares shall be distributed among the holders of the common shares on a pro rata basis. If our assets available for distribution are insufficient to repay all of the paid-up capital, the assets will be distributed so that the losses are borne by our shareholders proportionately.

*Calls on Shares and Forfeiture of Shares.* Our board of directors may from time to time make calls upon shareholders for any amounts unpaid on their shares in a notice served to such shareholders at least 14 days prior to the specified time and place of payment. The shares that have been called upon and remain unpaid on the specified time are subject to forfeiture.

*Redemption of Shares.* Subject to the provisions of the Companies Law, we may issue shares on terms that are subject to redemption, at our option or at the option of the holders, on such terms and in such manner as may be determined by special resolution.

*Variations of Rights of Shares.* All or any of the special rights attached to any class of shares may, subject to the provisions of the Companies Law, be varied either with the written consent of the holders of two-thirds of the issued shares of that class or with the sanction of a special resolution passed at a general meeting of the holders of the shares of that class.

*Inspection of Books and Records.* Holders of our common shares have no general right under Cayman Islands law to inspect or obtain copies of our list of shareholders or our corporate records. However, we will provide our shareholders with annual audited financial statements. See H. Documents on Display.

*Limitations on the Right to Own Shares.* There are no limitations on the right to own our shares.

*Disclosure of Shareholder Ownership.* There are no provisions in our amended and restated memorandum and articles of association governing the ownership threshold above which shareholder ownership must be disclosed.

## **Differences in Corporate Law**

The Companies Law is derived, to a large extent, from the older Companies Acts of England but does not follow recent statutory enactments in England. In addition, the Companies Law differs from laws applicable to United States corporations and their shareholders. Set forth below is a summary of the significant differences between the provisions of the Companies Law applicable to us and the laws applicable to companies incorporated in the United States.

*Mergers and Similar Arrangements.* The Companies Law permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. For these purposes, (a) merger means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company and (b) a consolidation means the combination of two or more constituent companies into a combined company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. In order to effect such a merger or consolidation, the directors of each

constituent company must approve a written plan of merger or consolidation, which must then be authorized by (a) a special resolution of the shareholders of each constituent company, and (b) such other authorization, if any, as may be specified in such constituent company's articles of association.



## Table of Contents

The written plan of merger or consolidation must be filed with the Registrar of Companies together with a declaration as to the solvency of the consolidated or surviving company, a list of the assets and liabilities of each constituent company and an undertaking that a copy of the certificate of merger or consolidation will be given to the members and creditors of each constituent company and that notification of the merger or consolidation will be published in the Cayman Islands Gazette. Dissenting shareholders have the right to be paid the fair value of their shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) if they follow the required procedures, subject to certain exceptions. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

In addition, there are statutory provisions that facilitate the reconstruction and amalgamation of companies, provided that the arrangement is approved by a majority in number of each class of shareholders and creditors with whom the arrangement is to be made, and who must, in addition, represent 75% in value of each such class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting, or meetings, convened for that purpose. The convening of the meetings and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder has the right to express to the court the view that the transaction ought not to be approved, the Grand Court of the Cayman Islands can be expected to approve the arrangement if it determines that (a) the statutory provisions as to the required majority vote have been met; (b) the shareholders have been fairly represented at the meeting in question and the statutory majority are acting bona fide without coercion of the minority to promote interests adverse to those of the class; (c) the arrangement is such that may be reasonably approved by an intelligent and honest man of that class acting in respect of his interest; and (d) the arrangement is not one that would more properly be sanctioned under some other provision of the Companies Law.

If an arrangement and reconstruction is thus approved, the dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of Delaware corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

When a takeover offer is made and accepted by holders of 90% of the shares affected within four months, the offeror may, within a two-month period commencing on the expiration of such four month period, require the holders of the remaining shares to transfer such shares on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands but this is unlikely to succeed in the case of an offer which has been so approved unless there is evidence of fraud, bad faith or collusion.

*Shareholders Suits.* In principle, we will normally be the proper plaintiff and as a general rule a derivative action may not be brought by a minority shareholder. However, based on English authorities, which would in all likelihood be of persuasive authority in the Cayman Islands, there are exceptions to the foregoing principle, including when (a) a company acts or proposes to act illegally or ultra vires; (b) the act complained of, although not ultra vires, could only be effected duly if authorized by more than a simple majority vote that has not been obtained; and (c) those who control the company are perpetrating a fraud on the minority .

*Indemnification of Directors and Executive Officers and Limitation of Liability.* Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Our amended and restated memorandum and articles of association permit indemnification of officers and directors for losses, damages, costs and expenses incurred in their capacities as such unless such losses or damages arise from dishonesty or fraud which may attach to such directors or officers. This standard of conduct is generally the same as permitted under the Delaware General Corporation Law for a Delaware corporation. In addition, we intend to enter into indemnification agreements with our directors and senior executive officers that will provide such persons with additional

indemnification beyond that provided in our amended and restated memorandum and articles of association.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to our directors, officers or persons controlling us under the foregoing provisions, we have been informed that, in the opinion of the SEC, such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

## Table of Contents

*Anti-Takeover Provisions in the Memorandum and Articles of Association.* Some provisions of our amended and restated memorandum and articles of association may discourage, delay or prevent a change in control of our company or management that shareholders may consider favorable, including provisions that authorize our board of directors to issue preference shares in one or more series and to designate the price, rights, preferences, privileges and restrictions of such preference shares without any further vote or action by our shareholders.

However, under Cayman Islands law, our directors may only exercise the rights and powers granted to them under our memorandum and articles of association, as amended and restated from time to time, for what they believe in good faith to be in the best interests of our company.

*Directors Fiduciary Duties.* As a matter of Cayman Islands law, a director of a Cayman Islands company is in the position of a fiduciary with respect to the company and therefore it is considered that he owes the following duties to the company a duty to act bona fide in the best interests of the company, a duty not to make a profit based on his or her position as director (unless the company permits him to do so) and a duty not to put himself in a position where the interests of the company conflict with his or her personal interest or his or her duty to a third party. A director of a Cayman Islands company owes to the company a duty to act with skill and care. It was previously considered that a director need not exhibit in the performance of his or her duties a greater degree of skill than may reasonably be expected from a person of his or her knowledge and experience. However, English and Commonwealth courts have moved towards an objective standard with regard to the required skill and care and these authorities are likely to be followed in the Cayman Islands.

In addition, directors of a Cayman Islands company must not place themselves in a position in which there is a conflict between their duty to the company and their personal interests. However, this obligation may be varied by the company's articles of association, which may permit a director to vote on a matter in which he has a personal interest provided that he has disclosed that nature of his interest to the board. Our amended and restated memorandum and articles of association provides that a director with an interest (direct or indirect) in a contract or arrangement or proposed contract or arrangement with the company must declare the nature of his interest at the meeting of the board of directors at which the question of entering into the contract or arrangement is first considered, if he knows his interest then exists, or in any other case at the first meeting of the board of directors after he is or has become so interested.

A general notice may be given at a meeting of the board of directors to the effect that (i) the director is a member/officer of a specified company or firm and is to be regarded as interested in any contract or arrangement which may after the date of the notice in writing be made with that company or firm; or (ii) he is to be regarded as interested in any contract or arrangement which may after the date of the notice in writing to the board of directors be made with a specified person who is connected with him, will be deemed sufficient declaration of interest. Following the disclosure being made pursuant to our amended and restated memorandum and articles of association and subject to any separate requirement for Audit Committee approval under applicable law or the listing rules of the NYSE, and unless disqualified by the chairman of the relevant board meeting, a director may vote in respect of any contract or arrangement in which such director is interested and may be counted in the quorum at such meeting. However, even if a director discloses his interest and is therefore permitted to vote, he must still comply with his duty to act bona fide in the best interest of our company.

In comparison, under Delaware corporate law, a director of a Delaware corporation has a fiduciary duty to the corporation and its shareholders. This duty has two components: the duty of care and the duty of loyalty. The duty of care requires that a director act in good faith, with the care that an ordinarily prudent person would exercise under similar circumstances. Under this duty, a director must inform himself of, and disclose to shareholders, all material information reasonably available regarding a significant transaction. The duty of loyalty requires that a director act in

a manner he or she reasonably believes to be in the best interests of the corporation. He or she must not use his or her corporate position for personal gain or advantage. This duty prohibits self-dealing by a director and mandates that the best interest of the corporation and its shareholders take precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the shareholders generally. In general, actions of a director are presumed to have been made on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation. However, this presumption may be rebutted by evidence of a breach of one of the fiduciary duties. Should such evidence be presented concerning a transaction by a director, a director must prove the procedural fairness of the transaction, and that the transaction was of fair value to the corporation.

## **Table of Contents**

*Shareholder Proposals.* Under the Delaware General Corporation Law, a shareholder has the right to put any proposal before the annual meeting of shareholders, provided it complies with the notice provisions in the governing documents. The Delaware General Corporation Law does not provide shareholders an express right to put any proposal before the annual meeting of shareholders, but in keeping with common law, Delaware corporations generally afford shareholders an opportunity to make proposals and nominations provided that they comply with the notice provisions in the certificate of incorporation or bylaws. A special meeting may be called by the board of directors or any other person authorized to do so in the governing documents, but shareholders may be precluded from calling special meetings.

There are no statutory requirements under Cayman Islands law allowing our shareholders to requisition a shareholders meeting. However, under our amended and restated articles of association, on the requisition of shareholders representing not less than 33% of the voting rights entitled to vote at general meetings, the board shall convene an extraordinary general meeting. As an exempted Cayman Islands company, we are not obliged by law to call shareholders annual general meetings, and our amended and restated articles of association does not require us to call such meetings every year.

*Cumulative Voting.* Under the Delaware General Corporation Law, cumulative voting for elections of directors is not permitted unless the corporation's certificate of incorporation specifically provides for it. Cumulative voting potentially facilitates the representation of minority shareholders on a board of directors since it permits the minority shareholder to cast all the votes to which the shareholder is entitled on a single director, which increases the shareholder's voting power with respect to electing such director. As permitted under Cayman Islands law, our amended and restated articles of association do not provide for cumulative voting. As a result, our shareholders are not afforded any less protections or rights on this issue than shareholders of a Delaware corporation.

*Removal of Directors.* Under the Delaware General Corporation Law, a director of a corporation with a classified board may be removed only for cause with the approval of a majority of the outstanding shares entitled to vote, unless the certificate of incorporation provides otherwise. Under our amended and restated articles of association, directors may be removed by an ordinary resolution of shareholders.

*Transactions with Interested Shareholders.* The Delaware General Corporation Law contains a business combination statute applicable to Delaware public corporations whereby, unless the corporation has specifically elected not to be governed by such statute by amendment to its certificate of incorporation or bylaws that is approved by its shareholders, it is prohibited from engaging in certain business combinations with an interested shareholder for three years following the date that such person becomes an interested shareholder. An interested shareholder generally is a person or a group who or which owns or owned 15% or more of the target's outstanding voting stock or who or which is an affiliate or associate of the corporation and owned 15% or more of the corporation's outstanding voting stock within the past three years. This has the effect of limiting the ability of a potential acquirer to make a two-tiered bid for the target in which all shareholders would not be treated equally. The statute does not apply if, among other things, prior to the date on which such shareholder becomes an interested shareholder, the board of directors approves either the business combination or the transaction which resulted in the person becoming an interested shareholder. This encourages any potential acquirer of a Delaware corporation to negotiate the terms of any acquisition transaction with the target's board of directors.

Cayman Islands law has no comparable statute. As a result, we cannot avail ourselves of the types of protections afforded by the Delaware business combination statute. However, although Cayman Islands law does not regulate transactions between a company and its significant shareholders, it does provide that such transactions must be entered into bona fide in the best interests of the company and for a proper corporate purpose and not with the effect of constituting a fraud on the minority shareholders.

*Dissolution; Winding Up.* Under the Delaware General Corporation Law, unless the board of directors approves the proposal to dissolve, dissolution must be approved by shareholders holding 100% of the total voting power of the corporation. Only if the dissolution is initiated by the board of directors may it be approved by a simple majority of the corporation's outstanding shares. Delaware law allows a Delaware corporation to include in its certificate of incorporation a supermajority voting requirement in connection with dissolutions initiated by the board. Under Cayman Islands law, a company may be wound up by either an order of the courts of the Cayman Islands or by a special resolution of its members or, if the company is unable to pay its debts as they fall due, by an ordinary resolution of its members. The court has authority to order winding up in a number of specified circumstances including where it is, in the opinion of the court, just and equitable to do so.

## **Table of Contents**

Under the Companies Law, our company may be dissolved, liquidated or wound up by a special resolution of our shareholders.

*Variation of Rights of Shares.* Under the Delaware General Corporation Law, a corporation may vary the rights of a class of shares with the approval of a majority of the outstanding shares of such class, unless the certificate of incorporation provides otherwise. Under Cayman Islands law and our amended and restated articles of association, if our share capital is divided into more than one class of shares, we may vary the rights attached to any class only with the consent in writing of the holders of two-thirds of the issued shares of that class, or with the sanction of a special resolution passed at a separate meeting of the holders of the shares of that class.

*Amendment of Governing Documents.* Under the Delaware General Corporation Law, a corporation's certificate of incorporation may be amended only if adopted and declared advisable by the board of directors and approved by a majority of the outstanding shares entitled to vote, and the bylaws may be amended with the approval of a majority of the outstanding shares entitled to vote and may, if so provided in the certificate of incorporation, also be amended by the board of directors. Under Cayman Islands law, our amended and restated memorandum and articles of association may only be amended by a special resolution of our shareholders.

*Rights of Non-Resident or Foreign Shareholders.* There are no limitations imposed by our amended and restated memorandum and articles of association on the rights of non-resident or foreign shareholders to hold or exercise voting rights on our shares. In addition, there are no provisions in our amended and restated memorandum and articles of association governing the ownership threshold above which shareholder ownership must be disclosed.

*Directors' Power to Issue Shares.* Subject to applicable law, our board of directors is empowered to issue or allot shares or grant options and warrants with or without preferred, deferred, qualified or other special rights or restrictions.

### **C. Material Contracts**

We have not entered into any material contracts other than in the ordinary course of business and other than those described in Item 4. Information on the Company C. Organizational Structure Contractual Arrangements with New Oriental China, Its Schools and Subsidiaries and Shareholder or elsewhere in this annual report on Form 20-F.

### **D. Exchange Controls**

See Item 4. Information on the Company B. Business Overview Regulation Foreign Currency Exchange.

### **E. Taxation**

The following discussion of the material Cayman Islands, PRC and United States federal income tax consequences of an investment in our ADSs or common shares is based upon laws and relevant interpretations thereof in effect as of the date of this annual report on Form 20-F, all of which are subject to change. This discussion does not deal with all possible tax consequences relating to an investment in our ADSs or common shares, such as the tax consequences under state, local and other tax laws. Accordingly, each investor should consult its own tax advisor regarding the tax consequences of an investment in our ADSs or common shares applicable under its particular circumstances.

### **Cayman Islands Taxation**

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to us levied by the government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or brought within the jurisdiction of the Cayman Islands. The Cayman Islands is a party to a double tax treaty entered into with the United Kingdom in 2010 but otherwise is not party to any double tax treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.



**Table of Contents****PRC Taxation**

Under the PRC Enterprise Income Tax Law, or the EIT Law, an enterprise established outside the PRC with de facto management body within the PRC is considered as a resident enterprise, meaning that it can be treated in a manner similar to a PRC enterprise for enterprise income tax purposes, although the dividends paid to one resident enterprise from another may qualify as tax-exempt income. The implementation rules of the EIT Law define de facto management as substantial and overall management and control over the production and operations, personnel, accounting, and properties of the enterprise. The State Administration of Taxation has issued circular to provide 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 body located within China if all of the following requirements are satisfied: (i) the senior management and core management departments in charge of its daily operations function are mainly in the PRC; (ii) its financial and human resources decisions are subject to determination or approval by persons or bodies in the PRC; (iii) 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 (iv) at least half of the enterprise's directors with voting right or senior management 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 State Administration of Taxation's general position on how the de facto management body test should be applied in determining the tax residency status of offshore enterprises and the administration measures should be implemented, regardless of whether they are controlled by PRC enterprises or PRC individuals. In addition, the State Administration of Taxation issued a bulletin on January 29, 2014, to provide more guidance on the implementation of the above circular. This bulletin further provided that, among other things, an entity that is classified as a resident enterprise in accordance with the circular shall file the application for classifying its status of residential enterprise with the local tax authorities where its main domestic investors registered. From the year in which the entity is determined as a resident enterprise, any dividend, profit and other equity investment gain shall be taxed in accordance with the Article 26 of EIT law and the Article 17 and Article 83 of its implementation rules. If we are deemed to be a PRC resident enterprise, dividends distributed to our non-PRC enterprise shareholders by us, or the gain our non-PRC enterprise shareholders 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.

For more information on PRC taxation applicable to our company, see Item 4. Information on the Company B. Business Overview Regulation Regulations on Taxation and Item 5. Operating and Financial Review and Prospects A. Operating Results Taxation.

**U.S. Federal Income Taxation**

The following discussion applies only to U.S. Holders (as defined below) that hold our ADSs or common shares as capital assets and that have the U.S. dollar as their functional currency. This discussion is based upon existing U.S. federal tax law as in effect on the date of this annual report, which is subject to differing interpretations or change (possibly with retroactive effect), and could affect the tax consequences described below.

The following discussion does not deal with the tax consequences to any particular holder or to persons in special tax situations such as:

banks;

financial institutions;

insurance companies;

broker dealers;

**Table of Contents**

traders that elect to mark to market;

tax-exempt entities (including private foundations);

pension plans;

cooperatives;

holders that are not U.S. Holders;

persons whose functional currency is not the U.S. dollar;

real estate investment trusts;

regulated investment companies;

persons liable for alternative minimum tax;

persons required to accelerate the recognition of any item of gross income with respect to our shares as a result of such income being recognized on an applicable financial statement;

persons holding ADSs or common shares as part of a straddle, hedging, conversion, constructive sale, or other integrated transaction for United States federal income tax purposes;

persons that actually or constructively own 10% or more of our stock (by vote or value);

persons holding ADSs or common shares through partnerships or other pass-through entities; or

persons who acquired ADSs or common shares pursuant to the exercise of any employee share option or otherwise as compensation.

**U.S. HOLDERS ARE URGED TO CONSULT THEIR TAX ADVISORS ABOUT THE APPLICATION OF THE U.S. FEDERAL TAX RULES TO THEIR PARTICULAR CIRCUMSTANCES AS WELL AS THE STATE, LOCAL AND FOREIGN TAX, MEDICARE TAX AND NON-INCOME TAX (SUCH AS THE UNITED STATES FEDERAL ESTATE OR GIFT TAX) CONSIDERATIONS OF THE OWNERSHIP AND DISPOSITION OF ADSS OR COMMON SHARES.**

The discussion below of the United States federal income tax consequences to U.S. Holders will apply if you are the beneficial owner of ADSs or common shares and you are, for U.S. federal income tax purposes,

a citizen or individual resident of the U.S.;

a corporation (or other entity taxable as a corporation for U.S. federal income tax purposes) organized under the laws of the United States, any State or the District of Columbia;

an estate whose income is subject to U.S. federal income taxation regardless of its source; or

a trust that (1) is subject to the supervision of a court within the U.S. and the control of one or more U.S. persons or (2) has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

If a partnership (including any entity treated as a partnership for United States federal income tax purposes) is a beneficial owner of common shares or ADSs, the tax treatment of a partner in such partnership will depend upon the status of the partner and the activities of the partnership. Partners in a partnership holding our common shares or ADSs should consult their tax advisors regarding the United States federal income tax considerations relating to the ownership or disposition of our common shares or ADSs.

## **Table of Contents**

The discussion below assumes that the representations contained in the deposit agreement are true and that the obligations in the deposit agreement and any related agreement will be complied with in accordance with the terms. Accordingly, if you hold ADSs, it is generally expected that you should be treated as the beneficial owner of the underlying common shares represented by those ADSs for U.S. federal income tax purposes. The remainder of this discussion assumes that a U.S. Holder of our ADSs will be treated in this manner.

### ***Taxation of Distributions on the ADSs or Common Shares***

Subject to the passive foreign investment company rules discussed below, the gross amount of all our distributions paid to you with respect to the ADSs or common shares out of our current or accumulated earnings and profits, generally will be included in your gross income as ordinary dividend income on the date of receipt by the depository, in the case of ADSs, or by you, in the case of common shares. Because we do not intend to determine our earnings and profits on the basis of U.S. federal income tax principles, any distribution paid will generally be reported as a dividend for U.S. federal income tax purposes. The dividends will not be eligible for the dividends-received deduction allowed to corporations in respect of dividends received from other U.S. corporations.

With respect to non-corporate U.S. Holders, including individuals, dividends may be qualified dividend income which is taxed at the lower applicable capital gains rate provided that (1) the ADSs or common shares, as applicable, are readily tradable on an established securities market in the United States, or we are eligible for the benefit of the income tax treaty between the U.S. and the PRC, (2) the non-United States corporation is not a passive foreign investment company (as discussed below) for either its taxable year in which the dividend was paid or the preceding taxable year and (3) certain holding period requirements are met. Although we expect our ADSs will be considered to be readily tradable on the NYSE, which is an established securities market in the U.S., there can be no assurance that our ADSs will be considered readily tradable on an established securities market in the future. Since we do not expect that our common shares will be listed on an established securities market in the U.S., it is unclear whether dividends that we pay on our common shares that are not backed by ADSs currently meet the conditions required for the reduced tax rate. In the event, however, that we are deemed to be a PRC resident enterprise under the EIT Law, we may be eligible for the benefits of the U.S. PRC income tax treaty. U.S. Holders are advised to consult their tax advisors regarding the availability of the lower rate for dividends paid with respect to our ADSs or common shares.

Dividends paid on our ADSs and common shares generally will be treated as income from foreign sources for U.S. foreign tax credit purposes and generally will constitute passive category income. In the event that we are deemed to be a PRC resident enterprise under the EIT Law, a U.S. Holder may be subject to a number of complex limitations, to claim a foreign tax credit in respect of any foreign withholding taxes imposed on dividends received on our ADSs or common shares. A U.S. Holder who does not elect to claim a foreign tax credit for foreign tax withheld may instead claim a deduction for U.S. federal income tax purposes in respect of such withholdings, but only for a year in which such U.S. Holder elects to do so for all creditable foreign income taxes. The rules governing the foreign tax credit are complex. U.S. Holders are advised to consult their tax advisors regarding the creditability of any PRC tax.

### ***Taxation of Disposition of Shares***

Subject to the passive foreign investment company rules discussed below, a U.S. Holder will recognize taxable gain or loss on any sale, exchange or other taxable disposition of an ADS or common share equal to the difference between the amount realized for the ADS or common share and such holder's tax basis in the ADS or common share. The gain or loss generally will be capital gain or loss. A non-corporate U.S. Holder, including an individual, who has held the ADS or common share for more than one year will be eligible for reduced capital gains rates. The deductibility of capital losses is subject to limitations. Any such gain or loss generally will be treated as U.S. source income or loss. In the event that we are deemed to be a PRC resident enterprise under the EIT Law and gain from the disposition of the

ADSs or common shares is subject to tax in the PRC, a U.S. Holder that is eligible for the benefits of the U.S.-PRC treaty may elect to treat the gain as PRC source income. See PRC Taxation. U.S. Holders are advised to consult their tax advisors regarding the tax consequences if a foreign tax is imposed on a disposition of our ADSs or common shares, including the availability of the foreign tax credit, under their particular circumstances.

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**Table of Contents*****Passive Foreign Investment Company Considerations***

A non-United States corporation, such as our company, will be a passive foreign investment company, or a PFIC, for United States federal income tax purposes, 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. For this purpose, cash and assets readily convertible into cash are categorized as passive assets and the company's goodwill and other unbooked intangibles associated with active business activities may generally be classified as active assets. If a non-U.S. corporation directly or indirectly owns at least 25% (by value) of the stock of another corporation, such corporation will be treated, for purposes of the PFIC tests, as owning a proportionate share of the assets and earning a proportionate share of the other corporation's assets and receiving a proportionate share of the other corporation's 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 United States federal income tax purposes, and based upon an analysis of the Company's income and assets in respect of the 2018 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, 2018. 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, the determination of whether we will be or become a PFIC will depend in large part upon the market value of our ADSs, which we cannot control. Accordingly, fluctuations in the market price of our ADSs may cause us to become a PFIC for the current taxable year or future taxable years. It is also possible, that the United States Internal Revenue Service may challenge our classification or valuation of our goodwill and other unbooked intangibles, which may result in our company being, or becoming a PFIC. The determination of whether we will be or become a PFIC will also depend, in part, upon the nature of our assets and income over time, which are subject to change from year to year. There can be no assurance 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.

***Passive Foreign Investment Company Rules***

If we are a PFIC for any taxable year during which a U.S. Holder holds our ADSs or common shares, and unless the U.S. Holder makes a mark-to-market election (as described below), the U.S. Holder will generally be subject to special tax rules that have a penalizing effect, regardless of whether we remain a PFIC, on (1) any excess distribution that we make to the U.S. Holder which generally means any distribution paid during a taxable year to a U.S. Holder that is greater than 125 percent of the average annual distributions paid in the three preceding taxable years or, (2) if shorter, the U.S. Holder's holding period for the ADSs or common shares. Under these PFIC rules:

such excess distribution and/or gain will be allocated ratably over the U.S. Holder's holding period for the ADSs or common shares;

such amount allocated to the current taxable year, and any taxable years in the U.S. Holder's holding period prior to the first taxable year in which we were a PFIC (a pre-PFIC year), will be taxable as ordinary income;

such amount allocated to each prior taxable year, other than the current taxable year or a pre-PFIC year, will be subject to tax at the highest tax rate in effect for individuals or corporations, as applicable, for each such year; and

an interest charge generally applicable to underpayments of tax will be imposed on the tax attributable to each prior taxable year, other than the current taxable year or a pre-PFIC year.



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**Table of Contents**

If we are a PFIC for any taxable year during which a U.S. Holder holds our ADSs or common shares and any of our non-U.S. subsidiaries is also a PFIC (i.e., a lower-tier PFIC), such U.S. Holder would be treated as owning a proportionate amount (by value) of the shares of the lower-tier PFIC and would be subject to the rules described above on certain distributions by a lower-tier PFIC and a disposition of shares of a lower-tier PFIC even though such U.S. Holder would not receive the proceeds of those distributions or dispositions. U.S. Holders are advised to consult their tax advisors regarding the application of the PFIC rules to any of our subsidiaries.

A U.S. Holder of marketable stock (as defined below) in a PFIC may make a mark-to-market election for such stock to elect out of the tax treatment discussed above. If a U.S. Holder makes a mark-to-market election for the ADSs or common shares, such holder will include in income for each year that we are treated as a PFIC with respect to such holder an amount equal to the excess, if any, of the fair market value of the ADSs or common shares as of the close of your taxable year over the holder's adjusted basis in such ADSs or common shares. A U.S. Holder will be allowed a deduction for the excess, if any, of the adjusted basis of the ADSs or common shares over their fair market value as of the close of the taxable year. However, deductions will be allowable only to the extent of any net mark-to-market gains on the ADSs or common shares included in a U.S. Holder's income for prior taxable years. Amounts included in a U.S. Holder's income under a mark-to-market election, as well as gain on the actual sale or other disposition of the ADSs or common shares, will be treated as ordinary income. Ordinary loss treatment will also apply to the deductible portion of any mark-to-market loss on the ADSs or common shares, as well as to any loss realized on the actual sale or disposition of the ADSs or common shares, to the extent that the amount of such loss does not exceed the net mark-to-market gains previously included for such ADSs or common shares. A U.S. Holder's basis in the ADSs or common shares will be adjusted to reflect any such income or loss amounts. If a U.S. Holder makes a valid mark-to-market election, the tax rules that apply to distributions by corporations which are not PFICs would apply to distributions by us, except that the lower capital gains rate applicable to qualified dividend income (discussed above under "Taxation of Distributions on the ADSs or Common Shares") would not apply.

The mark-to-market election is available only for marketable stock, which is stock that is traded in other than de minimis quantities on at least 15 days during each calendar quarter (regularly traded) on a qualified exchange or other market, as defined in applicable United States Treasury regulations. Our ADSs are listed on the NYSE, which is a qualified exchange or market for these purposes. Consequently, if the ADSs continue to be listed on the NYSE and are regularly traded, and a U.S. Holder holds ADSs, we expect that the mark-to-market election would be available to such U.S. Holder were we to be or become a PFIC although there can be no assurance in this regard. Because a mark-to-market election cannot be made for equity interests in any lower-tier PFICs that we own, a U.S. Holder may continue to be subject to the PFIC rules with respect to its indirect interest in any investments held by us that are treated as an equity interest in a PFIC for U.S. federal income tax purposes. In the case of a U.S. Holder who has held ADSs or common shares during any taxable year in respect of which we were classified as a PFIC and continues to hold such ADSs or common shares (or any portion thereof) and has not previously determined to make a mark-to-market election, and who is now considering making a mark-to-market election, special tax rules may apply relating to purging the PFIC taint of such ADSs or common shares.

Alternatively, a U.S. Holder of stock in a PFIC may make a qualified electing fund or QEF election with respect to such PFIC to elect out of the tax treatment discussed above. A U.S. Holder that makes a valid QEF election with respect to a PFIC will generally include in gross income for a taxable year such holder's pro rata share of the corporation's earnings and profits for the taxable year. However, the qualified electing fund election is available only if the PFIC provides such U.S. Holder with certain information regarding its earnings and profits as required under applicable United States Treasury regulations. We do not intend to prepare or provide the information that would enable a U.S. Holder to make a QEF election. Accordingly, U.S. Holders should assume that the QEF Election will not be available.

If a U.S. Holder holds ADSs or common shares in any year in which we are treated as a PFIC with respect to such U.S. Holder, the U.S. Holder will generally be required to file United States Internal Revenue Service Form 8621 and such other form as is required by the United States Treasury Department. U.S. Holders are urged to consult their tax advisor regarding the application of the PFIC rules to their ownership or disposition of our ADSs or common shares.

F. Dividends and Paying Agents

Not applicable.

**Table of Contents**

**G. Statement by Experts**

Not applicable.

**H. Documents on Display**

We previously filed with the SEC a registration statements on Form F-1 under the U.S. Securities Act of 1933, as amended, with respect to two offerings of our common shares represented by ADSs.

We are subject to the periodic reporting and other informational requirements of the Exchange Act. Under the Exchange Act, we are required to file reports and other information with the SEC. In particular, we are required to file annually a Form 20-F within four months after the end of each fiscal year. The SEC maintains a website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system. Copies of reports and other information, when filed, may also be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the SEC at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. The public may obtain information regarding the Washington, D.C. Public Reference Room by calling the SEC at 1- 800-SEC-0330. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

We will furnish Deutsche Bank Trust Company Americas, the depository of our ADSs, with our annual reports, which will include a review of operations and annual audited consolidated financial statements prepared in conformity with U.S. GAAP, and all notices of shareholders' meetings and other reports and communications that are made generally available to our shareholders. The depository will make such notices, reports and communications available to holders of ADSs and, upon our request, will mail to all record holders of ADSs the information contained in any notice of a shareholders' meeting received by the depository from us.

**I. Subsidiary Information**

Not applicable.

**ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

***Interest Rate Risk***

Our exposure to interest rate risk primarily relates to the interest income generated by excess cash invested in liquid investments with original maturities of three months or less and term deposits with maturities of greater than three months and less than a year. We have not used any derivative financial instruments to manage our interest risk exposure. Interest-earning instruments carry a degree of interest rate risk. We have not been exposed, nor do we anticipate being exposed, to material risks due to changes in interest rates. However, our future interest income may be lower than expected due to changes in market interest rates. A hypothetical one percentage point decrease in interest rates would have resulted in a decrease of approximately US\$24.2 million in our interest income for the year ended May 31, 2018.

***Foreign Exchange Risk***

All of our revenues and most of our expenses are denominated in RMB. Our exposure to foreign exchange risk primarily relates to cash and cash equivalent denominated in U.S. dollars. We do not believe that we currently have any significant direct foreign exchange risk and have not hedged exposures denominated in foreign currencies or used any other derivative financial instruments. Although in general, our exposure to foreign exchange risks should be limited, the value of your investment in our ADSs will be affected by the foreign exchange rate between U.S. dollars and RMB because the value of our business is effectively denominated in RMB, while the ADSs are traded in U.S. dollars.

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. Since June 2010, the Renminbi has fluctuated against the U.S. dollar, at times significantly and unpredictably. 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.

**Table of Contents**

To the extent that we need to convert U.S. dollar-denominated financial assets into RMB for our operations, appreciation of the RMB against the U.S. dollar would have an adverse effect on the RMB amount we receive from the conversion. A hypothetical 10% appreciation of the RMB against the U.S. dollar would have resulted in a decrease of RMB65.4 million in the value of our U.S. dollar denominated financial assets as of May 31, 2018.

**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

A. Debt Securities

Not applicable.

B. Warrants and Rights

Not applicable.

C. Other Securities

Not applicable.

D. American Depositary Shares

**Fees and Charges Our ADS holders May Have to Pay**

The depository of our ADS facility, Deutsche Bank Trust Company Americas, shall charge the following fees for the services performed under the terms of the deposit agreement, unless otherwise agreed in writing by us and the depository; provided, however, that no fees shall be payable upon distribution of cash dividends so long as the charging of such fee is prohibited by the exchange, if any, upon which the ADSs are listed:

to any person to whom ADSs are issued or to any person to whom a distribution is made in respect of ADS distributions pursuant to stock dividends or other free distributions of stock, bonus distributions, stock splits or other distributions (except where converted to cash), a fee not in excess of US\$5.00 per 100 ADSs (or fraction thereof) so issued under the terms of the deposit agreement to be determined by the depository;

to any person surrendering ADSs for cancellation and withdrawal of deposited securities including, inter alia, cash distributions made pursuant to a cancellation or withdrawal, a fee not in excess of US\$5.00 per 100 ADSs (or fraction thereof) so surrendered;

to any holder of ADSs, a fee not in excess of US\$0.05 per ADS held for the distribution of cash proceeds, including cash dividends or sale of rights and other entitlements, not made pursuant to a cancellation or withdrawal;

to any holder of ADSs, a fee not in excess of US\$5.00 per 100 ADSs (or portion thereof) issued upon the exercise of rights; and

for the operation and maintenance costs in administering the ADSs, an annual fee of US\$0.05 or less per ADSs (such fee to be assessed against holders of record as of the date or dates set by the depositary as it sees fit and collected at the sole discretion of the depositary by billing such holders for such fee or by deducting such fee from one or more cash dividends or other cash distributions).

**Table of Contents**

In addition, holders, beneficial owners, persons depositing our common shares for deposit and persons surrendering ADSs for cancellation and withdrawal of deposited securities will be required to pay the following charges:

taxes (including applicable interest and penalties) and other governmental charges;

such registration fees as may from time to time be in effect for the registration of our common shares or other deposited securities with the foreign registrar and applicable to transfers of common shares or other deposited securities to or from the name of the custodian, the depository or any nominees upon the making of deposits and withdrawals, respectively;

such cable, telex, facsimile and electronic transmission and delivery expenses as are expressly provided in the deposit agreement to be at the expense of the person depositing or withdrawing common shares or holders and beneficial owners of ADSs;

the expenses and charges incurred by the depository in the conversion of foreign currency;

such fees and expenses as are incurred by the Depository in connection with compliance with exchange control regulations and other regulatory requirements applicable to common shares, deposited securities, ADSs and ADRs;

the fees and expenses incurred by the depository in connection with the delivery of deposited securities, including any fees of a central depository for securities in the local market, where applicable; and

any additional fees, charges, costs or expenses that may be incurred by the depository from time to time. Any other charges and expenses of the depository under the deposit agreement will be paid by our company upon agreement between the depository and us. All fees and charges may, at any time and from time to time, be changed by agreement between the depository and our company but subject, in the case of fees and charges payable by holders or beneficial owners, to the limitations set forth in the Form of ADR.

We will pay all other charges and expenses of the depository and any agent of the depository (except the custodian) pursuant to agreements from time to time between us and the depository. The fees described above may be amended from time to time.

The depository collects its fees for issuance and cancellation of ADSs directly from investors depositing shares or surrendering ADSs for the purpose of withdrawal or from intermediaries acting for them. The depository collects fees for making distributions to investors by deducting those fees from the amounts distributed or by selling a portion of distributable property to pay the fees. The depository may collect its annual fee for depository services by deduction from cash distributions, or by directly billing investors, or by charging the book-entry system accounts of participants acting for them. The depository may generally refuse to provide services until its fees for those services and any other unpaid fees are paid.

**Fees and Other Payments Made by the Depositary to Us**

The depositary has agreed to reimburse us for the establishment and maintenance of the ADS program and to provide us with assistance in relation to our investor relations program, the training of staff and certain other matters. Further, the depositary has agreed to share with us certain fees payable to the depositary by holders of ADSs. Since the commencement of our most recent fiscal year, we have received a sum of US\$3.7 million for the expenses related to our investor relations program, directors and officers liability and company insurance reimbursement, listing fees and legal service fees. The payment we received is offset against general and administrative expenses.

**PART II.**

**ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

None.



**Table of Contents**

**ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS**

None.

**ITEM 15. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our chief executive officer and chief financial officer, has performed an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report, as required by Rule 13a-15(b) under the Exchange Act. Based on that evaluation, our management has concluded that, as of May 31, 2018, our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure.

**Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15 (f) under the Exchange Act. Our management, with the participation of our chief executive officer and our chief financial officer, evaluated the effectiveness of our internal control over financial reporting based on criteria established in the framework in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, our management has concluded that our internal control over financial reporting was effective as of May 31, 2018.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Our independent registered public accounting firm has audited our internal control over financial reporting as of May 31, 2018 and has issued an attestation report set forth below.

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of New Oriental Education & Technology Group Inc.

**Opinion on Internal Control over Financial Reporting**

We have audited the internal control over financial reporting of New Oriental Education & Technology Group Inc. (the Company), its subsidiaries, its variable interest entities (the VIEs) and the VIEs' subsidiaries and schools (collectively, the Group) as of May 31, 2018, based on criteria established in *Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of May 31, 2018, based on the criteria established in Internal Control - Integrated Framework (2013) issued by the COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements and the financial statement scheduled as of and for the year ended May 31, 2018 of the Company and our report dated September 27, 2018 expressed an unqualified opinion on those consolidated financial statements and financial statement schedule.

**Basis for Opinion**

## **Table of Contents**

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered in accordance with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. As it is required in those standards, we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

### **Definition and Limitations of Internal Control over Financial Reporting**

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations of internal control over financial reporting, may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Beijing, People's Republic of China

September 27, 2018

### **Changes in Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during the period covered by this annual report on Form 20-F that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

### **ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

Our board of directors has determined that Denny Lee, an independent director (under the standards set forth in Section 303A of the NYSE Listed Company Manual and Rule 10A-3 under the Exchange Act) and the chairman of our audit committee, is our audit committee financial expert.

**ITEM 16B. CODE OF ETHICS**

Our board of directors has adopted a code of ethics that applies to our directors, officers, employees and agents, including certain provisions that specifically apply to our chief executive officer, chief financial officer, vice presidents and any other persons who perform similar functions for us. We have posted a copy of our code of business conduct and ethics on our website at <http://investor.neworiental.org>.

**Table of Contents****ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by Deloitte Touche Tohmatsu Certified Public Accountants LLP, our independent registered public accounting firm, for the periods indicated. We did not pay any other fees to our independent registered public accounting firm during the periods indicated below.

<i>(in thousands of US\$)</i>	<b>For the Year Ended May 31,</b>	
	<b>2017</b>	<b>2018</b>
Audit fees <sup>(1)</sup>	2,013	2,358
Audit related fees <sup>(2)</sup>		804
Tax fees <sup>(3)</sup>	100	330
All other fees		340

- (1) Audit fees means the aggregate fees billed for professional services rendered by our independent registered public accounting firm for the audit of our annual consolidated financial statements and the review of our comparative interim financial information.
- (2) Audit related fees means the fees billed for the audit services provided to our subsidiary or potential investees.
- (3) Tax fees represents the aggregated fees billed for professional services rendered by our independent registered public accounting firm for tax compliance, tax advice, and tax planning. The policy of our audit committee is to pre-approve all audit and non-audit services provided by Deloitte Touche Tohmatsu Certified Public Accountants LLP, including audit services, audit-related services, tax services and other services as described above, other than those for de minimis services which are approved by the audit committee prior to the completion of the audit.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not applicable.

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

None.

**ITEM 16F. CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANTS**

Not applicable.

**ITEM 16G. CORPORATE GOVERNANCE**

Section 303A.12(a) of the NYSE Listed Company Manual requires each listed company's chief executive officer to certify to the NYSE each year that he or she is not aware of any violation by the company of NYSE corporate governance listing standards. We are a Cayman Islands company, and our chief executive officer is not required under applicable Cayman Islands law to make such a certification. Pursuant to the exception granted to foreign private issuers under Section 303A.00 of the NYSE Listed Company Manual, we have followed our home country practice in this regard and have not in the past submitted the certification set forth in Section 303A.12(a) of the NYSE Listed Company Manual.

Section 303A.01 of the NYSE Listed Company Manual requires each listed company to have a majority of independent directors on the board of directors after the first anniversary of the company's listing on the NYSE. We are not required under the laws of the Cayman Islands to have a majority of independent directors on our board of directors. Pursuant to the exception granted to foreign private issuers under Section 303A.00 of the NYSE Listed Company Manual, we have elected to follow our home country practice with respect to our board of directors. Currently, we have six directors on our board, consisting of three independent directors and three directors who are, or have been within the past three years, also our executive officers. Nevertheless, we have maintained fully independent audit, compensation and nominating and corporate governance committees on our board of directors since the first anniversary of our NYSE listing.

Section 303A.08 of the NYSE Listed Company Manual requires a listed company to obtain its shareholders' approval of all equity-compensation plans, and any material revisions to the terms of such plans. Under Cayman Islands law, we are not required to obtain shareholders' approval for adoption of new equity-compensation plans or amendments to our existing equity incentive plan. Our board amended our 2006 share incentive plan in September 2012 to clarify that the administrator of the plan has the power to reduce the exercise price of an outstanding option and also reduce the number of the underlying common shares without seeking shareholders' approval, if such modification would not result in significant additional share-based compensation expenses to be incurred by our company. In addition, our board adopted our 2016 share incentive plan in January 2016. We have followed the home country practice and obtained the board approval but not shareholder approval for amending our 2006 share incentive plan as well as adopting the 2016 share incentive plan as described above.

**Table of Contents**

Other than the requirements discussed above, there are no significant differences between our corporate governance practices and those followed by domestic listed companies as required under the NYSE Listed Company Manual. A copy of our corporate governance guidelines is available on our website at <http://investor.neworiental.org>.

**ITEM 16H. MINE SAFETY DISCLOSURE**

Not applicable.

**ITEM 17. FINANCIAL STATEMENTS**

We have elected to provide financial statements pursuant to Item 18.

**ITEM 18. FINANCIAL STATEMENTS**

The consolidated financial statements of New Oriental Education & Technology Group Inc. are included at the end of this annual report.

**Table of Contents****ITEM 19. EXHIBITS**

<b>Exhibit Number</b>	<b>Description of Document</b>
1.1	<u>Amended and Restated Memorandum and Articles of Association (incorporated by reference to Exhibit 3.2 of the Registrant's F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
2.1	<u>Form of Registrant American Depositary Receipt (incorporated by reference to Exhibit A to Exhibit (a)(4) of post-effective amendment No. 1 to the registration statement on Form F-6 (File No. 333-176069), filed with the Commission on April 25, 2012)</u>
2.2	<u>Registrant's Specimen Certificate for Common Shares (incorporated by reference to Exhibit 4.2 of the Registrant's F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
2.3	<u>Form of Deposit Agreement among the Registrant, the depositary and holders of the American Depositary Receipts (incorporated by reference to Exhibit 4.3 of the Registrant's F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
2.4	<u>Supplement and Amendment No. 2 to Deposit Agreement, dated as of August 5, 2011, between the Registrant, the depositary and holders and beneficial owners of American Depositary Receipts issued thereunder (incorporated by reference to Exhibit (a)(3) to the registration statement on Form F-6 (File No. 333-176069), filed with the Commission on August 5, 2011)</u>
2.5	<u>Supplement and Amendment No. 3 to Deposit Agreement, dated as of April 25, 2012, between the Registrant, the depositary and holders and beneficial owners of American Depositary Receipts issued thereunder (incorporated by reference to Exhibit (a)(4) of post-effective amendment No. 1 to the registration statement on Form F-6 (File No. 333-176069), filed with the Commission on April 25, 2012)</u>
4.1	<u>2006 Share Incentive Plan, as amended (incorporated by reference to Exhibit 4.1 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on October 12, 2012)</u>
4.2	<u>Form of Indemnification Agreement with the Registrant's directors and officers (incorporated by reference to Exhibit 10.2 of the Registrant's F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
4.3	<u>Form of Employment Agreement (incorporated by reference to Exhibit 10.3 of the Registrant's F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
4.4	<u>English Translation of Form of New Enrollment System Development Service Agreement between Beijing Decision and New Oriental schools (incorporated by reference to Exhibit 99.4 of our F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)</u>
4.5	



English Translation of Trademark License Agreement dated May 13, 2006 between the Registrant and New Oriental China (incorporated by reference to Exhibit 99.6 of our F-1 registration statement (File No. 333-136825), as amended, initially filed with the Commission on August 22, 2006)

4.6 English Translation of Equity Pledge Agreement, dated April 23, 2012 and its Supplemental Agreements dated September 19, 2014 and February 16, 2017 among New Oriental China, Beijing Century Friendship Education Investment Co., Ltd. and Beijing Hewstone Technology Co., Ltd. (incorporated by reference to Exhibit 4.6 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)

4.7 English Translation of Equity Pledge Agreement dated April 23, 2012 and its Supplemental Agreements dated September 19, 2014 and February 16, 2017 among New Oriental China, Beijing Century Friendship Education Investment Co., Ltd. and Beijing Decision Education & Consulting Co., Ltd. (incorporated by reference to Exhibit 4.7 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)

**Table of Contents**

Exhibit Number	Description of Document
4.8	<u>English Translation of Equity Pledge Agreement dated April 23, 2012 and its Supplemental Agreements dated September 19, 2014 and February 16, 2017 among New Oriental China, Beijing Century Friendship Education Investment Co., Ltd. and Beijing Pioneer Technology Co., Ltd. (incorporated by reference to Exhibit 4.9 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)</u>
4.9	<u>English Translation of Equity Pledge Agreement dated April 23, 2012 and its Supplemental Agreements dated September 19, 2014 and February 16, 2017 among New Oriental China, Beijing Century Friendship Education Investment Co., Ltd. and Beijing Smart Wood Software Technology Co., Ltd. (incorporated by reference to Exhibit 4.10 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)</u>
4.10	<u>Proxy Agreement and Power of Attorney, dated as of December 3, 2012, by and among Beijing Pioneer Technology Co., Ltd., Beijing Century Friendship Education Investment Co., Ltd. and New Oriental China (incorporated by reference to Exhibit 4.34 of amendment no. 2 to our annual report on Form 20-F/A (File No. 001-32993) filed with the Securities and Exchange Commission on February 22, 2013)</u>
4.11	<u>Master Exclusive Service Agreement, dated as of September 19, 2014, its Amendment No. 1 dated as of January 28, 2016 and Amendment No. 2 dated as of February 16, 2017, by and between Beijing Pioneer and New Oriental China (incorporated by reference to Exhibit 4.13 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)</u>
4.12	<u>English Translation of Option Agreement dated February 16, 2017 among New Oriental China, Beijing Century Friendship Education Investment Co., Ltd. and Beijing Decision Education &amp; Consulting Co., Ltd. (incorporated by reference to Exhibit 4.15 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2017)</u>
4.13	<u>2016 Share Incentive Plan (incorporated by reference to Exhibit 4.15 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 27, 2016)</u>
4.14*	<u>Deed of Non-Competition Undertakings, dated as of August 28, 2018 issued by New Oriental Education &amp; Technology Group Inc. in favor of Koolearn Technology Holding Limited</u>
4.15*	<u>English Translation of Equity Pledge Agreement, dated as of May 10, 2018 among Beijing Dexin Dongfang Network Technology Co., Ltd., Beijing New Oriental Xuncheng Network Technology Co., Ltd. and its shareholders</u>
4.16*	<u>English Translation of Exclusive Option Purchase Agreement, dated as of May 10, 2018 among Beijing Dexin Dongfang Network Technology Co., Ltd., Beijing New Oriental Xuncheng Network Technology Co., Ltd. and its shareholders</u>
4.17*	<u>English Translation of Powers of Attorney, dated as of May 10, 2018 issued by Beijing New Oriental Xuncheng Network Technology Co., Ltd and its shareholders.</u>
4.18*	

English Translation of Exclusive Management Consultancy and Cooperation Agreement, dated as of May 10, 2018 among Beijing Dexin Dongfang Network Technology Co., Ltd., Beijing New Oriental Xuncheng Network Technology Co., Ltd. and its subsidiaries and shareholders

4.19\*

English Translation of Letters of Undertaking, dated as of May 10, 2018, issued by (i) Beijing Century Friendship Education Investment Co., Ltd. and its shareholders and (ii) each of the general partners of limited partnerships that are shareholders of Beijing New Oriental Xuncheng Network Technology Co., Ltd. to Koolearn Technology Holding Limited and Beijing Dexin Dongfang Network Technology Co., Ltd.

**Table of Contents**

<b>Exhibit Number</b>	<b>Description of Document</b>
8.1*	<u>Subsidiaries of the Registrant</u>
11.1	<u>Amended and Restated Code of Business Conduct and Ethics of the Registrant (incorporated by reference to Exhibit 11.1 of our annual report on Form 20-F (File No. 001-32993) filed with the Securities and Exchange Commission on September 25, 2015)</u>
12.1*	<u>Certification by Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
12.2*	<u>Certification by Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
13.1**	<u>Certification by Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>
13.2**	<u>Certification by Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>
15.1*	<u>Consent of Tian Yuan Law Firm</u>
15.2*	<u>Consent of Deloitte Touche Tohmatsu Certified Public Accountants LLP</u>
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.

\*\* Furnished herewith.

**Table of Contents**

**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

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

By: /s/ Chenggang Zhou  
Name: Chenggang Zhou  
Title: Chief Executive Officer

Date: September 27, 2018

**Table of Contents**

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

***INDEX TO CONSOLIDATED FINANCIAL STATEMENTS***

***FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018***

CONTENTS	PAGE(S)
<u>REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM</u>	F-2
<u>CONSOLIDATED BALANCE SHEETS AS OF MAY 31, 2017 AND 2018</u>	F-3 - F-4
<u>CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018</u>	F-5
<u>CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018</u>	F-6
<u>CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018</u>	F-7 - F-8
<u>CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018</u>	F-9 - F-10
<u>NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018</u>	F-11 - F-58
<u>ADDITIONAL INFORMATION FINANCIAL STATEMENT SCHEDULE 1</u>	F-59 - F-64

**Table of Contents**

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

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF

NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.

**Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of New Oriental Education & Technology Group Inc., its subsidiaries, its variable interest entities (the VIEs ) and the VIEs subsidiaries and schools (collectively, the Group ) as of May 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income, changes in equity and cash flows for each of the three years in the period ended May 31, 2018, and the related notes and the schedule I listed in the Index (collectively referred to as the financial statements ).

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Group as of May 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended May 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company s internal control over financial reporting as of May 31, 2018, based on criteria established in Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated September 27, 2018, expressed an unqualified opinion on the Company s internal control over financial reporting.

**Basis for Opinion**

These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the Group s consolidated financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Beijing, the People s Republic of China

September 27, 2018

We have served as the Company's auditor since 2006.

F-2



**Table of Contents****CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share data, or otherwise noted)**

	As of May 31,	
	2017	2018
	US\$	US\$
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	641,018	983,319
Restricted cash	44	47
Term deposits	195,085	107,741
Short-term investments	1,312,942	1,623,763
Accounts receivable, net of allowance of US\$585 and US\$485 as of May 31, 2017 and 2018, respectively	3,343	3,179
Inventory, net	31,742	40,175
Prepaid expenses and other current assets, net of allowance of US\$595 and US\$914 as of May 31, 2017 and 2018, respectively	119,397	182,095
Amounts due from related parties, current	5,948	1,595
Long-term investments due within one year	16,743	
Total current assets	2,326,262	2,941,914
Restricted cash, non-current	3,608	3,399
Property and equipment, net	282,800	449,592
Land use rights, net	3,668	3,785
Amounts due from related parties, non-current	1,748	2,226
Long-term deposits	24,023	40,099
Long-term prepaid rents	849	191
Intangible assets, net	4,005	8,544
Goodwill, net	14,083	31,729
Long-term investments, net	217,259	433,333
Deferred tax assets, non-current, net	28,858	43,323
Other non-current assets	17,816	19,577
Total assets	2,924,979	3,977,712
<b>LIABILITIES, MEZZANINE EQUITY AND EQUITY</b>		
Current liabilities		
Accounts payable (including accounts payable of the consolidated variable interest entities without recourse to the Company of US\$24,138 and US\$39,279 as of May 31, 2017 and 2018, respectively)	24,258	39,889
Accrued expenses and other current liabilities (including accrued expenses and other current liabilities of the consolidated variable interest entities without recourse to the Company of US\$238,864 and US\$335,955 as of May 31, 2017 and 2018, respectively)	260,700	373,537
Income taxes payable (including income taxes payable of the consolidated variable interest entities without recourse to the Company of US\$40,306 and US\$54,844 as of May 31, 2017)	51,045	67,233

and 2018, respectively)		
Amounts due to related parties (including amounts due to related parties of the consolidated variable interest entities without recourse to the Company of US\$48 and US\$30 as of May 31, 2017 and 2018, respectively)	48	30
Deferred revenue (including deferred revenue of the consolidated variable interest entities without recourse to the Company of US\$833,932 and US\$1,244,748 as of May 31, 2017 and 2018, respectively)	866,630	1,270,195
Total current liabilities	1,202,681	1,750,884
Deferred tax liabilities, non-current (including deferred tax liabilities, non-current of the consolidated variable interest entities without recourse to the Company of US\$2,174 and US\$13,782 as of May 31, 2017 and 2018, respectively)	2,220	12,133
Total liabilities	1,204,901	1,763,017

**Table of Contents****CONSOLIDATED BALANCE SHEETS - CONTINUED****(In thousands, except share and per share data, or otherwise noted)**

	As of May 31,	
	2017	2018
	US\$	US\$
Commitments and contingencies (Note 21)		
Mezzanine equity		
Redeemable non-controlling interests		206,624
Equity		
Common shares (US\$0.01 par value; 300,000,000 shares authorized as of May 31, 2017 and 2018; 158,379,387 shares issued as of May 31, 2017 and 2018; 157,687,444 and 158,319,910 shares outstanding as of May 31, 2017 and 2018, respectively)	1,584	1,584
Treasury stock	(7)	(1)
Additional paid-in capital	249,126	129,059
Statutory reserves	219,975	263,518
Retained earnings	1,171,109	1,352,543
Accumulated other comprehensive income	39,161	244,886
<b>Total New Oriental Education &amp; Technology Group Inc. shareholders equity</b>	<b>1,680,948</b>	<b>1,991,589</b>
Non-controlling interests	39,130	16,482
<b>Total equity</b>	<b>1,720,078</b>	<b>2,008,071</b>
<b>Total liabilities, mezzanine equity and equity</b>	<b>2,924,979</b>	<b>3,977,712</b>

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****CONSOLIDATED STATEMENTS OF OPERATIONS****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	For the years ended May 31,		
	2016 US\$	2017 US\$	2018 US\$
<b>NET REVENUES</b>			
Educational programs and services	1,309,339	1,608,954	2,165,152
Books and other services	169,009	190,555	282,278
Total net revenues	1,478,348	1,799,509	2,447,430
<b>Operating cost and expenses</b>			
Cost of revenues	(614,364)	(749,586)	(1,065,740)
Selling and marketing	(197,897)	(232,826)	(324,249)
General and administrative	(471,010)	(554,948)	(794,482)
Total operating cost and expenses	(1,283,271)	(1,537,360)	(2,184,471)
Gain on disposal of a subsidiary	3,760		
<b>OPERATING INCOME</b>	198,837	262,149	262,959
<b>OTHER INCOME, NET</b>			
Interest income	66,861	61,445	84,838
Realized gain from long-term investments		7,086	7,366
Impairment loss from long-term investments		(2,338)	(980)
Miscellaneous income, net	1,586	2,367	2,841
Income before income taxes and loss from equity method investments	267,284	330,709	357,024
(Provision) Benefit for income taxes:			
Current	(39,467)	(51,142)	(72,785)
Deferred	1,936	518	13,377
Provision for income taxes	(37,531)	(50,624)	(59,408)
Loss from equity method investments	(4,425)	(3,289)	(379)
<b>Net income</b>	225,328	276,796	297,237
Less: Net income attributable to non-controlling interests	444	2,339	1,107
<b>Net income attributable to New Oriental Education &amp; Technology Group Inc. s shareholders</b>	224,884	274,457	296,130

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Net income per common share (Note 19)

- Basic	1.43	1.74	1.87
- Diluted	1.43	1.74	1.87

Weighted average shares used in calculating basic net income per share

- Basic	156,782,439	157,551,320	158,168,794
- Diluted	157,391,686	157,986,394	158,556,500

The accompanying notes are an integral part of these consolidated financial statements.

F-5

**Table of Contents****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(In thousands, except share and per share data, or otherwise noted)**

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Net income	225,328	276,796	297,237
Other comprehensive income, net of tax			
Foreign currency translation adjustment	(72,464)	(47,440)	79,293
Unrealized gain on available-for-sale investments, net of tax effect of nil, US\$3,762 and US\$8,825 for the years ended May 31, 2016, 2017 and 2018, respectively	36,635	22,521	129,545
Other comprehensive (loss) / income	(35,829)	(24,919)	208,838
Comprehensive income	189,499	251,877	506,075
Comprehensive income attributable to non-controlling interests	1,172	1,207	4,220
Comprehensive income attributable to New Oriental Education & Technology Group Inc. s shareholders	188,327	250,670	501,855

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

(All amounts in thousands, except for share data)

	Common shares		Additional paid-in capital	Treasury stock	Accumulated other comprehensive income	Statutory reserve	Retained earnings	Total New Oriental Education & Technology Group Inc. shareholders' equity	Non-controlling interests	Total shareholders' equity
	Number	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$
Balance as of May 31, 2015	156,486,763	1,584	141,653	(19)	99,505	153,610	824,015	1,220,348	3,496	1,223,844
Reissuance of treasury stock for the exercises of employee share options	240,304		2,428	3				2,431		2,431
Reissuance of treasury stock for non-vested equity shares	712,330		(7)	7						
Share-based compensation expenses			16,810					16,810		16,810
Transfer to statutory reserves						31,853	(31,853)			
Dividend declared (a)							(62,668)	(62,668)		(62,668)
Equity restructure of a subsidiary (b)			23,214			(766)	(22,448)			
Net income							224,884	224,884	444	225,328
Foreign currency translation adjustment					(72,193)			(72,193)	(271)	(72,464)
Unrealized gain on available-for-sale securities, net of tax effect of nil					35,636			35,636	999	36,635
Capital contribution from			39,579					39,579	28,919	68,498

non-controlling interests										
Repurchase of shares from non-controlling interests			(255)				(255)	(3,497)		(3,752)
Balance as of May 31, 2016	157,439,397	1,584	223,422	(9)	62,948	184,697	931,930	1,404,572	30,090	1,434,662
Reissuance of treasury stock for the exercises of employee share options	48,047		256					256		256
Reissuance of treasury stock for non-vested equity shares	200,000		(2)	2						
Share-based compensation expenses			20,287					20,287		20,287
Transfer to statutory reserves						35,278	(35,278)			
Net income							274,457	274,457	2,339	276,796
Foreign currency translation adjustment					(46,331)			(46,331)	(1,109)	(47,440)
Unrealized gain on available-for-sale investments, net of tax effect of US\$3,762					22,544			22,544	(23)	22,521
Capital contribution from non-controlling interests and new non-controlling interests recognized in an acquisition			5,163					5,163	7,833	12,996
Balance as of May 31, 2017	157,687,444	1,584	249,126	(7)	39,161	219,975	1,171,109	1,680,948	39,130	1,720,078
Reissuance of treasury stock for the exercises of employee share options	500		1					1		1



Reissuance of treasury stock for non-vested equity shares	631,966		(6)	6						
Share-based compensation expenses			57,443					57,443		57,443
Transfer to statutory reserves					43,543	(43,543)				
Dividend declared (c)							(71,153)	(71,153)	(231)	(71,384)
Net income							296,130	296,130	1,107	297,237
Foreign currency translation adjustment					76,344			76,344	2,949	79,293
Unrealized gain on available-for-sale investments, net of tax effect of US\$8,825					129,381			129,381	164	129,545
Capital contribution from non-controlling interests and new non-controlling interests recognized in acquisitions										
Repurchase of shares from non-controlling interests					(113,784)			(113,784)	2,015	(111,769)
Balance as of May 31, 2018	158,319,910	1,584	129,059	(1)	244,886	263,518	1,352,543	1,991,589	16,482	2,008,071

**Table of Contents**

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

**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY - CONTINUED**

**(All amounts in thousands, except for share data)**

- (a) On July 19, 2015, the Company declared a special cash dividend in the amount of US\$0.4 per American Depositary Share ( ADS ). The aggregate amount of cash dividend paid was US\$62,668, which was funded by retained earnings. The dividend was fully paid on October 7, 2015 to shareholders of record at the close of business on September 4, 2015. One ADS represents one common share.
  - (b) In January 2016, Beijing New Oriental Xuncheng Network Technology Co., Ltd. ( Xuncheng ), a subsidiary of the Group, transformed from a limited liability company to a joint stock limited company. The Group's accumulated retained earnings and statutory reserve related to Xuncheng were reclassified to additional paid-in-capital in the consolidation financial statements.
  - (c) On July 25, 2017, the Company declared a special cash dividend in the amount of US\$0.45 per ADS. The aggregate amount of cash dividend paid was US\$71,153, which was funded by retained earnings. The dividend was fully paid on October 6, 2017 to shareholders of record at the close of business on September 1, 2017.
- The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(All amounts in thousands)**

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Cash flows from operating activities			
Net income	225,328	276,796	297,237
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation of property and equipment	47,281	53,864	77,081
Amortization of intangible assets	1,122	1,419	1,839
Amortization of land use rights	112	106	110
Loss on disposal of property and equipment	2,061	1,747	2,032
Gain on disposal of a subsidiary	(3,760)		
Goodwill impairment		1,682	
Impairment loss from long-term investments		2,338	980
Realized gain from long-term investments		(7,086)	(7,366)
Share-based compensation expenses	16,810	20,287	57,443
Allowance (reversal) for doubtful accounts	904	486	576
Provision (reversal) for inventory	615	(152)	(461)
Loss from equity method investments	4,425	3,289	379
Deferred income taxes	(1,936)	(518)	(14,821)
Changes in operating assets and liabilities			
Accounts receivables	(187)	(75)	767
Inventory	(6,264)	(5,224)	(5,855)
Prepaid expenses and other current assets	(7,711)	(14,796)	(51,738)
Amounts due from related parties	1,108	(1,288)	4,250
Long-term deposits	(532)	(9,652)	(14,300)
Long term prepaid rent	169	(624)	1,185
Accounts payable	4,830	3,592	13,728
Accrued expenses and other current liabilities	54,364	40,331	68,226
Income taxes payable	7,878	18,529	15,473
Amounts due to related parties	(1,887)	8	(21)
Deferred revenue	179,583	237,635	334,383
Net cash provided by operating activities	524,313	622,694	781,127
Cash flows from investing activities			
Payments for restricted cash	(5,461)	(1,197)	(732)
Proceeds from release of restricted cash	4,747	1,333	1,159
Purchase of term deposits	(64,540)	(130,000)	(117,166)
Proceeds from maturity of term deposits	42,603	18,836	212,690

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Payments for short-term investments	(1,112,172)	(1,343,198)	(1,250,239)
Proceeds from maturity of short-term investments	851,250	820,380	1,025,721
Purchase of property and equipment	(64,401)	(105,736)	(214,255)
Proceeds from disposal of property and equipment	1,310	2,807	9,812
Purchase of Ainuo Shida, net of cash acquired of US\$2,499 (Note 3)		(908)	
Business acquisition, net of cash acquired of US\$12,210 (Note 3)			(999)
Payments for available-for-sale investments	(78,764)	(43,498)	(55,206)
Payments for equity method investments	(468)	(1,473)	(456)
Proceeds from held-to-maturity investments	115,178	112,200	
Purchase of land use rights			(5,357)
Payments for cost method investments			(11,688)
Proceeds from cost method investment	540		

F-9

**Table of Contents**

**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED**

(All amounts in thousands)

	For the years ended May 31,		
	2016 US\$	2017 US\$	2018 US\$
<b>Cash flows from investing activities</b>			
Loans provided to related parties	(2,575)	(1,810)	
Proceeds from disposal of Beijing Dianshi Jingwei Technology Co., Ltd ( Dianshi Jingwei )	1,520		
Proceeds from disposal of Boost Caring	1,496		
<b>Net cash used in investing activities</b>	<b>(309,737)</b>	<b>(672,264)</b>	<b>(406,716)</b>
<b>Cash flows from financing activities</b>			
Proceeds from issuances of common shares upon exercise of share option	2,176	542	1
Withholding tax for employees	(6,419)	(4,557)	(7,241)
Cash paid for dividend	(62,668)		(71,153)
Capital contribution from non-controlling interests	69,747	8,807	93,159
Repurchase of shares from non-controlling interests	(3,752)		(89,647)
<b>Net cash (used in) provided by financing activities</b>	<b>(916)</b>	<b>4,792</b>	<b>(74,881)</b>
<b>Effects of exchange rate changes</b>	<b>(35,749)</b>	<b>(23,413)</b>	<b>42,771</b>
<b>Net change in cash and cash equivalents</b>	<b>177,911</b>	<b>(68,191)</b>	<b>342,301</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>531,298</b>	<b>709,209</b>	<b>641,018</b>
<b>Cash and cash equivalents at end of year</b>	<b>709,209</b>	<b>641,018</b>	<b>983,319</b>
<b>Supplement disclosure of cash flow information</b>			
Income taxes paid	32,037	36,665	57,005
<b>Non-cash investing and financing activities</b>			
Payable for investments and acquisitions			5,420
Payable for purchase of property and equipment	11,953	21,445	45,590

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****1. ORGANIZATION AND PRINCIPAL ACTIVITIES**

New Oriental Education & Technology Group Inc. (the Company) was incorporated in the Cayman Islands. The Company, its consolidated subsidiaries and its variable interest entities (the VIEs) and the VIEs subsidiaries and schools are collectively referred to as the Group.

The Group provides educational services in the People's Republic of China (the PRC) primarily under the New Oriental brand. The Group offers a wide range of educational programs, services and products, consisting primarily of language training and test preparation, primary and secondary school education, online education, content development and distribution, overseas study consulting services, pre-school education and study tour.

As of May 31, 2018, details of the Company's major subsidiaries, its VIEs and the VIEs major subsidiaries and schools were as follows:

Name	Date of incorporation or acquisition	Place of incorporation (or establishment)/ operation	Legal ownership	Principal activity
<b>Major subsidiaries of the Company:</b>				
Beijing Decision Education & Consulting Company Limited ( Beijing Decision )	April 20, 2005	PRC	100%	Educational technology and management services
Beijing Judgment Education & Consulting Company Limited ( Beijing Judgment )	April 20, 2005	PRC	100%	Educational consulting and software development
Beijing Hewstone Technology Company Limited ( Beijing Hewstone )	April 20, 2005	PRC	100%	Educational software development
Elite Concept Holdings Limited ( Elite Concept )	December 3, 2007	Hong Kong	100%	Educational consulting

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Winner Park Limited ( Winner Park )	December 9, 2008	Hong Kong	100%	Educational consulting
Smart Shine International Limited ( Smart Shine )	December 9, 2008	Hong Kong	100%	Educational consulting
Beijing Pioneer Technology Company Limited ( Beijing Pioneer )	January 8, 2009	PRC	100%	Educational software development
Shanghai Smart Words Software Technology Company Limited ( Shanghai Smart Words )	December 8, 2010	PRC	100%	Educational consulting and software development
Beijing Smart Wood Software Technology Company Limited ( Beijing Smart Wood )	December 21, 2011	PRC	100%	Educational consulting and software development
Beijing New Oriental Walkite International Travel Co., Ltd.	May 22, 2012	PRC	100%	Study tour
Beijing Joy Tend Technology Company Limited ( Beijing Joy Tend )	January 31, 2013	PRC	100%	Educational consulting and software development
Beijing Right Time Technology Company Limited ( Beijing Right Time )	January 31, 2013	PRC	100%	Educational consulting and software development
Abundant State Limited ( Abundant )		The British Virgin Islands		
	March 20, 2013	( BVI )	100%	Educational consulting
Beijing Magnificence Technology Company Limited ( Beijing Magnificence )	November 1, 2013	PRC	100%	Educational consulting and software development
Beijing Top Technology Company Limited ( Beijing Top )	November 13, 2013	PRC	100%	Educational consulting and software development
Beijing Shenghe Technology Company Limited ( Beijing Shenghe )	May 27, 2014	PRC	100%	Educational consulting and software development
Walkite International Academy Co., Ltd. ( Walkite UK )	March 16, 2015	U.K.	100%	Study tour
Walkite International Academy (U.S.A.) Co., Ltd. ( Walkite US )	April 13, 2015	U.S.A.	100%	Study tour
	September 18, 2016	PRC	100%	

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Beijing Jinhong Software Technology Company Limited ( Beijing Jinhong )				Educational consulting and software development
New Oriental Vision Overseas Consulting Australia Pty Ltd. ( Overseas AU )	January 25, 2017	Australia	100%	Consulting
Zhuhai Zekai Software Technology Company Limited ( Zhuhai Zekai )	June 26, 2017	PRC	100%	Educational consulting and software development

F-11



**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

(All amounts in thousands, except for share and per share data, or otherwise noted)

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

Name	Date of incorporation or acquisition	Place of incorporation (or establishment)/ operation	Legal ownership	Principal activity
<b>Major subsidiaries of the Company:</b>				
Garden House Limited ( Garden House )	September 1, 2017	Hong Kong	70%	Pre-school education
One World Limited ( One World )	September 1, 2017	Hong Kong	70%	Pre-school education
Blingabc Limited ( Blingabc )	December 27, 2017	U.S.A.	100%	Educational consulting
Beijing Zhiyuan Hangcheng Software Technology Company Limited ( Beijing Zhiyuan Hangcheng )	January 16, 2018	PRC	100%	Educational consulting and software development
Koolearn Technology Holding Limited ( Koolearn Holding )	February 7, 2018	Cayman	68%	Online education service
New Oriental Xuncheng Technology (HK) Limited ( Koolearn Tech )	March 2, 2018	Hong Kong	100%	Online education service
Beijing Dexin Dongfang Network Technology Co., Ltd. ( Dexin Dongfang )	March 21, 2018	PRC	N/A	Educational consulting and software development
<b>VIEs of the Company:</b>				
New Oriental Education & Technology Group Co., Ltd ( New Oriental China )	August 2, 2001	PRC	N/A	Education consulting, software development and distributions and other services
Beijing New Oriental Xuncheng Network Technology Co., Ltd. ( Xuncheng )	March 11, 2005	PRC	N/A	Online education service

**Major subsidiaries and schools of the VIEs:**

Beijing Haidian District Privately-Funded New Oriental School ( Beijing Haidian School )	October 5, 1993	PRC	N/A	Language training and test preparation
Shanghai Yangpu District New Oriental Advanced Study School	June 1, 2000	PRC	N/A	Language training and test preparation
Guangzhou Haizhu District Privately-Funded New Oriental Training School ( Guangzhou Haizhu School ) (a)	September 8, 2000	PRC	N/A	Language training and test preparation
Wuhan New Oriental Training School	April 28, 2002	PRC	N/A	Language training and test preparation
Beijing New Oriental Yangzhou Foreign Language School	June 6, 2002	PRC	N/A	Primary and secondary school education
Tianjin New Oriental Training School	August 21, 2002	PRC	N/A	Language training and test preparation

F-12

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

(All amounts in thousands, except for share and per share data, or otherwise noted)

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

Name	Date of incorporation or acquisition	Place of incorporation (or establishment)/ operation	Legal ownership	Principal activity
<b>Major subsidiaries and schools of the VIEs:</b>				
Xi'an Yanta District New Oriental School	November 26, 2002	PRC	N/A	Language training and test preparation
Nanjing Gulou New Oriental Advanced Study School	November 28, 2002	PRC	N/A	Language training and test preparation
Beijing New Oriental Dogwood Cultural Communications Co., Ltd.	May 16, 2003	PRC	N/A	Content development and distribution
Chongqing New Oriental Training School	August 15, 2003	PRC	N/A	Language training and test preparation
Chengdu New Oriental School	August 18, 2003	PRC	N/A	Language training and test preparation
Shenzhen New Oriental Training School	October 15, 2003	PRC	N/A	Language training and test preparation
Beijing New Oriental Vision Overseas Consultancy Co., Ltd.	February 19, 2004	PRC	N/A	Overseas study consulting service
Beijing New Oriental Dogwood, Bookstore, Audio & Video Co., Ltd.	March 2, 2004	PRC	N/A	Content development and distribution
Taiyuan New Oriental Training School	April 20, 2005	PRC	N/A	Language training and test preparation
Jinan New Oriental School	May 31, 2005	PRC	N/A	Language training and test preparation
Zhengzhou New Oriental Training School	July 19, 2005	PRC	N/A	Language training and test preparation
Hangzhou New Oriental Advanced Study School	July 21, 2005	PRC	N/A	Language training and test preparation

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Qingdao Happy Alice Kindergarten	November 29, 2005	PRC	N/A	Pre-school education
Suzhou New Oriental School	April 26, 2006	PRC	N/A	Language training and test preparation
Nanchang Donghu District New Oriental Language School	March 16, 2007	PRC	N/A	Language training and test preparation
Beijing New Oriental Stars Education & Consulting Co., Ltd	July 11, 2007	PRC	N/A	Pre-school education
Beijing Chaoyang District Kindergarten of Stars	November 20, 2007	PRC	N/A	Pre-school education
Xiamen Siming District New Oriental Education Training School	July 8, 2008	PRC	N/A	Language training and test preparation
Changchun Tongwen Gaokao Training School	September 1, 2008	PRC	N/A	College admission examination training
Changchun Tongwen Senior High School	September 1, 2008	PRC	N/A	Primary and secondary school education
Nanjing Yuhuatai District New Oriental Kindergarten of Stars	April 10, 2009	PRC	N/A	Pre-school education
Beijing Changping New Oriental Foreign Language School	July 19, 2010	PRC	N/A	Primary and secondary school education
Shanghai Vision Overseas Service Co., Ltd.	March 24, 2011	PRC	N/A	Overseas study consulting service
Beijing Management Software Training Institute	September 1, 2012	PRC	N/A	Primary and secondary school education
Beijing New Oriental Kuxue Huisi Network Technology Co., Ltd.	February 1, 2013	PRC	N/A	Online education service
Guangzhou Panyu District Privately-Funded New Oriental Training Centre ( Guangzhou Panyu School ) (a)	June 19, 2013	PRC	N/A	Language training and test preparation
Guangzhou New Oriental Training School ( Guangzhou School ) (a)	August 20, 2013	PRC	N/A	Language training and test preparation

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

(All amounts in thousands, except for share and per share data, or otherwise noted)

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

Name	Date of incorporation or acquisition	Place of incorporation (or establishment)/ operation	Legal ownership	Principal activity
<b>Major subsidiaries and schools of the VIEs:</b>				
Beijing Dongfang Zhuoyong Investment Management Co., Ltd.	April 29, 2014	PRC	N/A	Investment management
Qingdao Alice Education & Technology Company Limited	August 21, 2014	PRC	N/A	Pre-school education
Yangzhou Guangling District New Oriental Kindergarten of Stars	August 26, 2014	PRC	N/A	Pre-school education
Qingdao Chengyang District Happy Alice Kindergarten	October 30, 2014	PRC	N/A	Pre-school education
Qingdao Laoshan District Happy Alice Kindergarten	December 4, 2014	PRC	N/A	Pre-school education
New Oriental Vision Overseas Consulting (U.K.) Ltd.	June 10, 2015	U.K.	N/A	Overseas study consulting service
Qingdao New Oriental Vision Overseas Consultancy Co., Ltd.	August 20, 2015	PRC	N/A	Overseas study consulting service
Beijing New Oriental Vision Overseas Service Co., Ltd.	February 24, 2016	PRC	N/A	Overseas study consulting service
Beijing Dongfang Youbo Network Technology Co., Ltd. ( Dongfang Youbo )	June 23, 2016	PRC	N/A	Online education service
	July 18, 2016	PRC	N/A	Consulting

Beijing Bright the Future Education & Technology Co., Ltd.				
Beijing Ainuo Shida Education & Technology Co., Ltd ( Ainuo Shida )	December 1, 2016	PRC	N/A	Oversea study consulting service
Beijing Chaoyang District Taiyanggong Kindergarten of Stars				
	January 20, 2017	PRC	N/A	Pre-school education
Ningbo Meishan Bonded Port Area Hexin Oriental Asset Management Co., Ltd.				
	April 28, 2017	PRC	N/A	Asset management
Beijing Haiwei Career Service Co., Ltd.				
	June 9, 2017	PRC	N/A	Oversea study consulting service
Hangzhou Shengshen Technology Co., Ltd ( Hangzhou Shengshen )				
	October 9, 2017	PRC	N/A	Language training and test preparation

- (a) Guangzhou Panyu School and Guangzhou School were established in the year ended May 31, 2014. Although they are separate legal entities, from the perspective of the Group's internal management, they together with Guangzhou Haizhu School are considered as one school since they are operated by the same local management in Guangzhou, the PRC.

#### The VIE arrangements

The 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 of China. The Company's offshore holding companies are not educational institutions and do not provide educational services outside of 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. Accordingly, the Company's offshore holding companies are not allowed to directly own and operate schools in China. The Company conducts substantially all of its education business in China through contractual arrangements with its VIEs, New Oriental China and its subsidiaries and schools and Xuncheng and its subsidiaries. Since the operations of New Oriental China and its subsidiaries and schools and Xuncheng and its subsidiaries are closely interrelated and almost indistinguishable from one another, the risks and rewards associated with their operations are substantially the same. In addition, the Company consolidates New Oriental China, its subsidiaries and schools, Xuncheng and its subsidiaries as disclosed. Therefore, the Company aggregates the disclosures related to New Oriental China, its subsidiaries and schools, and Xuncheng and its subsidiaries as the VIEs in the Company's consolidated financial statements. The VIEs hold the requisite licenses and permits necessary to conduct the Company's education business. In addition, the VIEs hold leases and other assets necessary to operate the Company's schools and learning centers, employ teachers and generate substantially all of the Company's revenues.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

**VIE Arrangements between New Oriental China and the Company's PRC subsidiaries**

The Company and its wholly owned subsidiaries in China (the "WFOEs") have entered into the following contractual arrangements with New Oriental China, New Oriental China's subsidiaries and schools and New Oriental China's shareholders that enable the Company to (1) have power to direct the activities that most significantly affects the economic performance of the VIEs, (2) receive substantially all of the economic benefits of the VIEs that could be significant to the VIEs 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 the 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 the Company's discretion. Accordingly, the Company is considered the primary beneficiary of the VIE and has consolidated the VIE's financial results of operations, assets and liabilities in the Company's consolidated financial statements. In making the conclusion that the Company is the primary beneficiary of the VIE, the Company believes the Company's rights under the terms of the exclusive option agreement provide it with the substantive kick-out rights. More specifically, the Company believes the terms of the exclusive option agreement are valid, binding and enforceable under the PRC laws and regulations currently in effect. The Company also believes that the minimum amount of consideration permitted by the applicable PRC law to exercise the option does not represent a financial barrier or disincentive for the Company to currently exercise its rights under the exclusive option agreement. A simple majority vote of the Company's board of directors is required to pass a resolution to exercise the Company's rights under the exclusive option agreement, for which Mr. Michael Minhong Yu (Mr. Yu)'s consent is not required. The Company's rights under the exclusive option agreement give the Company the power to control the shareholders of New Oriental China and thus the power to direct the activities that most significantly impact the schools' economic performance given that New Oriental China has the power to direct the activities of the schools via its sponsorship interest. In addition, the Company's rights under the power of attorney also reinforce the Company's abilities to direct the activities that most significantly impact the VIE's economic performance. The Company also believes that this ability to exercise control ensures that the VIE will continue to execute and renew service agreements and pay service fees to the Company. By charging service fees in whatever amounts the Company deems fit, and by ensuring that service agreements are executed and renewed indefinitely, the Company has the rights to receive substantially all of the economic benefits from the VIE.

**Service agreements.** There are four types of service agreements: (i) trademark license agreements, (ii) new enrollment system development service agreements, (iii) other operating service agreements, and (iv) sale of educational software agreements.

- (i) Trademark license agreements. Pursuant to the trademark license agreement dated May 13, 2006 between the Company as the licensor and New Oriental China as the licensee, the Company has licensed the trademarks to New Oriental China for its use in China. The Company has also allowed New Oriental China to enter into sub-license agreements with its subsidiaries and schools pursuant to which each of the subsidiaries and schools may use the trademarks in China by paying license fees. This license is valid from May 14, 2006 to December 31, 2050, subject to the renewal every ten years upon the expiration of the trademark registration.
  
- (ii) New enrollment system development service agreements. Beijing Decision has entered into new enrollment system development service agreements with the schools of New Oriental China, under which Beijing Decision agreed to provide new enrollment system development and regular maintenance services to those schools of New Oriental China for a fee equal to the applicable fee rate multiplied by the number of new student enrollments. These agreements can be renewed by both parties to the agreements.
  
- (iii) Other operating service agreements. Pursuant to operating service agreements between certain WFOEs and the subsidiaries or schools of New Oriental China, the WFOEs have agreed to provide certain operating services to the subsidiaries or schools of New Oriental China for fees that are calculated based on a percentage, ranging from 2.0% to 6.0%, of respective revenues of each of the subsidiaries and schools. A majority of these agreements provide unlimited two-year or five-year automatic renewal without consent of the WFOEs. The remaining agreements can be renewed by both parties to the agreements.
  
- (iv) Sale of educational software agreements. Eight WFOEs, namely Beijing Hewstone, Beijing Pioneer, Beijing Smart Wood, Beijing Joy Tend, Beijing Magnificence, Beijing Top, Beijing Shenghe and Beijing Jinghong, entered into agreements whereby the WFOEs sell various self-developed educational software to the subsidiaries or schools of New Oriental China. Except for four agreements that are silent on renewal, these agreements provide unlimited two-year automatic renewal terms, and the subsidiaries and schools of New Oriental China cannot terminate the agreements without the consent of the WFOEs in China.



**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

**VIE Arrangements between New Oriental China and the Company's PRC subsidiaries - Continued**

***Master exclusive service agreements.*** On September 19, 2014, Beijing Pioneer entered into a master exclusive service agreement with New Oriental China to enable the Company's wholly owned subsidiaries in China to receive substantially all of the economic benefits of New Oriental China and its subsidiaries and schools. Under the master exclusive service agreement, Beijing Pioneer has the exclusive rights to provide or designate any entities affiliated with it to provide New Oriental China and its subsidiaries and schools the technical and business support services, including new enrollment system development service, sale of educational software and other operating services. Each service provider specified in the service agreement (iv) has the rights to determine the fees associated with the services it provides based on the technical difficulty and complexity of the services and the actual labor costs it incurs for providing the services during the relevant period. The term of this agreement is ten years and will be automatically extended upon expiration. Beijing Pioneer may terminate the agreement at any time with a 30-day prior written notice to New Oriental China, whereas none of New Oriental China and its subsidiaries and schools can terminate this agreement. The various existing service agreements mentioned in service agreements (i)~(iv) will remain effective after the inclusion of the master exclusive service agreement; however, if they have any conflict with the terms and conditions of the master exclusive service agreement, the master exclusive service agreement will prevail. The master exclusive service agreement was effective on September 19, 2014.

***Equity pledge agreements.*** Pursuant to the equity pledge agreements dated May 25, 2006 among New Oriental China, all of the shareholders of New Oriental China, Beijing Hewstone and Beijing Decision, each shareholder of New Oriental China agreed to pledge his or its equity interest in New Oriental China to Beijing Hewstone and Beijing Decision to secure the performance of the VIEs' obligations 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 Hewstone and Beijing Decision.

In January 2012, ten former shareholders of New Oriental China completed the transfer, for no consideration, of all of their equity interests in New Oriental China to Beijing Century Friendship Education Investment Co., Ltd. ( Century Friendship ), a PRC domestic enterprise controlled by the Company's founder and chairman, Mr. Yu. Prior to the transfer, Century Friendship had held 53% of the equity interests in New Oriental China while the ten former shareholders of New Oriental China held the remaining equity interests. In connection to the transfer, five new equity pledge agreements dated April 23, 2012 were entered into among New Oriental China, Century Friendship and five WFOEs, whereby Century Friendship has agreed to pledge all of its equity interests in New Oriental China to the

WFOEs to secure the VIEs' performance of their obligations under the trademark license agreements, new enrollment system development service agreements, other operating service agreements and sale of educational software agreements. 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 the WFOEs. The terms of the April 2012 equity pledge agreements are substantially the same as the 2006 equity pledge agreements.

In February 2017, as part of efforts to streamline the corporate structure, the Group removed Shanghai Smart Words as a party to the contractual arrangements with New Oriental China and its subsidiaries and schools and the shareholders. The rights and obligations of Shanghai Smart Words under these contractual arrangements have been assumed by Beijing Decision. The April 2012 equity pledge agreements have been amended to reflect the foregoing change while the terms of these agreements remain unchanged. The equity pledges of Century Friendship under the amended agreements have been registered with the Haidian District, Beijing branch of the State Administration of Industry and Commerce (the SAIC).

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

**VIE Arrangements between New Oriental China and the Company's PRC subsidiaries - continued**

***Exclusive option agreement.*** Pursuant to the exclusive option agreements entered into on various dates, as amended on May 25, 2006, among the Company, New Oriental China and its shareholders, the shareholders of New Oriental China are obligated to sell to the Company, and the Company has an exclusive, irrevocable and unconditional rights to purchase, or cause the shareholders of New Oriental China to sell to the Company's designated party, in the Company's sole discretion, part or all of the shareholders' equity interests in New Oriental China when and to the extent that applicable PRC law permits the Company to own part or all of such equity interests in New Oriental China. In addition, pursuant to the exclusive option agreements, the Company has an exclusive, irrevocable and unconditional right to request any existing shareholders of New Oriental China to transfer all or part of the equity interest in New Oriental China held by such shareholder to another PRC person or entity designated by the Company at any time in the discretion. The price to be paid by the Company or a PRC person or entity designated by the WFOEs will be the minimum amount of consideration permitted by applicable PRC law at the time when such share transfer occurs. As a result of the ten former shareholders of New Oriental China transferring all of their equity interests in New Oriental China to Century Friendship in January 2012, Century Friendship executed a new option agreement with Shanghai Smart Words and New Oriental China on April 23, 2012. The terms of this new option agreement are substantially the same as the 2006 exclusive option agreements.

On February 16, 2017, Beijing Decision entered into a new option agreement with Century Friendship and New Oriental China, replacing the previous option agreement dated April 23, 2012. Pursuant to the current option agreement, Century Friendship is obligated to sell to Beijing Decision, and Beijing Decision has an exclusive, irrevocable and unconditional rights 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, Beijing Decision 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 Beijing Decision at any time in its discretion. The purchase price to be paid by Beijing Decision 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 the Company's 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 rights 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.

### **VIE Arrangements between Dexin Dongfang and Xuncheng**

On May 10, 2018, Dexin Dongfang, the wholly-owned subsidiary of Koolearn Holding, entered into the contractual arrangements (the Contractual Arrangements ) with Xuncheng and the shareholders of Xuncheng, which enable Koolearn Holding to obtain control over Xuncheng, Beijing Kuxue Huisi Network Technology Co., Ltd. ( Kuxue Huisi ) and Dongfang Youbo (together the Xuncheng VIE entities ).

The Contractual Arrangements include the Exclusive Management Consultancy and Business Cooperation Agreement, Exclusive Call Option Agreement, Equity Pledge Agreement, Powers of Attorney, Dispute resolution and Letters of undertaking.

Through these Contractual Agreements, the Company has the ability to (1) expose, or has rights, to variable returns from its involvement with the investee and has ability to affect those returns through its power over Xuncheng VIE entities; (2) exercise equity holders controlling voting rights of Xuncheng VIE entities; (3) receive substantially all of the economic benefits of Xuncheng VIE entities in consideration for the business support, technical and consulting services provided by Dexin Dongfang; (4) obtain an irrevocable and exclusive right to purchase all or part of equity interests in the Xuncheng VIE entities from the respective equity holders at nil consideration or a minimum purchase price permitted under the PRC Laws; (5) obtain a pledge over the entire equity interest of Xuncheng from their equity holders as collateral security for all of Xuncheng VIE entities payments.

### ***Risks in relation to the VIE structure***

The Company believes that the contractual arrangements with its VIEs and their respective shareholders are in compliance with the PRC laws and regulations and are legally enforceable. However, uncertainties in the PRC legal system could limit the Company's ability to enforce the contractual arrangements. If the legal structure and contractual arrangements were found to be in violation of the PRC laws and regulations, the PRC government could:

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED**

*Risks in relation to the VIE structure - continued*

revoke the business and operating licenses of the Company's PRC subsidiaries and the VIEs;

discontinue or restrict the operations of any related-party transactions between the Company's PRC subsidiaries and the VIEs;

limit the Group's business expansion in China by way of entering into contractual arrangements;

impose fines or other requirements with which the Company's PRC subsidiaries and the VIEs may not be able to comply;

require the Company or the Company's PRC subsidiaries or the VIEs to restructure the relevant ownership structure or operations; or

restrict or prohibit the Company's use of the proceeds of the additional public offering to finance the Group's business and operations in China.

The Company's ability to conduct its education business may be negatively affected if the PRC government were to carry out any of the aforementioned actions. As a result, the Company may not be able to consolidate its VIEs in its consolidated financial statements as it may lose the ability to exert effective control over the VIEs and their respective shareholders and it may lose the ability to receive economic benefits from the VIEs. The Company, however, does not believe such actions would result in the liquidation or dissolution of the Company, its PRC subsidiaries or the VIEs.

Mr. Yu is the controlling shareholder of Century Friendship, which owns all of the equity interests in New Oriental China, which in turn owns all of the equity interests in Xuncheng, and Mr. Yu is also a beneficial owner of the Company. The interests of Mr. Yu as the beneficial owner of the VIEs may differ from the interests of the Company as a whole, since Mr. Yu is one of the beneficial shareholders of the Company, holding 13.1% of the total common shares outstanding as of May 31, 2018. The Company cannot assure that when conflicts of interest arise, Mr. Yu will

act in the best interests of the Company or that conflicts of interests will be resolved in the Company's favor. Currently, the Company does not have existing arrangements to address potential conflicts of interest Mr. Yu may encounter in his capacity as a beneficial owner and director of the VIEs, on the one hand, and as a beneficial owner and director of the Company, on the other hand. The Company believes Mr. Yu will not act contrary to any of the contractual arrangements and the exclusive option agreement provides the Company with a mechanism to remove Mr. Yu as a beneficial shareholder of the VIEs should he act to the detriment of the Company. The Company relies on Mr. Yu, as a director and executive officer of the Company, to fulfill his fiduciary duties and abide by laws of the PRC and Cayman Islands and act in the best interest of the Company. If the Company cannot resolve any conflicts of interest or disputes between the Company and Mr. Yu, the Company would have to rely on legal proceedings, which could result in disruption of its business, and there is substantial uncertainty as to the outcome of any such legal proceedings.

In addition, the current shareholders of New Oriental China and Xuncheng are also beneficial owners of the Company and therefore have no current interest in seeking to act contrary to the contractual arrangements. However, to further protect the investors' interest from any risk that the shareholders of New Oriental China may act contrary to the contractual arrangements, the Company, through Beijing Pioneer, entered into an irrevocable power of attorney with Century Friendship on December 3, 2012, which replaces the powers of attorney executed by Century Friendship on April 23, 2012. Through the power of attorney, Century Friendship entrusted Beijing Pioneer as its proxy to exercise its rights as the shareholder of New Oriental China with respect to an aggregate of 100% of the equity interests in New Oriental China.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****1. ORGANIZATION AND PRINCIPAL ACTIVITIES - CONTINUED***Risks in relation to the VIE structure - continued*

The following financial statement balances and amounts of the VIEs were included in the accompanying consolidated financial statements after the elimination of intercompany balances and transactions among the offshore companies, WFOEs and the VIEs in the Group:

	As of May 31,	
	2017	2018
	US\$	US\$
Total current assets	1,590,750	2,081,374
Total non-current assets	488,709	750,316
<b>Total assets</b>	<b>2,079,459</b>	<b>2,831,690</b>
Total current liabilities	1,137,288	1,674,857
Total non-current liabilities	2,174	13,782
<b>Total liabilities</b>	<b>1,139,462</b>	<b>1,688,639</b>

  

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Net revenues	1,443,851	1,777,864	2,417,203
Net income	313,828	333,456	479,190
Net cash provided by operating activities	457,267	454,753	711,591
Net cash used in investing activities	(286,235)	(459,532)	(429,265)
Net cash provided by (used in) financing activities	63,328	4,250	(96,429)

The VIEs contributed an aggregate of 97.7%, 98.8% and 98.8% of the consolidated net revenues for the years ended May 31, 2016, 2017 and 2018, respectively. The Company's operations not conducted through contractual arrangements with the VIEs primarily consist of the lease of its commercial property. As of the fiscal years ended May 31, 2017 and 2018, the VIEs accounted for an aggregate of 71.1% and 71.2%, respectively, of the consolidated total assets, and 94.6% and 95.8%, respectively, of the consolidated total liabilities. The assets not associated with the VIEs were primarily consist of cash and cash equivalents, prepaid expenses, short-term investments and long-term investments.

There are no consolidated VIEs' assets that are collateralized for the VIEs' obligations and can only be used to settle the VIEs' obligations. There are no creditors (or beneficial interest holders) of the VIEs that have recourse to the general credit of the Company or any of its consolidated subsidiaries. There are no terms in any arrangements, considering both explicit arrangements and implicit variable interests that require the Company or its subsidiaries to provide financial support to the VIEs. However, if the VIEs ever need financial support, the Company or its subsidiaries may, at its option and subject to statutory limits and restrictions, provide financial support to its VIEs through loans to the shareholders of the VIEs or entrustment loans to the VIEs.

Relevant PRC laws and regulations restrict the VIEs from transferring a portion of its net assets, equivalent to the balance of its statutory reserve and its share capital, to the Company in the form of loans and advances or cash dividends. Please refer to Note 26 for disclosure of restricted net assets.



**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES**

**Basis of presentation**

The consolidated financial statements of the Group have been prepared in accordance with the accounting principles generally accepted in the United States of America ( US GAAP ).

**Basis of consolidation**

The consolidated financial statements include the financial statements of the Company, its subsidiaries, its VIEs and the VIEs' subsidiaries and schools. The Company and its WFOEs have entered into contractual arrangements with the VIEs and its shareholders, which enable the Company to (1) have power to direct activities that most significantly affect the economic performance of the VIEs, and (2) receive the economic benefits of the VIEs that could be significant to the VIEs. Accordingly, the Company is considered the primary beneficiary of the VIEs and has consolidated the VIEs' financial results of operations, assets and liabilities in the Company's consolidated financial statements. All inter-company transactions and balances have been eliminated upon consolidation.

**Use of estimates**

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, related disclosures of contingent liabilities at the balance sheet date, and revenue and expenses in the consolidated financial statements and accompanying notes. Significant accounting estimates reflected in the Group's consolidated financial statements include purchase price allocation relating to the business acquired, the valuation allowance for deferred tax assets, economic lives and impairment of property and equipment, impairment of goodwill, impairment of intangible assets, impairment of long-term investments, fair value of long-term available-for-sale investments, allowance for doubtful accounts, mezzanine equity and etc. Actual results could differ from those estimates.

**Business combinations**

Business combinations are recorded using the acquisition method of accounting. The purchase price of the acquisition is allocated to the tangible assets, liabilities, identifiable intangible assets acquired and non-controlling interest, if any, based on their estimated fair values as of the acquisition date. The excess of the purchase price over those fair values is recorded as goodwill. Acquisition-related expenses and restructuring costs are expensed as incurred.

In a business combination achieved in stages, the Group remeasures the previously held equity interest in the acquiree immediately before obtaining control at its acquisition-date fair value and the remeasurement gain or loss, if any, is recognized in the consolidated statements of operations.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and highly liquid investments which are unrestricted as to withdrawal or use, and which have original maturities of three months or less when purchased.

Restricted cash

Restricted cash represents Renminbi ( RMB ) deposit in bank accounts as deposits for establishing new subsidiaries and schools. Restricted cash is classified as either current or non-current based on when the funds will be released in accordance with the terms of the respective agreement.

Term deposits

Term deposits consist of deposits placed with financial institutions with original maturities of greater than three months and less than one year.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**Short-term investments

The Group's short-term held-to-maturity investments are classified as short-term investments on the consolidated balance sheets based on their contractual maturity dates which are less than one year and are stated at their amortized costs.

The Group reviews its held-to-maturity investments for other-than-temporary impairment ( OTTI ) based on the specific identification method. The Group considers available quantitative and qualitative evidence in evaluating the potential impairment of its short-term investments. If the cost of an investment exceeds the investment's fair value, the Group considers, among other factors, general market conditions, expected future performance of the investees, the duration and the extent to which the fair value of the investment is less than the cost, and the Group's intent and ability to hold the investments. OTTI is recognized as a loss in the consolidated statements of operations.

Allowance for doubtful accounts

Accounts receivable represents amounts due from corporate customers of the Group's various subsidiaries and schools. The Group provides allowance for doubtful accounts based on historical collection experience and a review of the current status of accounts receivable and other receivable. Accounts receivable and other receivable are presented net of allowance for doubtful accounts.

Changes in the allowance for doubtful accounts were as follows:

	As of May 31,	
	2017	2018
	US\$	US\$
Beginning balance	1,210	1,180
Charge during the year	486	576
Written-off	(516)	(357)
Ending balance	1,180	1,399

Inventory

Inventory mainly consists of books. Inventory is stated at the lower of cost or net realizable value.

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated on a straight line basis over the following estimated useful lives:

Buildings	20-50 years
Transportation equipment	10 years
Furniture and education equipment	5 years
Computer equipment and software	3 years
Leasehold improvements	Shorter of the lease term or estimated useful life

Table of Contents

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

Construction in progress

The Group constructs certain of its property and equipment. Construction in progress represents the costs incurred in connection with the construction of property and equipment. Costs classified as construction in progress include all costs of obtaining the asset and bringing it to the location and in the condition necessary for its intended use. Depreciation is recorded at the time the assets are ready for intended use.

Land use rights

Land use rights are recorded at cost and amortized on a straight-line basis over the remaining term of the land certificate, from 38.5 years to 50 years.

Impairment of long-lived assets

The Group reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may no longer be recoverable. When these events occur, the Group measures impairment by comparing the carrying value of the long-lived assets to the estimated undiscounted future cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flow is less than the carrying amount of the assets, the Group would recognize an impairment loss based on the fair value of the assets. The Group did not record any impairment losses on long-lived assets during the years ended May 31, 2016, 2017 and 2018.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired in business combinations. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

Goodwill is tested for impairment at the reporting unit level on an annual basis (May 31 for the Group) and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in the stock prices, business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and determination of the fair value of each reporting unit. The estimation of fair value of each reporting unit using a discounted cash flow methodology also requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, estimation of the long-term rate of growth for the Group's business, estimation of the useful life over which cash flows will occur, and determination of the Group's weighted average cost of capital. The estimates used to calculate the fair value of a reporting unit change from year to year based on operating results and market conditions. Changes in these estimates and assumptions could materially affect the determination of fair value and goodwill impairment for the reporting unit.

In order to test goodwill for impairment, the Group first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If it is more likely than not that the fair value of a reporting unit is less than its carrying amount, goodwill is then tested following a two-step process. The first step compares the fair value of each reporting unit to its carrying amount, including goodwill. If the fair value of each reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step compares the implied fair value of goodwill to the carrying value of a reporting unit's goodwill.

The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

**Goodwill** - continued

An impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill. The Group recorded nil, US\$1,682 and nil impairment losses during the years ended May 31, 2016, 2017 and 2018, respectively.

**Long-term investments**

The Group's long-term investments consist of cost method investments, equity method investments and available-for-sale investments.

(a) **Cost Method Investments**

For investee companies over which the Group does not have significant influence nor control through investment in common shares or in-substance common shares and which do not have readily determinable fair value, the Group carries the investment at cost and recognizes as income any dividend received from distribution of the investee's earnings.

The Group reviews its cost method investments for impairment whenever an event or circumstance indicates that an OTTI has occurred. The Group considers available quantitative and qualitative evidence in evaluating potential impairment of its cost method investments. An impairment charge is recorded if the cost of an investment exceeds its fair value and such excess is determined to be other-than temporary.

The Group estimates the fair value of these investee companies based on the discounted cash flow approach. Factors the Group considers in making such a determination include general market conditions, the duration and the extent to which the fair value of an investment is less than its cost, and the Group's intent and ability to hold such investment. The Group did not record any impairment losses on its cost method investments during the years ended May 31, 2016, 2017 and 2018.

(b) **Equity Method Investments**

Investee companies over which the Group has the ability to exercise significant influence, but does not have a controlling interest through investment in common shares or in-substance common shares, are accounted for using the equity method. Significant influence is generally considered to exist when the Group has an ownership interest in the voting stock of the investee between 20% and 50%. Other factors, such as representation on the investee's board of directors, voting rights and the impact of commercial arrangements, are also considered in determining whether the equity method of accounting is appropriate. For certain investments, where the Group holds more than 50% equity interest, the Group may only have significant influence but not have control over the investees. For certain investments, where the Group holds less than 20% equity or voting interest, the Group may also have significant influence. Equity method is also used to account for these investments.

Under the equity method, the Group initially records its investments at cost and subsequently recognizes its proportionate share of each equity investee's net income or loss after the date of investment into earnings and accordingly adjusts the carrying amount of the investment.

An impairment charge is recorded if the carrying amount of the investment exceeds its fair value and this condition is determined to be other-than temporary. The Group estimated the fair value of the investee company based on comparable quoted price for similar investment in active market, if applicable, or discounted cash flow approach which requires significant judgments, including the estimation of future cash flows, which depends on internal forecasts, the estimation of long term growth rate of a company's business, the estimation of the useful life over which cash flows will occur, and the determination of the weighted average cost of capital. The Company recorded nil impairment losses on its equity method investment during the years ended May 31, 2016, 2017 and 2018.



Table of Contents

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

Long-term investments - continued

(c) Available-for-sale Investments

For investments in investees' preferred shares which are determined to be debt securities, the Group accounts for them as long-term available-for-sale investments when they are not classified as either trading or held-to-maturity investments. Available-for-sale investments are carried at their fair values and the unrealized gains or losses from the changes in fair values are recorded in accumulated other comprehensive income. Realized gains or losses, and provision for decline in value judged to be other than temporary, if any, are recognized in the consolidated statements of operations.

The Group reviews its investments for OTTI based on the specific identification method. The Group considers available quantitative and qualitative evidence in evaluating potential impairment of its investments. If the cost of an investment exceeds the investment's fair value, the Group considers, among other factors, general market conditions, government economic plans, the duration and the extent to which the fair value of the investment is less than the cost, the Group's intent and ability to hold the investment, and the financial condition and near term prospects of the investees. The Company recorded nil, US\$2,338 and US\$980 impairment losses on its available-for-sale investments during the years ended May 31, 2016, 2017 and 2018, respectively.

Non-controlling interests and redeemable non-controlling interests

The Group's consolidated financial statements include entities in which the Company has a controlling financial interest. Earnings or losses attributable to minority shareholders of the consolidated affiliated company are classified separately as non-controlling interests in the Company's consolidated statements of operations.

Non-controlling interests in subsidiaries that are redeemable outside of the Company's control for cash or other assets are classified outside of permanent equity at the redemption value. If the redemption event is probable to occur, the Company adjusts the redeemable non-controlling interests to the redemption value on each balance sheet date with the changes recognized as an adjustment to retained earnings, or in the absence of retained earnings, as an adjustment to additional paid-in capital.

Value added tax ( VAT )

Pursuant to the PRC tax laws, in case of any product sales, generally the VAT rate is 3% of the gross sales for small scale VAT payer and 17% of the gross sales for general VAT payer. Most of the subsidiaries of the Company are deemed as general VAT payers for the sales of guidance materials and the intercompany sales of self-developed software. For general VAT payer, VAT on sales is calculated at 17% on revenue from product sales and paid after deducting input VAT on purchases. The net VAT balance between input VAT and output VAT is recorded as accrued expenses in the Group's consolidated financial statements.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

On January 1, 2012, the PRC Ministry of Finance and the State Administration of Taxation officially launched a pilot VAT reform program ( Pilot Program ), applicable to businesses in selected industries. Such VAT Pilot Program was phased in Beijing, Jiangsu, Anhui, Fujian, Guangdong, Tianjin, Zhejiang, and Hubei between September and December 2012. Business in the Pilot Program would pay VAT instead of sales tax. Starting from August 1, 2013, the Pilot Program was expanded to cover all regions in the PRC. Implementation of the Pilot Program, the new enrollment system development services and other operating services which were previously subject to business tax are therefore subject to VAT at the rate of 6% of revenue. The net VAT balance between input VAT and output VAT is recorded as accrued expenses in the Group s consolidated financial statements.

Since May 2016, in accordance with Cai Shui [2016] No. 68, the non-academic educational programs and services in short-term training schools are subject to a simple VAT collection method and apply for a 3% VAT rate. Therefore, the Group s non-academic educational programs and services in short-term language training schools which were previously subject to business tax are now subject to a VAT rate of 3%.

Since May 2018, in accordance with Cai Shui [2018] No.32, the VAT rate decreased to 16% of the gross sales for general VAT payer. Most of the Group s entities are deemed as general VAT payers for the sales of books and teaching materials and the intercompany sales of self-developed software. Therefore, for general VAT payer, VAT on sales is calculated at 16% on revenue from product sales and paid after deducting input VAT on purchases since May 1, 2018.

**Revenue recognition**

Revenue is recognized when persuasive evidence that an arrangement exists, delivery of the product or service has occurred, the selling price is both fixed and determinable and collection is reasonably assured. Revenue is reported net of business taxes, VAT and refunds. Business tax and VAT amounted to US\$52,993 for the year ended May 31, 2016. Subsequent to May 2016, the Group no longer incurred business taxes. The primary sources of the Group s revenues are as follows:

(a) Educational programs and services

The educational programs and services consist of language training and test preparation courses, pre-school education, primary and secondary school education and online education. Tuition is generally paid in advance and is initially recorded as deferred revenue. Revenue is recognized proportionately as the instruction is delivered over the period of the course for the course fees collected for enrollment in the language training and test preparation courses and online

education or ratably over the corresponding academic year for the school fees collected for enrollment in the pre-school education and primary and secondary school education, and is reported net of business taxes, VAT and refunds. Students are entitled to a short term trial period which commences on the date the course begins. 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 only those collected but unearned portion of the fee is available to be returned. Refunds have been insignificant for the years ended May 31, 2016, 2017 and 2018.

F-25

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED**

**Revenue recognition - continued**

**(b) Other services**

Other service revenues are primarily derived from consulting services to students regarding overseas studies and study tours. Revenue is recognized upon meeting the following criteria after a contract is signed, the price is fixed or determinable, services are delivered and collection is reasonably assured.

**(c) Books**

The Group sells books or other educational materials developed or licensed by the Group either through its own distribution channels or through third party distributors. Revenue from sales of books and other educational materials is recognized when the products are sold to the end customers. The Group provides books and other educational materials that are required for its courses and does not separately charge students for these items.

**Operating leases**

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases are charged to the consolidated statements of operations on a straight-line basis over the shorter of the lease term or estimated economic life.

**Advertising costs**

The Group expenses advertising costs as they incurred. Total advertising expenses were US\$39,753, US\$41,498 and US\$55,936, for the years ended May 31, 2016, 2017 and 2018, respectively, and have been included as part of selling and marketing expenses.

**Government subsidies**

The Group recognizes government subsidies as miscellaneous income when they are received because they are not subject to any past or future conditions, there are no performance conditions or conditions of use, and they are not subject to future return. Government subsidies received and recognized as miscellaneous income totaled US\$494, US\$1,325 and US\$2,945, for the years ended May 31, 2016, 2017 and 2018, respectively.

Foreign currency translation

The Company's functional and reporting currency is the United States dollars ( U.S. dollars ). The financial records of the Company's subsidiaries and the VIEs located in the PRC are maintained in their local currency, the RMB, which is the functional currency of these entities. The financial records of the Company's subsidiaries located in Hong Kong are maintained in U.S. dollars, which is the functional currency of these entities. The financial records of the Company's subsidiaries located in United Kingdom are maintained in their local currency, the Great Britain Pound ( GBP ), which is the functional currency of these entities. The financial records of the Company's subsidiary located in Australia are maintained in its local currency, the Australian Dollar ( AUD ), which is the functional currency of the entity. All financial records of the other entities are maintained in U.S. dollars.

Monetary assets and liabilities denominated in currencies other than the applicable functional currencies are translated into the reporting currency at the rates of exchange ruling at the balance sheet date. Equity accounts are translated at historical exchange rates, and revenues and expenses are translated using the average rate of exchange in effect during the reporting period. Translation adjustments are reported and shown as a separate component of other comprehensive income in the consolidated statements of changes in equity and consolidated statements of comprehensive income.

Transactions in currencies other than the functional currencies during the year are converted into the applicable functional currencies at the applicable rates of exchange prevailing at the dates of the transactions. Exchange gains and losses are recognized in the consolidated statements of operations.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED**

**Foreign currency risk**

The RMB is not a freely convertible currency. The State Administration for Foreign Exchange, under the authority of the People's Bank of China, controls the conversion of the RMB into other currencies. The value of the RMB is subject to changes in central government policies and to international economic and political developments affecting supply and demand in the China Foreign Exchange Trading System market. The Group's cash and cash equivalents, restricted cash, and term deposits denominated in RMB amounted to US\$762,895 and US\$989,070 as of May 31, 2017 and 2018, respectively.

**Fair value**

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Group considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when valuing the asset or liability. Authoritative literature provides a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The level in the hierarchy within which the fair value measurement in its entirety falls is based upon the lowest level of input that is significant to the fair value measurement as follows:

**Level 1**

Level 1 applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

**Level 2**

Level 2 applies to assets or liabilities for which there are inputs other than quoted prices included within Level 1 that are observable for the asset or liability such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which significant inputs are observable or can be derived principally from, or corroborated by, observable market data.

**Level 3**

Level 3 applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

Fair value of financial instruments

The Group's financial instruments consist primarily of cash and cash equivalents, restricted cash, term deposits, short-term investments, accounts receivable, amount due from/to related parties, long-term investment due within one year, available-for-sale investments, accounts payable and income tax payable. Available-for-sale investments are carried at fair value. The carrying amounts of cash and cash equivalents, restricted cash, term deposits, short-term investments, long-term investment due within one year, accounts receivable, amount due from/to related parties, accounts payable and income tax payable approximate their fair values due to the short-term maturities of these instruments.

Net income per share

Basic net income per share is computed by dividing net income attributable to the holders of common shareholders by the weighted average number of common shares outstanding during the year. Diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue common shares were exercised into common shares. Common share equivalents are excluded from the computation of the diluted net income per share in years when their effect would be anti-dilutive. The Group has share option and non-vested equity shares which could potentially dilute basic earnings per share in the future. To calculate the number of shares for diluted net income per share, the effect of the share options and non-vested equity shares is computed using the treasury stock method. The effect of mezzanine equity is computed using the if-converted method.



Table of Contents

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

Income taxes

The Group accounts for income taxes using the asset and liability approach. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax basis of assets and liabilities, net of operating loss carry forwards and credits, by applying enacted tax rates that will be in effect for the period in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in the consolidated statements of operations in the period of change. Deferred tax assets are reduced by a valuation allowance when it is considered more likely than not that some portion or all of the deferred tax assets will not be realized.

The Group accounts for uncertain tax positions by reporting a liability for unrecognized tax benefits resulting from uncertain tax positions taken or expected to be taken in a tax return. Tax benefits are recognized from uncertain tax positions when the Group believes that it is more likely than not that the tax position will be sustained on examination by the tax authorities based on the technical merits of the position. The Group recognizes interest and penalties, if any, related to unrecognized tax benefits in income tax expenses.

Comprehensive income

Comprehensive income includes net income, unrealized gain or loss on available-for-sale securities and foreign currency translation adjustments. Comprehensive income is reported in the consolidated statements of comprehensive income.

Share-based compensation

Share-based payments to employees and directors are measured based on the grant-date fair value of the equity instrument issued and recognized as compensation expenses net of forfeitures on a straight-line basis over the requisite service period, with a corresponding addition to paid-in capital. The Group uses the binomial option pricing model to measure the fair value of options granted and the quoted market price of the Company's common shares to measure the fair value of non-vested equity shares (NES) granted to employees at each measurement date. The binomial option pricing model is adopted because the Group believes that considering the possibility of exercise an option over the life of the option, as affected by the reality of changing stock prices and non-constant risk free rates, would better reflect the measurement objective of relevant accounting literature.

The amount of compensation expenses recognized at any date is at least equal to the portion of the fair value of the awards that are vested as of that date. The forfeitures are recognized based on the estimated forfeitures rate, upon the

adoption of ASU 2016-09 on June 1, 2017, they are recognized as they occur.

Concentration of credit risk

Financial instruments that potentially expose the Group to significant concentration of credit risk consist primarily of cash and cash equivalents, term deposits, restricted cash, short-term investments and accounts receivable. As of May 31, 2018, substantially all of the Group's cash and cash equivalents, term deposits, restricted cash and short-term investments were deposited with financial institutions with high-credit ratings and quality. Accounts receivable are typically unsecured and are derived from revenues earned from customers in the PRC. The Group performs periodic credit evaluations and provides an allowance for doubtful accounts to reduce the accounts receivable balance to its net realizable value. The Group did not have any customers constituting 10% or more of the consolidated net revenues and accounts receivable in the fiscal years 2016, 2017 and 2018, respectively.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

**Recent accounting pronouncements adopted**

In March 2016, the FASB issued ASU 2016-09, Compensation – Stock Compensation (Topic 718). The new guidance simplifies certain aspects related to income taxes, statement of cash flows, and forfeitures when accounting for share-based payment transactions. Certain of the amendments related to timing of the recognition of tax benefits and tax withholding requirements should be applied using a modified retrospective transition method. Amendments related to the presentation of the statement of cash flows should be applied retrospectively. All other provisions may be applied on a prospective or modified retrospective basis. For a public entity, the amendments in this ASU are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The Group adopted this ASU on June 1, 2017 and has elected to account for forfeitures as they occur rather than applying an estimated forfeiture rate to share-based compensation expenses on a prospective basis. The adoption did not have a material impact on the Group's financial position or results of operations. However, the retrospective application of cash paid for employee taxes on withheld shares from share-based awards resulted in a US\$6,419 and US\$4,557 reclassification of these cash outflows from operating activities to financing activities on the consolidated statements of cash flows for the years ended May 31, 2016 and 2017, respectively.

In March 2016, the FASB issued ASU No. 2016-07, simplifying the Transition to the Equity Method of Accounting. The amendments eliminate the requirement that when an investment qualified for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previous held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The amendments require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increase in the level of ownership interest or degree of influence that result in the adoption of the equity method. Earlier application is permitted. The Group adopted this ASU on June 1, 2017 and determined it had no impact on its consolidated financial statements as of May 31, 2018.

**Recently issued accounting pronouncements not yet adopted**

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 requires revenue recognition to depict the transfer of goods or services to customers in an amount that reflects the consideration that a company expects to be entitled to in exchange for the goods or services. To achieve this principle, a company must apply five steps including identifying the contract with a customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction price to the performance obligations, and recognizing revenue when (or as) the company satisfies the performance obligations. Additional quantitative and qualitative disclosure to enhance the understanding about the nature, amount, timing, and uncertainty of revenue and cash flows is also required. ASU 2014-09 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. In April 2016, the FASB issued ASU 2016-10, Identifying Performance Obligations and Licensing. ASU 2016-10 clarifies the following two aspects of ASU 2014-09: identifying performance obligations and licensing implementation guidance. The effective date of ASU 2016-10 is the same as the effective date of ASU 2014-09.

The Group expects to adopt ASU 2014-09 utilizing the modified retrospective method in the first quarter of fiscal year 2019. The Group has substantially completed the assessment of the impacts of the new standard to its existing portfolio of customer contracts. The Group does not believe the adoption of ASU 2014-09 would have a material effect on its current revenue recognition policies, except that it will be required to assess variable consideration included in its consulting service related to overseas study over the expected service period. The Group has also identified a provision under the new standard in relation to the incremental cost, commission fees, of obtaining a contract and will make judgments and estimates throughout the applicable periods. Certain additional financial statement disclosure are mandated by the new standard including disclosure of contract assets and contract liabilities as well as a disaggregated view of revenue.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

**Recently issued accounting pronouncements not yet adopted** - continued

In January 2016, the FASB issued a new pronouncement ASU 2016-01 Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities. The ASU requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. The ASU also requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments.

ASU 2016-01 was further amended in February 2018 by ASU 2018-03, Technical Corrections and Improvements to Financial Instruments Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. This update was issued to clarify certain narrow aspects of guidance concerning the recognition of financial assets and liabilities established in ASU 2016-01. This includes an amendment to clarify that an entity measuring an equity security using the measurement alternative may change its measurement approach to a fair valuation method in accordance with Topic 820, Fair Value Measurement, through an irrevocable election that would apply to that security and all identical or similar investments of the same issued.

ASU 2016-01 and ASU 2018-03 are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Adoption of the amendment must be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption, except for amendments related to equity instruments that do not have readily determinable fair values which should be applied prospectively. The Group will apply the new standard in the first quarter of fiscal year 2019. For investments in equity securities without readily determinable fair values, the Group will elect to use the measurement alternative defined as cost, less impairment, adjusted by observable price change. For investments in equity securities with readily determinable fair values, the Group will elect to account them at fair value change through earnings. The Group anticipates that the adoption of ASU 2016-01 may increase the volatility of its other income / expenses, as a result of the remeasurement of the equity securities upon the occurrence of observable price change.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The guidance supersedes existing guidance on accounting for leases with the main difference being that operating leases are to be recorded in the statement of financial position as right-of-use assets and lease liabilities, initially measured at the present value of the lease payments. For operating leases with a term of 12 months or less, a lessee is permitted to make an accounting policy

election not to recognize lease assets and liabilities. For public business entities, the guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application of the guidance is permitted. In transition, entities are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Group is in the process of evaluating the impact of the adoption of this pronouncement on its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Statements. This ASU requires a financial asset (or group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. This Accounting Standards Update affects entities holding financial assets and net investment in leases that are not accounted for at fair value through net income. The amendments affect loans, debt securities, trade receivables, net investments in leases, off balance sheet credit exposures, reinsurance receivables, and any other financial assets not excluded from the scope that have the contractual rights to receive cash. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. All entities may adopt the amendments in this Update through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). The Group is in the process of evaluating the impact of the adoption of this pronouncement on its consolidated financial statements.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**2. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

**Recently issued accounting pronouncements not yet adopted** - continued

In November 2016, the FASB issued ASU 2016-18: Statement of Cash Flows (Topic 230): Restricted Cash. The amendments in this Update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendments in this Update do not provide a definition of restricted cash or restricted cash equivalents. The amendments in this ASU on update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The amendments in this Update should be applied using a retrospective transition method to each period presented. The Group expects the adoption of this new ASU will change the presentation of restricted cash on the statement of cash flow.

In January 2017, the FASB issued ASU 2017-01: Business Combinations (Topic 805): Clarifying the Determination of Business. The Update requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This screen reduces the number of transactions that need to be further evaluated. If the screen is not met, the amendments in this ASU on update (1) required that to be considered a business, a set must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output and (2) remove the evaluation of whether a market participant could replace missing elements. Public business entities should apply the amendments in this Update to annual periods beginning after December 15, 2017, including interim period within those periods. Early adoption of the amendments in this Update is allowed. The amendments in this Update should be applied prospectively on or after the effective date. No disclosure are required at transition. The Group is in the process of evaluating the impact of the adoption of this pronouncement on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04: Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. To simplify the subsequent measurement of goodwill, the FASB eliminated Step 2 from the goodwill impairment test. Under the amendments in this Update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. An entity should apply the amendments in this ASU on update on a prospective basis. An entity is required to disclose the

nature of and reason for the change in accounting principle upon transition. A public business entity that is a SEC filer should adopt the amendments in this Update for its annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Group is in the process of evaluating the impact of the adoption of this pronouncement on its consolidated financial statements.

### **3. BUSINESS ACQUISITIONS**

Business acquisition in fiscal year 2017:

#### Acquisition of Ainuo Shida

In March 2015, the Group invested and paid US\$1,129 to obtain 18% equity interest in Ainuo Shida to expand the business of its oversea consulting and benefit from the synergistic effect expected from such investment. The investment was initially recognized as available-for-sale investment as the Group determined that it was a debt security and measured the investment subsequently at fair value. In December 2016, the Group acquired an additional 33% equity interest in Ainuo Shida, for a total consideration of US\$3,842, which was paid in full as of May 31, 2017. The acquisition resulted in the Group obtaining control of Ainuo Shida with an ownership of 51% equity interest.



**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****3. BUSINESS ACQUISITIONS - CONTINUED**

Business acquisition in fiscal year 2017: - continued

Acquisition of Ainuo Shida - continued

The Group recognized an investment gain of US\$723 as a result of remeasuring the 18% equity interest immediately to fair value before the business combination. The acquisition was recorded using the acquisition method of accounting. Accordingly, the acquired assets and liabilities were recorded at their fair value on the date of acquisition. The acquisition-date fair value of the equity interest held by the Group immediately prior to the acquisition date was measured at fair value using a discounted cash flow method and taking into account certain factors including the management projection of discounted future cash flow and an appropriate discount rate. The purchase price allocation was determined by the Group with assistance of an independent valuation appraiser. The purchase price was allocated on the date of acquisition as follows:

	US\$	Amortization period
Cash	2,499	
Other current assets	4,874	
Property and equipment	493	1-5 years
Intangible assets		
Trademark	1,708	10 years
Student base	1,069	1 year
Courseware	76	3 years
Goodwill	5,516	
Deferred revenue	(4,544)	
Other current liabilities	(1,496)	
Deferred tax liabilities	(713)	
Fair value of the 18% equity interest	(1,741)	
Non-controlling interests	(3,899)	

Total 3,842

Business acquisition in fiscal year 2018:

Acquisition of Hangzhou Shengshen

In October 2017, the Group acquired 100% equity interest in Hangzhou Shengshen, a K-12 education group located in Zhejiang, for a total consideration of US\$11,012, in which US\$5,309 had been paid during the year ended May 31, 2018. The acquisition was recorded using the acquisition method of accounting, accordingly, the acquired assets and liabilities were recorded at their fair value on the date of acquisition. The purchase price allocation was determined by the Group with assistance of an independent appraiser. The acquired goodwill is not deductible for tax purposes. The purchase price was allocated on the date of acquisition as follows:

	US\$	Amortization period
Cash	3,571	
Other current assets	704	
Property and equipment	1,148	1-5 years
Intangible assets		
Trademark	1,713	5 years
Student base	2,164	3 years
Goodwill	9,809	
Deferred revenue	(5,566)	
Other current liabilities	(1,562)	
Deferred tax liabilities	(969)	
<b>Total</b>	<b>11,012</b>	

F-32

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****3. BUSINESS ACQUISITIONS CONTINUED**

Business acquisition in fiscal year 2018: - continued

Other acquisitions

During the year ended May 31, 2018, the Group also made several other business acquisitions.

The total cash consideration of the business acquisitions was US\$6,992, in which US\$5,902 had been paid during the fiscal year 2018. The cash and cash equivalents, intangible assets, goodwill, deferred revenue and non-controlling interests acquired from these business acquisitions were US\$8,639, US\$2,294, US\$6,383, US\$15,215 and US\$1,683, respectively. The purchase price allocations were determined by the Group with assistance of an independent valuation appraiser.

The results of operations for all these acquired entities have been included in the Group's consolidated financial statements from their respective acquisition dates. The acquired goodwill is not deductible for tax purposes.

The following summarized unaudited pro forma results of operations for the years ended May 31, 2017 and 2018 assuming that these acquisitions during the year ended May 31, 2018 occurred as of June 1, 2017. These pro forma results have been prepared for comparative purpose only and do not purport to be indicative of the results of operations which actually would have resulted had the acquisitions occurred as of June 1, 2017, nor is it indicative of future operating results.

	For the years ended May 31,	
	2017 (unaudited) US\$	2018 (unaudited) US\$
Pro forma net revenues	1,815,660	2,451,735
Pro forma net income attributable to New Oriental Education and Technology Group Inc.	275,685	296,697
Pro forma net income per share basic	1.75	1.88
Pro forma net income per share diluted	1.75	1.87

**4. DISPOSAL OF SUBSIDIARIES****Disposal of Dianshi Jingwei**

In April 2016, the Group sold 51% equity interest in Beijing Dianshi Jingwei Technololy Co., Ltd ( Dianshi Jingwei ) to management of Dianshi Jingwei for a cash consideration of US\$2,325. As of the disposal date, Dianshi Jingwei had accumulated deficit resulting in the Group deriving a gain from the deconsolidation. The disposal gain recognized by the Group was US\$3,760 and was recorded in the consolidated statements of operations for the year ended May 31, 2016. Subsequent to this disposal, the Group accounted for its 49% investment in Dianshi Jingwei as an equity method investment because the Group retained the ability to exercise significant influence. The disposal of Dianshi Jingwei did not represent a strategic shift and did not have a major effect on the Group s operation.

The disposal gains from the transaction was presented as continuing operation.

**5. SHORT-TERM INVESTMENTS**

Short-term investments consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Held-to-maturity investments	1,312,942	1,623,763

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****5. SHORT-TERM INVESTMENTS - CONTINUED**

Short-term investments consist of various financial products purchased from Chinese banks and trusts and are classified as held-to-maturity investments as the Group has the positive intent and ability to hold the investments to maturity. The maturities of these financial products range from one month to less than one year, with variable interest rates. They are classified as short-term investments on the consolidated balance sheets as their contractual maturity dates are equal to or less than one year.

While these fixed-income financial products are not publicly traded, the Group estimated that their fair value approximate their amortized costs considering their short term maturities and high credit quality. No OTTI loss was recognized for the years ended May 31, 2016, 2017 and 2018, respectively.

**6. INVENTORY, NET**

Inventory, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Course materials in schools	7,419	12,020
Publications in bookstores	24,323	28,155
	31,742	40,175

Inventory was marked to the lower of cost or net realizable value and the inventory provision was reversed in the amount of US\$152 and US\$461 for the years ended May 31, 2017 and 2018, respectively.

**7. PREPAID EXPENSES AND OTHER CURRENT ASSETS, NET**

Prepaid expenses and other current assets, net, consisted of the following:

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	As of May 31,	
	2017	2018
	US\$	US\$
Prepaid rent	44,746	56,531
Advances to suppliers	29,358	43,913
Interest receivable	14,005	23,647
Rental deposits	8,355	10,953
Staff advances (a)	2,514	9,544
Receivable from exercise of options/NES		7,300
Prepaid advertising fees	4,235	6,917
Receivable from third parties platforms	3,211	5,967
VAT recoverable	2,305	3,493
Deposits of advertising and decoration	1,411	3,342
Prepaid property taxes and other taxes	947	212
Others (b)	8,905	11,190
Less: allowance for other receivables	(595)	(914)
	119,397	182,095

- (a) Staff advances were provided to staff for traveling and related use which are expensed as incurred.  
(b) Others primarily included prepaid maintenance fees, other receivables and other miscellaneous prepayments.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****8. LONG -TERM INVESTMENT DUE WITHIN ONE YEAR**

In October 2015, the Group invested US\$15,654 in a two-year trust named Trust 556 with an expected annualized interest rate of 8.5%. The principal and the interest are not guaranteed during the Group's holding period and will be paid upon maturity. The investments were classified as available-for-sale investments as the Group determined that the shares were debt security and unrealized gains of US\$706 and US\$1,089 were reported in other comprehensive income for the years ended May 31, 2016 and 2017, respectively. As of May 31, 2017, the investment amounting to US\$16,743 was reclassified to long-term investment due within one year.

In October 2017, Trust 556 was due and the Group accordingly redeemed the principal and interest for a total of US\$18,475 with realized gain of US\$2,821.

**9. PROPERTY AND EQUIPMENT, NET**

Property and equipment, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Buildings	141,477	156,324
Transportation equipment	8,618	9,936
Furniture and education equipment	88,671	128,670
Computer equipment and software	48,385	65,227
Leasehold improvements	216,848	349,953
	503,999	710,110
Less: accumulated depreciation	(243,035)	(275,940)
Exchange differences	7,182	(15,499)
Construction in progress	14,654	30,921
	282,800	449,592

Depreciation expenses for the years ended May 31, 2016, 2017 and 2018 were US\$47,281, US\$53,864 and US\$77,081, respectively.

**10. LAND USE RIGHTS, NET**

Land use rights, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Land use rights	5,003	5,315
Less: accumulated amortization	(1,307)	(1,417)
Exchange differences	(28)	(113)
Land use rights, net	3,668	3,785

Amortization expenses for land use rights for the years ended May 31, 2016, 2017 and 2018 were US\$112, US\$106 and US\$110, respectively. The Group expects to recognize US\$110 in amortization expense for each of the next five years and US\$3,235 thereafter.



Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****11. INTANGIBLE ASSETS, NET**

Intangible assets, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Intangible assets with indefinite lives:		
Trademark	241	256
Intangible assets with finite lives:		
Trademark	2,976	5,575
Courseware	122	129
Student base	2,995	7,014
Favorable lease	689	732
License	415	415
	7,438	14,121
Less: accumulated amortization	(3,498)	(5,272)
Exchange differences	65	(305)
	4,005	8,544

Amortization expenses for the intangible assets for the years ended May 31, 2016, 2017 and 2018, were US\$1,122, US\$1,419 and US\$1,839, respectively. As of May 31, 2018, the Group expects to record amortization expenses related to intangible assets US\$2,004, US\$1,982, US\$1,332, US\$1,037 and US\$720 for the years ended May 31, 2019, 2020, 2021, 2022, 2023, respectively, and US\$1,213 thereafter.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****12. GOODWILL, NET**

Goodwill, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Beginning balance	10,545	15,765
Acquisition	5,516	16,192
Exchange differences	(296)	1,454
Ending balance	15,765	33,411
Accumulated impairment	(1,682)	(1,682)
Goodwill, net	14,083	31,729

The goodwill reflects the excess of the consideration paid or transferred over the fair values of the identifiable net assets acquired. The Company acquired Tongwen Gaokao and Tongwen High School (collectively Tongwen ) in September 2008. For the fiscal year ended May 31, 2017, the Group performed its annual goodwill impairment testing and determined there was an impairment. As a result, the entire balance of goodwill associated with Tongwen and amounting to US\$1,682 was written off. The Group did not incur impairment loss for the year ended May 31, 2018.

**13. LONG-TERM INVESTMENTS, NET**

Long term investments, net, consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Cost method investments:		
Asia Pacific Montessori Education Co., Ltd.( Asia Pacific ) (a)		11,216
Other cost method investments (b)	8,132	27,291
Equity method investments: (c)	11,537	9,131
Available-for-sale investments:		

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Sunlands Online Education Group ( Sunlands ) (d)	32,644	134,423
Shanghai Golden Education & Training Co., Ltd.( Golden Finance ) (e)	44,809	86,937
Boxfish Education Group Limited ( Boxfish ) (f)		15,000
Shanghai ALO7 Technology Co., Ltd.( Alo7.com ) (g)	17,370	14,395
Tianjin Uhozz Internet Technology Co., Ltd ( Uhozz ) (h)	9,552	12,826
Beijing Kaisheng Culture Media Ltd. ( Kaisheng Culture ) (i)	7,342	11,263
Tarena International, Inc. ( Tarena ) (j)	25,695	9,610
Dr. Cuiyutao Healthcare Limited ( Yuxueyuan ) (k)		9,316
Beijing Shengtong Printing Co., Ltd ( Shengtong ) (l)	10,711	9,261
Lele Global Limited ( Lele ) (m)	9,105	9,157
Xiamen Shenzhouying Software & Technology Co., Ltd ( Shenzhouying ) (n)	6,856	8,451
Special assets management plan-Guotai Yuanxin & New Oriental ( Assets Management Plan ) (o)	7,486	8,336
Other available-for-sale investments (p)	26,020	56,720
	217,259	433,333

F-37

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**13. LONG-TERM INVESTMENTS - CONTINUED**

- (a) In April and November 2017, the Group paid US\$3,205 and US\$8,011, respectively, in Asia Pacific, a company engaging in pre-school education, for 35% equity interests. Asia Pacific's equity interest was equity security but not in-substance common shares due to substantial liquidation preference rights. Accordingly, the investment in Asia Pacific was accounted for as a cost method investment.
- (b) As to the other investments, they represent several insignificant investments in third-party private companies classified as cost method investments as of May 31, 2017 and 2018. The Group accounts for these investments under the cost method as the Group has no ability to exercise significant influence over the investees.
- (c) The Group holds 6.86% to 50% equity interests in nine third-party companies through investments in their common shares or in-substance common shares. Majority of the long-term investments are engaged in educational services. The Group accounts for these investment under the equity method because the Group has the ability to exercise significant influence but does not have control over the investees. The Group recognized impairment loss from equity method investments of US\$4,425, US\$3,289 and US\$379 for the years ended May 31, 2016, 2017 and 2018, respectively.
- (d) In January 2016, the Group invested US\$12,310 in Sunlands, which focuses on online education specific to vocational qualification training, for subscribing the convertible bonds. In July 2016, the Group converted all of the convertible bonds into redeemable preferred shares of Sunlands for 4.9% equity interests. In the meantime, the Group invested an additional US\$12,205 redeemable preferred shares for another 4.9% equity interest in Sunlands. Upon the additional investment, the Group holds 9.8% equity interest in Sunlands. On March 23, 2018, Sunlands was listed in the New York Stock Exchange Market. All of the preferred shares were converted to 529,426 Class A ordinary shares immediately upon the completion of the listing. The Group additional invested US\$10,000 for 34,783 Class A ordinary shares in April, 2018 and holds 8% aggregate equity interests in Sunlands. Unrealized gains of nil, US\$8,129 and US\$101,779 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.
- (e) In April and November 2015, the Group invested US\$3,398 and US\$11,437, respectively, in Golden Finance, a company focusing on training programs associated with finance and business management, for 19.5% equity interests. Unrealized gain of US\$19,407, US\$10,567 and US\$42,128 were reported in other comprehensive

income for the years ended May 31, 2016, 2017 and 2018, respectively.

- (f) In April 2018, the Group paid US\$15,000 in Boxfish, an online educational institution in China focusing on K-12 English training, for 6.52% equity interests. The equity interests acquired in Boxfish were classified as available-for-sale investment as the Group determined the interests were debt security and measured at fair value. No fair value change was recognized for the year ended May 31, 2018.
- (g) On March 5, 2012, the Group acquired a convertible promissory note from Alo7.com for US\$1,000, which entitled the Group to automatically convert the note into equity security upon certain conditions were met. On July 1, 2012, the Group converted the US\$1,000 promissory note into convertible redeemable preferred shares for 3.4% equity interests in Alo7.com on an as-converted basis. In March, June and September 2014, the Group further invested US\$2,576, US\$300 and US\$10,000 of redeemable preferred shares into Alo7.com. As of May 31, 2018, the Company had 14.3% equity interests in Alo7.com. Unrealized gain of US\$1,704, losses of US\$8,678 and US\$2,975 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.
- (h) In May 2015, the Group invested US\$460 in Uhozz, a company providing oversea rental agency services, for 10% equity interests. The equity interests acquired by the Group were classified as available-for-sale investment and measured at fair value. In March 2018, the Group further subscribed 15.18% equity interests with a cash consideration of US\$9,000. New subscribed equity interests were still classified as available-for-sale investment and measured at fair value. Unrealized gains of US\$4,254 and US\$4,838 and loss of US\$5,726 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**13. LONG-TERM INVESTMENTS - CONTINUED**

- (i) In April 2017, the Group invested US\$7,342 in Kaisheng Culture, a company engaging in providing educational services to students aging from 2 to 12, for 8.33% equity interests. The equity interests acquired in Kaisheng Culture were classified as available-for-sale investment and measured at fair value. Unrealized gain of nil and US\$3,921 were reported in other comprehensive income for the years ended May 31, 2017 and 2018, respectively.
- (j) In March 2014, the Group invested US\$13,500 in Tarena, a listed A-share company that provides IT professional education services in China, for 3% equity interests. Unrealized loss of US\$1,005 and gain of US\$9,750 were reported in other comprehensive income for the years ended May 31, 2016 and 2017, respectively. In July 2017, the Group sold 1% equity interest in Tarena to third parties and the realized gain of US\$4,545 was recognized in investment income for the year ended May 31, 2018. Unrealized loss of US\$7,040 was reported in other comprehensive income for the year ended May 31, 2018.
- (k) In February 2018, the Group invested US\$15,516 in Yuxueyuan, a company engaging in providing professional childcare and medical services for children aging from 1 to 6, for 10% equity interests. The investment consists of two tranches. The first tranche was to obtain 8,490,642 series B-1 preferred shares at US\$6,200 and the other tranche was to obtain 11,073,049 series C+ preferred shares at US\$9,316. The investment in series B-1 preferred shares was classified as a cost method investment because the series B-1 preferred shares were not in-substance common shares due to its liquidation preference rights and the Group does not have significant influence in the investee. The investment in series C+ preferred shares was classified as available-for-sale investment as the Group determined that it was a debt security due to redemption and liquidation preference rights and measured the investment subsequently at fair value. No fair value change was recognized for the year ended May 31, 2018.
- (l) In April 2015, the Group acquired 18% equity interest in Beijing ROBOROBO Technology Co., Ltd. ( ROBOROBO ) for a cash consideration of US\$4,356, a company applying various robots build training course for kids with different ages. In February 2017, the Group disposed all of the ownership in ROBOROBO, totaling in exchange for 1.87% common shares issued by Shengtong, which is a listed A-share company in China. Realized gain of US\$7,086 was recognized for the year ended May 31, 2017. The equity interests acquired in Shengtong were classified as available-for-sale investment since the Group determined that the shares were debt securities and measured at fair value. Unrealized gain of US\$423 and loss of US\$1,450 were reported in other comprehensive income for the years ended May 31, 2017 and 2018, respectively.

- (m) In September 2015, the Group invested US\$8,500 in Lele, a company providing online learning and tutoring services for students from kindergarten through 12th grade, to acquire 48,796,296 convertible redeemable preferred shares for 8.5% equity interests. The investment was classified as available-for-sale investment as the Group determined that the shares were debt securities due to the redemption option available to the investor and measured the investment subsequently at fair value. Unrealized gains of nil, US\$605 and US\$52 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.
- (n) In May 2016, the Group invested US\$6,839 in Shenzhouying, a company engaging in providing remote video monitoring control, for 10% equity interests. In August 2017, the Group further invested US\$759 to subscribe 139,094 series C+ convertible redeemable preferred shares. The investment was classified as available-for-sale investment as the Group determined that the investment was a debt security and measured the investment subsequently at fair value. Unrealized gains of nil, nil and US\$836 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.
- (o) In August 2015, the Group invested US\$7,315 in Assets Management Plan with a maturity of five years and owned 50% interests in the fund. The other 50% interests were invested by Mr. Yu and some other employees in the Group. The investment was classified as available-for-sale investment as the Group determined that the investment was a debt security and measured the investment subsequently at fair value. Unrealized gains of US\$61, US\$110 and US\$850 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively.
- (p) The other available-for-sale represent several insignificant investments classified as available-for-sale investments as of May 31, 2017 and 2018. Unrealized gain of US\$8,155, US\$323 and US\$2,700 were reported in other comprehensive income for the years ended May 31, 2016, 2017 and 2018, respectively. The Group recognized impairment loss from long term investments of nil, US\$2,338 and US\$980 for the years ended May 31, 2016, 2017 and 2018, respectively.

Table of Contents

## NEW ORIENTAL EDUCATION &amp; TECHNOLOGY GROUP INC.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

## FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018

(All amounts in thousands, except for share and per share data, or otherwise noted)

**14. FAIR VALUE MEASUREMENT**Assets and liabilities measured at fair value on a recurring basis

The Group measured its financial assets and liabilities primarily including available-for-sale investments at fair value on a recurring basis as of May 31, 2017 and 2018.

As of May 31, 2017 and 2018, the available-for-sale investments recorded in long-term investments include redeemable preferred shares, convertible note, common shares of three listed companies and Assets Management Plan (Refer to Note 13). Those are measured and recorded at fair value on a recurring basis in periods subsequent to their initial recognition and are as follows:

Description	As of May 31, 2017				Total US\$
	Quoted Prices in			Significant Unobservable Inputs Level 3 US\$	
	Active Market for	Significant Other	Significant		
	Identical	Observable	Unobservable		
	Assets Level 1 US\$	Inputs Level 2 US\$	Inputs Level 3 US\$		
<b>Available-for-sales investments:</b>					
Common shares	36,406				36,406
Redeemable preferred shares		30,669	123,029		153,698
Assets Management Plan		7,486			7,486
<b>Total</b>	<b>36,406</b>	<b>38,155</b>	<b>123,029</b>		<b>197,590</b>

Description	As of May 31, 2018				Total US\$
	Quoted Prices in			Significant Unobservable Inputs Level 3 US\$	
	Active Market for	Significant Other	Significant		
	Identical	Observable	Unobservable		
	Assets Level 1 US\$	Inputs Level 2 US\$	Inputs Level 3 US\$		
<b>Available-for-sales investments:</b>					
Common shares	153,294				153,294
		90,168	133,897		224,065



Redeemable preferred shares and convertible note				
Assets Management Plan		8,336		8,336
Total	153,294	98,504	133,897	385,695

The long-term investments accounted for as available-for-sale investments on a recurring basis are as follows:

	Available-for-sale investments US\$
Balance as of June 1, 2016	163,804
Purchase	19,893
Changes in fair value	22,521
Impairment amount	(2,876)
Foreign exchange difference	(5,752)
Balance as of May 31, 2017	197,590
Purchase	62,980
Disposal	(25,308)
Changes in fair value	129,545
Impairment amount	(138)
Foreign exchange difference	21,026
Balance as of May 31, 2018	385,695

The Company measured the fair value of its investments in common shares using the market approach based on the quoted stock price of its investee in the active market and has classified it as level 1 measurement.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**14. FAIR VALUE MEASUREMENT - CONTINUED**

**Assets and liabilities measured at fair value on a recurring basis continued**

The Company measured the fair value of its investment in convertible note and Assets Management Plan based on the respective principal and expected returns and has classified those as level 2 measurement.

For redeemable preferred shares do not have a quoted market rate, the Company measured their fair value based on recent transactions or based on the market approach or income approach when no recent transactions are available. Recent transactions include the purchase price agreed by an independent third party for an investment with similar terms or a recent transaction agreed by the Company and the investee and has been classified as level 2 measurement. When no recent transactions are available, a market approach or income approach will be used by the Company to measure fair value. The market approach takes into consideration a number of factors including market multiple and discount rates from traded companies in the industry and requires the Company to make certain assumptions and estimates regarding industry factors. Specifically, some of the significant unobservable inputs included the investee's historical earning on sale, discount of lack of marketability, investee's time to the Initial Public Offering as well as related volatility. The income approach takes into consideration a number of factors including management projection of discounted future cash flow of the investee as well as an appropriate discount rate. The Company has classified those as level 3 measurement. The assumptions are inherently uncertain and subjective. Changes in any unobservable inputs may have a significant impact on the fair values.

The Group did not have any transfers between level 1 and level 2 fair value measurements during the periods presented. During the year ended May 31, 2017, the Group transferred several redeemable preferred shares from level 2 to level 3 for a total of US\$31,505 as the Group changed its fair value measurements for those investees. Specifically, the Group changed its measurement method from recent transactions to a market approach or income approach described in the previous paragraph to determine the investment's fair value as no recent transactions were available as of May 31, 2017. During the year ended May 31, 2018, the Group transferred one redeemable preferred share from level 3 to level 1 for a total of US\$32,644.

The following table provides additional information about the reconciliation of the fair value measurements of assets and liabilities using significant unobservable inputs (level 3).

	Available-for-sale investments US\$
Balance as of June 1, 2016	69,873
Transfer from level 2 fair value measurements	31,505
Initial recognition	
Unrealized gain	21,651
<b>Balance as of May 31, 2017</b>	<b>123,029</b>
Transfer to level 1 fair value measurements	(32,644)
Initial recognition	
Unrealized gain	43,512
<b>Balance as of May 31, 2018</b>	<b>133,897</b>

Assets and liabilities measured at fair value on a nonrecurring basis

Goodwill and acquired intangible assets are measured at fair value on a non-recurring basis when an impairment is recognized.

The Group measures goodwill at fair value annually or whenever events or changes in circumstances indicate that carrying amount of a reporting unit exceeds its fair value. The Group measures acquired intangible assets using the income approach discounted cash flow method, when events or changes in circumstances indicate that the carrying amount of an asset may no longer be recoverable. The Group did not recognize any impairment loss related to intangible assets acquired for the years ended May 31, 2016, 2017 and 2018. The fair value of goodwill is determined using discounted cash flows, and an impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill.

The Group measures cost method investments and equity method investments at fair value on a non-recurring basis whenever events or changes in circumstances indicate that the carrying value may no longer be recoverable.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****15. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accrued expenses and other current liabilities consisted of the following:

	As of May 31,	
	2017	2018
	US\$	US\$
Accrued payroll	163,621	212,677
Payable for purchase of property and equipment	21,445	45,590
Rent payable	7,532	18,210
Amounts reimbursable to employees (a)	11,022	16,157
VAT payable	9,516	12,125
Refundable fees received from students (b)	8,687	11,541
Welfare payable	6,102	9,187
Accrued advertising fees	7,798	8,548
Refundable deposits (c)	5,382	7,290
Payable for investments and acquisitions		5,420
Royalty fees payable (d)	4,011	4,410
Other taxes payable	1,604	2,945
Accrued professional service fees	1,486	1,134
Others (e)	12,494	18,303
<b>Total</b>	<b>260,700</b>	<b>373,537</b>

- (a) Amounts reimbursable to employees include traveling and the related expenses.
- (b) Refundable fees received from students represent (1) the miscellaneous expenses other than tuition fees received from students which will be paid out on behalf of students; and (2) tuition fees refundable to students for classes withdrawn.
- (c) Refundable deposits represent student deposits for dormitory or other fees that will be refunded upon graduation and student security deposits refunded upon completion of the study tour.
- (d) Royalty fees payable relate to payments to content providers for on-line learning programs and those to counterparties for copyrights and resource sharing.
- (e) Others primarily include transportation expenses, utility fees, property management fees and other miscellaneous expenses payable.



**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**16. REDEEMABLE NON-CONTROLLING INTERESTES**

On April 24, 2018, Koolearn Holding entered into preferred share purchase agreements with a group of investors to issue an aggregate of 64,396,251 Series B convertible redeemable participating preferred shares ( Series B ) for an aggregate consideration of \$92,699. On May 17, 2018, Koolearn Holding entered into preferred share purchase agreement with an investor to issue 90,416,181 Series A convertible redeemable participating preferred shares ( Series A ).

The transactions were completed in May 2018. After the issuance of Series B and Series A preferred shares, the Group held approximately 68% equity interests in Koolearn Holding on a fully-diluted basis.

The Group classified Series B and Series A preferred shares as mezzanine equity since they are contingently redeemable at any time after December 31, 2019 by the holders in the event that (i) a qualified initial public offering ( QIPO ) has not occurred, or (ii) any material violation of applicable laws, or (iii) material breach of representations, warranties, undertaking or other obligations by Koolearn Holding s group entities or shareholders, or (iv) at any time any other preferred shareholder requests for redemption. These matters are not certain to occur, and they are not solely within the control of Koolearn Holding. As of May 31, 2018, the Company determined the redemption is not probable and accordingly, did not adjust the carrying amount of the Series B and Series A preferred shares to the redemption value as Koolearn Holding was in the process of an initial public offering and has made an application for listing its securities on the Stock Exchange of Hong Kong Limited.

The key terms of the Series B and Series A preferred shares are summarized as below:

**Voting rights**

Preferred shareholders have the right to one vote for each ordinary share into which each outstanding preferred share held could then be converted.

**Dividends**

Each holder of the Series A preferred shares and the Series B preferred shares shall be entitled to receive dividends and distributions from Koolearn Holding. Any dividend available for distribution shall be distributed ratably among all shareholders, on an as-converted basis.

**Liquidation preference**

In the event of any liquidation, all assets and funds of Koolearn Holding legally available for distribution to the shareholders (the Liquidation Proceeds ), shall be distributed to the shareholders in the following manners:

- (i) Before any distribution or payment shall be made to the holders of any ordinary shares, the Series A shareholders, the Series B shareholders shall be entitled to receive for each outstanding Series B shares held, the higher of the following: (i) an amount equal to 100% of the Series B issue price, together with a 10% annual compound interest accrued thereon (calculated from the Series B issuance date to the date of the liquidation), plus all declared but unpaid dividends; or (ii) the pro rata share of the Liquidation Proceeds of the Series B shareholders calculated on an as-converted basis.
  
- (ii) Before any distribution or payment shall be made to the holders of any ordinary shares, each Series A shareholder shall be entitled to receive the higher of the following; (i) an amount equal to 120% of the Series A issue price, plus all declared but unpaid dividends; or (ii) the pro rata share of the Liquidation Proceeds of the Series A shareholders calculated on an as-converted basis.
  
- (iii) After distribution or payment in full in pursuant to (i) and (ii), the remaining Liquidation Proceeds shall be distributed ratably among the ordinary shareholders of Koolearn Holding in proportion to the number of ordinary shares they held.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**16. REDEEMABLE NON-CONTROLLING INTERESTES - CONTINUED**

**Redemption**

To the extent permitted by applicable law and upon the occurrence of redemption events as defined in the articles of association of the Company, the Company is contractually obligated to redeem all or part of the issued and outstanding preferred shares upon request.

**Conversion**

Each preferred share shall automatically be converted into ordinary share of Koolearn Holding based on the then-effective conversion ratio (the Conversion Price ) applicable to such preferred share (i) upon the approval of Series A shareholders with respect to the conversion of Series A preferred shares, (ii) upon the approval of Series B shareholders with respect to the conversion of the Series B preferred shares, or (iii) immediately prior to the occurrence of a QIPO.

The Conversion Price of the preferred shares was initially the issuance price of the preferred shares at an initial conversion ratio of 1:1, and shall be adjusted from time to time for proportional adjustment (the Proportional Adjustment ), which means the Conversion Price adjustment in the event that if at any time the number of outstanding ordinary shares proportionately changes.

Koolearn Holding has determined that there was no beneficial conversion feature attributable to the various series of preferred shares because the initial conversion prices was higher than the fair value of Koolearn Holding s ordinary shares on issue date of each series preferred shares.

The Group recorded non-controlling interest of US\$206,624 upon issuance of shares for the year ended May 31, 2018.

**17. SHARE-BASED COMPENSATION**

**2006 Share Incentive Plan**

On January 20, 2006, the Company adopted 2006 Share Incentive Plan ( 2006 Share Incentive Plan ), under which the Company may grant share options to purchase up to 8,000,000 common shares of the Group, to its employees, directors and consultants. 2006 Share Incentive Plan is effective upon its adoption by the board and continue in effect for a term of ten years unless sooner terminated. The number of common shares available for grant under 2006 Share Incentive Plan may be increased by (i) an additional 5,000,000 shares on January 1, 2007, (ii) an additional 5,000,000



shares on January 1, 2008, and (iii) an annual increase in common shares to be added on the first business day of each calendar year beginning in 2009 equal to the lesser of (x) 3,000,000 shares, (y) two percent (2%) of total common shares outstanding as of such date, or (z) a lesser number of shares as determined by the plan administrator. Since the adoption of 2006 Share Incentive Plan, the Company have granted share options to purchase 15,826,000 common shares, of which 2,277,546 options to purchase common shares had been forfeited under 2006 Share Incentive Plan. In addition, since the adoption of 2006 Share Incentive Plan, the Company has granted a total of 8,608,671 NES under 2006 Share Incentive Plan. In general, one-sixth of the common shares underlying the share option and NES will vest on each six-month anniversary of the vesting commencement date specified in the option award notice. The vesting will be suspended if the grantee's leave of absence exceeds 90 days and will resume upon the grantee's return to service to the Group. The vesting schedule of NES is subject to the applicable award agreement. In January 2016, the Company's 2006 Share Incentive Plan expired. However, the expiration of 2006 Share Incentive Plan did not affect the exercise right of options granted prior to such expiration.

#### 2016 Share Incentive Plan

The Company adopted 2016 Share Incentive Plan ( 2016 Share Incentive Plan ) in January 2016 to provide incentives to employees and directors after the expiration of 2006 Share Incentive Plan. Under 2016 Share Incentive Plan, the Company is authorized to issue up to 10,000,000 common shares pursuant to awards (including options) granted to its employees, directors and consultants. 2016 Share Incentive Plan is effective upon its adoption by the board and continue in effect for a term of ten years unless sooner terminated. Since the adoption of 2016 Share Incentive Plan, the Company has granted a total of 1,921,646 NES, among which, 436,016 and 1,485,630 were granted in the years ended May 31, 2017 and 2018, respectively. 4,050 and 47,006 shares were forfeited in the years ended May 31, 2017 and 2018, respectively.

The Company's board of directors may at any time amend, suspend or terminate 2016 Share Incentive Plan. Unless the following amendments to 2016 Share Incentive Plan require approval from the shareholders (i) increase of the number of shares available under 2016 Share Incentive Plan, (ii) extension of the term of 2016 Share Incentive Plan, (iii) extension of the exercise period of an option beyond ten years, and (iv) any other amendments about which shareholders' approval are necessary and desirable under applicable laws or stock exchange rules. The remaining terms of 2016 Share Incentive Plan are substantially identical to the terms of 2006 Share Incentive Plan.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****17. SHARE-BASED COMPENSATION CONTINUED**Share options

Information regarding the share options granted under 2006 Share Incentive Plan is as follows:

Grant date	Share options granted	Grant-date fair value US\$	Exercise price US\$
February 28, 2006	7,099,500	1.00	2.02
July 21, 2006	1,620,000	1.15	2.38
September 7, 2006	100,000	2.38	3.75
March 5, 2007	3,946,500	4.09	8.75
January 17, 2012	3,060,000	10.33	12.19
Total	15,826,000		

The share option activities for the years ended May 31, 2016, 2017 and 2018 are summarized as follows:

	Number of share options	Weighted- average exercise prices US\$	Weighted-average remaining contractual life years	Aggregated intrinsic value US\$
Options outstanding as of May 31, 2015	318,641	5.30	1.92	5,903
Exercised	(240,304)	5.03		
Options outstanding as of May 31, 2016	78,337	6.13	0.58	2,829
Exercised	(48,047)	5.37		

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Canceled	(23,938)	8.75		
Options outstanding as of May 31, 2017	6,352	2.02	1.58	442
Exercised	(500)	2.02		
Options outstanding as of May 31, 2018	5,852	2.02	0.57	475
Options exercisable as of May 31, 2018	5,852	2.02	0.57	475

The total intrinsic value of share options exercised during the years ended May 31, 2016, 2017 and 2018 were US\$4,802, US\$2,133 and US\$38, respectively. As of May 31, 2018, no unrecognized compensation expense related to share options granted.

As of May 31, 2018, the Company transferred 17,000,000 common shares to its depository bank for the issuance to employees and directors upon the exercise of their vested share options or upon the vesting of NES. In 2013, the Company launched a share repurchase program and has since repurchased a cumulative 5,246,349 of common shares from the open market. Such shares are reserved for the employees to exercise of their vested share options and NES in the future. The share repurchase program was completed in April 2015. As of May 31, 2018, 59,477 treasury shares were available for future issuance upon exercise the vested share options and NES.

The exercise price of share options is at least 100% of the common share fair value on the date of the grant. The term of a share option is up to ten years from the date of grant. During the year ended May 31, 2016, the Group extended the terms of share options granted on February 28, 2006 for another three years. The extension did not have a material impact on the Group's consolidated financial statements. The share options generally vest over three years at six-month vesting increments per year. During the year ended May 31, 2017, the Group canceled 23,938 outstanding share options granted on March 5, 2007 due to the validity period of 10 years.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****17. SHARE-BASED COMPENSATION - CONTINUED**NES

As of May 31, 2018, 4,714,490 common shares out of 17,000,000 common shares held by the depository bank had been issued to employees and directors upon the vesting of their NES, and 2,929,780 shares out of 5,246,349 treasury shares had been reissued to employees and directors upon the vesting of their NES.

The NES activities under 2006 and 2016 Share Incentive Plan for the years ended May 31, 2016, 2017 and 2018 are summarized as follows:

	Number of NES	Weighted- average grant date fair value and intrinsic value US\$
NES outstanding as of May 31, 2015	606,400	18.55
Granted	546,330	22.66
Vested	(712,330)	21.39
Forfeited	(40,400)	20.61
NES outstanding as of May 31, 2016	400,000	18.91
Granted	436,016	47.19
Vested	(200,000)	18.91
Forfeited	(4,050)	47.19
NES outstanding as of May 31, 2017	631,966	38.24
Granted	1,485,630	82.75
Vested	(631,966)	38.24
Forfeited	(47,006)	82.75
NES outstanding as of May 31, 2018	1,438,624	82.75

NES vested and expect to vest as of May 31, 2018      1,438,624

The total fair value of NES vested during the years ended May 31, 2016, 2017 and 2018 were US\$15,235, US\$3,783 and US\$24,167, respectively. The weighted average grant date fair value of NES granted during the years ended May 31, 2016, 2017 and 2018 were US\$22.66, US\$47.19 and US\$82.75, respectively. As of May 31, 2018, the total unrecognized compensation expenses for NES of US\$65,719 are expected to be recognized over a weighted average period of 1.57 years.

The total compensation expense is recognized on a straight-line basis over the respective vesting periods. The Group recorded the related compensation expense of US\$16,810, US\$20,287 and US\$57,443 for the years ended May 31, 2016, 2017 and 2018, respectively.

Table of Contents

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**18. INCOME TAXES**

Cayman Islands & BVI

The Company and Koolearn Holding are tax-exempted companies incorporated in the Cayman Islands. Under the current law of the Cayman Islands, the Company and Koolearn Holding are not subject to income, corporate or capital gains tax, and the Cayman Islands currently have no form of estate duty, inheritance tax or gift tax. In addition, payments of dividends and capital in respect of their shares are not subject to taxation and no withholding will be required in the Cayman Islands on the payment of any dividend or capital to any holder of their shares, nor will gains derived from the disposal of their shares be subject to the Cayman Islands income or corporation tax.

The Company's subsidiary, Abundant, is incorporated in BVI and is not subject to income tax.

United States ( US )

Walkite US and Blingabc are incorporated in the U.S.A. and are subject to state income tax and federal income tax at 21% and 29.84%, respectively, depending upon the taxable income levels.

In December 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the Tax Act). The Tax Act makes broad and complex changes to the U.S. tax code including, but not limited to, (1) reducing the U.S. federal corporate tax rate, (2) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries that is payable over eight years, and (3) bonus depreciation that will allow for full expensing of qualified property. The impact of the Tax Act is not material to the Group's operation and resulted in a decrease in income tax rate from 35% before January 1, 2018 to 21% after January 1, 2018 for tax and income earned as determined in accordance with the relevant tax rules and regulations.

United Kingdom ( UK )

Walkite UK is incorporated in the UK and is subject to income tax rate at 20%.

Australia

New Oriental Vision Overseas Consulting Australia Pty Ltd is incorporated in Australia and is subject to income tax rate at 27.5%.

Hong Kong

Smart Shine, Winner Park, Elite Concept, One World, Garden House and Koolearn Tech are incorporated in Hong Kong and are subject to an income tax rate of 16.5% for taxable income generated from operations in Hong Kong. Elite Concept and Smart Shine received special dividend of US\$75,898, nil and US\$69,567 during the years ended May 31, 2016, 2017 and 2018, respectively. Withholding taxes of US\$7,590, nil and US\$6,957 in connection with the dividends were fully paid during the years ended May 31, 2016, 2017 and 2018, respectively.

The Company's PRC subsidiaries and the VIEs are subject to 25% standard enterprise income tax except for those accepted as deemed profit method enterprises, or qualified for small-scale enterprises, or granted preferential tax treatment.

Significant components of provision for income taxes for the years ended May 31, 2016, 2017 and 2018 were as follows:

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Current:			
PRC	39,467	51,142	72,785
Deferred:			
PRC	(1,936)	(518)	(13,377)
Total provision for income taxes	37,531	50,624	59,408

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****18. INCOME TAXES - CONTINUED**

Enterprises that qualify as a high and new technology enterprise ( HNTTE ) are subject to a tax rate of 15%. Beijing Decision, Beijing Hewstone and Xuncheng continued to qualify as HNTTE and were subject to a tax rate of 15% during the years ended May 31, 2016, 2017 and 2018. Beijing Smart Wood, Beijing Right Time and Beijing Joy Tend were qualified as HNTTE and enjoys a tax rate of 15% from January 2017 to December 2019, from January 2018 to December 2019 and from January 2018 to December 2019, respectively. Beijing Pioneer's HNTTE certificate terminated as of December 31, 2017. According to the application timetable required by the local tax bureau, Beijing Pioneer will launch the application for new HNTTE certificate in November 2018. Once qualified as HNTTE, Beijing Pioneer will be subject to a tax rate of 15% starting January 1, 2018.

Enterprises that qualify as the newly established software enterprise ( NESE ) are exempt from Enterprise Income Tax ( EIT ) for two years beginning the enterprise's first profitable year followed by a tax rate of 12.5% for the succeeding three years. Beijing Smart Wood, Beijing Right Time and Beijing Joy Tend were qualified as NESE and enjoyed the EIT tax benefit that from January 2012 to December 2016, from January 2013 to December 2017, from January 2013 to December 2017, respectively. Beijing Top, Beijing Shenghe, Beijing Magnificence and Beijing Jinghong were qualified as NESE and enjoyed the EIT tax benefit from January 2014 to December 2018, from January 2014 to December 2018, from January 2015 to December 2019 and from January 2017 to December 2021, respectively.

Since its establishment through May 31, 2018, Beijing Haidian School was not required by the governing tax bureau to pay any EIT. If Beijing Haidian School is required to pay EIT in the future, this could have material impact to the Group's consolidated financial statements. However, the Group believes that it is more likely than not that any change to the tax treatment of Beijing Haidian School shall be prospectively applied.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Group's deferred tax assets and liabilities are as follows:

	As of May 31,	
	2017	2018
	US\$	US\$
Deferred tax assets		
Allowance doubtful accounts	2,017	1,965
Accrued expenses	22,126	32,253
Net operating loss carry-forward	8,696	14,611



Total deferred tax assets	32,839	48,829
Less: valuation allowance	(3,981)	(5,506)
Net, deferred tax assets	28,858	43,323
Deferred tax liabilities		
Acquired of intangible assets and tax impact from the unrealized gain on available-for-sale investments	2,220	12,133
Total deferred tax liabilities	2,220	12,133

The Group does not file combined or consolidated tax returns, therefore, losses from individual subsidiaries or the VIEs may not be used to offset other subsidiaries' earnings within the Group.

The Group determined the valuation allowance on an entity by entity basis. The valuation allowance, which is primarily related to entities with net operating loss carry-forwards for which the Company does not believe it will ultimately be realized, was US\$3,981 and US\$5,506 as of May 31, 2017 and 2018, respectively.

As of the year ended May 31, 2018, the Group had net operating loss carried-forwards of US\$54,949 from the Company's PRC subsidiaries and the VIEs, which will expire on various dates from May 31, 2019 to May 31, 2024.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****18. INCOME TAXES - CONTINUED**

A reconciliation of the effective tax rates from 25% statutory tax rates for the years ended May 31, 2016, 2017 and 2018 is as follows:

	For the years ended		
	May 31,		
	2016	2017	2018
	%	%	%
Statutory tax rate	25.00	25.00	25.00
Effect of not deductible expenses for tax purposes	4.57	2.03	4.35
Tax effect of exempt entities	(14.00)	(7.85)	(8.10)
Effect of tax holiday	(4.05)	(5.56)	(5.70)
Changes in valuation allowance	0.25	0.11	0.43
Effect of dividend withholding tax	2.27	1.58	0.66
Effective tax rate	14.04	15.31	16.64

If WFOE and certain subsidiaries and schools of the VIEs did not enjoy income tax exemptions and preferential tax rates for the years ended May 31, 2016, 2017 and 2018, the increase in income tax expenses and the decrease in net income per share amounts would be as follows:

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Increase in income tax expenses	47,559	42,895	48,444
Decrease in net income per share - basic	0.30	0.27	0.31
Decrease in net income per share - diluted	0.30	0.27	0.31

Under the New Income Tax Law effective from January 1, 2008, the rules for determining whether an entity is resident in the PRC for tax purposes have changed and the determination of residence depends among other things on the place of actual management. If the Group, or its non-PRC subsidiaries, were to be determined as a PRC resident for tax purposes, they would be subject to a 25% income tax rate on their worldwide income including the income

arising in jurisdictions outside the PRC. The Group does not believe that its legal entities organized outside of the PRC are considered the PRC residents.

If the Company were to be a non-resident for the PRC tax purposes, dividends paid to it out of profits earned after January 1, 2008 would be subject to a withholding tax. In the case of dividends paid by the PRC schools and subsidiaries to their foreign investors, the withholding tax would be 10%, unless any such foreign investor's jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement. During the year ended May 31, 2016, Beijing Hewstone, Shanghai Smart Words and Beijing Decision paid US\$7,590 withholding tax when they paid a special dividend to their parent companies, Elite Concept. During the year ended May 31, 2018, Beijing Hewstone, Shanghai Smart Words, Beijing Smart Wood and Beijing Pioneer paid US\$6,957 withholding tax when they paid a special dividend to their parent companies, Elite Concept and Smart Shine.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**18. INCOME TAXES - CONTINUED**

Aggregate undistributed earnings of the Company's PRC subsidiaries and the VIEs that are available for distribution were US\$1,457,705 and US\$1,819,317 as of May 31, 2017 and 2018, respectively. Upon distribution of such earnings, the Company will be subject to the PRC EIT, the amount of which is impractical to estimate. The Company did not record any withholding tax on any of the aforementioned undistributed earnings because the relevant subsidiaries and the VIEs do not intend to declare dividends and the Company intends to permanently reinvest it within the PRC. Additionally, no deferred tax liability was recorded for taxable temporary differences attributable to the undistributed earnings because the Company believes the undistributed earnings can be distributed in a manner that would not be subject to income tax.

The Group did not identify any significant unrecognized tax benefits for the years ended May 31, 2016, 2017 and 2018. The Group did not incur any significant interest and penalties related to potential underpaid income tax expenses and also does not anticipate any significant increases or decreases in unrecognized tax benefits in the next twelve months. The Group has no material unrecognized tax benefits which would favorably affect the effective income tax rate in future periods.

According to the PRC Tax Administration and Collection Law, the tax authority may require the taxpayer or the withholding agent to make delinquent tax payment within three years if the underpayment of taxes is resulted from the tax authority's act or error. No late payment surcharge will be assessed under such circumstances. The statute of limitation will be three years if the underpayment of taxes is due to the computational errors made by the taxpayer or the withholding agent. Late payment surcharge will be assessed in such case. The statute of limitation will be extended to five years under special circumstances which are not clearly defined (but an underpayment of tax liability exceeding US\$16 (RMB0.1 million) is specifically listed as a special circumstance). The statute of limitation for transfer pricing related issue is ten years. There is no statute of limitation in the case of tax evasion. Therefore, the Group's PRC domiciled entities are subject to examination by the PRC tax authorities based on the above.

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****19. NET INCOME PER SHARE**

The computation of basic and diluted net income per share for the years ended May 31, 2016, 2017 and 2018 is as follows:

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
<b>Numerator:</b>			
Net income attributable to New Oriental Education & Technology Group Inc. s shareholders	224,884	274,457	296,130
Net income available for future distribution	224,884	274,457	296,130
<b>Denominator</b>			
Weighted average common shares outstanding Basic	156,782,439	157,551,320	158,168,794
Plus: incremental weighted average common shares from assumed exercise of share options and vesting of NES using the treasury stock method	609,247	435,074	387,706
Weighted average common shares outstanding Diluted	157,391,686	157,986,394	158,556,500
<b>Net income per common share</b>			
- Basic	1.43	1.74	1.87
- Diluted	1.43	1.74	1.87

The weighted average of 1,596,948, 828,067 and 210,593 treasury shares have been excluded in computing basic net income per share for the years ended May 31, 2016, 2017 and 2018, respectively.

There was no employee share options excluded from the dilutive share calculation for the years ended May 31, 2016, 2017 and 2018 due to anti-dilutive effects.



**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****20. RELATED-PARTIES TRANSACTIONS**

The Group had the following balances and transactions with related parties:

(a) Balances:

	Notes	Relationship	Amounts due from related parties, current		Amounts due to related parties, current	
			As of May 31, 2017 US\$	2018 US\$	As of May 31, 2017 US\$	2018 US\$
Metropolis Holding China Limited ( Metropolis )	(1)	Company controlled by the Executive Chairman	1,895	787		
MaxEn		Joint Venture		374	12	13
Beijing Haiwei Career Services Co., Ltd ( Haiwei Career )	(2)	Joint Venture	3,965			
Others	(4)		88	434	36	17
<b>Total</b>			<b>5,948</b>	<b>1,595</b>	<b>48</b>	<b>30</b>

	Notes	Relationship	Amounts due from related parties, non-current	
			As of May 31, 2017 US\$	2018 US\$
Metropolis	(1)	Company controlled by the Executive Chairman	1,064	2,226
MaxEn		Joint Venture	684	
<b>Total</b>			<b>1,748</b>	<b>2,226</b>

(b) Transactions:

		Rental expenses		
		For the years ended May 31,		
		2016	2017	2018
		US\$	US\$	US\$
Metropolis	Company controlled by the			
	(1) Executive Chairman	7,139	6,790	7,899



Table of Contents

## NEW ORIENTAL EDUCATION &amp; TECHNOLOGY GROUP INC.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

## FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018

(All amounts in thousands, except for share and per share data, or otherwise noted)

## 20. RELATED-PARTIES TRANSACTIONS CONTINUED

(b) Transaction continued:

			Loans provided to related parties		
			For the years ended May 31,		
			2016	2017	2018
			US\$	US\$	US\$
Haiwei Career	(2)	Joint Venture	1,520	3,965	
Beijing Weixue Mingri Network Technology Co., Ltd. ( Weixue Mingri )	(3)	Joint Venture	998	1,733	
Great Thanks Holdings Limited		Company established by the shareholder of the Joint Venture		1,450	
Total			2,518	7,148	

			Revenues		
			For the years ended May 31,		
			2016	2017	2018
			US\$	US\$	US\$
MaxEn		Joint Venture	177		
Beijing Tongban Education & Technology Co., Ltd ( Tongban )		Long-term investee	3	12	
STEMedu.cn		Long-term investee	11	60	66
Golden Finance		Long-term investee		18	26
Total			191	90	92

Cost  
For the years ended May 31,

		2016	2017	2018
		US\$	US\$	US\$
STEMedu.cn	Long-term investee	30	23	

- (1) Since April 2010, the Group began renting a large portion of a building owned by Metropolis for office space. In March 2012, Metropolis was acquired by a company wholly -owned by Mr. Yu, the Group s executive chairman. As a result, Metropolis became a related party of the Group thereafter. As of May 31, 2018, the current and non-current amounts due from Metropolis were US\$787 and US\$2,226, respectively, which represented prepaid rent and deposit for the building. The amount of the rental payments was determined based on the prevailing market rates and was duly approved by the Board.
- (2) In October 2014, Haiwei Career formed a joint venture with the Group. As a result, Haiwei Career became a related party of the Group. In 2018, Haiwei Career was consolidated by the Group. All transaction and balances between the Group and Haiwei Career are eliminated since then.
- (3) The amount due from Weixue Mingri in 2017 represented the non-interest bearing loans provided by the Group to support its daily operation and the outstanding loans were fully written off by the Group in fiscal year 2017. Weixue Mingri was a long-term investment under equity method and carrying amount of such investment was nil.
- (4) As of May 31, 2018, the balance in others included the current receivables from long-term investees.

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****21. COMMITMENTS AND CONTINGENCIES**Operating leases

The Group has certain operation-leases for offices, classroom and warehouse facilities. The terms of substantially all of these leases are ten years or less. Future minimum lease payments under non-cancelable operating leases as of May 31, 2018 were as follows:

	US\$
Years ending May 31:	
2019	296,575
2020	271,387
2021	225,424
2022	176,188
2023	123,444
Thereafter	164,444
Total	1,257,462

Rental expenses for the years ended May 31, 2016, 2017 and 2018 related to all cancelable and non-cancelable leases were US\$173,797, US\$199,329 and US\$320,877, respectively.

Capital commitments

As of May 31, 2018, the future minimum capital commitments were as follows:

	US\$
Capital commitment for the purchase of property and equipment	2,112
Capital commitment for leasehold improvements	29,875
	31,987

Contingent liabilities

The Group has been named in a number of lawsuits arising in its ordinary course of business. Although the outcome of those lawsuits are uncertain, the Group does not believe the possibility of loss is probable. The Group is unable to estimate a range of loss, if any, that could result if there would be an adverse decision, as such, and the Group has not accrued any liabilities.

F-54

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

(All amounts in thousands, except for share and per share data, or otherwise noted)

**22. NON-CONTROLLING INTERESTS**

	Non-controlling interests US\$
Balance as of June 1, 2015	3,496
Capital contribution from non-controlling interests	28,919
Repurchase shares from non-controlling interests	(3,497)
Unrealized gain on available-for-sale investments	999
Foreign currency translation adjustment	(271)
Net income attributed to non-controlling interests	444
<b>Balance as of June 1, 2016</b>	<b>30,090</b>
Capital contribution from non-controlling interests	3,924
Addition of non-controlling interests in connection with acquisition	3,909
Unrealized (loss) on available-for-sale investments	(23)
Foreign currency translation adjustment	(1,109)
Net income attributed to non-controlling interests	2,339
<b>Balance as of May 31, 2017</b>	<b>39,130</b>
Capital contribution from non-controlling interests	2,015
Repurchase shares from non-controlling interests	(28,652)
Dividend declared	(231)
Unrealized gain on available-for-sale investments	164
Foreign currency translation adjustment	2,949

Net income attributed to non-controlling interests	1,107
Balance as of May 31, 2018	16,482

The effects of changes in the Company's ownership interest on the Company's equity is as follows:

	For the years ended May 31,	
	2017	2018
	US\$	US\$
Net income attribute to New Oriental Education & Technology Group Inc.'s shareholders	274,457	296,130
Increase in the Group's additional paid-in capital resulting from capital injection of Beijing Fishpond Software Technology Co., Ltd. Fishpond and Huoerguosi Oriental Xinchuang Equity Investment Partnership (Limited Partnership)'s non-controlling interests		138
Increase in the Group's additional paid-in capital resulting from capital injection of Dongfang Youbo's non-controlling interests	138	
Increase in the Group's additional paid-in capital resulting from capital injection of Xuncheng's non-controlling interests	4,733	(113,922)
Decrease in the Group's additional paid-in capital resulting from repurchase shares from Xuncheng's non-controlling interests	(5,412)	(63,721)
Increase in the Group's additional paid-in capital resulting from transferring Xuncheng's common shares to non-controlling interests	5,704	
Changes from net income attributable to New Oriental Education & Technology Group Inc.'s shareholders and transfers from/to non-controlling interests	279,620	118,625

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****23. SEGMENT INFORMATION**

The Group's chief operating decision maker has been identified as the Chief Executive Officer who reviews financial information of operating segments based on US GAAP amounts when making decisions about allocating resources and assessing performance of the Group. The Group identified seven operating segments, including language training and test preparation, primary and secondary school education, online education, content development and distribution, overseas study consulting services, pre-school education and study tour, for the years ended May 31, 2016, 2017 and 2018. Language training and test preparation has been identified as a reportable segment. Online education, content development and distribution, overseas study consulting services, pre-school education, primary and secondary school education and study tour operating segments were aggregated as others because individually they do not exceed the 10% quantitative threshold.

The Group primarily operates in the PRC and substantially all of the Group's long-lived assets are located in the PRC.

The Group's chief operating decision maker evaluates performance based on each reporting segment's net revenue, operating cost and expenses, and operating income. Net revenues, operating cost and expenses, operating income, and total assets by segment were as follows:

For the year ended May 31, 2016

	Language training and test preparation courses US\$	Others US\$	Consolidated US\$
Net revenues	1,238,572	239,776	1,478,348
Operating cost and expenses:			
Cost of revenues	(516,370)	(97,994)	(614,364)
Selling and marketing	(125,815)	(48,999)	(174,814)
General and administrative	(296,686)	(68,495)	(365,181)
Unallocated corporate expenses			(128,912)
Total operating cost and expenses	(938,871)	(215,488)	(1,283,271)
Gain on disposal of a subsidiary		3,760	3,760
Operating income	299,701	28,048	198,837

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Segment assets	1,120,580	490,300	1,610,880
Unallocated corporate assets			743,954
Total assets	1,120,580	490,300	2,354,834

For the year ended May 31, 2017

	Language training and test preparation courses US\$	Others US\$	Consolidated US\$
Net revenues	1,510,497	289,012	1,799,509
Operating cost and expenses:			
Cost of revenues	(623,364)	(126,222)	(749,586)
Selling and marketing	(146,544)	(61,919)	(208,463)
General and administrative	(363,949)	(74,723)	(438,672)
Unallocated corporate expenses			(140,639)
Total operating cost and expenses	(1,133,857)	(262,864)	(1,537,360)
Operating income	376,640	26,148	262,149
Segment assets	1,361,261	606,955	1,968,216
Unallocated corporate assets			956,763
Total assets	1,361,261	606,955	2,924,979

F-56



**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018****(All amounts in thousands, except for share and per share data, or otherwise noted)****23. SEGMENT INFORMATION - CONTINUED**For the year ended May 31, 2018

	Language training and test preparation courses US\$	Others US\$	Consolidated US\$
Net revenues	2,022,978	424,452	2,447,430
Operating cost and expenses:			
Cost of revenues	(869,012)	(196,728)	(1,065,740)
Selling and marketing	(193,851)	(99,549)	(293,400)
General and administrative	(504,985)	(108,343)	(613,328)
Unallocated corporate expenses			(212,003)
Total operating cost and expenses	(1,567,848)	(404,620)	(2,184,471)
Operating income	455,130	19,832	262,959
Segment assets	1,898,504	844,691	2,743,195
Unallocated corporate assets			1,234,517
Total assets	1,898,504	844,691	3,977,712

**24. MAINLAND CHINA CONTRIBUTION PLAN**

The Group's full time employees in the PRC participate in a government-mandated multiemployer defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund and other welfare benefits are provided to employees. The PRC labor regulations require the Group to accrue for these benefits based on certain percentages of the employees' salaries. The total contributions for such employee benefits were US\$71,434, US\$89,709 and US\$129,334 for the years ended May 31, 2016, 2017 and, 2018, respectively.

## **25. STATUTORY RESERVE**

Prior to payment of dividends, pursuant to the laws applicable to the PRC's Foreign Investment Enterprises, the Company's subsidiaries and the VIEs in the PRC must make appropriations from after-tax profit to non-distributable reserve funds as determined by the Board of Directors of each company. These reserves include (i) general reserve and (ii) the development fund.

Subject to certain cumulative limits, the general reserve requires annual appropriations of 10% of after-tax profits as determined under the PRC laws and regulations at each year-end until the balance reaches 50% of the PRC entity registered capital; the other reserve appropriations are at the Company's discretion. These reserves can only be used for specific purposes of enterprise expansion and are not distributable as cash dividends. During the years ended May 31, 2016, 2017 and 2018, US\$695, US\$1,749 and US\$1,830 was accrued for the general reserve, respectively.

The PRC laws and regulations require private schools that require reasonable returns to make annual appropriations of 25% of after-tax income prior to payments of dividend to its development fund, which is to be used for the construction or maintenance of the school or procurement or upgrading of educational equipment, while in the case of a private school that does not require reasonable return, this amount should be equivalent to no less than 25% of the annual increase of net assets of the school as determined in accordance with generally accepted accounting principles in the PRC. During the years ended May 31, 2016, 2017 and 2018, appropriations to the development fund amounted to US\$31,158, US\$33,529 and US\$41,713, respectively.

**Table of Contents**

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED MAY 31, 2016, 2017 AND 2018**

**(All amounts in thousands, except for share and per share data, or otherwise noted)**

**25. STATUTORY RESERVE - CONTINUED**

These reserves are included as statutory reserves in the consolidated statements of changes in equity and comprehensive income. The Group allocated US\$31,853, US\$ 35,278 and US\$ 43,543 to statutory reserves during the years ended May 31, 2016, 2017 and 2018, respectively.

**26. RESTRICTED NET ASSETS**

Relevant PRC laws and regulations restrict the WFOEs and the VIEs from transferring a portion of their net assets, equivalent to the balance of their statutory reserves and their share capital, to the Company in the form of loans, advances or cash dividends, except in the event of liquidation. The balance of restricted net assets was US\$488,560 and US\$542,534, of which US\$425,927 and US\$448,103 was attributed to the paid-in capital, additional paid-in capital and statutory reserves of the VIEs and US\$62,633 and US\$94,431 was attributed to the paid-in capital, additional paid-in capital and statutory reserves of the WFOEs, as of May 31, 2017 and 2018, respectively. The WFOEs' accumulated profits may be distributed as dividends to the Company without the consent of a third party. The VIEs' revenues and accumulated profits may be transferred to the Company through contractual arrangements without the consent of a third party. Under applicable PRC law, loans from the PRC companies to their offshore affiliated entities require governmental approval, and advances by the PRC companies to their offshore affiliated entities must be supported by bona fide business transactions.

**27. SUBSEQUENT EVENTS**

Koolearn Holding initiated its initial public offering process and has made the application for listing its securities on the Stock Exchange of Hong Kong Limited in July 2018.

On June 15, 2018, Koolearn Holding issued 13,858,832 ordinary shares with par value of US\$0.00002 each at a price of US\$1.4914 per share for a total consideration of US\$20,668 to Tigerstep Developments Limited ( "Tigerstep" ). Tigerstep is controlled by Mr. Yu, Minhong, the Director and Chairman of the Koolearn Holding.

On July 13, 2018, the board of directors of Koolearn Holding approved an employees' share option plan (the "Pre-IPO Share Option Scheme" ), under which Koolearn Holding is authorised to grant options to purchase up to an aggregate of 47,836,985 ordinary shares. Koolearn Holding adopted the Pre-IPO Share Option Scheme on the same day and subsequently granted 27,904,930 options to the employees. The exercise price of all the options granted under the plan is US\$1.13 per share.

In July 2018, New Oriental Education Industry Fund (the Education Industry Fund ), with the total committed capital of US\$234,000 (RMB1.5 billion), was established. An entity controlled by Mr. Yu and an unrelated third party act as the joint general partners of the Education Industry Fund. The Company participates in the Education Industry Fund as a limited partner and has committed to invest US\$78,000 (RMB500 million) in the Education Industry Fund.

F-58

Table of Contents**NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Balance Sheets****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	As of May 31,	
	2017	2018
	US\$	US\$
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	11,472	5,537
Term deposits	10,000	
Prepaid expenses and other current assets	210	7,358
Total current assets	21,682	12,895
Amounts due from related parties	56,965	80,603
Deferred tax assets		1,170
Long-term investments	120,260	228,471
Investments in its subsidiaries and the VIEs	1,569,358	1,758,551
Total assets	1,768,265	2,081,690
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities		
Accrued expenses and other current liabilities	3,675	1,021
Amounts due to related parties	83,642	89,080
Total current liabilities	87,317	90,101
Equity:		
Common shares (US\$0.01 par value; 300,000,000 shares authorized as of May 31, 2017 and 2018; 158,379,387 shares issued as of May 31, 2017 and 2018; 157,687,444 and 158,319,910 shares outstanding as of May 31, 2017 and 2018, respectively)	1,584	1,584
Treasury stock	(7)	(1)
Additional paid-in capital	249,126	129,059
Retained earnings	1,391,084	1,616,061
Accumulated other comprehensive income	39,161	244,886
Total shareholders equity	1,680,948	1,991,589

Total liabilities and equity	1,768,265	2,081,690
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F-59

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Statements of Operations****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Operating expenses			
General and administrative	16,732	18,236	14,435
Total operating expenses	16,732	18,236	14,435
Operating loss	(16,732)	(18,236)	(14,435)
Interest income	1	122	16
Equity in earnings of its subsidiaries, the VIEs and the VIEs subsidiaries and schools	241,615	292,571	310,549
Net income	224,884	274,457	296,130

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Statements of Comprehensive Income****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Net income	224,884	274,457	296,130
Other comprehensive income, net of tax			
Foreign currency translation adjustment	(72,193)	(46,331)	76,344
Unrealized gain on available-for-sale investment, net of tax effect of nil, nil and US\$(1,170) for the years ended May 31, 2016, 2017 and 2018, respectively	35,636	22,544	129,381
Other comprehensive (loss)/ income	(36,557)	(23,787)	205,725
Comprehensive income attributable to New Oriental Education & Technology Group Inc. s shareholders	188,327	250,670	501,855



**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Statements of Changes in Equity****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	Common shares		Additional paid-in capital US\$	Treasury stock US\$	Accumulated other comprehensive income US\$	Retained earnings US\$	Total shareholders equity US\$
	Unrestricted shares	Amount US\$					
Balance as of May 31, 2015	156,486,763	1,584	141,653	(19)	99,505	977,625	1,220,348
Reissuance of treasury stock for the exercises of employee share options	240,304		2,428	3			2,431
Reissuance of treasury stock for non-vested equity shares	712,330		(7)	7			
Share-based compensation expenses			16,810				16,810
Dividend declared						(62,668)	(62,668)
Net income						224,884	224,884
Foreign currency translation adjustment					(72,193)		(72,193)
Unrealized gain on available-for-sale investments, net of tax effect of nil					35,636		35,636
Capital injection of non-controlling interests			39,579				39,579
Repurchase share from non-controlling interests			(255)				(255)
Equity restructure of a subsidiary			23,214			(23,214)	
Balance as of May 31, 2016	157,439,397	1,584	223,422	(9)	62,948	1,116,627	1,404,572

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Reissuance of treasury stock for the exercises of employee share options	48,047		256				256
Reissuance of treasury stock for non-vested equity shares	200,000		(2)	2			
Share-based compensation expenses			20,287				20,287
Net income						274,457	274,457
Foreign currency translation adjustment					(46,331)		(46,331)
Unrealized gain on available-for-sale investments, net of tax effect of nil					22,544		22,544
Capital injection of non-controlling interests and new non-controlling interests recognized in an acquisition			5,163				5,163
Balance as of May 31, 2017	157,687,444	1,584	249,126	(7)	39,161	1,391,084	1,680,948
Reissuance of treasury stock for the exercises of employee share options	500		1				1
Reissuance of treasury stock for non-vested equity shares	631,966		(6)	6			
Share-based compensation expenses			57,443				57,443
Dividend declared						(71,153)	(71,153)
Net income						296,130	296,130
Foreign currency translation adjustment					76,344		76,344
Unrealized gain on available-for-sale investments, net of tax effect of US\$(1,170)					129,381		129,381
Capital injection of non-controlling interests			(113,784)				(113,784)
Repurchase shares from Non-controlling interests			(63,721)				(63,721)
Balance as of May 31, 2018	158,319,910	1,584	129,059	(1)	244,886	1,616,061	1,991,589

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Statements of Cash Flows****(All amounts in thousands, except for share and per share data, or otherwise noted)**

	For the years ended May 31,		
	2016	2017	2018
	US\$	US\$	US\$
Cash flows from operating activities			
Net income	224,884	274,457	296,130
Adjustments to reconcile net income to net cash provided by operating activities			
Equity in earnings of its subsidiaries and the VIEs	(241,615)	(292,571)	(310,549)
Dividend received from subsidiaries	49,984	43,417	38,471
Realized gain from long-term investments			(4,785)
Share-based compensation expenses	16,810	20,287	57,443
Changes in operating assets and liabilities:			
Prepaid expenses and other current assets	5,135	5,404	(7,148)
Amounts due from related parties			(30,307)
Accrued expenses and other current liabilities	(3,673)	(2,341)	(2,653)
Amounts due to related parties	(1,446)	(40,207)	12,903
Net cash provided by operating activities	50,079	8,446	49,505
Cash flows from investing activities			
Investments in term deposits	(10,000)		10,000
Payment for available-for-sale investments	(9,500)	(1,000)	(2,766)
Proceed from long-term investments	540		9,285
Loans to related parties	1,487		(1,487)
Investments in a subsidiary		(8,500)	(10)
Repayment from related parties	8,512		
Net cash (used in)/provided by investing activities	(8,961)	(9,500)	15,022
Cash flows from financing activities			
Proceeds from issuance of common shares upon exercise of share options	2,176	542	1
Loan from a related party	8,610		690
Cash paid for dividend	(62,668)		(71,153)

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Net cash (used in)/provided by financing activities	(51,882)	542	(70,462)
Net decrease in cash and cash equivalents	(10,764)	(512)	(5,935)
Cash and cash equivalents, beginning of year	22,748	11,984	11,472
Cash and cash equivalents, end of year	11,984	11,472	5,537

F-63

**Table of Contents****NEW ORIENTAL EDUCATION & TECHNOLOGY GROUP INC.****Additional Information - Financial Statement Schedule I****Condensed Financial Information of Parent Company****Note to the Financial Statements****1. BASIS FOR PREPARATION**

The condensed financial information of the Company has been prepared using the same accounting policies as set out in the Group's consolidated financial statements except that the Company used the equity method to account for investments in its subsidiaries, the VIEs and the VIEs' subsidiaries and schools. The parent company's condensed financial information should be read in conjunction with the Group's consolidated financial statements.

**2. INVESTMENTS IN SUBSIDIARIES AND VIEs**

The Company, its subsidiaries, the VIEs and the VIEs' subsidiaries and schools were included in the consolidated financial statements where the inter-company balances and transactions were eliminated upon consolidation. For purpose of the Company's stand-alone financial statements, its investments in subsidiaries, the VIEs and the VIEs' subsidiaries and schools were reported using the equity method of accounting. The Company's share of income from its subsidiaries, the VIEs and the VIEs' subsidiaries and schools were reported as equity in earnings of its subsidiaries, the VIEs and the VIEs' subsidiaries and schools in the condensed statements of operations.

**3. INCOME TAXES**

The Company is a company incorporated in the Cayman Islands, therefore, is not subject to income taxes for all the years presented.

**4. RELATED-PARTY TRANSACTIONS**

The following represented the related party balances as of May 31, 2017 and 2018:

	As of May 31,	
	2017	2018
	US\$	US\$
Amounts due from related parties:		
Winner Park	12	12
Smart Shine		1,420
Abundant	40,000	

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Elite Concept	10,104	79,171
Koolearn Holdings Limited (a)	180	
New Oriental China	6,669	
	56,965	80,603
Amounts due to related parties:		
Elite Concept	357	359
Abundant	81,798	82,487
Smart Shine	1,487	
New Oriental China		6,234
	83,642	89,080

All related party balances were non-interest bearing and unsecured. The amounts due to related parties will be paid upon demand.

- (a) Koolearn Holdings Limited was a HK subsidiary of the Group which dissolved in the fiscal year of 2018.