Kip McGrath Education Centres Limited

ACN 003 415 889

Annual Financial Report
30 June 2003

Contents

Corporate Governance Statement For the Year Ended 30 June 2003

For the year under review Kip McGrath Education Centres Limited operated as an unlisted public company with the two founders as the only shareholders. On 15 August 2003, the company listed on the ASX. On 19 June 2003, in preparation for listing, the company implemented a restructure of its Board and prepared and approved a detailed Corporate Governance Charter. This charter details the key reporting requirements and includes:

- Defining the Board responsibility for the stewardship of the assets of the company, focusing on adding value to these assets, working with management to build a successful company and enhance shareholder value.
- Formation of Remuneration Committee and guidelines for membership and operation of this committee.
- Formation of Audit Committee and guidelines for membership and operation of this committee.
- Appointment of two independent non executive directors to Board in the roles of:
    - Chairman of the company;
    - Chairman of the Remuneration Committee
    - Chairman of the Audit Committee
- Commitment to implementing best practices relating to Board processes and Corporate Governance.
- Monitoring management and the implementation of the strategy, financial plans, internal controls and overseeing the operations of the company
- Monthly Board meetings which will include:
    - Reviewing monthly financial statements, actual versus budget and forecasts, growth of franchise numbers against budgets, domestically and overseas; cash flows and forecasts
    - Reviewing performance against strategic plans and KPI's

Directors' report

The directors present their report together with the financial report of Kip McGrath Education Centres Limited ("the Company") for the year ended 30 June 2003 and the auditor's report thereon.

Directors

The directors of the Company at any time during or since the end of the financial year are:

Name	*Age*	*Experience*
Mr Phil Arnall Chairman Independent Non-executive Director	58	Member - Audit Committee, Chairman- Remuneration Committee. Director of Felix Ventures, Director of Capral Aluminium Ltd and Director of Ludowici Ltd Director since 19 June 2003.
Mr Kip McGrath Managing Director	56	Director since incorporation in 1987
Mrs Dagnija McGrath Education Director	60	Director since incorporation in 1987
Mr Lewis Ting Independent Non-executive Director	62	Chairman – Audit Committee, Member Remuneration Committee. Director since 19 June 2003
Mr Storm McGrath Executive Director	33	Company Secretary Projects Director Director since 1997

Directors' meetings

The number of directors' meetings (including meetings of committee) and number of meetings attended by each of the directors of the Company during the financial year are:

Director	Board Meetings	
	A	B
P Arnall	3	3
K McGrath	5	5
D McGrath	5	5
L Ting	3	3
S McGrath	5	5

A – number of meetings attended

B – number of meetings held during the time the director held office

Principal Activities

The principal continuing activities of the company during the course of the financial year were the provision of educational facilities for franchisees.

Directors' report (continued)

Significant changes in state of affairs

There were no significant changes to the nature of the operations during the current financial year. However subsequent to year end the company has listed on the Australian Stock Exchange.

Review and result of operations

Operating profit before income tax $780,615 (2002: $652,194).

The company has shown continued growth for the 2003 financial year in line with the Prospectus forecast. Both domestic and overseas Franchise sales have increased with the number of worldwide franchise sales for the 2003 year increasing by 11%. Overall the Pre-tax profits increased by 20% over the previous period in line with revenue growth.

During the year the company continued to develop plans for expansion into overseas markets and refined new products including "Kindy Kip" and "English as a Foreign Language". It is expected these products will contribute to revenues in the 2004 financial year.

Dividends

The directors recommend that no dividends be paid for the year ended 30 June 2003 (2002:nil). No dividends have been paid or declared since the end of the previous financial year.

Environmental regulation

The company's operations are not regulated by a significant environmental regulation under a law of the Commonwealth, State or Territory.

Directors' and senior executives emoluments'

The Remuneration Committee is responsible for making recommendations to the Board on remuneration policies and packages applicable to the Board members and senior executives of the Company. The broad remuneration policy is to ensure the remuneration package properly reflects the person's duties and responsibilities and level of performance and that remuneration is competitive in attracting, retaining and motivating people of the highest quality.

Executive directors and senior executives may receive bonuses based on the achievement of specific goals related to the performance of the company. Non-executive directors do not receive any performance related remuneration.

Details of the nature and amount of each major element of the emoluments of each director of the Company are:

	Base emolument $	Bonuses $	Non Cash Benefits $	Super contributions $	Options issued (A) $	Retirement Benefits $	Total $
Director							
Non Executive							
Mr P Arnall	-	-	-	-	4,190	-	4,190
Mr L Ting	-	-	-	-	4,190	-	4,190
Executive Officers							
Mr K McGrath	55,923	-	5,454	4,498	-	-	65,875
Mrs D McGrath	53,231	-	11,198	4,498	-	-	68,927
Mr S McGrath	123,097	14,500	-	9,417	17,120	-	164,134

Directors' report (continued)

Directors' and senior executives emoluments' (continued)

(A) All options expire on the 15 August 2008 and each option entitles the holder to purchase one ordinary share in the company. No options may be exercised until the Company's shares have been quoted on the Australian Stock Exchange for more than 12 months. The estimated value disclosed above is calculated at the date of grant. Further detail of options granted during the year are set out under "Options" below.

Options

The Company granted options over unissued ordinary shares to the following directors as part of their remuneration.

Directors	Number of options granted	Exercise price	Expiry date
Mr S McGrath	200,000	$0.60	15 August 2008
Mr S McGrath	200,000	$0.70	15 August 2008
Mr P Arnall	100,000	$0.65	15 August 2008
Mr L Ting	100,000	$0.65	15 August 2008

All options were granted during the financial year. No options have been granted since the end of the financial year.

Directors' interests

The relevant interest of each director in the shares, and rights or options over such instruments issued by the company, as notified by the directors to the Australian Stock Exchange in accordance with S205G(1) of the Corporations Act 2001, at the date of this report is as follows:

	Ordinary Shares	Options over ordinary shares
Mr K McGrath	4,175,000	-
Mrs D McGrath	4,175,000	-
Mr S McGrath	8,000	400,000
Mr P Arnall	165,000	100,000
Mr L Ting	25,000	100,000
Kip McGrath Investments Pty Limited	1,000,000	-

Directors' report (continued)

Events Subsequent to Balance Date

Since 30 June 2003 the company has listed on the Australian Stock Exchange. The shares on offer at listing were 7,650,000, for consideration of $3,825,000, with total shares after listing of 17,000,000. The funds raised are being used to:

- Develop overseas franchises
- Repay Interest Bearing Liabilities of $400,000 and Non Interest Bearing Liabilities of $1,000,000 currently shown as Current Liabilities;
- Offset intangible prospectus costs of $236,590 currently shown as Current Assets against contributed equity from the capital raising proceeds; and
- Provide sufficient working capital to support the company's underlying business operations.

The financial effects of these transactions have not been brought to account in the financial statements for the year ended 30 June 2003.

Other than the matter addressed above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the company, to affect significantly the operations of the entity, the results of those operations, or the state of affairs of the company, in future financial years.

Likely developments

For the first two months of the 2003/04 financial year the company has traded within expectations. The developments outlined in the company's prospectus are underway and the directors expect that the 2003/04 year will achieve results outlined in the prospectus.

Indemnification and insurance of officers and auditors

To the extent permitted by law, the company will indemnify each officer of the company against any liability for costs and expenses incurred by that person as an officer of the company, unless liability arises out of conduct involving a lack of good faith.

Signed in Newcastle in accordance with a resolution of the directors:

Phil Arnall *Director*	11 September 2003
Kip McGrath *Director*	11 September 2003

Independent Audit Report to Members of Kip McGrath Education Centres Limited

Scope

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for Kip McGrath Education Centres Limited (the Company), for the year ended 30 June 2003.

The directors of the Company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Corporations Act 2001. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit Approach

We conducted an independent audit in order to express an opinion to the members of the Company. Our audit was conducted in accordance with Australian Auditing Standards in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001, Australian Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the Company's financial position, and of its performance as represented by the results of its operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

Independence

In conducting our audit, we followed applicable independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001.

KPMG

Independent Audit Report to Members of Kip McGrath Education Centres Limited

Audit Opinion

In our opinion, the financial report of Kip McGrath Education Centres Limited is in accordance with:

a) the Corporations Act 2001, including:

  i) giving a true and fair value of the Company's financial position as at 30 June 2003 and of its performance for the financial year ended on that date; and

  ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

b) Other mandatory professional reporting requirements in Australia.

KPMG

D A Turner
Partner

Newcastle 12 September 2003

Directors' declaration

In the opinion of the directors of Kip McGrath Education Centres Limited ("the Company"):

(a) the financial statements and notes, set out on pages 10 to 35, are in accordance with the Corporations Act 2001, including:

 (i) giving a true and fair view of the financial position of the Company as at 30 June 2003 and of its performance, as represented by the results of its operations and its cash flows for the year ended on that date; and

 (ii) complying with Accounting Standards and the Corporations Regulations 2001; and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in Newcastle in accordance with a resolution of the directors:

Phil Arnall — 11 September 2003
Director

Kip McGrath — 11 September 2003
Director

Statement of Financial Performance
For the year ended 30 June 2003

	Note	2003 $	2002 $
Revenue from franchise operations	2	2,186,041	1,814,317
Other revenues from ordinary activities	2	70,442	31,162
Total revenue		2,256,483	1,845,479
Employee expenses		(478,286)	(368,255)
Depreciation and amortisation expenses	3	(307,703)	(310,715)
Borrowing costs	3	(83,267)	(120,325)
Commission expenses		(50,909)	-
Marketing expenses		(137,664)	(47,532)
Administration expenses		(184,342)	(165,165)
Merchandising expenses		(132,587)	(95,665)
Other expenses from ordinary activities		(101,110)	(85,628)
Profit from ordinary activities before related income tax expense		780,615	652,194
Income tax expense relating to ordinary activities	5	(250,977)	(229,944)
Net profit attributable to members		529,638	422,250
Basic earnings per share:			
Ordinary shares	28	$0.057	$211,125

The statement of financial performance is to be read in conjunction with the notes to the financial statements set out on pages 13 to 35.

Statement of Financial Position
As at 30 June 2003

	Notes	2003 $	2002 $
Current assets			
Cash assets		407,031	182,270
Receivables	7	184,850	230,102
Inventories	8	38,333	-
Other	9	250,988	6,281
Total current assets		881,202	418,653
Non-current assets			
Property, plant and equipment	10	1,407,750	1,500,153
Intangibles	11	2,763,787	2,928,298
Other	12	831,852	614,206
Deferred tax assets	5	18,808	11,406
Total non-current assets		5,026,148	5,054,063
Total assets		5,907,350	5,472,716
Current liabilities			
Payables	13	314,240	125,822
Interest-bearing liabilities	14	400,000	280,672
Non interest-bearing liabilities	15	1,000,000	120,000
Current tax	5	169,675	131,188
Provisions	17	37,370	22,455
Total current liabilities		1,921,285	680,137
Non-current liabilities			
Interest-bearing liabilities	14	270,521	659,579
Non interest-bearing liabilities	15	1,019,838	2,019,838
Deferred tax liabilities	5	255,217	206,025
Provisions	17	7,560	3,846
Total non-current liabilities		1,553,136	2,889,288
Total liabilities		3,474,421	3,569,425
Net assets		2,432,929	1,903,291
Equity			
Contributed equity	18	2	2
Reserves	19	441,216	441,216
Retained profits	20	1,991,711	1,462,073
Total equity		2,432,929	1,903,291

The statement of financial position is to be read in conjunction with the notes to the financial statements set out on pages 13 to 35.

Statement of Cash Flows

For the year ended 30 June 2003

	Note	2003 $	2002 $
Cash flows from operating activities			
Cash receipts in the course of operations		2,296,835	1,800,203
Cash payments in the course of operations		(1,180,602)	(683,291)
Income tax paid		(157,148)	(25,221)
Interest received		11,060	3,925
Borrowing costs paid		(83,267)	(120,325)
Net cash provided by operating activities	24	886,878	975,291
Cash flows from investing activities			
Payments for property, plant and equipment		(23,707)	(49,426)
Payment of research and development costs		(248,679)	(331,056)
Proceeds from sale of shares		-	1,237
Net cash used in investing activities		(272,386)	(379,245)
Cash flows from financing activities			
Proceeds from borrowings		-	46,940
Repayment of borrowings		(306,905)	(387,179)
Finance lease payments		(82,826)	(61,380)
Net cash used in financing activities		(389,731)	(401,619)
Net increase in cash held		224,761	194,427
Cash at the beginning of the financial year		182,270	(12,157)
Cash at the end of the financial year	24	407,031	182,270

The statement of cash flows is to be read in conjunction with the notes to the financial statements set out on pages 13 to 35.

Notes to the financial statements For the year ended 30 June 2003

1 Statement of significant accounting policies

The significant policies which have been adopted in the preparation of this financial report are:

(a) Basis of preparation

The financial report is a general purpose financial report, which has been prepared in accordance with Accounting Standards, Urgent Issues Group Consensus Views, other authoritative pronouncements of the Australian Accounting Standards Board and the Corporations Act 2001.

It has been prepared on the basis of historical costs and except where stated, does not take into account changing money values or fair values of non-current assets.

The accounting policies have been consistently applied and, except where there is a change in accounting policy, are consistent with those of the previous year.

(b) Revenue recognition

Revenues are recognised at fair value of the consideration received net of the amount of goods and services tax (GST). Exchanges of goods or services of the same nature and value without any cash consideration are not recognised as revenues.

Rendering of services

Revenue from the rendering of services is recognised proportionally over the life of the service contract.

Sale of goods

Revenue from sales of products is recognised at the time the control of the product passes to the customer. This control will pass when the customer places an order for the product.

Interest revenue

Interest revenue is recognised as it accrues.

(c) Borrowing costs

Borrowing costs include interest, amortisation of discounts or premiums relating to borrowings, amortisation of ancillary costs incurred in connection with arrangement of borrowings, including trade creditors and lease finance charges.

Notes to the financial statements
For the year ended 30 June 2003

1 Statement of significant accounting policies (continued)

(d) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of GST incurred is not recoverable from the Australian Tax Office (ATO). In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

(e) Foreign currency

Transactions

Foreign currency transactions are translated to Australian currency at the rates of exchange ruling at the dates of the transactions. Amounts receivable and payable in foreign currencies at balance date are translated at the rates of exchange ruling on that date.

Exchange differences relating to amounts payable and receivable in foreign currencies are brought to account as exchange gains or losses in the statement of financial performance in the financial year in which the exchange rates change.

(f) Taxation

The company adopts the income statement liability method of tax effect accounting.

Income tax expense is calculated on operating profit adjusted for permanent differences between taxable and accounting income. The tax effect of timing differences which arise from items being brought to account in different periods for income tax and accounting purposes, is carried forward in the statement of financial position as a future income tax benefit or a provision for deferred income tax.

Future income tax benefits are not brought to account unless realisation of the asset is assured beyond reasonable doubt. Future income tax benefits relating to tax losses are only brought to account when their realisation is virtually certain. The tax effect of capital losses is not recorded unless realisation is virtually certain.

Notes to the financial statements
For the year ended 30 June 2003

1 Statement of significant accounting policies (continued)

(g) Acquisitions of assets

All assets acquired including property, plant and equipment are initially recorded at their cost of acquisition at the date of acquisition, being the fair value of the consideration provided plus incidental costs directly attributable to the acquisition.

Expenditure other than research and development, is only recognised as an asset when the entity controls future economic benefits as a result of the costs incurred, it is probable that those future economic benefits will eventuate, and the costs can be measured reliably. Costs attributable to feasibility and alternative approach assessments are expensed as incurred.

Research and development

Research and development expenditure is expensed as incurred except to the extent that its recoverability is assured beyond reasonable doubt, in which case it is deferred, and amortised over the useful life, not exceeding 20 years.

(h) Revisions of accounting estimates

Revisions to accounting estimates are recognised prospectively in current and future periods only.

(i) Cash assets and bank overdrafts

Cash assets and bank overdrafts are carried at face value of the amounts deposited or drawn. The carrying amounts of cash assets and bank overdrafts approximate net fair value.

(j) Receivables

The collectability of debts is assessed at year-end and specific provision is made for any doubtful accounts.

The carrying amount of receivables approximates net fair value.

Trade debtors

Trade debtors are generally settled within 30 days and are carried at amounts due.

Notes to the financial statements
For the year ended 30 June 2003

1 Statement of significant accounting policies (continued)

(k) Recoverable amount of non-current assets valued on cost basis

The carrying amounts of non-current assets valued on the cost basis are reviewed to determine whether they are in excess of their recoverable amount at balance date. If the carrying amount of a non-current amount asset exceeds its recoverable amount, the asset is written down to the lower amount. The write-down is recognised as an expense in the net profit or loss in the reporting period in which it occurs.

Where a group of assets working together supports the generation of cash inflows, recoverable amount is assessed in relation to that group of assets.

In assessing recoverable amounts of non-current assets the relevant cash flows have not been discounted to their present value, except where specifically stated

Intellectual property

The cost value of intellectual property arose from a director related party transaction. The recoverability of this cost value is annually assessed by the directors and has been supported by an independent valuation performed by Mr Peter Sweeney CA.

(l) Depreciation and amortisation

Useful lives

All non-current assets, including intangibles, have limited useful lives and are depreciated/amortised using the straight line method over their estimated useful lives.

Assets are depreciated or amortised from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

The depreciation/amortisation rates used for each class of asset are as follows:

	2003	2002
Property, plant and equipment		
Buildings and improvements	10-40 years	10-40 years
Plant and equipment	4-10 years	4-10 years
Intangibles	20 years	20 years

(m) Payables

Liabilities are recognised for amounts to be paid in the future for goods or services received. Trade accounts payable are normally settled within 30 days. The carrying amount of accounts payable approximates net fair value.

Notes to the financial statements
For the year ended 30 June 2003

1 Statement of significant accounting policies (continued)

(n) Loans

Loans from related parties are carried on the statement of financial position at their principal amount. The carrying amounts of loans approximate their net fair value.

(o) Employee entitlements

The carrying amount of provisions for employee entitlements approximates net fair value.

Wages, salaries and annual leave
The provisions for employee entitlements to wages, salaries, annual leave represent present obligations resulting from employees' services provided up to the balance date, calculated at undiscounted amounts based on current wage and salary rates including related on-costs.

Long service leave
The provision for employee entitlements to long service leave represents present obligations resulting from employees' services provided up to balance date. The provision in based on current wage and salary rates including related on-costs.

(p) Leases

Finance leases, which effectively transfer to the company substantially all of the risks and benefits incidental to ownership of the leased item are capitalised at the present value of the minimum lease payments, disclosed as leased property, plant and equipment, and amortised over the period the company is expected to benefit from the use of the leased assets.

Operating lease payments, where the lessor effectively retains substantially all of the risks and benefits of ownership of the leased items, are included in the determination of the operating profit in equal instalments over the lease term.

(q) Earning per share

Basic earning per share ("EPS") is calculated by dividing the net profit attributable to members of the Company for the reporting period, after excluding any costs of servicing equity (other than ordinary shares and converting preference shares classified as ordinary shares for EPS calculation purposes), by the weighted average number of ordinary shares of the Company.

Notes to the financial statements
For the year ended 30 June 2003

2 Revenue from ordinary activities

	2003 $	2002 $
Revenue from franchise operations – domestic	1,657,939	1,283,128
Revenue from franchise operations – overseas	528,102	531,189
Total revenue from franchise operations	2,186,041	1,814,317
Other revenues:		
From operating activities		
Product sales	39,119	-
Freight	3,704	2,642
Interest - Other parties	11,060	3,927
Other	7,420	20,540
Website advertising	9,139	3,790
From outside operating activities		
Investment income	-	128
Total other revenues	70,442	31,162
Total revenue from ordinary activities	2,256,483	1,845,479

Notes to the financial statements For the year ended 30 June 2003

	2003 $	2002 $
3 Profit from ordinary activities before income tax expense		
a) Profit from ordinary activities before income tax expense has been arrived at after charging/(crediting) the following items:		
Borrowing costs:		
Other parties	31,555	65,403
Finance leases	51,712	54,922
	83,267	120,325
Depreciation of:		
Buildings	14,660	14,660
Plant and equipment	43,500	40,427
Amortisation		
Intellectual property	164,511	164,511
Plant and equipment under lease	57,950	57,950
Product development	27,082	33,167
Total depreciation and amortisation	307,703	310,715
Net bad and doubtful debts expense including movements in provision of doubtful debts	16,260	190
Net expense for movements in provision for employee entitlements	18,629	5,607
4 Auditors' Services:		
Auditors of the company		
KPMG		
- Audit and review of financial reports	21,000	10,000
- Other regulatory audit services	4,500	1,500
	25,500	11,500
Other services:		
Auditors of the company		
KPMG		
- taxation services	3,250	-
KPMG related practices		
Due diligence services	49,500	-
	52,750	-

Notes to the financial statements
For the year ended 30 June 2003

	2003 $	2002 $
5 Income tax		
(a) Income tax expense		
Prima facie income tax expense calculated at 30% on the profit from ordinary activities	234,185	195,658
Increase in income tax expense due to:		
Amortisation – Intellectual Property and Product Development	49,353	49,353
Building depreciation	8,303	4,398
Sundry	-	5,219
Decrease in income tax expense due to:		
Research and development allowance	(40,864)	(24,684)
Income tax expense	250,977	229,944
(b) Current tax liabilities		
Provision for current income tax		
Balance at beginning of year	131,188	30,787
Income tax paid	(157,148)	(25,221)
Current year income tax expense	195,635	125,622
	169,675	131,188
(c) Deferred tax liabilities		
Provision for deferred income tax		
Provision for deferred income tax comprises the estimated expense at the applicable rate of 30% on the following items:		
Leased assets	20,286	12,698
Research and development costs	218,632	184,261
Trading stock	11,500	-
Prospectus costs deferred	4,799	-
Difference in depreciation for accounting and income tax purposes	-	8,796
	255,217	206,025

Notes to the financial statements
For the year ended 30 June 2003

	2003 $	2002 $
5 Income tax (continued)		
(d) Deferred tax assets		
Future income tax benefit		
Future income tax benefit comprises the estimated future benefit at the applicable rate of 30% on the following items:		
Employee leave provisions	13,479	11,406
Doubtful debt provision	1,188	-
Unrealised foreign currency	3,873	-
Difference in depreciation for accounting and income tax purposes	268	-
	18,808	11,406

6 Franking Account

	2003 $	2002 $
Dividend franking account		
30% franking credits available to shareholders of the company for subsequent financial years	684,528	1,140,751

The above available amounts are based on the balance of the dividend franking account at year end adjusted for franking credits that will arise from the payment of the amount of the current tax liability.

The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends.

Change in measurement of dividend franking account

In accordance with the New Business Tax System (Imputation) Act 2002, the measurement basis of the dividend franking account changed on July 2002 from an after tax profits basis to an income tax paid basis.

The amount of franking credits available to shareholders disclosed as at 30 June 2003 has been measured under the new legislation and represents income tax paid amounts available to frank distributions. The balance disclosed as at 30 June 2002 has been measured under the legislation existing at 30 June 2002 and represents after tax profits able to be distributed fully franked at the current tax rate.

The change in the basis of measurement does not change the underlying value of franking credits or tax offsets available to shareholders from the dividend franking account.

Comparative information has not been restated for this change in measurement. Had the comparative information been calculated on the new basis, the "franking credits available" balance as at 30 June 2002 would have been $488,893.

Notes to the financial statements
For the year ended 30 June 2003

	Note	2003 $	2002 $
7 Receivables			
Current			
Trade debtors		178,690	214,558
Less: provision for doubtful debts		(3,959)	-
		174,731	214,558
Loans to related parties		10,119	15,544
		184,850	230,102
8 Inventories			
Finished goods – at cost		38,333	-
9 Other current assets			
Capitalised fund raising costs	29	236,590	-
Prepayments		8,605	-
Other debtors		5,793	6,281
		250,988	6,281
10 Property, plant and equipment			
Freehold land			
At cost		150,000	150,000
Buildings			
At cost		678,000	678,000
Accumulated depreciation		(43,980)	(29,320)
		634,020	648,680
Plant and equipment			
At cost		211,641	187,934
Accumulated depreciation		(117,924)	(94,949)
		93,717	92,985
Leased equipment			
At cost		579,500	579,500
Accumulated depreciation		(193,167)	(135,217)
		386,333	444,283
Motor vehicles			
At cost		205,257	205,257
Accumulated depreciation		(61,577)	(41,025)
		143,680	164,205
Total property, plant and equipment		1,407,750	1,500,153

Notes to the financial statements For the year ended 30 June

10. Property, plant and equipment (continued)

Reconciliations

Reconciliations of the carrying amounts for each class of property, plant and equipment are set out below:

	2003 $	2002 $
Freehold land		
Carrying amount at beginning and end of year	150,000	150,000
Buildings		
Carrying amount at beginning of year	648,680	663,340
Depreciation	(14,660)	(14,660)
Carrying amount at end of year	634,020	648,680
Plant and equipment		
Carrying amount at beginning of year	92,985	61,504
Additions	23,707	51,388
Depreciation	(22,975)	(19,907)
Carrying amount at end of year	93,717	92,985
Leased equipment		
Carrying amount at beginning of year	444,283	502,233
Amortisation	(57,950)	(57,950)
Carrying amount at end of year	386,333	444,283
Motor vehicle		
Carrying amount at beginning of year	164,205	184,731
Depreciation	(20,525)	(20,526)
Carrying amount at end of year	143,680	164,205

11. Intangible Assets

	2003 $	2002 $
Intellectual property – at cost	3,290,223	3,290,223
Accumulated amortisation	(526,436)	(361,925)
	2,763,787	2,928,298

12. Other non-current assets

	2003 $	2002 $
Product development costs		
Expenditure brought forward	676,056	346,956
Expenditure capitalised	221,552	329,100
	897,608	676,056
Accumulated amortisation	(104,956)	(61,850)
	792,652	614,206

Notes to the financial statements
For the year ended 30 June 2003

	Note	2003 $	2002 $
12. Other non current assets			
Deferred expenditure – UK market expansion		39,200	-
Accumulated amortisation		-	-
		39,200	-
		831,852	614,206
13. Payables			
Trade creditors		270,786	44,642
Related parties		-	32,333
GST payable		27,606	26,024
Other creditors and accruals		15,848	22,823
		314,240	125,822
14. Interest-bearing liabilities			
Current			
GIO mortgage		57,516	36,900
Bank loans		142,556	117,828
Lease liabilities		113,168	82,802
Hire purchase		86,760	43,142
	29	400,000	280,672
Non-current			
GIO mortgage		-	55,349
Bank loans		-	133,776
Lease liabilities		205,545	318,737
Hire purchase		64,976	151,717
		270,521	659,579

Security

Mortgage loan is secured by registered first mortgage over land and buildings.

Bank loan is secured by registered first mortgage over assets and undertakings of the company, joint and several guarantees by K McGrath and D McGrath and registered second mortgage over land and buildings of the company.

Notes to the financial statements For the year ended 30 June 2003

	Note	2003 $	2002 $
14 Interest-bearing liabilities (continued)			
Financing arrangements			
The entity has access to the following lines of credit:			
Total facilities available:			
Bank loans		142,556	251,604
Property mortgage		57,516	92,249
Cheque facility		500	500
		200,572	344,353
Facilities utilised at balance date:			
Bank loans		142,556	251,604
Property mortgage		57,516	92,249
Cheque facility		-	-
		200,072	343,853
Facilities not utilised at balance date:			
Bank loans		-	-
Property mortgage		-	-
Cheque facility		500	500
		500	500
15 Non interest-bearing liabilities			
Current			
Shareholder loans	29	1,000,000	120,000
Non-current			
Shareholder loans		1,019,838	2,019,838

16 Amounts payable/receivable in foreign currencies

There are no amounts payable or receivable foreign currencies at year end.

Notes to the financial statements For the year ended 30 June 2003

	2003 $	2002 $
17 Provisions		
Current		
Employee entitlements	37,370	22,455
Non-current		
Employee entitlements	7,560	3,846
Employee entitlements		
Aggregate employee entitlements including on-costs	44,930	26,301
Number of employees		
Number of employees at year end: 11 (2002: 17)		
18 Contributed equity		
Issued and paid-up share capital		
9,350,000 (2002:2) ordinary shares, fully paid	2	2

During the year, the shares of the company were divided and split into 9,350,000 ordinary shares with K McGrath receiving 4,175,000 shares and D McGrath receiving 4,175,000 shares. In addition, 1,000,000 ordinary shares were issued to Kip McGrath Investments Pty Limited as Trustee for the McGrath Family Trust. After the successful listing, the total shares on offer will be 17,000,000.

Ordinary shares

Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholder meetings.

	2003 $	2002 $
19 Reserves		
Asset revaluation	441,216	441,216
20 Retained profits		
Retained profits at beginning of year	1,462,073	1,039,823
Net profit	529,638	422,250
Retained profits at end of year	1,991,711	1,462,073

Notes to the financial statements
For the year ended 30 June 2003

	2003 $	2002 $
21 Total equity reconciliation		
Total equity at beginning of year	1,903,289	1,481,039
Total changes in equity recognised in statement of financial performance	529,638	422,250
Total equity at end of year	2,432,927	1,903,289

22 Additional financial instruments disclosures

Interest rate risk exposures

The company's exposures to interest rate risk and the effective weighted average interest rate for classes of financial assets and financial liabilities is set out below:

2003 $	Note	Weighted average interest rate	Floating Interest Rate	1 year or less	Over 1 to 5 years	Non-interest bearing	Total
Financial assets							
Cash		3.9%	104,140	-	-	302,891	407,031
Receivables	7		-	-	-	184,850	184,850
Other	9		-	-	-	14,398	14,398
			104,140	-	-	503,139	606,279
Financial Liabilities							
Payables	13		-	-	-	314,240	314,240
Borrowings	14,15	8.7%	200,072	86,760	64,976	2,019,838	2,371,646
Lease liabilities	14	8.1%	-	113,168	205,545	-	318,713
Employee entitlements	17		-	-	-	44,930	44,930
			200,072	199,928	270,521	2,379,008	3,049,529

2002 $	Note	Weighted average interest rate	Floating Interest Rate	1 year or less	Over 1 to 5 years	Non-interest Bearing	Total
Financial assets							
Cash		3.9%	100,000	-	-	82,270	182,270
Receivables	7		-	-	-	230,102	230,102
Other	9		-	-	-	6,281	6,281
			100,000	-	-	318,653	418,653

Notes to the financial statements
For the year ended 30 June 2003

22. Additional Financial Instruments disclosures

2002 $	Note	Weighted average interest rate	Floating Interest Rate	1 year or less	Over 1 to 5 years	Non-interest Bearing	Total
Financial Liabilities							
Payables	13		-	-	-	125,822	125,822
Borrowings	14,15	8.6%	343,853	43,142	151,717	2,139,838	2,678,550
Lease Liabilities	14	8.2%	-	82,802	318,737	-	401,539
Employee entitlements	17		-	-	-	26,301	26,301
			343,853	125,944	470,454	2,291,961	3,232,212

23. Commitments

	Note	2003 $	2002 $
Finance lease Commitments			
- Not later than one year		113,168	113,168
- Later than one year but not later than two years		239,864	113,168
- Later than two year but no later than five years		-	239,863
Minimum lease payments		353,032	466,199
Less: future finance charges		34,319	64,660
Total lease liability		318,713	401,539
Representing lease liabilities:			
- Current	14	113,168	82,802
- Non-current	14	205,545	318,737
		318,713	401,539
Hire purchase Commitments			
- Not later than one year		86,760	58,374
- Later than one year but not later than two years		84,554	58,374
- Later than two year but no later than five years		-	112,755
Minimum hire purchase payments		171,314	229,503
Less: future finance charges		19,578	34,644
Total hire purchase liability		151,736	194,859
Representing hire purchase liabilities:			
- Current	14	86,760	43,142
- Non-current	14	64,976	151,717
		151,736	194,859

Notes to the financial statements
For the year ended 30 June 2003

24 Notes to the statement of cash flows

a) Reconciliation of cash

For the purposes of the statement of cash flows, cash includes cash on hand and at bank net of outstanding bank overdrafts. Cash as at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

	2003 $	2002 $
Cash assets	407,031	182,270

b) Reconciliation of profit from ordinary activities after income tax to net cash provided by operating activities

	2003 $	2002 $
Profit from ordinary activities after income tax	529,638	422,250
Add/(less) non-cash items		
Increase in provision for doubtful debts	3,959	-
Depreciation	116,110	55,087
Amortisation	191,593	255,628
	841,300	732,965
Change in operating assets and liabilities:		
(Increase)/decrease in trade debtors	51,412	(47,728)
(Increase)/decrease in other assets	(236,590)	-
(Increase)/decrease in other debtors and prepayments	(18,236)	(1,958)
(Increase)/decrease in inventory	(38,333)	-
(Increase)/decrease in FITB	(7,402)	5,616
Increase/(decrease) in trade creditors	188,419	81,682
Increase/(decrease) in income tax payable	38,487	100,401
Increase/(decrease) in provision for deferred income tax	49,192	98,706
Increase/(decrease) leave provisions	18,629	5,607
Net cash inflow from operating activities	886,878	975,291

Notes to the financial statements For the year ended 30 June 2003

25 Directors remuneration

Directors' income	**2003**	**2002**
The number of directors of the company whose income from the company or any related party falls within the following bands:		
$50,000 - $59,999	-	2
$60,000 - $69,999	2	-
$100,000 - $109,999	-	1
$140,000 - $149,999	1	-
	2003 **$**	**2002** **$**
Total income paid or payable, or otherwise made available, to all directors from the company or any related party.	281,876	205,758

26 Related parties

Directors

The names of each person holding the position of director of the company during the financial year are Messrs K. McGrath, S. McGrath, P. Arnall, L. Ting and Mrs D. McGrath.

Apart from the details disclosed in this note, no director has entered into a material contract with the Company since the end of the previous financial year and there were no material contracts involving directors' interests existing at year-end.

Directors' holdings of shares and share options

The interests of directors of the reporting entity and their director-related entities in shares and share options of the company at year-end are set out below.

	2003	**2002**
Ordinary shares	9,350,000	2
Options over ordinary shares	600,000	Nil

Director share option plan (DSOP)

The Company has a director share option plan approved at the meeting of members 19 June 2003.

Each option is convertible to one ordinary share. The exercise price of the options, is determined in accordance with the Rules of the plan.

If the options are granted contemporaneously with the introduction of the DSOP a price set by the directors which will not be less that $0.60.

Notes to the financial statements For the year ended 30 June 2003

26. Related parties (continued)

Director share option plan (DSOP) (continued)

No option may be exercised under the DSOP until the company's shares have been quoted on the ASX for more than 12 months.

There are no voting or dividend rights attached to the options. There are no voting rights attached to the unissued ordinary shares. Voting rights will be attached to the unissued ordinary shares when the options have been exercised.

Summary of options over unissued ordinary shares

Details of options over unissued shares as at beginning and ending of the reporting date and movements during the year are set out on page 32.

Notes to the financial statements
For the year ended 30 June 2003

26. Related parties (continued)

Summary of options over unissued ordinary shares (continued)

Grant date	Exercise date on or after	Expiry date	Exercise price $	Number of options at beginning of year	Options granted	Options lapsed	Options exercised	Number of options at end of year	Proceeds received $	Date issued	Number of shares issued	Fair value per share $	Fair value aggregate $
19 June 2003	15 August 2004	15 August 2008	0.60	-	200,000	-	-	200,000	-	-	-	-	-
19 June 2003	15 August 2004	15 August 2008	0.65	-	200,000	-	-	200,000	-	-	-	-	-
19 June 2003	15 August 2004	15 August 2008	0.70	-	200,000	-	-	200,000	-	-	-	-	-

Notes to the financial statements For the year ended 30 June 2003

26 Related parties (continued)

Director's transactions with the Company

A number of directors of the Company, or their director-related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of the company.

The terms and conditions of the transactions with directors and their director related entities were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to non-director related entities on an arm's length basis.

The aggregate amounts recognised during the year relating to directors and their director-related entities were as follows:

Director	Transaction	2003 $	2002 $
S McGrath	Purchase of materials	72,681	81,732

During the year, the Company repaid $120,000 (2002:$186,904) of the outstanding loan balance to K McGrath and D McGrath.

For all loans from directors, no interest is payable. Principal amounts were repayable in monthly instalments of $10,000, however there are no terms of repayment. All loans are unsecured.

Director's transactions with the Company

		2003 $	2002 $
Amounts receivable from and payable to directors and their director-related entities at balance date arising from these transactions were as follows:			
Receivables			
Trade debtors – Newcastle Plastics Pty Ltd		-	251
Unsecured loans at call – Pentat Pty Ltd	(i)	-	5,425
KME Pty Ltd		10,119	10,119
Total current receivables		10,119	15,795

(i) Pentat Pty Limited was wound up in the period. All outstanding balances with this company were written off in the period.

	2003 $	2002 $
Payables		
Unsecured loans payable – K & D McGrath	2,019,838	2,139,838
Trade Creditors – Newcastle Plastics Pty Limited	2,525	-

Notes to the financial statements
For the year ended 30 June 2003

27 Segmental reporting

Business segments

The entity consists of one business segment being the sale of education service franchises.

Geographical segments

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets and liabilities are contained in one geographical area being Australia.

The entity's business segments provide customers for the sale of franchises, geographically as follows:

	Australia & New Zealand		United Kingdom		South Africa		Asia Pacific		Other		Total	
	2003	2002	2003	2002	2003	2002	2003	2002	2003	2002	2003	2002
	$	$	$	$	$	$	$	$	$	$	$	$
External segment revenue by location of customers	1,811,574	1,403,907	193,831	270,939	105,316	70,613	54,346	120,799	20,974	68,858	2,186,041	1,814,317

Notes to the financial statements
For the year ended 30 June 2003

28 Earnings per share

Classification of securities as ordinary shares

The following securities have been classified as ordinary shares and included in basic earnings per share:

a) Ordinary shares

Earnings reconciliation	**2003** **$**	**2002** **$**
Basic Earnings	529,638	422,250
Allocations of earning to category of ordinary share:		
Basic ordinary shares	529,638	422,250
Weighted average number of shares used as the denominator		
Number of basic earnings per share		
Ordinary shares	9,350,000	2
Earnings per share	0.057	211,125

Subsequent to reporting date, ordinary shares were issued (refer Note 29). These shares have not been included in the calculation of basic EPS as at 30 June 2003.

The Director Share Options have not been included in the calculation of diluted EPS as they are not dilutive.

29 Events Subsequent to reporting date

Since 30 June 2003 the company has listed on the Australian Stock Exchange. The shares on offer at listing were 7,650,000, for consideration of $3,825,000, with total shares after listing of 17,000,000. The funds are being used to:

a. Develop overseas franchises

b. Repay Interest Bearing Liabilities of $400,000 and Non Interest Bearing Liabilities of $1,000,000 currently shown as Current Liabilities;

c. Offset intangible prospectus costs of $236,590 currently shown as Current Assets against contributed equity from the capital raising proceeds; and

d. Provide sufficient working capital to support the company's underlying business operations.

The financial effects of these transactions have not been brought to account in the financial statements for the year ended 30 June 2003.

ASX Additional Information

Additional information required by the Australian Stock Exchange Limited Rules and not disclosed elsewhere in this report is set out below.

Shareholdings (as at 29 August 2003)

Substantial shareholders

The number of shares held by substantial shareholders and their associates are set out below:

Shareholder	Number of ordinary shares
Mrs D McGrath	4,175,000
Mr K McGrath	4,175,000
Kip McGrath Investments Pty Limited	1,000,000

Voting rights

Ordinary shares

Refer to note 18

Options

Refer to note 26

Distribution of equity security holders

Category	Ordinary shares
1 – 1,000	27
1,001 – 5,000	298
5,001 – 10,000	298
10,001– 50,000	159
50,001- 100,000	5
100,001 and over	4
	791

There are no shareholders holding less than marketable amounts of ordinary shares.

On-market buy-back

There is no current on-market buy-back.

ASX Additional Information

Twenty Largest shareholders

Name	Number of ordinary shares held	Percentage of capital held
Mrs D McGrath	4,175,000	24.56
Mr K McGrath	4,175,000	24.56
Kip McGrath Investment Pty Limited	1,000,000	5.88
Merrill Lynch (Australia)	401,959	2.36
Mr A R Biggs & Ms L Biggs	100,000	0.59
Famarn Pty Limited	100,000	0.59
Berne No 132 Nominees Pty Limited	99,549	0.59
SMP Dawson Pty Limited	76,000	0.45
Mrs P E Foley	60,000	0.35
Berne No 132 Nominees Pty Limited (Account 323731)	50,000	0.29
Mr A Legge	45,000	0.26
Mr J D Pappin	45,000	0.26
Berne No 132 Nominees Pty Limited (Account 269700)	40,000	0.24
Berne No 132 Nominees Pty Limited (Account 313839)	40,000	0.24
Felix Ventures Pty Limited	40,000	0.24
Mr P Noss & Ms J Noss	40,000	0.24
SM Provident Pty Limited	40,000	0.24
Jelrif Investments Pty Limited	40,000	0.24
Peplon Nominees Pty Limited	34,790	0.20
Mrs D L Marszal	34,000	0.20
	10,636,298	62.6

Officer and Offices

Company Secretary

Mr Storm McGrath

Principal Registered Office

McGrath House
35 Watt Street
Newcastle NSW 2300
Telephone: (02) 4929 6711
Facsimile: (02) 4929 6338

Locations of Share Registries

Computershare Investor Services Pty Ltd
Level 27 Central Plaza One
345 Queen Street
Brisbane QLD 4000

Stock Exchange

The Company is listed on the Australian Stock Exchange. The Home Exchange is Sydney.

Other information

Kip McGrath Education Centres Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.