Farleigh Schools Limited

Directors' report and financial statements

Year ended 31 December 2005

Registered number 3225255

Contents

Directors' report

The directors present their report and the audited financial statements for the year ended 31 December 2005.

Principal activities

The company's principal activity is the provision of special boarding education for children with Asperger's Syndrome.

Business review

The results for the year are set out in the profit and loss account on page 5.

On 9 November 2005, the company entered into sale and leaseback agreements with Priory Finance Property LLP in relation to the sale of its properties. The properties were sold for a consideration of £35,730,000 and the resulting profit on sale was £8,578,000. The fixtures and fittings such as stock, furniture, catering equipment, medical equipment and other chattels which were solely related to the business of the company were retained. Other fixtures and fittings were sold to Priory Finance Property LLP and leased back under the sale and leaseback agreements.

Dividends

Dividends of £30.3 million were paid during the year *(2004: £nil).*

Directors and directors' interests

The directors who held office during the year were as follows:

PJ Greensmith
Dr CB Patel
T Mack (resigned 30 November 2005)

In accordance with the articles of association, no directors retire by rotation. None of the directors who held office at the end of the financial year had any disclosable interest in the shares of the company.

The interests of Dr CB Patel in the shares of Priory Investments Holdings Limited (the ultimate parent company) are disclosed in the financial statements of that company.

The interests of PJ Greensmith in the shares of Priory Investments Holdings Limited are set out below:

	Interest at end of year				Interest at beginning of year			
	A Ordinary shares	**B Ordinary shares**	**Non Voting B Ordinary shares**	**Preference shares**	A Ordinary shares	B Ordinary shares	Non Voting B Ordinary shares	Preference shares
PJ Greensmith	**-**	**200,000**	**300,000**	**1,500,000**	-	-	-	-

Directors' report *(continued)*

Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of PricewaterhouseCoopers LLP as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

Provision of information to auditors

So far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware. Each director has taken all the steps that he ought to have taken as director in order to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

By order of the board

David Spruzen
Company Secretary

Priory House
Randalls Way
Leatherhead
Surrey
KT22 7TP

24 May 2006

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

Independent auditors' report to the members of Farleigh Schools Limited

We have audited the financial statements of Farleigh Schools Limited for the year ended 31 December 2005 which comprise the profit and loss account, the balance sheet, the statement of total recognised gains and losses, the note of historical cost profits and losses, the reconciliation of movement in shareholders' funds and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2005 and of its profit for the year then ended; and
- the financial statements have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

24 May 2006

Profit and loss account
for the year ended 31 December 2005

	Note	2005 £000	2004 £000
Turnover		**7,453**	5,456
Cost of sales		**(5,369)**	(4,093)
Gross profit		**2,084**	1,363
Administrative expenses		**(777)**	(301)
Operating profit		**1,307**	1,062
Profit on disposal of fixed assets		**8,578**	-
Profit on ordinary activities before interest and taxation		**9,885**	1,062
Income from shares in group undertakings		**319**	-
Net interest payable and similar charges	5	**(53)**	(97)
Profit on ordinary activities before taxation	2	**10,151**	965
Tax on profit on ordinary activities	6	**(560)**	(386)
Profit for the financial year		**9,591**	579
Dividends		**(30,318)**	-
Amounts transferred to reserves		**(20,727)**	579

The results for the both the current period and prior year derive from continuing activities.

Balance sheet
at 31 December 2005

	Note		2005		2004
		£000	£000	£000	£000
Fixed assets					
Tangible assets	7		830		28,166
Investments	8		-		-
			830		28,166
Current assets					
Debtors	9	5,841		777	
Cash at bank and in hand		3,131		2,364	
		8,972		3,141	
Creditors: amounts falling due within one year	10	(8,640)		(8,127)	
Net current assets/(liabilities)			332		(4,986)
Total assets less current assets			1,162		23,180
Creditors: amounts falling due after more than one year	11		(119)		(1,410)
Provisions for liabilities and charges	12		-		-
Net assets			1,043		21,770
Capital and reserves					
Called up share capital	13		-		-
Revaluation reserve	14		-		20,137
Profit and loss account	14		1,043		1,633
Shareholders' funds – equity	14		1,043		21,770

These financial statements were approved by the board of directors on 24 May 2006 and were signed on its behalf by:

P J Greensmith
Director

Statement of total recognised gains and losses
for the year ended 31 December 2005

	2005	2004
	£000	£000
Profit for the financial year	9,591	579
Unrealised surplus on revaluation of properties	-	16,105
Total recognised gains for the year	9,591	16,684

Note of historical cost profits and losses
for the year ended 31 December 2005

	2005	2004
	£000	£000
Reported profit on ordinary activities before taxation	10,151	965
Difference between a historical cost depreciation charge and the actual depreciation charge calculated on the re-valued amount	259	62
Historical cost profit on ordinary activities before taxation	10,410	1,027
Historical cost (loss)/profit for the year retained after taxation and dividends	(20,468)	641

Reconciliation of movements in shareholders' funds
for the year ended 31 December 2005

	2005	2004
	£000	£000
Profit for the financial year	9,591	579
Dividends	(30,318)	-
	(20,727)	
Revaluation surplus	-	16,105
Net (reduction in)/addition to shareholders' funds	(20,727)	16,684
Opening shareholders' funds	21,770	5,086
Closing shareholders' funds	1,043	21,770

Notes
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the company's financial statements.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules, modified to include the revaluation of certain land and buildings.

The company is exempt by virtue of section 228 of the Companies Act 1985 from the requirement to prepare group accounts. These financial statements present information about the company as an individual undertaking and not about its group.

Under Financial Reporting Standard 1 (revised) the company is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the company in its own published consolidated financial statements.

As the company is a wholly owned subsidiary of Priory Investments Holdings Limited, the company has taken advantage of the exemption contained in Financial Reporting Standard 8 and has therefore not disclosed transactions or balances with entities which form part of the group.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost or valuation, net of depreciation and any provision for impairment.

Assets in course of construction represent the direct costs of purchasing, constructing and installing tangible fixed assets ahead of their productive use. No depreciation is provided on an asset that is in the course of construction until it is completed and transferred to an asset heading that is appropriate.

Depreciation is provided to write off the cost or valuation less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Freehold buildings and long leasehold properties	-	50 years
Short leasehold properties	-	over the period of the lease
Plant, fixtures and fittings	-	3 to 16 years
Motor vehicles	-	over the shorter of the lease and 4 years

Land is not depreciated on the basis that land has an unlimited life. Where the valuation of land and buildings cannot be split, the Directors have estimated that the value attributable to land is 22% of the valuation of the land and buildings.

Revaluation of properties

The company has adopted a policy of revaluation of its properties, as permitted by Financial Reporting Standard 15 - Tangible Fixed Assets. The assets are valued by independent Chartered Surveyors each year at the balance sheet date, on a rolling basis designed to ensure that all properties are specifically valued at least every five years. Any surplus or deficit on book value is transferred to the revaluation reserve, except that a deficit, which is in excess of any previously recognised surplus over depreciated cost relating to the same property, or the reversal of such a deficit, is charge (or credited) to the profit and loss account.

Investments

Fixed asset investments are stated at cost less provision for any impairment in value.

Notes *(continued)*

1 Accounting policies *(continued)*

Leases

Assets acquired under finance leases are capitalised and the outstanding future lease obligations are shown in creditors. Operating lease rentals are charged to the profit and loss account on a straight-line basis over the period of the lease.

Post-retirement benefits

The company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the company in an independently administered fund. The amount charged against profits represents the contributions payable to the scheme in respect of the accounting period.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Group relief

Payment is generally made for group relief at a rate of 30% at the time of first estimating the tax provision. To the extent that amendments are subsequently made to the group relief plan, there is generally no payment or receipt in respect of change.

Turnover and revenue recognition

Turnover represents the amounts (excluding value added tax) derived from the provision of services to customers. Revenue is recognised as the services are provided.

2 Profit on ordinary activities before taxation

	2005	2004
Profit on ordinary activities before taxation is stated	**£000**	£000
after charging:		
Auditors' remuneration (inclusive of VAT):		
Audit	**8**	8
Depreciation and other amounts written off tangible fixed assets:		
Owned	**599**	374
Leased	**82**	71
Rentals under operating leases:		
Hire of plant and machinery	**12**	5
Other operating leases	**249**	8
after crediting:		
Profit on disposal of fixed assets	**8,578**	-

Notes *(continued)*

3 Remuneration of directors

The directors received no emoluments for services to the company during the year *(2004: £nil)*.

4 Staff numbers and costs

The average number of persons employed by the company (including directors) during the year, analysed by category, was as follows:

	Number of employees	
	2005	2004
Teachers and social workers	**185**	147
Administrative staff	**55**	29
	240	176

The aggregate payroll costs of these persons were as follows:

	2005	2004
	£000	£000
Wages and salaries	**3,487**	2,512
Social security costs	**299**	213
Other pension costs	**65**	60
	3,851	2,785

5 Net interest payable and similar charges

	2005	2004
	£000	£000
Interest payable and similar charges		
On bank loans and overdrafts	**86**	87
Finance charges payable in respect of finance leases	**12**	10
	98	97
Other interest receivable and similar income		
Inter-company interest receivable	**(45)**	-
	53	97

Notes *(continued)*

6 Taxation

	2005 £000	2004 £000
UK corporation tax		
Current tax on income for the year	**562**	392
Adjustment relating to prior years	**(2)**	(6)
	560	386

The tax charge of £562,000 *(2004: £392,000)* on profits for the year has been relieved by the surrender of losses by other group companies in exchange for payment of the same amount.

The standard rate of tax for the year, based on the UK standard rate of corporation tax is 30% (2003: 30%). The actual tax charge for the year is above the standard rate for the reasons set out in the following reconciliation:

	2005 £000	2004 £000
Profit on ordinary activities before tax	**10,151**	965
Tax on profit on ordinary activities at standard rate	**3,045**	290
Factors affecting charge for the year		
Capital allowances for year in excess of depreciation	**95**	58
Other timing differences	**(24)**	(22)
Depreciation on non-qualifying assets	**109**	65
Income from shares in group undertakings	**(96)**	-
Profit/loss on non-qualifying assets	**(2,573)**	-
Expenses not deductible for tax purposes	**6**	1
Adjustment to tax charge in respect of prior years	**(2)**	(6)
Total actual amount of current tax	**560**	386

Notes *(continued)*

7 Tangible assets

	Freehold land and buildings £000	Assets in course of construction £000	Fixtures and fittings £000	Motor vehicles £000	Total £000
Cost					
At beginning of the year	26,755	18	1,792	343	28,908
Additions	61	43	353	60	517
Disposals	-	-	-	(41)	(41)
Disposal to group undertaking	(26,816)	(60)	(680)	-	(27,556)
At end of the year	-	1	1,465	362	1,828
Depreciation					
At beginning of the year	-	-	600	142	742
Charge for the year	349	-	250	82	681
On disposals	-	-	-	(21)	(21)
On disposal to group undertaking	(349)	-	(55)	-	(404)
At end of the year	-	-	795	203	998
Net book value					
At 31 December 2005	**-**	**1**	**670**	**159**	**830**
At 31 December 2004	26,755	18	1,192	201	28,166

Included in the total net book value of motor vehicles is £159,000 *(2004: £201,000)* in respect of assets held under finance leases. Depreciation for the year on these assets was £82,000 *(2004: £71,000).*

Analysis of land and buildings at cost or valuation	**2005 £000**	2004 £000
At cost	-	-
At valuation	-	26,755
	-	26,755

The Company's land and buildings were re-valued at 31 December 2004, on the basis of existing use value by independent qualified valuers. The valuations were undertaken in accordance with the Practice Statements set out in the Royal Institution of Chartered Surveyors Appraisal and Valuation Standards – 5th Edition, as amended, by Colliers Conrad Ritblat Erdman, a firm of independent Chartered Surveyors.

The valuations were incorporated into the financial statements and the resulting revaluation adjustments were taken to the revaluation reserve. The revaluations during the year ended 31 December 2004 resulted in a revaluation surplus of £16,105,000.

Notes *(continued)*

7 Tangible fixed assets *(continued)*

The historical net book value of land and buildings is given below:

	2005 £000	2004 £000
Historical cost of land and buildings	-	6,871
Aggregate depreciation thereon	-	(191)
Historical cost net book value	-	6,680

No deferred tax is provided on timing differences arising from the revaluation of fixed assets unless, by the balance sheet date, a binding commitment to sell the asset has been entered into and it is unlikely that any gain will be rolled over.

8 Fixed asset investments

	Total
Shares in group undertaking	£
Cost and net book value	
At the beginning and end of the year	1

The undertaking in which the company's interest at the year end is more than 20% are as follows:

Subsidiary undertaking	Principal activities	Class and percentage of share held
North Hill House Limited	Specialist school for children with Asperger Syndrome	100% ordinary

North Hill House Limited is registered in England and Wales.

Notes *(continued)*

9 Debtors

	2005	2004
	£000	£000
Trade debtors	**721**	658
Amounts owed by group undertakings	**5,086**	106
Prepayments and accrued income	**34**	13
	5,841	777

10 Creditors: amounts falling due within one year

	2005	2004
	£000	£000
Obligations under finance lease contracts	**71**	62
Trade creditors	**77**	85
Amounts owed to group undertakings	**5,107**	4,807
Group relief payable	**562**	392
Other taxes and social security	**98**	76
Other creditors	**4**	15
Accruals and deferred income	**2,721**	2,690
	8,640	8,127

Notes *(continued)*

11 Creditors: amounts falling due after more than one year

	2005	2004
	£000	£000
Bank loans and overdrafts	**-**	1,253
Obligations under finance lease contracts	**119**	157
	119	1,410

Obligations under finance leases are payable as follows:

	2005	2004
	£000	£000
Within one year or less	**71**	62
Within one to two years	**63**	62
Within two to five years	**56**	95
	190	219

12 *Provisions for liabilities and charges*

	£
Deferred tax	
At beginning and end of the year	-

Deferred tax has been provided in full as follows:

	2005	2004
	£	£
Difference between accumulated depreciation and capital allowances	**-**	-

No provision has been made for deferred tax on gains recognised on revaluing property to its market value. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. At 31 December 2005, the total amount un-provided for was £nil *(31 December 2004: £5.9 million).* At present it is not envisaged that any such tax will become payable in the foreseeable future.

Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the period in which timing differences reverse, based on tax rates and laws substantively enacted at the balance sheet date.

Notes *(continued)*

13 Called up share capital

	2005 £	2004 £
Authorised		
1,000 *(2004: 1,000)* Ordinary shares of £1 each	**1,000**	1,000
Allotted, called up and fully paid		
2 *(2004: 2)* Ordinary shares of £1 each	**2**	2

14 Reserves

	Revaluation reserve £000	Profit and loss account £000
At beginning of the year	20,137	1,633
Retained loss for the year	-	(20,727)
Transfers	(20,137)	20,137
At end of the year	**-**	**1,043**

15 Commitments

a) Capital commitments at the end of the financial year, for which no provision has been made, are as follows:

	2005 £000	2004 £000
Contracted	-	110

b) Annual commitments under non-cancellable operating leases are as follows:

	2005 Land and buildings £000	2005 Other £000	2004 Land and buildings £000	2004 Other £000
Operating leases which expire:				
Within one year	**16**	-	8	-
Over five years	**1,716**	-	-	-
	1,732	-	8	-

Notes *(continued)*

16 Contingent liabilities

(a) The company has entered into banking facilities set-off agreements in respect of which guarantees have been given. The aggregate amount outstanding under the agreements was £nil at 31 December 2005 *(2004: £nil)*.

(b) A fellow subsidiary undertaking has issued secured fixed and floating rate notes amounting to £201.1 million as at 31 December 2004 *(31 December 2003: £206.2 million)*. These notes are secured on the freehold and leasehold properties of certain of its subsidiaries. In addition, the company's share capital has been pledged as security for this loan.

17 Pension scheme

The company operates a defined contribution pension scheme. The pension cost charge for the year represents contributions payable by the company to the fund and amounted to £23,000 *(2004: £11,000)*.

As at 31 December 2005, there were outstanding contributions of £4,000 *(31 December 2004: £1,000)*.

The company participated in the Teachers' Pension Scheme ("the scheme") which is a government funded final salary scheme. The pension charge for the year was £42,000 *(2004: £49,000)*. The company is unable to identify its share of the underlying assets and liabilities of the scheme in which it participates on a consistent and reliable basis. It has therefore taken advantage of the exemption under Financial Reporting Standard 17 paragraph 9 to treat the scheme as a defined contribution scheme.

18 Ultimate parent company

The company is a subsidiary undertaking of Priory Education Services Limited, which is incorporated in England.

The largest group in which the results of the company are consolidated is that headed by Priory Investments Holdings Limited. No other group accounts include the results of the company.