

LINCOLN EDUCATIONAL SERVICES CORP
Form 10-K
March 10, 2017

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2016

Commission File Number 000-51371

LINCOLN EDUCATIONAL SERVICES CORPORATION
(Exact name of registrant as specified in its charter)

New Jersey 57-1150621
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

200 Executive Drive, Suite 340
West Orange, NJ 07052
(Address of principal executive offices)

(973) 736-9340
(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Name of exchange on which registered</u>
Common Stock, no par value per share	The NASDAQ Stock Market LLC

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

None

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. 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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The aggregate market value of the 22,107,983 shares of common stock held by non-affiliates of the registrant issued and outstanding as of June 30, 2016, the last business day of the registrant's most recently completed second fiscal quarter, was \$44,658,126. This amount is based on the closing price of the common stock on the Nasdaq Global Select Market of \$2.02 per share on June 30, 2016. Shares of common stock held by executive officers and directors and persons who own 5% or more of outstanding common stock have been excluded since such persons may be deemed affiliates. This determination of affiliate status is not a determination for any other purpose.

The number of shares of the registrant's common stock outstanding as of March 8, 2017 was 24,719,105.

Documents Incorporated by Reference

Portions of the Proxy Statement for the Registrant's 2017 Annual Meeting of Stockholders are incorporated by reference in Part III of this Annual Report on Form 10-K. With the exception of those portions that are specifically incorporated by reference in this Annual Report on Form 10-K, such Proxy Statement shall not be deemed filed as part of this Report or incorporated by reference herein.

LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES

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Forward-Looking Statements

This Annual Report on Form 10-K contains “forward-looking statements,” within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, which include information relating to future events, future financial performance, strategies, expectations, competitive environment, regulation and availability of resources. These forward-looking statements include, without limitation, statements regarding: proposed new programs; expectations that regulatory developments or other matters will or will not have a material adverse effect on our consolidated financial position, results of operations or liquidity; statements concerning projections, predictions, expectations, estimates or forecasts as to our business, financial and operating results and future economic performance; and statements of management’s goals and objectives and other similar expressions concerning matters that are not historical facts. Words such as “may,” “should,” “could,” “would,” “predicts,” “potential,” “continue,” “expects,” “anticipates,” “intends,” “plans,” “believes,” “estimates,” and similar expressions, as well as statements in future tense, identify forward-looking statements.

Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times at, or by, which such performance or results will be achieved. Forward-looking statements are based on information available at the time those statements are made and/or management’s good faith belief as of that time with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in or suggested by the forward-looking statements. Important factors that could cause such differences include, but are not limited to:

- our failure to comply with the extensive existing regulatory framework applicable to our industry or our failure to obtain timely regulatory approvals in connection with a change of control of our company or acquisitions;
- the promulgation of new regulations in our industry as to which we may find compliance challenging;
- our success in updating and expanding the content of existing programs and developing new programs in a cost-effective manner or on a timely basis;
- our ability to implement our strategic plan;
- risks associated with changes in applicable federal laws and regulations including pending rulemaking by the U.S. Department of Education;
- uncertainties regarding our ability to comply with federal laws and regulations regarding the 90/10 rule and cohort default rates;
- risks associated with opening new campuses and closing existing campuses;
- risks associated with integration of acquired schools;
- industry competition;
- conditions and trends in our industry;
- general economic conditions; and
- other factors discussed under the headings “Business,” “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Forward-looking statements speak only as of the date the statements are made. Except as required under the federal securities laws and rules and regulations of the United States Securities and Exchange Commission (the “SEC”), we undertake no obligation to update or revise forward-looking statements to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information. We caution you not to unduly rely on the forward-looking statements when evaluating the information presented herein.

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PART I.

ITEM 1. BUSINESSOVERVIEW

Lincoln Educational Services Corporation and its subsidiaries (collectively, the “Company”, “we”, “our” and “us”, as applicable) provide diversified career-oriented post-secondary education to recent high school graduates and working adults. The Company, which currently operates 28 schools in 15 states, offers programs in automotive technology, skilled trades (which include HVAC, welding and computerized numerical control and electronic systems technology, among other programs), healthcare services (which include nursing, dental assistant, medical administrative assistant and pharmacy technician, among other programs), hospitality services (which include culinary, therapeutic massage, cosmetology and aesthetics) and business and information technology (which includes information technology and criminal justice programs). The schools operate under Lincoln Technical Institute, Lincoln College of Technology, Lincoln College of New England, Lincoln Culinary Institute, and Euphoria Institute of Beauty Arts and Sciences and associated brand names. Most of the campuses serve major metropolitan markets and each typically offers courses in multiple areas of study. Five of the campuses are destination schools, which attract students from across the United States and, in some cases, from abroad. The Company’s other campuses primarily attract students from their local communities and surrounding areas. All of the campuses are nationally or regionally accredited and are eligible to participate in federal financial aid programs by the U.S. Department of Education (the “DOE”) and applicable state education agencies and accrediting commissions which allow students to apply for and access federal student loans as well as other forms of financial aid.

In the first quarter of 2015, we reorganized our operations into three reportable business segments: (a) Transportation and Skilled Trades, (b) Healthcare and Other Professions (“HOPS”), and (c) Transitional which refers to businesses that have been or are currently being taught out. In November 2015 the Board of Directors approved a plan for the Company to divest the schools included in the HOPS business segment. Divestiture of the Company’s HOPS business segment marks a strategic shift in business strategy that will enable us to focus energy and resources predominantly on the Transportation and Skilled Trades business segment. The Company continues to actively market the schools comprising the HOPS business segment and has offers which are under consideration. The results of operations of the campuses included in the HOPS business segment are reflected as discontinued operations in the consolidated financial statements.

The following table lists the schools that are included in the HOPS and Transitional Segments and their status as of December 31, 2016 and 2015:

School	Segment		Status		
	2015	2016	2015	2016	
Allentown, PA	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Edison, NJ	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Moorestown, NJ	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Paramus, NJ	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Lincoln, RI	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Brockton, MA	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1

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Somerville, MA	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Lowell, MA	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
New Britain, CT	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Shelton, CT	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Las Vegas (Summerlin), NV	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Southington, CT	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Marietta, GA	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Held for sale	1
Hartford, CT	Transitional (Continuing Operations)	HOPS (Discontinued Operations)	Teach-out	Closed	2
Henderson (Green Valley), NV	HOPS (Discontinued Operations)	HOPS (Discontinued Operations)	Held for sale	Closed	3
Center City Philadelphia, PA	HOPS (Discontinued Operations)	Transitional (Continuing Operations)	Held for sale	Teach-out	4
Northeast Philadelphia, PA	HOPS (Discontinued Operations)	Transitional (Continuing Operations)	Held for sale	Teach-out	4
West Palm Beach, FL	HOPS (Discontinued Operations)	Transitional (Continuing Operations)	Held for sale	Teach-out	5
Fern Park, FL	Transitional (Continuing Operations)	Transitional (Continuing Operations)	Teach-out	Closed	6

¹ In November 2015, the Board of Directors approved a plan to divest these schools and thus they are included in discontinued operations as of December 31, 2016 and 2015.

² In November 2015, the Board of Directors approved a plan to divest this school. In December 2015, the Board of Directors approved a plan to cease operations at this school. The school was included in the Transitional Segment and included in continuing operations until it closed in the fourth quarter of 2016; it is included in discontinued operations as of December 31, 2016.

³ In November 2015, the Board of Directors approved a plan to divest this school. In the fourth quarter of 2016, the Board of Directors approved a plan to cease operations at this school, which closed in the fourth quarter of 2016 and is included in discontinued operations as of December 31, 2016.

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In November 2015, the Board of Directors approved a plan to divest these schools. In the fourth quarter of 2016, the Board of Directors approved a plan to cease operations at these schools which are being taught-out and expected to be closed in 2017. These schools are included in the Transitional segment and continuing operations as of December 31, 2016.

In November 2015, the Board of Directors approved a plan to divest this school. In the third quarter of 2016, the Board of Directors approved a plan to teach-out certain programs at this school. Then, in the fourth quarter of 2016, the Board of Directors approved a plan to teach-out the remainder of the programs at this school. The school is expected to be closed in 2017. This school's operations are included in the Transitional segment and continuing operations as of December 31, 2016. However, as part of this plan, the Board of Directors approved the divestiture of the properties for this school and therefore the properties are included in held for sale as of December 31, 2016. On February 27, 2015, our Board of Directors approved a plan to cease operations at this school, which was fully taught out and officially closed as of March 31, 2016 and is included in the Transitional segment and continuing operations as of December 31, 2016. The plan to teach out this school was approved prior to the plan to exit the HOPS segment and as such does not meet the discontinued operations criteria.

As of December 31, 2016, we had 11,235 students enrolled at 28 campuses, 7,295 of those students are enrolled at campuses that are included in continuing operations. Our average enrollment for the year ended December 31, 2016 was 11,864 students which represented a decrease of 8.6% from average enrollment in 2015. Average enrollment at campuses that are included in continuing operations of 7,725 students represented a decrease of 8.0% from average enrollment in 2015 from such continuing operations. For the year ended December 31, 2016, our revenues were \$285.6 million, which represented a decrease of 6.7 % from the prior year. Revenues were \$196.9 million from continuing operations, which represented a decrease of 5.4% from the prior year. For more information relating to our revenues, profits and financial condition, please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements included in this Annual Report on Form 10-K.

We believe that we provide our students with the highest quality career-oriented training available for our areas of study in our markets. We offer programs in areas of study that we believe are typically underserved by traditional providers of post-secondary education and for which we believe there exists significant demand among students and employers. Furthermore, we believe our convenient class scheduling, career-focused curricula and emphasis on job placement offer our students valuable advantages that have been neglected by the traditional academic sector. By combining substantial hands-on training with traditional classroom-based training led by experienced instructors, we believe we offer our students a unique opportunity to develop practical job skills in many of the key areas of expected job demand. We believe these job skills enable our students to compete effectively for employment opportunities and to pursue on-going salary and career advancement.

The Company was incorporated in New Jersey in 2003 but a predecessor entity had opened its first campus in Newark, New Jersey in 1946.

AVAILABLE INFORMATION

Our website is www.lincolnedu.com. We make available on this website our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, annual proxy statements on Schedule 14A and amendments to those reports and statements as soon as reasonably practicable after we electronically file or furnish such materials to the SEC. You can access this information on our website, free of charge, by clicking on "Investor Relations." The information contained on or connected to our website is not a part of this Annual Report on Form 10-K. We will provide paper copies of such filings free of charge upon request. The public may read and copy any materials filed by us with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Information regarding the operation of the SEC's Public Reference Room is available by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet site that contains reports, proxy and information statements and other

information regarding us, which is available at www.sec.gov.

BUSINESS STRATEGY

Our goal is to strengthen our position as a leading provider of career oriented post-secondary education by continuing to pursue the following strategy:

Expand Existing Areas of Study and Existing Facilities. We believe we can leverage our operations to expand our program offerings in existing areas of study and expand into new areas of study in the Transportation and Skilled Trades segment to capitalize on demand from students and employers in our target markets. Whenever possible, we seek to replicate programs across our campuses.

Maximize Utilization of Existing Facilities. We are focused on improving capacity utilization of existing facilities through increased enrollments, the introduction of new programs and partnerships with industry.

Expand Market. We believe that we can enter new markets and broaden the Lincoln brand by partnering with nationally recognized brands to provide the skills needed to train our nation's workforce. We continue to expand our industry relationships both to attract new students and to offer our graduates more employment opportunities. We continue to establish partnerships with companies like BMW,

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Chrysler (FCA), Raytheon, Volkswagen and Audi that will enable graduates to receive higher wages. We expect to continue investing in marketing, recruiting and retention resources to increase enrollment.

Concentrate on Transportation and Skilled Trades. During the fourth quarter of 2015 we announced our plan to sell 17 of the 18 schools comprising our HOPS business segment. The planned divestiture allows us to concentrate our resources on our Transportation and Skilled Trades business segment. We believe that we can further penetrate this market and create a more profitable Company.

PROGRAMS AND AREAS OF STUDY

We structure our program offerings to provide our students with a practical, career-oriented education and position them for attractive entry-level job opportunities in their chosen fields. Our diploma/certificate programs typically take between 22 to 136 weeks to complete, with tuition ranging from \$6,600 to \$36,000. Our associate's degree programs typically take between 48 to 156 weeks to complete, with tuition ranging from \$20,000 to \$70,000. Our bachelor's degree programs typically take between 104 and 208 weeks to complete, with tuition ranging from \$40,000 to \$80,000. As of December 31, 2016, all of our schools offer diploma and certificate programs, 12 of our schools are currently approved to offer associate's degree programs and one school is approved to offer bachelor's degree programs. In order to accommodate the schedules of our students and maximize classroom utilization at some of our campuses, we typically offer courses four to five days per week in three shifts per day and start new classes every month. Other campuses are structured more like a traditional college and start classes every quarter. We update and expand our programs frequently to reflect the latest technological advances in the field, providing our students with the specific skills and knowledge required in the current marketplace. Classroom instruction combines lectures and demonstrations by our experienced faculty with comprehensive hands-on laboratory exercises in simulated workplace environments.

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The following table lists the programs offered as of December 31, 2016:

Current Programs Offered

Area of Study	Bachelor's Degree	Associate's Degree	Diploma and Certificate
Automotive		Automotive Service Management, Automotive Technology, Collision Repair & Refinishing Service Management, Diesel & Truck Service Management	Automotive Mechanics, Automotive Technology, Automotive Technology with BMW FastTrack, Automotive Technology with Mopar X-Press, Automotive Technology with High Performance, Collision Repair and Refinishing Technology, Diesel & Truck Mechanics, Diesel & Truck Technology, Diesel & Truck Technology with Transport Refrigeration, Diesel & Truck with Automotive Technology, Heavy Equipment Maintenance Technology, Heavy Equipment and Truck Technology
Health Sciences	Health Information Administration, RN to BSN	Medical Assisting Technology, Dental Office Management, Health Information Technology, Medical Office Management, Mortuary Science, Occupational Therapy Assistant, Dental Hygiene, Dental Administrative Assistant, Advanced Medical Coding & Billing	Medical Office Assistant, Medical Assistant, Patient Care Technician, Pharmacy Technician, Medical Coding & Billing, Dental Assistant, Licensed Practical Nursing
Skilled Trades		Electronic Engineering Technology, HVAC, Electronics Systems Service Management	Electrical Technology & Electronic Systems Technology, Electrical Technology, Electronics Systems Technician, HVAC, Welding Technology, CNC
Hospitality Services			Culinary Arts, Cosmetology, Aesthetics, International Baking and Pastry, Nail Technology, Therapeutic Massage & Bodywork Technician
Business and Information Technology	Business Management, Criminal Justice, Funeral Service Management	Criminal Justice, Business Management, Broadcasting and Communications, Paralegal, Computer Networking and Support, Human Services	Criminal Justice, Computer & Network Support Technician

Automotive Technology. Automotive technology is our largest area of study, with 42% of our total average student enrollment for the year ended December 31, 2016. Our automotive technology programs are 28 to 136 weeks in length, with tuition rates of \$11,500 to \$37,000. We believe we are a leading provider of automotive technology education in each of our local markets. Graduates of our programs are qualified to obtain entry level employment

ranging from positions as technicians and mechanics to various apprentice level positions. Our graduates are employed by a wide variety of companies, ranging from automotive and diesel dealers, to independent auto body paint and repair shops to trucking and construction companies.

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As of December 31, 2016, 12 campuses offered programs in automotive technology and most of these campuses offer other technical programs. Our campuses in East Windsor, Connecticut; Nashville, Tennessee; Grand Prairie, Texas; Indianapolis, Indiana; and Denver, Colorado are destination campuses, attracting students throughout the United States and, in some cases, from abroad.

Health Sciences. For the year ended December 31, 2016, health sciences was our second largest area of study, representing 29% of our total average student enrollment. Our health science programs are 32 to 208 weeks in length, with tuition rates of \$13,600 to \$76,000. Graduates of our programs are qualified to obtain positions such as licensed practical nurse, registered nurse, dental assistant, medical assistant, medical administrative assistant, EKG technician, claims examiner and pharmacy technician. Our graduates are employed by a wide variety of employers, including hospitals, laboratories, insurance companies, doctors' offices and pharmacies. Our practical nursing and medical assistant programs are our largest health science programs. As of December 31, 2016, we offered health science programs at 13 of our campuses.

Skilled Trades. For the year ended December 31, 2016, 19% of our total average student enrollment was in our skilled trades programs. Our skilled trades programs are 36 to 97 weeks in length, with tuition rates of \$16,800 to \$32,000. Our skilled trades programs include electrical, heating and air conditioning repair, welding, computerized numerical control and electronic systems technology. Graduates of our programs are qualified to obtain entry level employment positions such as electrician, cable installer, welder, wiring and heating, ventilating and air conditioning, or HVAC installer. Our graduates are employed by a wide variety of employers, including residential and commercial construction, telecommunications installation companies and architectural firms. As of December 31, 2016, we offered skilled trades programs at 13 campuses.

Hospitality Services. For the year ended December 31, 2016, 7% of our total average student enrollment was in our hospitality services programs. Our hospitality services programs are 22 to 66 weeks in length, with tuition rates of \$6,600 to \$20,000. Our hospitality programs include culinary, therapeutic massage, cosmetology and aesthetics. Graduates work in salons, spas or cruise ships or are self-employed. We offer massage programs at two campuses and cosmetology programs at one campus. Our culinary graduates are employed by restaurants, hotels, cruise ships and bakeries. As of December 31, 2016, we offered culinary programs at one campus.

Business and Information Technology. For the year ended December 31, 2016, 3% of our total average student enrollment was in our business and information technology programs, which include our diploma and degree criminal justice programs. Our business and information technology programs are 40 to 208 weeks in length, with tuition rates of \$13,000 to \$80,000. We have focused our current information technology, or IT, program offerings on occupations that are most in demand, such as computer and network support technician. Our IT and business graduates work in entry level positions for both small and large corporations. Our criminal justice graduates work in the security industry and for various government agencies and departments. As of December 31, 2016, we offered these programs at 8 of our campuses.

MARKETING AND STUDENT RECRUITMENT

We utilize a variety of marketing and recruiting methods to attract students and increase enrollment. Our marketing and recruiting efforts are targeted at prospective students who are high school graduates entering the workforce, or who are currently underemployed or unemployed and require additional training to enter or re-enter the workforce.

Marketing and Advertising. We utilize an integrated marketing approach in our admissions efforts that includes the use of traditional media such as television, radio, billboards, direct mail, various print media and event marketing campaigns. Our digital marketing efforts, including paid search, search engine optimization and online video and display advertising, have grown significantly in recent years and currently drive the majority of our new student leads and enrollments. Our website's integrated marketing campaigns direct prospective students to call or visit the Lincoln

website where they may request additional information on a program or campus of interest. Our internal systems enable us to closely monitor and track the effectiveness of each advertisement on a daily or weekly basis and make adjustments accordingly to enhance efficiency and limit our student acquisition costs. In 2016, we relaunched our website with a new primary domain. The new structure of the website has enhanced the user experience providing easier access to key content and information. The site was also redesigned using a “mobile first” approach that maintains the website’s format and structure even on smaller devices including smart phones and tablets on which the growing majority of initial online searches for education options are conducted.

Referrals. Referrals from current students, high school counselors and satisfied graduates and their employers have historically represented 17% of our new enrollments. Our school administrators actively work with our current students to encourage them to recommend our programs to prospective students. We continue to build strong relationships with high school guidance counselors and instructors by offering annual seminars at our training facilities to further familiarize these individuals on the strengths of our programs.

Recruiting. Our recruiting efforts are conducted by a group of approximately 250 field and campus-based representatives who meet directly with prospective students during presentations conducted at high schools, in the prospective students homes or during a visit to one of our campuses.

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During 2016, we recruited approximately 24% of our students directly out of high school. In addition, we have added ten field representatives to our team of 83. Field sales continues to be a large part of our business and developing local community relationships is one of our most important functions.

STUDENT ADMISSIONS, ENROLLMENT AND RETENTION

Admissions. In order to attend our schools, students must complete an application and pass an entrance assessment. While each of our programs has different admissions criteria, we screen all applications and counsel the students on the most appropriate program to increase the likelihood that our students complete the requisite coursework and obtain and sustain employment following graduation.

Enrollment. We enroll students continuously throughout the year, with our largest classes enrolling in late summer or early fall following high school graduation. From continuing operations, we had 7,295 students enrolled as of December 31, 2016 and our average enrollment for the year ended December 31, 2016 was 7,725 students, a decrease of 8.0% in average enrollment from December 31, 2015. We had 7,545 students enrolled as of December 31, 2015 and our average enrollment for that year was 8,395 students, a decrease of 7.1% in average enrollment from December 31, 2014.

Retention. To maximize student retention, the staff at each school is trained to recognize the early warning signs of a potential drop and to assist and advise students on academic, financial, employment and personal matters. We monitor our retention rates by instructor, course, program and school. When we become aware that a particular instructor or program is experiencing a higher than normal dropout rate, we quickly seek to determine the cause of the problem and attempt to correct it. When we identify that a student is experiencing difficulty academically, we offer tutoring.

JOB PLACEMENT

We believe that assisting our graduates in securing employment after completing their program of study is critical to our ability to attract high quality students and enhancing our reputation in the industry. In addition, we believe that high job placement rates result in low student loan default rates, an important requirement for continued participation in Title IV of the Higher Education Act of 1965, as amended ("Title IV Programs"). See "Regulatory Environment—Regulation of Federal Student Financial Aid Programs." Accordingly, we dedicate significant resources to maintaining an effective graduate placement program. Our non-destination schools work closely with local employers to ensure that we are training students with skills that employers need. Each school has an advisory council comprised of local employers who provide us with direct feedback on how well we are preparing our students to succeed in the workplace. This enables us to tailor our programs to the marketplace. The placement staff in each of our destination schools maintains databases of potential employers throughout the country, allowing us to more effectively assist our graduates in securing employment in their career field upon graduation. Throughout the year, we hold numerous job fairs at our facilities where we provide the opportunity for our students to meet and interact with potential employers. In addition, many of our schools have internship programs that provide our students with opportunities to work with employers prior to graduation. For example, some of the students in our automotive programs have the opportunity to complete a portion of their hands-on training in an actual work environment. In addition, some of our healthcare students are required to participate in an externship program during which they work in the field as part of their career training. We also assist students with resume writing, interviewing and other job search skills.

FACULTY AND EMPLOYEES

We hire our faculty in accordance with established criteria, including relevant work experience, educational background and accreditation and state regulatory standards. We require meaningful industry experience of our teaching staff in order to maintain the quality of instruction in all of our programs and to address current and

industry-specific issues in our course content. In addition, we provide intensive instructional training and continuing education, including quarterly instructional development seminars, annual reviews, technical upgrade training, faculty development plans and weekly staff meetings.

The staff of each school typically includes a school director, a director of graduate placement, an education director, a director of student services, a financial-aid director, an accounting manager, a director of admissions and instructors, all of whom are industry professionals with experience in our areas of study.

As of December 31, 2016, we had approximately 2,197 employees, including 533 full-time faculty and 432 part-time instructors. At six of our campuses, the teaching professionals are represented by unions. These employees are covered by collective bargaining agreements that expire between 2017 and 2020. We believe that we have good relationships with these unions and with our employees.

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COMPETITION

The for-profit, post-secondary education industry is highly competitive and highly fragmented with no one provider controlling significant market share. Direct competition between career-oriented schools like us and traditional four-year colleges or universities is limited. Thus, our main competitors are other for-profit, career-oriented schools, not-for-profit public, private schools, public and private two-year junior and community colleges most of which are eligible to receive funding under the federal programs of student financial aid authorized by Title IV Programs. Competition is generally based on location, the type of programs offered, the quality of instruction, placement rates, reputation, recruiting and tuition rates. Public institutions are generally able to charge lower tuition than our school, due in part to government subsidies and other financial sources not available to for-profit schools. In addition, some of our other competitors have a more extensive network of schools and campuses than we do, which enables them to recruit students more efficiently from a wider geographic area. Nevertheless, we believe that we are able to compete effectively in our local markets because of the diversity of our program offerings, quality of instruction, the strength of our brands, our reputation and our graduates' success in securing employment after completing their program of study.

Our competition differs in each market depending on the curriculum that we offer. For example, a school offering automotive, healthcare and skilled trades programs will have a different group of competitors than a school offering healthcare, business/IT and skilled trades. Also, because schools can add new programs within six to twelve months, competition can emerge relatively quickly. Moreover, with the introduction of online education, the number of competitors in each market has increased because students can now attend classes from an online institution. On average, each of our schools has at least three direct competitors and at least a dozen indirect competitors.

ENVIRONMENTAL MATTERS

We use hazardous materials at our training facilities and campuses, and generate small quantities of waste such as used oil, antifreeze, paint and car batteries. As a result, our facilities and operations are subject to a variety of environmental laws and regulations governing, among other things, the use, storage and disposal of solid and hazardous substances and waste, and the clean-up of contamination at our facilities or off-site locations to which we send or have sent waste for disposal. We are also required to obtain permits for our air emissions and to meet operational and maintenance requirements. In the event we do not maintain compliance with any of these laws and regulations, or are responsible for a spill or release of hazardous materials, we could incur significant costs for clean-up, damages, and fines or penalties. Climate change has not had and is not expected to have a significant impact on our operations.

REGULATORY ENVIRONMENT

Students attending our schools finance their education through a combination of family contributions, individual resources, private loans and federal financial aid programs. Each of our schools participates in the Title IV Programs, which are administered by the DOE. For the year ended December 31, 2016, approximately 79% (calculated based on cash receipts) of our revenues were derived from the Title IV Programs. Students obtain access to federal student financial aid through a DOE prescribed application and eligibility certification process.

In connection with the students' receipt of federal financial aid under the Title IV Programs, our schools are subject to extensive regulation by governmental agencies and licensing and accrediting bodies. In particular, the Higher Education Act of 1965, as amended, and the regulations issued thereafter by the DOE, subject us to significant regulatory scrutiny in the form of numerous standards that each of our schools must satisfy in order to participate in the Title IV Programs. To participate in the Title IV Programs, a school must be authorized to offer its programs of instruction by the applicable state education agencies in the states in which it is physically located, be accredited by an accrediting commission recognized by the DOE and be certified as an eligible institution by the DOE. The DOE

defines an eligible institution to consist of both a main campus and its additional locations, if any. Each of our schools is either a main campus or an additional location of a main campus. Each of our schools is subject to extensive regulatory requirements imposed by state education agencies, accrediting commissions, and the DOE. Because the DOE periodically revises its regulations and changes its interpretations of existing laws and regulations, we cannot predict with certainty how Title IV Program requirements will be applied in all circumstances. Our schools also participate in other federal and state financial aid programs that assist students in paying the cost of their education and that impose standards that we must satisfy.

State Authorization

Each of our schools must be authorized by the applicable education agencies in the states in which the school is physically located, and in some cases other states, in order to operate and to grant degrees, diplomas or certificates to its students. State agency authorization is also required in each state in which a school is physically located in order for the school to become and remain eligible to participate in Title IV Programs. If we are found not to be in compliance with the applicable state regulation and a state seeks to restrict one or more of our business activities within its boundaries, we may not be able to recruit or enroll students in that state and may have to stop providing services in that state, which could have a significant impact on our business and results of operations. Currently, each of our schools is authorized by the applicable state education agencies in the states in which the school is physically located and in which it recruits students.

Our schools are subject to extensive, ongoing regulation by each of these states. State laws typically establish standards for instruction, curriculum, qualifications of faculty, location and nature of facilities and equipment, administrative procedures, marketing, recruiting, financial operations, student outcomes and other operational matters. State laws and regulations may limit our ability to offer educational programs and to award degrees, diplomas or certificates. Some states prescribe standards of financial responsibility that are different from, and in certain cases more stringent than, those prescribed by the DOE. Some states require schools to post a surety bond. We have posted surety bonds on behalf of our schools and education representatives with multiple states in a total amount of approximately \$14.3 million.

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The DOE published regulations that took effect on July 1, 2011, that expanded the requirements for an institution to be considered legally authorized in the state in which it is physically located for Title IV purposes. In some cases, the regulations required states to revise their current requirements and/or to license schools in order for institutions to be deemed legally authorized in those states and, in turn, to participate in Title IV Programs. If the states do not amend their requirements where necessary and if schools do not receive approvals where necessary that comply with these new requirements, then the institution could be deemed to lack the state authorization necessary to participate in Title IV Programs. The DOE stated when it published the final regulations that it will not publish a list of states that meet, or fail to meet, the requirements, and it is uncertain how the DOE will interpret these requirements in each state.

If any of our schools fail to comply with state licensing requirements, they are subject to the loss of state licensure or authorization. If any one of our schools lost its authorization from the education agency of the state in which the school is located, or failed to comply with the DOE's state authorization requirements, that school would lose its eligibility to participate in Title IV Programs, the Title IV eligibility of its related additional locations could be affected, the impacted schools would be unable to offer its programs, and we could be forced to close the schools. If one of our schools lost its state authorization from a state other than the state in which the school is located, the school would not be able to recruit students or to operate in that state.

Due to state budget constraints in certain states in which we operate, it is possible that those states may continue to reduce the number of employees in, or curtail the operations of, the state education agencies that oversee our schools. A delay or refusal by any state education agency in approving any changes in our operations that require state approval could prevent us from making such changes or could delay our ability to make such changes. States periodically change their laws and regulations applicable to our schools and such changes could require us to change our practices and could have a significant impact on our business and results of operations.

Accreditation

Accreditation is a non-governmental process through which a school submits to ongoing qualitative and quantitative review by an organization of peer institutions. Accrediting commissions primarily examine the academic quality of the school's instructional programs, and a grant of accreditation is generally viewed as confirmation that the school's programs meet generally accepted academic standards. Accrediting commissions also review the administrative and financial operations of the schools they accredit to ensure that each school has the resources necessary to perform its educational mission.

Accreditation by an accrediting commission recognized by the DOE is required for an institution to be certified to participate in Title IV Programs. In order to be recognized by the DOE, accrediting commissions must adopt specific standards for their review of educational institutions. As of December 31, 2016, 15 of our campuses are accredited by the Accrediting Commission of Career Schools and Colleges, or ACCSC; 12 of our campuses are accredited by the Accrediting Council for Independent Colleges and Schools, or ACICS; and one of our campuses is accredited by the New England Association of Schools and Colleges of Technology, or NEASC. The following is a list of the dates on which each campus was accredited by its accrediting commission, the date by which its accreditation must be renewed and the type of accreditation.

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Accrediting Commission of Career Schools and Colleges Reaccreditation Dates

School	Last Accreditation Letter	Next Accreditation	Type of Accreditation
Philadelphia, PA ²	September 30, 2013	May 1, 2018	National
Union, NJ ¹	May 29, 2014	February 1, 2019	National
Mahwah, NJ ¹	March 11, 2015	August 1, 2019	National
Melrose Park, IL ²	March 13, 2015	November 1, 2019	National
Denver, CO ¹	June 14, 2016	February 1, 2021	National
Columbia, MD	March 8, 2017	February 1, 2022	National
Grand Prairie, TX ¹	December 7, 2011	August 1, 2016 ³	National
Allentown, PA ²	March 8, 2017	February 1, 2022	National
Nashville, TN ¹	November 30, 2012	May 1, 2017	National
Indianapolis, IN	November 30, 2012	November 1, 2017 ³	National
New Britain, CT	June 5, 2014	January 1, 2018	National
Shelton, CT ²	March 5, 2014	September 1, 2018	National
Queens, NY ¹	June 4, 2013	June 1, 2018	National
East Windsor, CT ²	December 4, 2013	February 1, 2018 ³	National
South Plainfield, NJ ¹	September 2, 2014	August 1, 2019	National

¹ Branch campus of main campus in Indianapolis, IN

² Branch campus of main campus in New Britain, CT

³ Campus undergoing re-accreditation. Campus has received written confirmation that it remains accredited pending consideration of its application for reaccreditation.

Accrediting Council for Independent Colleges and Schools Reaccreditation Dates

School	Last Accreditation Letter	Next Accreditation	Type of Accreditation
Brockton, MA ¹	August 28, 2014	December 31, 2020	National
Lincoln, RI ¹	August 28, 2014	December 31, 2019	National
Lowell, MA ¹	January 5, 2015	December 31, 2019	National
Somerville, MA ¹	August 28, 2014	December 31, 2019	National
Philadelphia (Center City), PA ¹	September 14, 2016	August 31, 2017	National
Iselin, NJ	December 20, 2016	December 31, 2022	National
Marietta, GA ¹	August 28, 2014	December 31, 2019	National
Moorestown, NJ ¹	December 20, 2016	December 31, 2022	National
Paramus, NJ ¹	December 20, 2016	December 31, 2022	National
Philadelphia (Northeast), PA ¹	December 20, 2016	December 31, 2022	National
West Palm Beach, FL ¹	August 28, 2014	December 31, 2019	National
Las Vegas (Summerlin), NV ¹	August 29, 2014	December 31, 2019	National

¹ Branch campus of main campus in Iselin, NJ

² Campus undergoing re-accreditation.

New England Association of Schools and Colleges of Technology Reaccreditation Dates

School	Last Accreditation Letter	Comprehensive Evaluation	Type of Accreditation
Southington, CT	June 29, 2012	Fall 2017	Regional

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On December 12, 2016, the DOE Secretary upheld a decision by a senior DOE official to cease DOE's recognition of ACICS as a nationally recognized accrediting agency and denying ACICS's petition for DOE recognition based on conclusions that ACICS was in violation of various DOE regulatory criteria. ACICS has appealed the DOE Secretary's decision to Federal court; however, unless otherwise directed by the court, the DOE Secretary's decision is not stayed during the appeal to Federal court and, therefore, ACICS is not a DOE-recognized accrediting agency.

Under DOE regulations, the DOE may (but is not required to) provisionally certify our ACICS-accredited institution and its campuses to continue participating in the Title IV programs for a period of up to 18 months after the date that DOE withdrew its recognition of ACICS in order to provide the institution with time to apply for and obtain accreditation from another DOE-recognized accrediting body. In December 2016, the DOE issued an addendum to the program participation agreement for our ACICS-accredited institution that moved the institution to provisional certification and imposed several conditions on the institution's Title IV participation.

We are in the process of applying for accreditation of our ACICS-accredited institution and its campuses from ACCSC. Our efforts to obtain accreditation could be unsuccessful and could result in the loss of the institution's eligibility to participate in the Title IV programs. We have met all the milestones established by the DOE, thus far, to continue in the Title IV programs for the schools accredited by ACICS.

The loss of DOE recognition by an institution's accrediting agency also could result in a loss of state authorization (and, in turn, Title IV eligibility), programmatic accreditation, and/or authorization to participate in certain state or federal financial aid programs if accreditation by a DOE-recognized accrediting agency is required for the impacted campuses of our ACICS-accredited institution to qualify for such state authorization, programmatic accreditation, or state or federal financial aid programs. We have not identified any state, federal or accrediting agencies that condition approval of our ACICS-accredited campuses on accreditation by a DOE-recognized accrediting body. However, agency requirements are imprecise or unclear in some instances and could be subject to different interpretation by one or more agencies.

If one of our schools fails to comply with accrediting commission requirements, the institution and its main and/or branch campuses are subject to the loss of accreditation or may be placed on probation or a special monitoring or reporting status which, if the noncompliance with accrediting commission requirements is not resolved, could result in loss of accreditation. If any one of our schools loses its accreditation, students attending that school would no longer be eligible to receive Title IV Program funding, and we could be forced to close that school.

Programmatic accreditation is the process through which specific programs are reviewed and approved by industry and program-specific accrediting entities. Although programmatic accreditation is not generally necessary for Title IV eligibility, such accreditation may be required to allow students to sit for certain licensure exams or to work in a particular profession or career or to meet other requirements. Failure to obtain or maintain such programmatic accreditation may lead to a decline in enrollments in such programs. Under new gainful employment issued by the DOE, institutions may be required to certify that they have programmatic accreditation under certain circumstances. See “—Regulatory Environment – Gainful Employment.”

Nature of Federal and State Support for Post-Secondary Education

The federal government provides a substantial part of the support for post-secondary education through Title IV Programs, in the form of grants and loans to students who can use those funds at any institution that has been certified as eligible by the DOE. Most aid under Title IV Programs is awarded on the basis of financial need, generally defined as the difference between the cost of attending the institution and the expected amount a student and his or her family can reasonably contribute to that cost. A recipient of Title IV Program funds must maintain a satisfactory grade point average and progress in a timely manner toward completion of his or her program of study and must meet other applicable eligibility requirements for the receipt of Title IV funds. In addition, each school must ensure that Title IV

Program funds are properly accounted for and disbursed in the correct amounts to eligible students.

Other Financial Assistance Programs

Some of our students receive financial aid from federal sources other than Title IV Programs, such as programs administered by the U.S. Department of Veterans Affairs and under the Workforce Investment Act. In addition, some states also provide financial aid to our students in the form of grants, loans or scholarships. The eligibility requirements for state financial aid and these other federal aid programs vary among the funding agencies and by program. States that provide financial aid to our students are facing significant budgetary constraints. Some of these states have reduced the level of state financial aid available to our students. Due to state budgetary shortfalls and constraints in certain states in which we operate, we believe that the overall level of state financial aid for our students is likely to continue to decrease in the near term, but we cannot predict how significant any such reductions will be or how long they will last. Federal budgetary shortfalls and constraints, or decisions by federal lawmakers to limit or prohibit access by our institutions or their students to federal financial aid, could result in a decrease in the level of federal financial aid for our students.

In addition to Title IV and other government-administered programs, all of our schools participate in alternative loan programs for their students. Alternative loans fill the gap between what the student receives from all financial aid sources and what the student may need to cover the full cost of his or her education. Students or their parents can apply to a number of different lenders for this funding at current market interest rates.

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We also extend credit for tuition and fees to many of our students that attend our campuses.

Regulation of Federal Student Financial Aid Programs

To participate in Title IV Programs, an institution must be authorized to offer its programs by the relevant state education agencies in the state in which it is physically located, be accredited by an accrediting commission recognized by the DOE and be certified as eligible by the DOE. The DOE will certify an institution to participate in Title IV Programs only after reviewing and approving an institution's application to participate in the Title IV Programs. The DOE defines an institution to consist of both a main campus and its additional locations, if any. Under this definition, for DOE purposes, we had the following five institutions as of December 31, 2016, collectively consisting of five main campuses and 23 additional locations:

Main Institution/Campus(es)	Additional Location(s)
Iselin, NJ	Moorestown, NJ Paramus, NJ Philadelphia, PA (Center City) Philadelphia, PA (Northeast) Somerville, MA Lowell, MA Brockton, MA Lincoln, RI Marietta, GA West Palm Beach, FL Las Vegas, NV (Summerlin)
New Britain, CT	Shelton, CT Philadelphia, PA East Windsor, CT Melrose Park, IL Allentown, PA
Indianapolis, IN	Grand Prairie, TX Nashville, TN Denver, CO Union, NJ Mahwah, NJ Queens, NY South Plainfield, NJ

Columbia, MD

Southington, CT

Each institution must periodically apply to the DOE for continued certification to participate in Title IV Programs. The institution also must apply for recertification when it undergoes a change in ownership resulting in a change of control. The institution also may come under DOE review when it undergoes a substantive change that requires the submission of an application, such as opening an additional location or raising the highest academic credential it offers. All institutions are recertified on various dates for various amounts of time. The following table sets forth the expiration dates for each of our institutions' current Title IV Program participation agreements:

Institution	Expiration Date of Current Program Participation Agreement
Columbia, MD	September 30, 2017
Iselin, NJ	June 12, 2018 ¹
Indianapolis, IN	September 30, 2016 ^{1 2}
New Britain, CT	March 31, 2020
Southington, CT	June 30, 2017

¹Provisionally certified.

²Month-to-month certification during review process.

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The DOE typically provides provisional certification to an institution following a change in ownership resulting in a change of control and also may provisionally certify an institution for other reasons, including, but not limited to, noncompliance with certain standards of administrative capability and financial responsibility. Two of our five institutions (Iselin and Indianapolis) generate 71% of the Company's revenues are provisionally certified. Indianapolis is provisionally certified based on the existence of pending program reviews with DOE. Iselin is provisionally certified based on its accrediting agency's loss of DOE recognition. An institution that is provisionally certified receives fewer due process rights than those received by other institutions in the event the DOE takes certain adverse actions against the institution, is required to obtain prior DOE approvals of new campuses and educational programs, and may be subject to heightened scrutiny by the DOE. However, provisional certification does not otherwise limit an institution's access to Title IV Program funds. Our Iselin campus also is subject to additional conditions on its Title IV participation based on its accrediting agency's loss of DOE recognition.

The DOE is responsible for overseeing compliance with Title IV Program requirements. As a result, each of our schools is subject to detailed oversight and review, and must comply with a complex framework of laws and regulations. Because the DOE periodically revises its regulations and changes its interpretation of existing laws and regulations, we cannot predict with certainty how the Title IV Program requirements will be applied in all circumstances.

Significant factors relating to Title IV Programs that could adversely affect us include the following:

Congressional Action. Political and budgetary concerns significantly affect Title IV Programs. Congress periodically revises the Higher Education Act of 1965, as amended ("HEA") and other laws governing Title IV Programs. Congress is currently considering reauthorization of Title IV Programs, but it is unknown when Congress will complete that process or what changes will be made to the HEA or other laws affecting federal student aid.

In addition, Congress reviews and determines federal appropriations for Title IV Programs on an annual basis. Congress can also make changes in the laws affecting Title IV Programs in the annual appropriations bills and in other laws it enacts between the HEA reauthorizations. Because a significant percentage of our revenues are derived from Title IV Programs, any action by Congress or the DOE that significantly reduces Title IV Program funding, that limits or restricts the ability of our schools, programs, or students to receive funding through the Title IV Programs, or that imposes new restrictions or constraints upon our business or operations could reduce our student enrollment and our revenues, and could increase our administrative costs and require us to modify our practices in order for our schools to comply fully with Title IV Program requirements.

In addition, current requirements for student or school participation in Title IV Programs may change or one or more of the present Title IV Programs could be replaced by other programs with materially different student or school eligibility requirements. If we cannot comply with the provisions of the HEA, as they may be amended, or if the cost of such compliance is excessive, or if funding is materially reduced, our revenues or profit margin could be materially adversely affected.

Gainful Employment. In October 2014, the DOE issued final gainful employment regulations requiring each educational program offered by our institutions to achieve threshold rates in at least one of two debt measure categories related to an annual debt to annual earnings ratio and an annual debt to discretionary income ratio. The various formulas are calculated under complex methodologies and definitions outlined in the final regulations and, in some cases, are based on data that may not be readily accessible to institutions, such as income information compiled by the Social Security Administration. The regulations outline various scenarios under which programs could lose Title IV eligibility for failure to achieve threshold rates in one or more measures over certain periods of time ranging from two to four years. The regulations also require an institution to provide warnings to students in programs which may lose Title IV eligibility at the end of an award year. The final regulations also contain other provisions that, among other things, include disclosure, reporting, new program approval, and certification requirements. The

certification requirements require each institution to certify to the DOE, among other things, that each gainful employment program is programmatically accredited, if such accreditation is required by a Federal governmental entity or by governmental entity in the state in which the institution is physically located.

The final regulations had a general effective date of July 1, 2015. In January 2017, the DOE issued the first set of gainful employment rates for each of our programs for the 2015 debt measure year. Sixty of our programs achieved passing rates, 13 of our programs had rates that are in a category called the “zone,” and five of our programs had failing rates. Our programs with rates in the zone are not subject to loss of Title IV eligibility unless they accumulate a combination of zone and failing rates for four consecutive years (or failing rates for two out of any three consecutive years). We are in the process of appealing to the DOE one of the five programs that failed; teaching out one of the programs that failed; and the remaining three failing programs are from schools that have closed or are closing. Each of our programs with failing rates will lose its Title IV eligibility if it receives a failing gainful employment rate for either of the 2016 or 2017 debt measure years. The gainful employment rates for the 2016 debt measure year are expected to be issued in late 2017. If, in fact, we lost the appeal to the DOE the applicable school would need to notify its current and future students that it may lose Title IV eligibility. Moreover, the potential for one or more of these programs to lose their Title IV eligibility could trigger a requirement to submit a letter of credit or other financial protection to the DOE under the new Borrower Defense to Repayment Regulations that take effect on July 1, 2017. On March 6, 2017, the DOE published information in the form of an electronic announcement that provides additional time for institutions to appeal a zone or failing rate and to update disclosures for all gainful employment programs. The new deadline established by the DOE is now July 1, 2017, for appeals and disclosures. See “Financial Responsibility Standards.”

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Borrower Defense to Repayment Regulations. In January 2016, the DOE began negotiated rulemaking to develop proposed regulations regarding, among other things, a borrower's ability to allege acts or omissions by an institution as a defense to the repayment of certain Title IV loans and the consequences to the borrower, the DOE, and the institution. On November 1, 2016, the DOE published in the Federal Register the final version of these regulations with a general effective date of July 1, 2017 and which, among other things, include rules for:

- establishing new processes, and updating existing processes, for enabling borrowers to obtain from the DOE a discharge of some or all of their federal student loans based on circumstances such as certain acts or omissions of the institution and for the DOE to impose and collect liabilities against the institution following the loan discharges;
- establishing expanded standards of financial responsibility (see "Regulatory Environment – Financial Responsibility Standards");
- requiring institutions to make disclosures to current and prospective students regarding the existence of certain of the circumstances identified in the expanded standards of financial responsibility;
- calculating a loan repayment rate for each proprietary institution under standards established by the regulations and
- requiring institutions to provide warnings to current and prospective students if the institution has a loan repayment rate below specified thresholds;
- prohibiting certain contractual provisions imposed by or on behalf of schools on students regarding arbitration, dispute resolution, and participation in class actions; and
- expanding the existing definition of misrepresentations that could result in grounds for discharge of student loans and in liabilities and sanctions against the institution, including, without limitation, potential loss of Title IV eligibility.

On January 19, 2017, the DOE issued new regulations with an effective date of January 19, 2017 that update the Department's hearing procedures for actions to establish liability against an institution and to establish procedural rules governing recovery proceedings under the DOE's borrower defense to repayment regulations. We are still in the process of evaluating the impact of these new and complex regulations on our business. Among other things, the precise standards for student loan discharges are unclear and may be subject to unfavorable interpretations that could result in liabilities and other sanctions for our schools.

The "90/10 Rule." Under the HEA, a proprietary institution that derives more than 90% of its total revenue from Title IV Programs (its "90/10 Rule percentage") for two consecutive fiscal years becomes immediately ineligible to participate in Title IV Programs and may not reapply for eligibility until the end of at least two fiscal years. An institution with revenues exceeding 90% for a single fiscal year will be placed on provisional certification and may be subject to other enforcement measures. If an institution violated the 90/10 Rule and became ineligible to participate in Title IV Programs but continued to disburse Title IV Program funds, the DOE would require the institution to repay all Title IV Program funds received by the institution after the effective date of the loss of eligibility.

We have calculated that, for our 2016 fiscal year, our institutions' 90/10 Rule percentages ranged from 55% to 84%. For 2015 and 2014, none of our existing institutions derived more than 90% of their revenues from Title IV Programs. Our calculations are subject to review by the DOE.

If Congress or the DOE were to amend the 90/10 Rule to treat other forms of federal financial aid as Title IV revenue for 90/10 Rule purposes, lower the 90% threshold, or otherwise change the calculation methodology (each of which has been proposed by some Congressional members in proposed legislation), or make other changes to the 90/10 Rule, those changes could make it more difficult for our institutions to comply with the 90/10 Rule. If any of our institutions loses eligibility to participate in Title IV Programs, that loss would have a significant impact on the rate at which our students enroll in our programs and on our business and results of operations.

Student Loan Defaults. The HEA limits participation in Title IV Programs by institutions whose former students defaulted on the repayment of federally guaranteed or funded student loans above a prescribed rate (the "cohort default rate"). The DOE calculates these rates based on the number of students who have defaulted, not the dollar amount of

such defaults. The cohort default rate is calculated on a federal fiscal year basis and measures the percentage of students who enter repayment of a loan during the federal fiscal year and default on the loan on or before the end of the federal fiscal year or the subsequent two federal fiscal years.

Under the HEA, an institution whose Federal Family Education Loan, or FFEL, and Federal Direct Loan, or FDL, cohort default rate is 30% or greater for three consecutive federal fiscal years loses eligibility to participate in the FFEL, FDL, and Pell programs for the remainder of the federal fiscal year in which the DOE determines that such institution has lost its eligibility and for the two subsequent federal fiscal years. An institution whose FFEL and FDL cohort default rate for any single federal fiscal year exceeds 40% loses its eligibility to participate in the FFEL and FDL programs for the remainder of the federal fiscal year in which the DOE determines that such institution has lost its eligibility and for the two subsequent federal fiscal years. If an institution's three-year cohort default rate equals or exceeds 30% in two of the three most recent federal fiscal years for which the DOE has issued cohort default rates, the institution may be placed on provisional certification status and, under new regulations that take effect on July 1, 2017, could be required to submit a letter of credit to the DOE.

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In September 2016, the DOE released the final cohort default rates for the 2013 federal fiscal year. These are the most recent final rates published by the DOE. The rates for our existing institutions for the 2013 federal fiscal year range from 10.5% to 15.4%. None of our institutions had a cohort default rate equal to or greater than 30% for the 2013 federal fiscal year.

In February 2016, the DOE released draft three-year cohort default rates for the 2014 federal fiscal year. The draft cohort default rates are subject to change pending receipt of the final cohort default rates, which the DOE is expected to publish in September 2017. The draft rates for our institutions for the 2014 federal fiscal year range from 5.2% to 13.6%. None of our institutions had draft cohort default rates of 30% or more.

Financial Responsibility Standards.

All institutions participating in Title IV Programs must satisfy specific standards of financial responsibility. The DOE evaluates institutions for compliance with these standards each year, based on the institution's annual audited financial statements, as well as following a change in ownership resulting in a change of control of the institution.

The most significant financial responsibility measurement is the institution's composite score, which is calculated by the DOE based on three ratios:

- The equity ratio, which measures the institution's capital resources, ability to borrow and financial viability;
- The primary reserve ratio, which measures the institution's ability to support current operations from expendable resources; and
- The net income ratio, which measures the institution's ability to operate at a profit.

The DOE assigns a strength factor to the results of each of these ratios on a scale from negative 1.0 to positive 3.0, with negative 1.0 reflecting financial weakness and positive 3.0 reflecting financial strength. The DOE then assigns a weighting percentage to each ratio and adds the weighted scores for the three ratios together to produce a composite score for the institution. The composite score must be at least 1.5 for the institution to be deemed financially responsible without the need for further oversight.

If an institution's composite score is below 1.5, but is at least 1.0, it is in a category denominated by the DOE as "the zone." Under the DOE regulations, institutions that are in the zone typically may be permitted by the DOE to continue to participate in the Title IV Programs by choosing one of two alternatives: 1) the "Zone Alternative" under which an institution is required to make disbursements to students under the Heightened Cash Monitoring 1 (HCM1) payment method and to notify the DOE within 10 days after the occurrence of certain oversight and financial events or 2) submit a letter of credit to the DOE equal to 50 percent of the Title IV Program funds received by the institution during its most recent fiscal year. The DOE permits an institution to participate under the "Zone Alternative" for a period of up to three consecutive fiscal years. Under the HCM1 payment method, the institution is required to make Title IV disbursements to eligible students and parents before it requests or receives funds for the amount of those disbursements from the DOE. As long as the student accounts are credited before the funding requests are initiated, an institution is permitted to draw down funds through the DOE's electronic system for grants management and payments for the amount of disbursements made to eligible students. Unlike the HCM2 and reimbursement payment methods, the HCM1 payment method typically does not require schools to submit documentation to the DOE and wait for DOE approval before drawing down Title IV Program funds. Effective July 1, 2016, a school under HCM1, HCM2 or reimbursement payment methods must also pay any credit balances due to a student before drawing down funds for the amount of those disbursements from the DOE, even if the student or parent provides written authorization for the school to hold the credit balance.

If an institution's composite score is below 1.0, the institution is considered by the DOE to lack financial responsibility. If the DOE determines that an institution does not satisfy the DOE's financial responsibility standards,

depending on its composite score and other factors, that institution may establish its financial responsibility on an alternative basis by, among other things:

Posting a letter of credit in an amount equal to at least 50% of the total Title IV Program funds received by the institution during the institution's most recently completed fiscal year;

Posting a letter of credit in an amount equal to at least 10% of such prior year's Title IV Program funds, accepting provisional certification, complying with additional DOE monitoring requirements and agreeing to receive Title IV Program funds under an arrangement other than the DOE's standard advance funding arrangement

The DOE has evaluated the financial responsibility of our institutions on a consolidated basis. We have submitted to the DOE our audited financial statements for the 2015 and 2014 fiscal year reflecting a composite score of 1.9 and 1.3, respectively, based upon our calculations. The DOE reviewed our 2015 composite score and concluded that we were no longer required to operate under the Zone Alternative requirements that we had operated under following the DOE's review of our 2014 composite score.

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For the 2016 fiscal year, we have calculated our composite score to be 1.5. This number is subject to determination by the DOE once it receives and reviews our audited financial statements for the 2016 fiscal year.

On November 1, 2016, the DOE published new regulations that establish expanded standards of financial responsibility that could result in a requirement that we submit to DOE a substantial letter of credit or other form of financial protection in an amount determined by the DOE, and be subject to other conditions and requirements, based on any one of an extensive list of triggering circumstances. The expanded financial responsibility regulations may result in the DOE recalculating and reducing our composite score to account for DOE estimates of potential losses under some of the circumstances listed above and also may result in requirements to provide financial protection in amounts that are difficult to predict, calculated by the DOE under potentially subjective standards, and, in some cases, may be based solely on the existence of proceedings or circumstances that ultimately may lack merit or otherwise not result in liabilities or losses. For example, the regulations state that the letter of credit or other form of financial protection required for an institution under the provisional certification alternative must equal 10 percent of the total amount of Title IV funds received by the institution during its most recently completed fiscal year plus any additional amount that DOE determines is necessary to fully cover any estimated losses unless the institution demonstrates that the additional amount is unnecessary to protect, or is contrary to, the Federal interest.

Return of Title IV Funds. An institution participating in Title IV Programs must calculate the amount of unearned Title IV Program funds that have been disbursed to students who withdraw from their educational programs before completing them, and must return those unearned funds to the DOE or the applicable lending institution in a timely manner, which is generally within 45 days from the date the institution determines that the student has withdrawn.

If an institution is cited in an audit or program review for returning Title IV Program funds late for 5% or more of the students in the audit or program review sample, the institution may be required to post a letter of credit in favor of the DOE in an amount equal to 25% of the total amount of Title IV Program funds that should have been returned for students who withdrew in the institution's previous fiscal year. None of our institutions are currently required to submit a letter of credit to the DOE based on late return of Title IV Program funds.

School Acquisitions. When a company acquires a school that is eligible to participate in Title IV Programs, that school undergoes a change of ownership resulting in a change of control as defined by the DOE. Upon such a change of control, a school's eligibility to participate in Title IV Programs is generally suspended until it has applied for recertification by the DOE as an eligible school under its new ownership, which requires that the school also re-establish its state authorization and accreditation. The DOE may temporarily and provisionally certify an institution seeking approval of a change of control under certain circumstances while the DOE reviews the institution's application. The time required for the DOE to act on such an application may vary substantially. DOE recertification of an institution following a change of control will be on a provisional basis. Thus, any plans to expand our business through acquisition of additional schools and have them certified by the DOE to participate in Title IV Programs must take into account the approval requirements of the DOE and the relevant state education agencies and accrediting commissions.

Change of Control. In addition to school acquisitions, other types of transactions can also cause a change of control. The DOE, most state education agencies and our accrediting commissions have standards pertaining to the change of control of schools, but these standards are not uniform. DOE regulations describe some transactions that constitute a change of control, including the transfer of a controlling interest in the voting stock of an institution or the institution's parent corporation. For a publicly traded corporation, DOE regulations provide that a change of control occurs in one of two ways: (a) if a person acquires ownership and control of the corporation so that the corporation is required to file a Current Report on Form 8-K with the Securities and Exchange Commission disclosing the change of control or (b) if the corporation has a shareholder that owns at least 25% of the total outstanding voting stock of the corporation and is the largest shareholder of the corporation, and that shareholder ceases to own at least 25% of such stock or ceases to be the largest shareholder. These standards are subject to interpretation by the DOE. A significant purchase or

disposition of our common stock could be determined by the DOE to be a change of control under this standard.

Most of the states and our accrediting commissions include the sale of a controlling interest of common stock in the definition of a change of control although some agencies could determine that the sale or disposition of a smaller interest would result in a change of control. A change of control under the definition of one of these agencies would require the affected school to reaffirm its state authorization or accreditation. Some agencies would require approval prior to a sale or disposition that would result in a change of control in order to maintain authorization or accreditation. The requirements to obtain such reaffirmation from the states and our accrediting commissions vary widely.

A change of control could occur as a result of future transactions in which our Compan