ITT EDUCATIONAL SERVICES INC
Form 10-Q/A
March 14, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Amendment No. 1)

(Mark One)

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

For the quarterly period ended June 30, 2015

OR

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

For the transition period from __________ to __________

Commission file number 1-13144

ITT EDUCATIONAL SERVICES, INC.

(Exact name of registrant as specified in its charter)

Delaware	**36-2061311**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
13000 North Meridian Street Carmel, Indiana	**46032-1404**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (317) 706-9200

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 x No ¨

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

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. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

23,578,109

Number of shares of Common Stock, $.01 par value, outstanding at June 30, 2015

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EXPLANATORY NOTE

Restatement of Condensed Consolidated Financial Statements

ITT Educational Services, Inc. (we, us or our) is filing this Amendment No. 1 (Amended Filing) to its Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, originally filed with the United States Securities and Exchange Commission (SEC) on July 31, 2015 (the Original Filing), to amend and restate its unaudited condensed consolidated financial statements and related disclosures for the three and six months ended June 30, 2015.

As a result of the execution of enhanced internal controls over financial reporting that were implemented as part of the remediation of material weaknesses identified in a prior period, we determined there was an error in the application of the interest method used to calculate the interest rate used in accounting for the accretion of the debt discount associated with a senior debt arrangement (the PEAKS Senior Debt) that resulted in the misstatement of interest expense in previously reported interim periods.

Within this Amended Filing, we are restating our previously issued condensed consolidated financial statements as of and for the three and six months ended June 30, 2015 to reflect this adjustment to the interest rate used in the application of the interest method to the discount on the PEAKS Senior Debt in that period.

The effects of the restatement on our unaudited condensed consolidated financial statements are a reduction in the amount of the debt discount and an increase in the carrying value of the PEAKS Senior Debt. The change in accretion in the three and six months ended June 30, 2015 was not materially different from the amount previously recorded. The restatement does not increase the total amount of non-cash interest expense that will be reported from the accretion of the debt discount on the PEAKS Senior Debt, but instead changes the timing of the recognition of that interest expense through the maturity date. The restatement also has no effect on our cash and cash equivalents or liquidity; cash flows from operating activities, financing activities or investing activities; or projections of our future cash payment obligations under our private education loan program guarantees.

In this Amended Filing, we are restating:

- our Condensed Consolidated Balance Sheet as of June 30, 2015 (unaudited);
- our Condensed Consolidated Statements of Shareholders Equity for the six months ended June 30, 2015 (unaudited); and
- the Notes to those condensed consolidated financial statements.

See Note 2 Restatement of Previously Issued Financial Statements of the Notes to Condensed Consolidated Financial Statements for additional information. Our previously restated condensed consolidated financial statements as of and for the three and six months ended June 30, 2014 included in this Amended Filing also reflect the correction of this error. A reconciliation of those previously reported amounts to the restated amounts is set forth in our Quarterly Report on Form 10-Q/A (Amendment No. 1) for the quarterly period ended June 30, 2014 filed with the SEC on the date hereof.

In connection with the filing of our Annual Report on Form 10-K for the year ended December 31, 2014, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective as a result of material weaknesses in our internal control over financial reporting.

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For ease of reference, this Amended Filing amends and restates the Original Filing in its entirety. The following Items have been revised to reflect the impact of the restatement on the affected line items of our condensed consolidated financial statements:

- Part I, Item 1 Financial Statements
- Part I, Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations
- Part II, Item 6 Exhibits

We have also updated the signature page, the certifications of our Chief Executive Officer and Chief Financial Officer in Exhibits 31.1, 31.2, 32.1 and 32.2, and our unaudited consolidated financial statements formatted in eXtensible Business Reporting Language (XBRL) in Exhibit 101. In addition, we have revised certain other Items in this Amended Filing solely to change cross-references to the numbers of the notes to our condensed consolidated financial statements resulting from a renumbering of the notes to add a note regarding the restatement.

Except as provided in this Explanatory Note, or as indicated in the applicable disclosure, this Amended Filing has not been updated to reflect other events occurring after the filing of the Original Filing and does not modify or update information and disclosures in the Original Filing affected by subsequent events. Accordingly, this Amended Filing should be read in conjunction with our filings with the SEC subsequent to the date on which we filed the Original Filing, together with any amendments to those filings.

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ITT EDUCATIONAL SERVICES, INC.

Carmel, Indiana

Quarterly Report to Securities and Exchange Commission

June 30, 2015

PART I

FINANCIAL INFORMATION

Item 1. Financial Statements.

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ITT EDUCATIONAL SERVICES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)

(unaudited)

	As of		
	June 30, 2015 (as restated, see Note 2)	December 31, 2014	June 30, 2014
Assets			
Current assets:			
Cash and cash equivalents	$ 124,632	$ 135,937	$ 224,956
Restricted cash	6,936	6,040	2,768
Accounts receivable, net	45,204	46,383	68,937
Private education loans, net	9,379	10,584	7,420
Deferred income taxes	24,795	34,547	67,415
Prepaid expenses and other current assets	57,294	57,923	36,056
Total current assets	268,240	291,414	407,552
Property and equipment, net	150,095	157,072	158,947
Private education loans, excluding current portion, net	69,724	80,292	65,997
Deferred income taxes	67,125	71,719	80,486
Collateral deposits	97,873	97,932	8,627
Other assets	61,921	54,409	56,878
Total assets	$ 714,978	$ 752,838	$ 778,487
Liabilities and Shareholders Equity			
Current liabilities:			
Current portion of long-term debt	$ 14,546	$ 9,635	$ 50,000
Current portion of PEAKS Trust senior debt	23,068	37,545	132,429
Current portion of CUSO secured borrowing obligation	19,750	20,813	0
Accounts payable	76,476	67,848	75,918
Accrued compensation and benefits	16,535	12,264	23,320
Other current liabilities	27,391	27,153	46,049
Deferred revenue	119,568	147,475	131,378
Total current liabilities	297,334	322,733	459,094
Long-term debt, excluding current portion	77,579	86,714	0
PEAKS Trust senior debt, excluding current portion	40,515	48,166	64,301
CUSO secured borrowing obligation, excluding current portion	91,339	100,194	0

Other liabilities	59,049	52,959	138,361
Total liabilities	565,816	610,766	661,756
Commitments and contingent liabilities (see Note 13)			
Shareholders equity:			
Preferred stock, $.01 par value, 5,000,000 shares authorized, none issued	0	0	0
Common stock, $.01 par value, 300,000,000 shares authorized, 37,068,904 issued	371	371	371
Capital surplus	186,501	198,883	198,806
Retained earnings	974,900	963,737	941,024
Accumulated other comprehensive income	725	1,201	2,670
Treasury stock, 13,490,795, 13,619,010 and 13,665,129 shares, at cost	(1,013,335)	(1,022,120)	(1,026,140)
Total shareholders equity	149,162	142,072	116,731
Total liabilities and shareholders equity	$ 714,978	$ 752,838	$ 778,487

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

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ITT EDUCATIONAL SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands, except per share data)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Revenue	$ 214,231	$ 238,096	$ 444,206	$ 476,019
Costs and expenses:				
Cost of educational services	101,865	116,276	205,418	236,391
Student services and administrative expenses	91,408	97,547	181,660	196,785
Legal and professional fees related to certain lawsuits, investigations and accounting matters	6,005	8,380	13,291	13,927
Provision for private education loan losses	3,313	9,071	4,557	9,071
Total costs and expenses	202,591	231,274	404,926	456,174
Operating income	11,640	6,822	39,280	19,845
Interest income	22	15	35	34
Interest (expense)	(9,991)	(7,211)	(20,379)	(19,023)
Income (loss) before provision for income taxes	1,671	(374)	18,936	856
Provision (benefit) for income taxes	955	(222)	7,773	249
Net income (loss)	$ 716	$ (152)	$ 11,163	$ 607
Earnings (loss) per share:				
Basic	$ 0.03	$ (0.01)	$ 0.47	$ 0.03
Diluted	$ 0.03	$ (0.01)	$ 0.47	$ 0.03
Weighted average shares outstanding:				
Basic	23,621	23,459	23,591	23,453
Diluted	24,086	23,459	23,953	23,651

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

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ITT EDUCATIONAL SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Net income (loss)	$ 716	$ (152)	$ 11,163	$ 607
Other comprehensive (loss), net of tax:				
Net actuarial pension loss amortization, net of income tax of $0, $0, $0 and $0	0	0	1	0
Prior service cost (credit) amortization, net of income tax of $151, $150, $301 and $301	(238)	(238)	(477)	(476)
Other comprehensive (loss), net of tax	(238)	(238)	(476)	(476)
Comprehensive income (loss)	$ 478	$ (390)	$ 10,687	$ 131

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

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ITT EDUCATIONAL SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(unaudited)

	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Cash flows from operating activities:				
Net income (loss)	$ 716	$ (152)	$ 11,163	$ 607
Adjustments to reconcile net income (loss) to net cash flows from operating activities:				
Depreciation and amortization	6,061	6,508	12,042	12,970
Provision for doubtful accounts	8,692	13,767	20,875	30,382
Deferred income taxes	2,554	(1,961)	12,423	(4,278)
Stock-based compensation expense	1,364	2,311	3,260	4,862
Accretion of discount on private education loans	(2,948)	(3,239)	(6,029)	(6,372)
Accretion of discount on long-term debt	385	0	776	0
Accretion of discount on PEAKS Trust senior debt	1,365	2,389	3,020	8,841
Accretion of discount on CUSO secured borrowing obligation	214	0	433	0
Provision for private education loan losses	3,313	9,071	4,557	9,071
Other	(148)	(248)	(415)	(428)
Changes in operating assets and liabilities, net of acquisition:				
Restricted cash	(608)	1,525	(896)	2,868
Accounts receivable	(7,696)	(5,320)	(19,696)	982
Private education loans	6,601	4,083	13,245	8,093
Accounts payable	848	8,582	6,390	17,897
Other operating assets and liabilities	(1,931)	(5,582)	(1,214)	(9,614)
Deferred revenue	(20,288)	(10,171)	(27,907)	(17,400)
Net cash flows from operating activities	(1,506)	21,563	32,027	58,481
Cash flows from investing activities:				
Capital expenditures, net	(1,640)	(1,147)	(2,509)	(2,657)
Acquisition of company	0	(584)	0	(5,033)
Collateralization of letters of credit	60	0	60	0
Proceeds from repayment of notes	0	97	0	193
Purchases of investments	(1)	(1)	(1)	(1)
Net cash flows from investing activities	(1,581)	(1,635)	(2,450)	(7,498)
Cash flows from financing activities:				
Repayment of long-term debt	(2,500)	0	(5,000)	0

Repayment of PEAKS Trust senior debt	(9,380)	0	(25,026)	(41,070)
Repayment of CUSO secured borrowing obligation	(6,314)	0	(10,351)	0
Common shares tendered for taxes	(38)	(7)	(505)	(728)
Net cash flows from financing activities	(18,232)	(7)	(40,882)	(41,798)
Net change in cash and cash equivalents	(21,319)	19,921	(11,305)	9,185
Cash and cash equivalents at beginning of period	145,951	205,035	135,937	215,771
Cash and cash equivalents at end of period	$ 124,632	$ 224,956	$ 124,632	$ 224,956

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

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ITT EDUCATIONAL SERVICES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(Dollars and shares in thousands)

(unaudited)

	Common Stock Shares	Common Stock Amount	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Common Stock in Treasury Shares	Common Stock in Treasury Amount	Total
Balance as of December 31, 2013	37,069	$ 371	$ 200,040	$ 940,449	$ 3,146	(13,699)	$ (1,028,360)	$ 115,646
For the six months ended June 30, 2014:								
Net income				607				607
Other comprehensive (loss), net of income tax					(476)			(476)
Equity award vesting			(2,878)			52	2,878	0
Tax benefit from equity awards			(3,218)					(3,218)
Stock-based compensation			4,862					4,862
Shares tendered for taxes						(19)	(728)	(728)
Issuance of shares for Director s compensation				(32)		1	70	38
Balance as of June 30, 2014	37,069	371	198,806	941,024	2,670	(13,665)	(1,026,140)	116,731
For the six months ended December 31, 2014:								
Net income				22,713				22,713
Other comprehensive (loss), net of income tax					(1,469)			(1,469)
Equity award vesting			(4,206)			69	4,206	0
Tax benefit from equity awards			(1,191)					(1,191)
Stock-based compensation			5,474					5,474
						(23)	(186)	(186)

Shares tendered for taxes								
Balance as of December 31, 2014	37,069	371	198,883	963,737	1,201	(13,619)	(1,022,120)	142,072
For the six months ended June 30, 2015:								
Net income				11,163				11,163
Other comprehensive (loss), net of income tax					(476)			(476)
Equity award vesting			(9,290)			198	9,290	0
Tax benefit from equity awards			(6,352)					(6,352)
Stock-based compensation			3,260					3,260
Shares tendered for taxes						(70)	(505)	(505)
Balance as of June 30, 2015 (as restated, see Note 2)	37,069	$ 371	$ 186,501	$ 974,900	$ 725	(13,491)	$ (1,013,335)	$ 149,162

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ITT EDUCATIONAL SERVICES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(As Restated)

June 30, 2015

(Dollars in thousands, except per share data and unless otherwise stated)

1. The Company and Basis of Presentation

ITT Educational Services, Inc. is a leading proprietary provider of postsecondary degree programs in the United States based on revenue and student enrollment. References in these Notes to we, us and our refer to ITT Educational Services, Inc., its wholly-owned subsidiaries and the variable interest entities (VIEs) that it consolidates, unless the context requires or indicates otherwise. As of June 30, 2015, we were offering:

- master, bachelor and associate degree programs to approximately 47,000 students at ITT Technical Institute and Daniel Webster College locations; and

- short-term information technology and business learning solutions for career advancers and other professionals through the Center for Professional Development @ ITT Technical Institute (the CPD).

In addition, we offered one or more of our online degree programs to students who are located in 50 states. As of June 30, 2015, we had 141 college locations in 39 states. All of our college locations are authorized by the applicable education authorities of the states in which they operate and are accredited by an accrediting commission recognized by the U.S. Department of Education (ED). We have provided career-oriented education programs since 1969 under the ITT Technical Institute name and since 2009 under the Daniel Webster College name. In January 2014, we acquired certain assets and assumed certain liabilities of CompetenC Solutions, Inc. and Great Equalizer, Inc. CompetenC Solutions, Inc. and Great Equalizer, Inc. were education companies that operated primarily under the name of Ascolta (Ascolta) and offered short-term information technology and business learning solutions for career advancers and other professionals. See Note 4 Acquisition, for additional discussion of the acquisition of the Ascolta business. Our corporate headquarters are located in Carmel, Indiana.

The accompanying unaudited condensed consolidated financial statements include the accounts of ITT Educational Services, Inc., its wholly-owned subsidiaries and, beginning on February 28, 2013 and September 30, 2014, two VIEs that we consolidate in our consolidated financial statements, and have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) for interim periods and pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC). Certain information and footnote disclosures, including significant accounting policies, normally included in a complete presentation of financial statements prepared in accordance with those principles, rules and regulations have been omitted. All significant intercompany balances and transactions are eliminated upon consolidation. We reclassified certain amounts that were previously reported in Other assets on our Condensed Consolidated Balance Sheet as of June 30, 2014 to the line item Collateral deposits to conform to the current year presentation. We also reclassified amounts that were previously reported in Facility expenditures in our Condensed Consolidated Statements of Cash Flows for the three and six months ended

June 30, 2014 to the line item Capital Expenditures, net to conform to the current year presentation. These reclassifications had no impact on previously reported net income, total shareholders equity or cash flows.

The Condensed Consolidated Balance Sheet as of December 31, 2014 was derived from audited financial statements but, as presented in this report, may not include all disclosures required by GAAP. We review the operations of our business on a regular basis to determine our reportable operating segments, as defined in Accounting Standards Codification (ASC or Codification) 280, Segment Reporting. As of June 30, 2015, we reported our financial results under one reportable operating segment.

In the opinion of our management, the condensed consolidated financial statements reflect all adjustments that are normal, recurring and necessary for a fair presentation of our financial condition and results of operations. The interim financial information should be read in conjunction with the audited consolidated financial statements and notes thereto contained in our Annual Report on Form 10-K as filed with the SEC for the fiscal year ended December 31, 2014 (2014 Form 10-K).

2. Restatement of Previously Issued Financial Statements

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Subsequent to the Original Filing, we determined there was an error in the application of the interest method used to calculate the interest rate used in accounting for the accretion of the debt discount associated with our PEAKS Senior Debt. In our Original Filing, we accreted the debt discount associated with the PEAKS Senior Debt using the interest method based on the amounts and timing of the repayments that we estimated at the time that the PEAKS Senior Debt was initially included in our consolidated financial statements. We subsequently determined that the interest method should take into consideration actual repayments and updated projections for future repayments on the PEAKS Senior Debt to determine the interest rate used to calculate the amount of the debt discount recognized as interest expense in each period.

As a result, we have restated the previously-issued unaudited condensed consolidated financial statements in our Quarterly Reports on Form 10-Q for each of the fiscal quarters ended March 31, 2014, June 30, 2014, September 30, 2014, March 31, 2015, June 30, 2015 and September 30, 2015, and our audited consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2014, and that those previously-issued financial statements should no longer be relied upon.

Our restated condensed consolidated financial statements as of and for the three and six months ended June 30, 2015 included in this Amended Filing reflect the correction of this error. A reconciliation of previously reported amounts to the restated amounts is set forth in the tables below.

The following table sets forth the effect of the restatement on the affected line items on our Condensed Consolidated Balance Sheet as of June 30, 2015:

	As of June 30, 2015		
	As Previously Reported	**Interest Method Adjustment**	**As Restated**
Condensed Consolidated Balance Sheet Data:			
Deferred income taxes	$ 63,447	$ 3,678	$ 67,125
Total assets	711,300	3,678	714,978
Other current liabilities	27,288	103	27,391
Total current liabilities	297,231	103	297,334
PEAKS Trust senior debt, excluding current portion	31,007	9,508	40,515
Total liabilities	556,205	9,611	565,816
Retained earnings	980,833	(5,933)	974,900
Total shareholders equity	155,095	(5,933)	149,162
Total liabilities and shareholders equity	711,300	3,678	714,978

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The following table sets forth the effect of the restatement on the affected line items in our Condensed Consolidated Statement of Shareholders Equity for the six months ended June 30, 2015:

	Six Months Ended June 30, 2015		
	As Previously Reported	Interest Method Adjustment	As Restated
Condensed Consolidated Statement of Shareholders Equity Data Retained Earnings:			
Net income	$ 11,163	$ 0	$ 11,163
Balance as of June 30, 2015	980,833	(5,933)	974,900

The change in accretion in the three and six months ended June 30, 2015 was not materially different from the amount previously recorded.

3. New Accounting Guidance

In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2015-03, Simplifying the Presentation of Debt Issuance Costs, which is included in the Codification under ASC 835, Interest (ASC 835). This guidance requires that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the carrying amount of that liability. This guidance will be effective for our interim and annual reporting periods beginning January 1, 2016, with early adoption permitted. We are assessing the impact that this guidance may have on our consolidated financial statements.

In February 2015, the FASB issued ASU No. 2015-02, Amendment to the Consolidation Analysis (ASU 2015-02), which is included in the Codification under ASC 810, Consolidation (ASC 810). This guidance changes the analysis that an entity must perform to determine whether it should consolidate certain types of legal entities. This guidance will be effective for our interim and annual reporting periods beginning January 1, 2016, with early adoption permitted. We do not expect the adoption of ASU 2015-02 to have a material impact on our consolidated financial statements.

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In January 2015, the FASB issued ASU No. 2015-01, Income Statement Extraordinary and Unusual Items (ASU 2015-01), which is included in the Codification under ASC 225, Income Statement (ASC 225). This guidance eliminates the concept of extraordinary items from GAAP. This guidance will be effective for our interim and annual reporting periods beginning January 1, 2016, with early adoption permitted. We do not expect the adoption of ASU 2015-01 to have a material impact on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements Going Concern (ASU 2014-15), which is included in the Codification under ASC 205, Presentation of Financial Statements (ASC 205). This guidance was issued to define management s responsibility to evaluate whether there is substantial doubt about an entity s ability to continue as a going concern and to provide related footnote disclosure in certain circumstances. Under the new guidance, management is required to evaluate, at each annual and interim reporting period, whether there are conditions or events that raise substantial doubt about the entity s ability to continue as a going concern within one year after the date the financial statements are issued and to provide related disclosures. The guidance will be effective for our interim and annual reporting periods beginning January 1, 2017, with early adoption permitted. We are assessing the impact that this guidance may have on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which is included in the Codification under ASC 606, Revenue Recognition (ASC 606). This guidance requires the recognition of revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration expected in exchange for those goods or services. Originally, this guidance was to become effective for our interim and annual reporting periods beginning January 1, 2017. In July 2015, the FASB voted to approve a one-year deferral of the effective date. Therefore, this guidance will become effective for our interim and annual reporting periods beginning January 1, 2018. Early adoption is permitted, but not any earlier than the original effective date. We are assessing the impact that this guidance may have on our consolidated financial statements.

In April 2014, the FASB issued ASU No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity (ASU 2014-08), which is included in the Codification under ASC 205, Presentation of Financial Statements (ASC 205). This update changes the requirements for reporting discontinued operations and clarifies when disposals of groups of assets qualify for a discontinued operations presentation under ASC 205. This guidance became effective for our interim and annual reporting periods beginning January 1, 2015. The adoption of ASU 2014-08 did not have a material impact on our consolidated financial statements.

4. Acquisition

On January 31, 2014, we acquired certain assets and assumed certain liabilities of CompetenC Solutions, Inc. and Great Equalizer, Inc. for approximately $5,220, of which $5,033 was paid in the six months ended June 30, 2014 and the remaining $187 was paid by October 31, 2014. CompetenC Solutions, Inc. and Great Equalizer, Inc. were education companies that operated primarily under the name of Ascolta and offered short-term information technology and business learning solutions for career advancers and other professionals. The acquisition of the Ascolta business allowed us to expand our offerings in the short-term learning solutions market by integrating the Ascolta operations into the CPD.

Our condensed consolidated financial statements include the results of the Ascolta business beginning as of the acquisition date. The revenue and expenses of the Ascolta business included in our Condensed Consolidated Statements of Income for the three and six months ended June 30, 2015 and 2014 were not significant. Our revenue, net income and earnings per share would not have been significantly affected, if the revenue and expenses of the Ascolta business were presented for the three and six months ended June 30, 2014 as if the transaction had occurred at the beginning of the earliest period presented. The costs incurred to acquire the Ascolta business were expensed and were not significant.

We accounted for the acquisition of the Ascolta business in accordance with ASC 805, Business Combinations (ASC 805), which requires the use of the acquisition method of accounting for all business combinations. The excess of the consideration paid over the estimated fair values of the identifiable net assets acquired was recognized as goodwill and is expected to be deductible for income tax purposes. The identifiable intangible assets acquired consist of customer relationships and non-compete agreements, which are being amortized over a weighted-average life of approximately five years.

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The following table sets forth the estimated fair values allocated to the major classes of assets acquired and liabilities assumed in the Ascolta business acquisition as of the acquisition date:

	Assets Acquired	Liabilities Assumed
Accounts receivable and other current assets	$ 849	
Furniture and equipment	370	
Identifiable intangible assets	1,670	
Goodwill	3,332	
Other liabilities		$ 1,001

5. Fair Value and Credit Risk of Financial Instruments

Fair value for financial reporting is defined as the price that would be received upon the sale of an asset or paid upon the transfer of a liability in an orderly transaction between market participants at the measurement date. The fair value measurement of our financial assets utilized assumptions categorized as observable inputs under the accounting guidance. Observable inputs are assumptions based on independent market data sources.

The following table sets forth information regarding the recurring fair value measurement of our financial assets as reflected on our Condensed Consolidated Balance Sheet as of June 30, 2015:

		Fair Value Measurements at Reporting Date Using		
Description	As of June 30, 2015	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Cash equivalents:				
Money market fund	$ 124,564	$ 124,564	$ 0	$ 0
Restricted cash:				
Money market fund	1,820	1,820	0	0
Collateral deposits:				
Money market fund	8,629	8,629	0	0
	$ 135,013	$ 135,013	$ 0	$ 0

The following table sets forth information regarding the recurring fair value measurement of our financial assets as reflected on our Condensed Consolidated Balance Sheet as of June 30, 2014:

		Fair Value Measurements at Reporting Date Using	
		(Level 1)	(Level 2)

Description	As of June 30, 2014	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Cash equivalents:				
Money market fund	$ 219,440	$ 219,440	$ 0	$ 0
Restricted cash:				
Money market fund	1,345	1,345	0	0
Collateral deposits:				
Money market fund	8,627	8,627	0	0
	$ 229,412	$ 229,412	$ 0	$ 0

We used quoted prices in active markets for identical assets as of the measurement dates to value our financial assets that were categorized as Level 1.

The carrying value for cash and cash equivalents, restricted cash, accounts receivable, accounts payable and other current liabilities approximate fair value, because of the immediate or short-term maturity of these financial instruments. We did not have any financial assets or liabilities recorded at estimated fair value on a non-recurring basis on our Condensed Consolidated Balance Sheets as of June 30, 2015, December 31, 2014 or June 30, 2014.

As of June 30, 2015, the aggregate carrying value of the private education loans (PEAKS Trust Student Loans) owned by a trust (the PEAKS Trust) that purchased, owns and collects private education loans made under the PEAKS Private Student Loan Program (the PEAKS Program) and the private education loans (CUSO Student Loans) owned by an entity (the CUSO) that purchased, owns and collects private education loans made under a private education loan program for our students (the CUSO Program) was $79,103 and the estimated fair value was approximately $89,138. As of December 31, 2014, the carrying value of the PEAKS Trust Student Loans and the CUSO Student Loans (collectively, the Private Education Loans) was $90,876 and the estimated fair value was approximately $101,623. As of June 30, 2014, the carrying value of the PEAKS Trust Student Loans was $73,417 and the estimated fair value was approximately $86,600. No CUSO Student Loans were included on our Condensed Consolidated Balance Sheet as of June 30, 2014, because the CUSO was not consolidated in our consolidated financial statements until September 30, 2014. The fair value of the Private Education Loans was estimated using the income approach with estimated discounted expected cash flows. We utilized inputs that were unobservable in determining the estimated fair value of the Private Education Loans. The significant inputs used in determining the estimated fair value included the default rate, repayment rate and discount rate. Fair value measurements that utilize significant unobservable inputs are categorized as Level 3 measurements under the accounting guidance.

As of June 30, 2015, the carrying value of our debt under our Financing Agreement (as defined in Note 10 Debt) was $92,125 and the estimated fair value was approximately $93,000. As of December 31, 2014, each of the carrying value and the estimated fair value of our debt under our Financing Agreement was approximately $96,300. The fair value of our debt under our Financing Agreement was estimated by discounting the future cash flows using current rates for similar loans with similar characteristics and remaining maturities. We utilized inputs that were unobservable in determining the estimated fair value of the debt under the Financing Agreement. The significant input used in determining the estimated fair value was the discount rate utilized for both credit and liquidity purposes. Fair value measurements that utilize significant unobservable inputs are categorized as Level 3 measurements under the accounting guidance.

As of June 30, 2015, the carrying value of the senior debt issued by the PEAKS Trust in the initial aggregate principal amount of $300,000 (the PEAKS Senior Debt) was $63,583 and the estimated fair value was approximately $62,313. As of December 31, 2014, the carrying value of the PEAKS Senior Debt was $85,711 and the estimated fair value was approximately $85,248. As of June 30, 2014, the carrying value of the PEAKS Senior Debt was $196,730 and the estimated fair value was approximately $205,400. The fair value of the PEAKS Senior Debt was estimated using the income approach with estimated discounted cash flows. We utilized inputs that were unobservable in determining the estimated fair value of the PEAKS Senior Debt. The significant input used in determining the estimated fair value was the discount rate utilized for both credit and liquidity purposes. Fair value measurements that utilize significant unobservable inputs are categorized as Level 3 measurements under the accounting guidance.

As of June 30, 2015, the carrying value of the liability that the CUSO was required to record (the CUSO Secured Borrowing Obligation) on its balance sheet for the cash received from the owners of the CUSO (the CUSO Participants), which liability we now consolidate, was $111,089 and the estimated fair value was approximately $105,147. As of December 31, 2014, the carrying value of the CUSO Secured Borrowing Obligation was $121,007 and the estimated fair value was approximately $116,933. The fair value of the CUSO Secured Borrowing Obligation was estimated using the income approach with estimated discounted cash flows. We utilized inputs that were unobservable in determining the estimated fair value of the CUSO Secured Borrowing Obligation. The significant input used in determining the estimated fair value was the discount rate utilized for both credit and liquidity purposes. Fair value measurements that utilize significant unobservable inputs are categorized as Level 3 measurements under the accounting guidance.

Financial instruments that potentially subject us to credit risk consist primarily of accounts receivable, cash equivalents and the Private Education Loans. There is no concentration of credit risk of our accounts receivable, as the total is comprised of a large number of individual balances owed by students whose credit profiles vary and who are located throughout the United States. Our cash equivalents generally consist of money market funds which invest in high-quality securities issued by various entities. The Private Education Loans consist of a large number of individual loans owed by borrowers, whose credit profiles vary and who are located throughout the United States.

6. **<u>Equity Compensation</u>**

The amount of stock-based compensation expense and the line items in which those amounts are included in our Condensed Consolidated Statements of Income and the related estimated income tax benefit recognized in the periods indicated were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Cost of educational services	$ 703	$ 1,119	$ 1,645	$ 2,337
Student services and administrative expenses	661	1,192	1,615	2,525
Total stock-based compensation expense	$ 1,364	$ 2,311	$ 3,260	$ 4,862
Income tax (benefit)	$ (525)	$ (890)	$ (1,255)	$ (1,872)

As of June 30, 2015, we estimated that pre-tax compensation expense for unvested stock-based compensation grants in the amount of approximately $6,900, net of estimated forfeitures, will be recognized in future periods. This expense will be recognized over the remaining service period applicable to the grantees which, on a weighted-average basis, is approximately 1.5 years.

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The stock options granted, forfeited, exercised and expired in the period indicated were as follows:

	Six Months Ended June 30, 2015				
	# of Shares	Weighted Average Exercise Price	Aggregate Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (1)
Outstanding at beginning of period	1,153,273	$ 76.92	$ 88,711		
Granted	121,208	$ 4.91	595		
Forfeited	(10,001)	$ 25.10	(251)		
Exercised	0	$ 0	0		
Expired	(138,773)	$ 86.40	(11,990)		
Outstanding at end of period	1,125,707	$ 68.46	$ 77,065	2.1	$ 0
Exercisable at end of period	853,660	$ 85.10	$ 72,648	1.8	$ 0

(1) The aggregate intrinsic value of the stock options was calculated by identifying those stock options that had a lower exercise price than the closing market price of our common stock on June 30, 2015 and multiplying the difference between the closing market price of our common stock and the exercise price of each of those stock options by the number of shares subject to those stock options that were outstanding or exercisable, as applicable. Since the closing market price of our common stock on June 30, 2015 was lower than the exercise price of all outstanding stock options and exercisable stock options, the aggregate intrinsic value of the stock options was zero.

The following table sets forth information regarding the stock options granted and exercised in the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Shares subject to stock options granted	121,208	0	121,208	168,500
Weighted average grant date fair value per share	$ 3.65	$ 0	$ 3.65	$ 12.62
Shares subject to stock options exercised	0	0	0	0
Intrinsic value of stock options exercised	$ 0	$ 0	$ 0	$ 0
Proceeds received from stock options exercised	$ 0	$ 0	$ 0	$ 0
Tax benefits realized from stock options exercised	$ 0	$ 0	$ 0	$ 0

The intrinsic value of a stock option is the difference between the fair market value of the stock and the option exercise price.

The fair value of each stock option grant was estimated on the date of grant using the following assumptions in the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Risk-free interest rates	1.55%	Not applicable	1.55%	1.32%
Expected lives (in years)	4.7	Not applicable	4.7	4.7
Volatility	107%	Not applicable	107%	55%
Dividend yield	None	Not applicable	None	None

For the three months ended June 30, 2014, the assumptions listed above were not applicable because we did not grant any stock options in that period.

The following table sets forth the number of restricted stock units (RSUs) that were granted, forfeited and vested in the period indicated:

	Six Months Ended June 30, 2015	
	# of RSUs	Weighted Average Grant Date Fair Value
Unvested at beginning of period	831,307	$ 30.17
Granted	399,720	$ 4.93
Forfeited	(54,269)	$ 23.00
Vested	(198,478)	$ 61.87
Unvested at end of period	978,280	$ 13.83

The total fair market value of the RSUs that vested and were settled in shares of our common stock was:

- $123 in the three months ended June 30, 2015;
- $18 in the three months ended June 30, 2014;
- $1,383 in the six months ended June 30, 2015; and
- $1,942 in the six months ended June 30, 2014.

7. Variable Interest Entities

Under ASC 810, an entity that holds a variable interest in a VIE and meets certain requirements would be considered to be the primary beneficiary of the VIE and required to consolidate the VIE in its consolidated financial statements. In order to be considered the primary beneficiary of a VIE, an entity must hold a variable interest in the VIE and have both:

- the power to direct the activities that most significantly impact the economic performance of the VIE; and
- the right to receive benefits from, or the obligation to absorb losses of, the VIE that could be potentially significant to the VIE.

We hold variable interests in the PEAKS Trust as a result of:

- a subordinated note issued to us by the PEAKS Trust in exchange for the portion of each private education loan disbursed to us under the PEAKS Program that we transferred to the PEAKS Trust (Subordinated Note); and
- our guarantee of the payment of the principal and interest owed on the PEAKS Senior Debt, the administrative fees and expenses of the PEAKS Trust and a minimum required ratio of assets of the PEAKS Trust to outstanding PEAKS Senior Debt (PEAKS Guarantee).

We hold variable interests in the CUSO as a result of:

- a risk sharing agreement (the CUSO RSA) that we entered into with the CUSO in connection with the CUSO Program; and

- a revolving note owed to us by the CUSO (the Revolving Note).

Primary Beneficiary Analysis. The PEAKS Trust and the CUSO are VIEs as defined under ASC 810. To determine whether we are the primary beneficiary of the PEAKS Trust or the CUSO, we:

- assessed the risks that the VIE was designed to create and pass through to its variable interest holders;
- identified the variable interests in the VIE;
- identified the other variable interest holders and their involvement in the activities of the VIE;
- identified the activities that most significantly impact the VIE s economic performance;
- determined whether we have the power to direct those activities; and
- determined whether we have the right to receive the benefits from, or the obligation to absorb the losses of, the VIE that could potentially be significant to the VIE.

We determined that the activities of the PEAKS Trust and the CUSO that most significantly impact the economic performance of the PEAKS Trust and the CUSO involve the servicing (which includes the collection) of the PEAKS Trust Student Loans and the CUSO Student Loans. To make that determination, we analyzed various possible scenarios of student loan portfolio performance to evaluate the potential economic impact on the PEAKS Trust and the CUSO. In our analysis, we made what we believe are reasonable assumptions based on historical data for the following key variables:

- the composition of the credit profiles of the borrowers;
- the interest rates and fees charged on the loans;
- the default rates and the timing of defaults associated with similar types of loans; and
- the prepayment and the speed of repayment associated with similar types of loans.

Based on our analysis, we concluded that we became the primary beneficiary of the PEAKS Trust on February 28, 2013. This was the first date that we had the power to direct the activities of the PEAKS Trust that most significantly impact the economic performance of the PEAKS Trust, because we could have exercised our right to terminate the servicing agreement that governs the servicing activities of the PEAKS Trust Student Loans (the PEAKS Servicing Agreement), due to the failure of the entity that performs those servicing activities for the PEAKS Trust Student Loans on behalf of the PEAKS Trust to meet certain performance criteria specified in the PEAKS Servicing Agreement. We have not, however, exercised our right to terminate the PEAKS Servicing Agreement. As a result of our primary beneficiary conclusion, we consolidated the PEAKS Trust in our consolidated financial statements beginning on February 28, 2013 (the PEAKS Consolidation). Prior to February 28, 2013, the PEAKS Trust was not required to be consolidated in our consolidated financial statements, because we concluded that we were not the primary beneficiary of the PEAKS Trust prior to that time. The PEAKS Trust is discussed in more detail below.

Our consolidated financial statements for periods as of and after February 28, 2013 include the PEAKS Trust, because we were considered to have control over the PEAKS Trust under ASC 810, as a result of our substantive unilateral right to terminate the PEAKS Servicing Agreement. We do not, however, actively manage the operations of the PEAKS Trust, and the assets of the consolidated PEAKS Trust can only be used to satisfy the obligations of the PEAKS Trust. Our obligations under the PEAKS Guarantee remain in effect, until the PEAKS Senior Debt and the PEAKS Trust s fees and expenses are paid in full. See Note 13 Commitments and Contingencies, for a further discussion of the PEAKS Guarantee.

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Based on our analysis, we concluded that we became the primary beneficiary of the CUSO on September 30, 2014. This was the first date that we determined we had the power to direct the activities of the CUSO that most significantly impact the economic performance of the CUSO, because the entity that performs the servicing activities on behalf of the CUSO (the CUSO Program Servicer) failed to meet certain performance criteria specified in the servicing agreement that governs the servicing activities of the CUSO Student Loans (the CUSO Servicing Agreement) on that date. The CUSO Servicing Agreement provides that in the event that the CUSO Program Servicer fails to meet certain performance criteria specified in the CUSO Servicing Agreement, and the CUSO Program Servicer does not affect a cure of that failure during a specified cure period, we would have the right to terminate the CUSO Servicing Agreement. We determined that it was not reasonably possible that the CUSO Program Servicer would be able to affect a cure during the specified cure period and, therefore, because the cure period was not substantive, we effectively had the right to terminate the CUSO Servicing Agreement as of the date that the CUSO Program Servicer failed to meet the performance criteria. We have not, however, exercised our right to terminate the CUSO Servicing Agreement.

As a result of our primary beneficiary conclusion, we consolidated the CUSO in our consolidated financial statements beginning on September 30, 2014. Prior to September 30, 2014, the CUSO was not required to be consolidated in our consolidated financial statements, because we concluded that we were not the primary beneficiary of the CUSO prior to that time. The CUSO is discussed in more detail below.

Our consolidated financial statements for periods as of and after September 30, 2014 include the CUSO, because we were considered to have control over the CUSO under ASC 810, as a result of our substantive right to terminate the CUSO Servicing Agreement after a cure period that was not substantive. We do not, however, actively manage the operations of the CUSO, and the assets of the consolidated CUSO can only be used to satisfy the obligations of the CUSO. Our obligations under the CUSO RSA remain in effect, until all CUSO Student Loans are paid in full. See Note 13 Commitments and Contingencies, for a further discussion of the CUSO RSA.

The PEAKS Trust and the CUSO are not included in our consolidated income tax returns. We do not recognize income tax expense or benefit for the financial results of the PEAKS Trust or CUSO in the provision for income taxes included in our Condensed Consolidated Statements of Income, even though the PEAKS Trust and the CUSO are included in our consolidated financial statements. In the three and six months ended June 30, 2015 and 2014, the financial results of the PEAKS Trust and CUSO were not significant and, therefore, did not have a significant impact on our effective income tax rate. Our deferred income tax assets as of June 30, 2015 were lower as compared to December 31, 2014, in part due to the significant payments that we made under the PEAKS Guarantee and CUSO RSA in the six months ended June 30, 2015, which are generally deductible for income tax purposes when the payments are made.

PEAKS Private Student Loan Program. On January 20, 2010, we entered into agreements with unrelated third parties to establish the PEAKS Program, which was a private education loan program for our students. We entered into the PEAKS Program to offer our students another source of private education loans that they could use to help pay their education costs owed to us and to supplement the limited amount of private education loans available to our students under other private education loan programs, including the CUSO Program. Under the PEAKS Program, our students had access to a greater amount of private education loans, which resulted in a reduction in the amount of internal financing that we provided to our students in 2010 and 2011. No new private education loans were or will be originated under the PEAKS Program after July 2011, but immaterial amounts related to loans originated prior to that date were disbursed by the lender through March 2012.

Under the PEAKS Program, an unrelated lender originated private education loans to our eligible students and, subsequently, sold those loans to the PEAKS Trust. The PEAKS Trust issued the PEAKS Senior Debt to investors.

The lender disbursed the proceeds of the private education loans to us for application to the students account balances with us that represented their unpaid education costs. We transferred a portion of the amount of each private education loan disbursed to us under the PEAKS Program to the PEAKS Trust in exchange for the Subordinated Note.

The Subordinated Note issued by the PEAKS Trust to us does not bear interest and matures in March 2026. Principal is due on the Subordinated Note following:

- the repayment of the PEAKS Senior Debt;
- the repayment of fees and expenses of the PEAKS Trust; and
- the reimbursement of the amounts of any payments made by us under the PEAKS Guarantee, other than Payments on Behalf of Borrowers (as defined below).

The carrying value of the Subordinated Note was eliminated from our consolidated balance sheet when we consolidated the PEAKS Trust in our consolidated financial statements beginning on February 28, 2013. In the three months ended December 31, 2012, we determined it was probable that we would not collect the carrying value of the Subordinated Note and, therefore, recorded an impairment charge for the total carrying value of the Subordinated Note.

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The PEAKS Trust utilized the proceeds from the issuance of the PEAKS Senior Debt and the Subordinated Note to purchase the private education loans made by the lender to our students. The assets of the PEAKS Trust (which include, among other assets, the PEAKS Trust Student Loans) serve as collateral for, and are intended to be the principal source of, the repayment of the PEAKS Senior Debt and the Subordinated Note.

Under the PEAKS Guarantee, we guarantee payment of the principal and interest owed on the PEAKS Senior Debt, the administrative fees and expenses of the PEAKS Trust and a minimum required ratio of assets of the PEAKS Trust to outstanding PEAKS Senior Debt (the Asset/Liability Ratio). Our guarantee obligations under the PEAKS Program remain in effect until the PEAKS Senior Debt and the PEAKS Trust s fees and expenses are paid in full. At such time, we will be entitled to repayment of the amounts that we paid under the PEAKS Guarantee (which do not include Payments on Behalf of Borrowers, as defined below), to the extent of available funds remaining in the PEAKS Trust. See Note 13 Commitments and Contingencies, for a further discussion of our obligations to make guarantee payments pursuant to the PEAKS Guarantee.

Assets and Liabilities of the PEAKS Trust. We concluded that we became the primary beneficiary of the PEAKS Trust on February 28, 2013 and, therefore, were required to consolidate the PEAKS Trust in our consolidated financial statements. The following table sets forth the carrying value of assets and liabilities of the PEAKS Trust that were included on our Condensed Consolidated Balance Sheets as of the dates indicated:

	As of June 30, 2015	As of December 31, 2014	As of June 30, 2014
Assets			
Restricted cash	$ 1,629	$ 1,556	$ 1,423
Current portion of PEAKS Trust student loans	6,250	7,169	7,420
PEAKS Trust student loans, excluding current portion, less allowance for loan losses of $36,921, $42,353 and $38,420	50,937	59,902	65,997
Total assets	$ 58,816	$ 68,627	$ 74,840
Liabilities			
Current portion of PEAKS Trust senior debt	$ 23,068	$ 37,545	$ 132,429
Other current liabilities	158	199	395
PEAKS Trust senior debt, excluding current portion	40,515	48,166	64,301
Total liabilities	$ 63,741	$ 85,910	$ 197,125

The assets of the PEAKS Trust can only be used to satisfy the obligations of the PEAKS Trust. Payment of the administrative fees and expenses of the PEAKS Trust and the principal and interest owed on the PEAKS Senior Debt are guaranteed by us under the PEAKS Guarantee.

Revenue and Expenses of the PEAKS Trust. The following table sets forth the revenue and expenses of the PEAKS Trust, which were included in our Condensed Consolidated Statements of Income for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Revenue	$ 2,246	$ 3,239	$ 4,659	$ 6,372
Student services and administrative expenses	489	1,221	1,030	2,637
Provision for private education loan losses	4,615	9,071	5,418	9,071
Interest expense	2,826	6,456	6,085	17,473
(Loss) before provision for income taxes	$ (5,684)	$ (13,509)	$ (7,874)	$ (22,809)

The revenue of the PEAKS Trust consists of interest income on the PEAKS Trust Student Loans, which is the accretion of the accretable yield on the PEAKS Trust Student Loans. The servicing, administrative and other fees incurred by the PEAKS Trust are included in Student services and administrative expenses in our Condensed Consolidated Statements of Income. The provision for private education loan losses represents the increase in the allowance for loan losses that occurred during the period. The allowance for loan losses related to the PEAKS Trust Student Loans represents the difference between the carrying value and the total present value of the expected principal and interest collections of each loan pool of the PEAKS Trust Student Loans, discounted by the loan pool s effective interest rate as of the end of the reporting period. Interest expense of the PEAKS Trust represents interest expense on the PEAKS Senior Debt, which includes the contractual interest obligation and the accretion of the discount on the PEAKS Senior Debt.

Payments on Behalf of Borrowers. Beginning in the fourth quarter of 2012 and continuing through January 2014, we made payments on behalf of certain student borrowers under the PEAKS Program to the PEAKS Trust to avoid defaults by those borrowers on their PEAKS Trust Student Loans (Payments on Behalf of Borrowers), which defaults would have triggered much larger contractually required payments by us under the PEAKS Guarantee. At the time we made Payments on Behalf of Borrowers, we believed that those payments were contractually permitted and a form of payment to the PEAKS Trust that would satisfy obligations that were contractually required. Since that time, however, we have determined that Payments on Behalf of Borrowers are not permitted or required to support the PEAKS Trust. If we had not made Payments on Behalf of Borrowers, we would have had to make contractually required payments under the PEAKS Guarantee in greater amounts. We made Payments on Behalf of Borrowers after assessing:

- the likelihood of us being contractually required to make payments under the PEAKS Guarantee in the near future;
- the effect on our liquidity that would result from making payments under the PEAKS Guarantee compared to making Payments on Behalf of Borrowers;
- the effect that Payments on Behalf of Borrowers may have on the funds available to the PEAKS Trust to repay the Subordinated Note to us following full payment of the PEAKS Trust s other obligations; and
- the fact that we will not be able to recover Payments on Behalf of Borrowers from the PEAKS Trust or the student borrowers on whose behalf we made those payments.

Payments on Behalf of Borrowers assisted in:

- maintaining the Asset/Liability Ratio at the required level; and
- satisfying the following month s required payment of interest on the PEAKS Senior Debt and administrative fees and expenses of the PEAKS Trust.

Prior to the PEAKS Consolidation, Payments on Behalf of Borrowers were reflected on our financial statements as a reduction to our contingent liability. Following the PEAKS Consolidation, Payments on Behalf of Borrowers were not reflected on our financial statements, since those payments were intercompany transactions that were eliminated from our financial statements as a result of the PEAKS Consolidation.

In January 2014, we made Payments on Behalf of Borrowers of $1,832. We entered into a letter agreement, dated as of March 17, 2014, with the trustee under the PEAKS Program and the holders of the PEAKS Senior Debt (the PEAKS Letter Agreement), in order to resolve differing interpretations of the permissibility of the Payments on Behalf of Borrowers under the PEAKS Program documents. Pursuant to the PEAKS Letter Agreement, the trustee agreed to waive, and the holders of the PEAKS Senior Debt consented to the waiver of, any:

- breach of the PEAKS Program documents caused by us making Payments on Behalf of Borrowers, including any failure to make payments under the PEAKS Guarantee as a result thereof; and event of default under the PEAKS Program documents that may have arisen or resulted by us making Payments on Behalf of Borrowers.

In the PEAKS Letter Agreement, we agreed that, after the date of the PEAKS Letter Agreement, we would not make any further payments of any kind on behalf of any borrower in respect of a private education loan made under the PEAKS Program, and that any such payments in lieu of making payments to maintain the applicable required Asset/Liability Ratio would constitute a breach of the terms of the PEAKS Guarantee and an event of default under the indenture and credit agreement for the PEAKS Program. In accordance with the terms of the PEAKS Letter Agreement, we paid $40,000 on March 20, 2014, which is considered to be a payment under the PEAKS Guarantee and was applied primarily to make a mandatory prepayment of the PEAKS Senior Debt.

PEAKS Guarantee Payments and Payments on Behalf of Borrowers. The following table sets forth the PEAKS Guarantee payments and Payments on Behalf of Borrowers that were made in the periods indicated:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2015	**2014**	**2015**	**2014**
PEAKS Guarantee	$ 6,820	$ 1,088	$ 20,457	$ 41,801
Payments on Behalf of Borrowers	0	0	0	1,832
Total	$ 6,820	$ 1,088	$ 20,457	$ 43,633

CUSO Program. On February 20, 2009, we entered into agreements with the CUSO to create the CUSO Program. Under the CUSO Program, an unrelated lender originated private education loans to our eligible students and, subsequently, sold those loans to the CUSO. The CUSO purchased the private education loans from the lender utilizing funds received from its owners in exchange for participation interests in the private education loans acquired by the CUSO. The lender disbursed the proceeds of the private education loans to us for application to the students account balances with us that represented their unpaid education costs. No new private education loans were or will be originated under the CUSO Program after December 31, 2011, but immaterial amounts related to loans originated prior to that date were disbursed by the lender through June 2012.

In connection with the CUSO Program, we entered into the CUSO RSA with the CUSO. Under the CUSO RSA, we guarantee the repayment of any private education loans that are charged off above a certain percentage of the private education loans made under the CUSO Program, based on the annual dollar volume. Under the CUSO RSA, we have an obligation to make the monthly payments due and unpaid on those private education loans that have been charged off above a certain percentage (Regular Payments). Instead of making Regular Payments, however, we may elect to discharge our obligations to make Regular Payments on specified charged-off private education loans by:

paying the then outstanding balance (plus accrued and unpaid interest) of those private education loans that have been charged off above a certain percentage and, with respect to which, an amount equal to at least ten monthly payments has been paid; or

paying the then outstanding balance (plus accrued and unpaid interest) of those private education loans that have been charged off above a certain percentage and, with respect to which, an amount equal to at least ten monthly payments has not been paid, plus any interest that would otherwise have been payable until ten monthly payments had been made, discounted at the rate of 10% per annum

(collectively, Discharge Payments).

See Note 13 Commitments and Contingencies, for a further discussion of our obligations to make guarantee payments pursuant to the CUSO RSA.

Assets and Liabilities of the CUSO. We concluded that we became the primary beneficiary of the CUSO on September 30, 2014 and, therefore, were required to consolidate the CUSO in our consolidated financial statements (the CUSO Consolidation). In accordance with ASC 810, the consolidation of the CUSO was treated as an acquisition of assets and liabilities and, therefore, the assets and liabilities of the CUSO were included in our consolidated financial statements at their fair value as of September 30, 2014.

The CUSO Participants purchased participation interests in the CUSO Student Loans from the CUSO. The terms of the agreements between the CUSO Participants and the CUSO did not meet the requirements under ACC 860, Transfers and Servicing, to be considered a sale. As a result, the CUSO was required to record the CUSO Secured Borrowing Obligation on its balance sheet for the cash received from the CUSO Participants.

We recorded the CUSO Secured Borrowing Obligation at the time of the CUSO Consolidation. The CUSO Secured Borrowing Obligation represents the estimated amount that the CUSO owes to the CUSO Participants related to their participation interests in the CUSO Student Loans, which amount is expected to be paid to the CUSO Participants by the CUSO from payments received by the CUSO related to the CUSO Student Loans, whether from the borrower or from us under the CUSO RSA.

In accordance with ASC 810, we included the CUSO Secured Borrowing Obligation on our Condensed Consolidated Balance Sheet at its fair value as of September 30, 2014, the date of the CUSO Consolidation. The difference between the estimated fair value of the CUSO Secured Borrowing Obligation and the amount expected to be paid by the CUSO to the CUSO Participants was recorded as an accrued discount on our Condensed Consolidated Balance Sheet at the date of the CUSO Consolidation. The accrued discount is being recognized in interest expense at a level rate of return over the expected life of the CUSO Secured Borrowing Obligation.

The expected life of the CUSO Secured Borrowing Obligation is an estimate of the period of time over which payments are expected to be made by the CUSO to the CUSO Participants related to their participation interests in the CUSO Student Loans. The period of time over which payments are expected to be made by the CUSO to the CUSO Participants is based upon when the CUSO Student Loans enter a repayment status and the period of time they remain in a repayment status. Since all of the CUSO Student Loans have not entered repayment, and those loans that have entered a repayment status may be granted forbearances or deferments, the period of time over which payments are expected to be made to the CUSO Participants is an estimate. The assumptions used to estimate the expected life of the CUSO Secured Borrowing Obligation are reviewed periodically and updated accordingly, which may result in an adjustment to the expected life of the CUSO Secured Borrowing Obligation and the related recognized interest expense.

The following table sets forth the fair value and the carrying value of the assets and liabilities of the CUSO as of September 30, 2014 that were included on our Condensed Consolidated Balance Sheet on that date:

	As of September 30, 2014	
	Assets	**Liabilities**
Restricted cash	$ 2,738	
Current portion of CUSO Student Loans	3,406	
CUSO Student Loans, excluding current portion	23,793	
Other assets	199	
Current portion of CUSO Secured Borrowing Obligation		$ 20,662
Other current liabilities		624
CUSO Secured Borrowing Obligation, excluding current portion		101,880
Other liabilities		1,940
Total	$ 30,136	$ 125,106

The assets of the CUSO can only be used to satisfy the obligations of the CUSO.

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The following table sets forth the carrying value of the assets and liabilities related to the CUSO Program as of September 30, 2014 that we eliminated from our consolidated balance sheet when we consolidated the CUSO in our consolidated financial statements, and the line items within which those assets and liabilities were included:

	As of September 30, 2014 Assets	As of September 30, 2014 Liabilities
Prepaid expenses and other current assets	$ 3,260	
Other current liabilities		$ 23,887
Other liabilities		90,974
Total	$ 3,260	$ 114,861

Upon the CUSO Consolidation, we recorded the CUSO s assets and liabilities at their fair value in our consolidated financial statements and we eliminated the carrying value of the assets and liabilities related to the CUSO Program that had been recorded in our consolidated financial statements as of September 30, 2014. The fair value of the CUSO s liabilities exceeded the fair value of the CUSO s assets as of September 30, 2014 by $94,970. As of September 30, 2014, the carrying value of the liabilities related to the CUSO Program that had been recorded in our consolidated financial statements exceeded the carrying value of the assets related to the CUSO Program that had been recorded in our consolidated financial statements by $111,601. As a result, we recognized a total gain of $16,631 in our Condensed Consolidated Statements of Income in the three and nine months ended September 30, 2014, which represented the difference between (i) the fair value of the net liabilities of the CUSO that we recorded upon the CUSO Consolidation, and (ii) the carrying value of the net liabilities related to the CUSO Program that had been recorded in our consolidated financial statements and were eliminated upon the CUSO Consolidation, in each case, as of September 30, 2014.

The following table sets forth the carrying values of assets and liabilities of the CUSO that were included on our Condensed Consolidated Balance Sheets as of the dates indicated:

	As of June 30, 2015	As of December 31, 2014
Assets		
Restricted cash	$ 3,487	$ 2,517
Current portion of CUSO Student Loans	3,129	3,415
CUSO Student Loans, excluding current portion, less allowance for loan losses of $1,178 and $2,039	18,787	20,390
Other assets	198	284
Total assets	$ 25,601	$ 26,606
Liabilities		
Current portion of CUSO Secured Borrowing Obligation	$ 19,750	$ 20,813
Other current liabilities	302	179

CUSO Secured Borrowing Obligation, excluding current portion	91,339	100,194
Other liabilities	1,879	1,073
Total liabilities	$ 113,270	$ 122,259

The assets of the CUSO can only be used to satisfy the obligations of the CUSO.

Revenue and Expenses of the CUSO. The following table sets forth the revenue and expenses of the CUSO, excluding the gain on consolidation of the CUSO, which were included in our Condensed Consolidated Statements of Income for the periods indicated:

	Three Months Ended June 30, 2015	**Six Months Ended June 30, 2015**
Revenue	$ 1,185	$ 2,249
Student services and administrative expenses	483	879
Provision for private education loan losses	(1,302)	(861)
Interest expense	3,573	7,214
(Loss) before provision for income taxes	$ (1,569)	$ (4,983)

The revenue of the CUSO consists of interest income on the CUSO Student Loans, which is the accretion of the accretable yield on the CUSO Student Loans, and an administrative fee paid by the CUSO Participants to the CUSO on a monthly basis. The servicing, administrative and other fees incurred by the CUSO are included in Student services and administrative expenses in our Consolidated

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Statements of Income. The provision for private education loan losses represents the increase in the allowance for loan losses that occurred during the period. The allowance for loan losses related to the CUSO Student Loans represents the difference between the carrying value and the total present value of the expected principal and interest collections of each loan pool of the CUSO Student Loans, discounted by the loan pool s effective interest rate as of the end of the reporting period. Interest expense of the CUSO represents interest expense on the CUSO Secured Borrowing Obligation, which includes the contractual interest obligation on the CUSO Student Loans and the accretion of the discount on the CUSO Secured Borrowing Obligation.

We did not recognize any revenue or expenses of the CUSO in our Condensed Consolidated Statements of Income in the three or six months ended June 30, 2014, because the CUSO Consolidation was effective on September 30, 2014.

CUSO RSA Payments, Recoveries and Offsets. Pursuant to the CUSO RSA, we are entitled to all amounts that the CUSO recovers from loans in a particular loan pool made under the CUSO Program that have been charged off, until all payments that we made under the CUSO RSA with respect to that loan pool have been repaid to us by the CUSO. We have the right to offset payment amounts that we owe under the CUSO RSA by the amount of recoveries from charged-off loans made under the CUSO Program that are owed, but have not been paid, to us. We exercised this offset right in the three and six months ended June 30, 2015. We did not exercise this offset right in the three or six months ended June 30, 2014.

The following table sets forth the payments that we made to the CUSO related to our guarantee obligations under the CUSO RSA in the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Regular Payments	$ 1,560(1)	$ 1,589	$ 3,840(2)	$ 2,747
Discharge Payments	6,544	0	9,253	0
Total	$ 8,104	$ 1,589	$ 13,093	$ 2,747

(1) This amount is net of $231 of recoveries from charged-off loans owed to us that we offset against the amount we owed under the CUSO RSA.
(2) This amount is net of $521 of recoveries from charged-off loans owed to us that we offset against the amount we owed under the CUSO RSA.

The CUSO did not remit to us, and we did not offset payments under the CUSO RSA for, the following amounts of recoveries from charged-off loans that were owed to us:

$0 in the three months ended June 30, 2015;

$256 in the three months ended June 30, 2014;

$0 in the six months ended June 30, 2015; and