

LINCOLN EDUCATIONAL SERVICES CORP
Form 10-K
March 11, 2014

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2013

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 o No x

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 o No x

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 o

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 x
No o

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. x

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 o Accelerated filer x Non-accelerated filer o Smaller reporting company o

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

The aggregate market value of the 22,093,312 shares of common stock held by non-affiliates of the registrant issued and outstanding as of June 30, 2013, the last business day of the registrant's most recently completed second fiscal quarter, was \$116,431,754. This amount is based on the closing price of the common stock on the Nasdaq Global Select Market of \$5.27 per share on June 30, 2013. 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 7, 2014 was 23,882,147.

Documents Incorporated by Reference

Portions of the Proxy Statement for the Registrant's 2014 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 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,” “future,” “intends,” “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 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;
- 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;
- risks associated with changes in applicable federal laws and regulations, including final rules that took effect during 2011 and other 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;
- our ability to continue to execute our growth strategies;
- 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 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. BUSINESS

OVERVIEW

We are a leading provider of diversified career-oriented post-secondary education as measured by total enrollment. As of December 31, 2013, we operated 33 campuses and five training sites in 15 states. We offer recent high school graduates and working adults degree and diploma programs in five areas of study: automotive technology, health sciences, skilled trades, hospitality services and business and information technology. For the year ended December 31, 2013, our automotive technology program, our health sciences program, our skilled trades program, our hospitality services program and our business and information technology program accounted for approximately 42%, 30%, 13%, 9%, and 6%, respectively, of our average enrollment. As of December 31, 2013, we had 13,740 students enrolled in diploma and degree programs and an additional 104 students enrolled in certificate programs. Our average enrollment for the year ended December 31, 2013 was 15,009 students in diploma and degree programs and 315 students in certificate programs, which represented a decrease of 12.3% from average enrollment in 2012 of 17,121 students in diploma and degree programs and 220 students in certificate programs. For the year ended December 31, 2013, our revenues were \$345.0 million, which represented a decrease of 9.9% from the year ended December 31, 2012. For the year ended December 31, 2012, our revenues were \$382.8 million, which represented a decrease of 16.2% from the year ended December 31, 2011. 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.

Our schools operate under the Lincoln Technical Institute, Lincoln College of Technology, Lincoln College of New England, and Euphoria Institute of Beauty Arts and Sciences brand names. Most of our campuses serve major metropolitan markets and each typically offers courses in multiple areas of study. Five of our campuses are destination schools, which attract students from across the United States and, in some cases, from abroad. Our other campuses primarily attract students from their local communities and surrounding areas. All of our campuses are nationally or regionally accredited and are eligible to participate in federal financial aid programs by the U.S. Department of Education, or 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.

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.

Each of our schools is a reporting unit and an operating segment. Our operating segments have been aggregated into one reportable segment because, in our judgment, the reporting units have similar products, production processes, types of customers, methods of distribution, regulatory environment and economic characteristics.

We are a New Jersey corporation organized in 2003.

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 statement on Schedule 14A and amendments to those reports as soon as reasonably practicable after we electronically file or furnish such materials to the Securities and Exchange Commission. 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.

BUSINESS STRATEGY

Our goal is to strengthen our position as a leading and diversified 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 to capitalize on demand from students and employers in our target markets. Whenever possible, we seek to replicate programs across our campuses. In 2013, we introduced one new program to our campuses in Indianapolis, Indiana and Grand Prairie, Texas. In 2012, we introduced one new program to our facilities in Florida. In 2011, we introduced seven new programs to our facilities in Colorado, Kentucky and Massachusetts.

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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. In 2013, we continued to partner with several high schools in New Jersey to provide students with introductory classes in automotive technologies and entered into several partnerships with industry including Chrysler, Raytheon, and BMW. We expect to continue investing in marketing, recruiting and retention resources to increase enrollment.

Expand Geographic Presence. We believe that we can leverage our marketing and recruiting programs by opening additional campuses in selected markets and obtaining greater market penetration. We believe we can also increase our student enrollments by entering selected new geographic markets that we believe have significant growth potential and where we can leverage our reputation and operating expertise.

Pursue Strategic Acquisitions. We continue to evaluate acquisition candidates. In evaluating potential acquisitions, we seek to identify schools that provide the potential for program replication at our existing campuses, expand our program and degree offerings, and extend our presence into markets with attractive growth opportunities. In 2012, we purchased Florida Medical Training Institute (“FMTI”) which offers short term certificate programs in the fields of Emergency Medical Technician, Paramedic, EKG/Phlebotomy, Nursing Assistant and Fire Fighter, and Associate of Science Degrees in Emergency Medical Services and Fire Science Technology.

Expand Market. We believe that we can enter new markets and broaden the Lincoln brand by partnering with nationally well-known brands to provide the skills needed to train our nation’s workforce.

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 106 weeks to complete, with tuition ranging from \$5,000 to \$36,000. Our associate’s degree programs typically take between 48 to 156 weeks to complete, with tuition ranging from \$16,000 to \$70,000. Our bachelor’s degree programs typically take between 142 and 208 weeks to complete, with tuition ranging from \$58,000 to \$80,000. As of December 31, 2013, all of our schools offer diploma and certificate programs, 13 of our schools are currently approved to offer associate’s degree programs and two schools are 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 a 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, 2013 with the average number of students enrolled in each area of study for the year ended December 31, 2013:

Programs Offered

Area of Study	Bachelor's Degree	Associate's Degree	Diploma and Certificate	Average Enrollment	Percent of Total Enrollment
Automotive -		Collision Repair & Refinishing Service Management, Diesel & Truck Service Management, Automotive Service Management, Maintenance 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, Heavy Equipment Maintenance Technology, Diesel & Truck Technology with Transport Refrigeration, Diesel & Truck with Automotive Technology, Heavy Equipment and Truck Technology, Motorcycle Technology	6,299	42%
Health Sciences -		Medical Assisting Technology, Health Information Administration, Dental Office Management, Child Development, Health Information Technology, Medical Office Management, Mortuary Science, Nuclear Medicine Technology, Occupational Therapy Assistant, Dental Hygiene, Dental Administrative Assistant, Surgical Technology, Advanced Medical Coding & Billing, Nursing	Medical Office Assistant, Medical Assistant, Pharmacy Technician, Medical Coding & Billing, Dental Assistant, Licensed Practical Nursing, Phlebotomy, Medical Assistant w/Basic X-ray, Basic X-Ray Technician, Surgical Technologist, Paramedic	4,568	30%
Skilled Trades -		Electronic Engineering Technology, HVAC, Electronics Systems Service Management	Electrical Technology, Electronics Systems Technician, HVAC, Welding Technology, CNC	2,009	13%

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Programs Offered (Continued)

Area of Study	Bachelor's Degree	Associate's Degree	Diploma or Certificate	Average Enrollment	Percent of Total Enrollment
Hospitality Services	Culinary Arts	Culinary Arts, Salon Management, International Baking and Pastry	Culinary Arts, Cosmetology, Aesthetics, Therapeutic Massage & Bodywork Technician, Italian Culinary Arts, International Baking and Pastry	1,325	9%
Business and Information Technology	Business Management, Criminal Justice, Funeral Service Management	PC Systems & Networking Technology, Business Administration, Criminal Justice, Business Management, Broadcasting and Communications, Paralegal, Computer Networking and Security, Accounting	PC Support Technician, Criminal Justice, Business Office Technology, Computer Networking and Security	808	6%
Total:				15,009	100%

Automotive Technology. Automotive technology was our largest area of study, with 42% of our total average student enrollment for the year ended December 31, 2013. Our automotive technology programs are 28 to 106 weeks in length, with tuition rates of \$11,000 to \$36,000. 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.

As of December 31, 2013, 13 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, 2013, health sciences was our second largest area of study, representing 30% of our total average student enrollment. Our health science programs are 24 to 208 weeks in length, with tuition rates of \$5,000 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, medical assistant and medical administrative assistant programs are our largest health science programs. As of December 31, 2013, we offered health science programs at 18 of our campuses and five training sites.

Skilled Trades. For the year ended December 31, 2013, 13% of our total average student enrollment was in our skilled trades programs. Our skilled trades programs are 36 to 98 weeks in length, with tuition rates of \$16,500 to \$30,000. Our skilled trades programs include electrical, heating, and air conditioning repair, welding, computerized numerical control and electronic system technician. 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, 2013, we offered skilled trades programs at 14 campuses.

Hospitality Services. For the year ended December 31, 2013, 9% of our total average student enrollment was in our hospitality services programs. Our hospitality services programs are 22 to 142 weeks in length, with tuition rates of \$13,000 to \$58,000. 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 three campuses and cosmetology programs at five campuses. Our culinary graduates are employed by restaurants, hotels, cruise ships and bakeries. As of December 31, 2013, we offered culinary programs at four campuses.

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Business and Information Technology. For the year ended December 31, 2013, 6% 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 30 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 those that are most in demand, such as our personal computer, or PC, systems technician, computer networking and security and business administration programs. 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, 2013, we offered these programs at 13 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 potential students who are entering the workforce, or who are underemployed or unemployed and require additional training to enter or re-enter the workforce.

Marketing and Advertising. Our marketing program utilizes integrated advertising such as the Internet, television, and various print media, direct mail, and event marketing campaigns. These campaigns are enhanced by student and alumni referrals. Internet lead generation is our most successful medium, built upon successful search engine optimization and specific keywords. Our website inquiries incorporate integrated campaigns that direct potential students to the Lincoln website where they may request additional information on a program 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.

Referrals. Referrals from current students, high school counselors and satisfied graduates and their employers have historically represented 17% to 25% of our new enrollments. Our school administrators actively work with our current students to encourage them to recommend our programs to potential students. We continue to build strong relationships with high school guidance counselors and instructors by offering annual seminars at our training facilities to further educate these individuals on the strengths of our programs. Graduates who have gone on to enjoy success in the workforce frequently recommend our programs, as do employers who are pleased with the performance of our graduates whom they have hired.

Recruiting. Our recruiting efforts are conducted by a group of approximately 366 field and campus-based representatives who meet directly with potential students during presentations conducted at high schools, in the potential student's home or during a visit to one of our campuses.

Field-Based Recruiting. Our field-based recruiting representatives make presentations at high schools to attract students to both our local and destination campuses. Our field-based representatives also visit directly with potential students in their homes. During 2013, we recruited approximately 25% of our students directly out of high school.

Campus-Inquiries. When a potential student contacts us as a result of our marketing and outreach efforts, an admissions representative contacts the potential student to follow up on an individual basis. The admissions representative provides information on the programs of interest available at the campus location selected by the potential student and offers an appointment to visit the school and tour the school's facilities.

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. We had 13,740 students enrolled in diploma and degree programs and an additional 104 students enrolled in certificate programs as of December 31, 2013 and our average enrollment for the year ended December 31, 2013 was 15,009 students in diploma and degree programs and 315 in certificate programs, a decrease of 12.3% in average enrollment from December 31, 2012. We had 15,516 students enrolled in diploma and degree programs and 160 in certificate programs as of December 31, 2012 and our average enrollment for the year ended December 31, 2012 was 17,121 students in diploma and degree programs and 220 in certificate programs, a decrease of 20.0% in average enrollment from December 31, 2011.

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 notice 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 having trouble academically, we offer tutoring.

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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. 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 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 made up 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 market. 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. We also 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 allied health 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, 2013, we had approximately 3,085 employees, including 676 full-time faculty and 676 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 2014 and 2017. We believe that we have good relationships with these unions and our employees.

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 and traditional four-year colleges or universities is limited. Thus, our main competitors are other for-profit, career-oriented schools, as well as public and private two-year junior and community colleges. 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 schools, 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.

We compete with other institutions that are eligible to receive Title IV funding. This includes four-year, not-for-profit public and private colleges and universities, community colleges and all for-profit institutions whether they are four years, two years or less. Our competition differs in each market depending on the curriculum that we offer. For example, a school offering automotive, allied health and skilled trades programs will have a different group of competitors than a school offering allied health, 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 learning, the number of competitors in each market has increased because students can now attend classes from an online institution.

Our primary competition for students are community colleges and other career schools, both for-profit and not-for-profit. We focus on programs that are in high demand. We compete against community colleges by seeking to offer more frequent start dates, more flexible hours, better instructional resources, more hands on training, shorter program length and greater assistance with job placement. We compete against the other career schools by seeking to offer a higher quality of education, higher quality instructional equipment and a better overall value. On average, each of our schools has at least three direct competitors and at least a dozen indirect competitors. As we continue to add courses and degree programs, our competitors within a given market increase.

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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 effect 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 federal programs of student financial aid authorized under Title IV of the Higher Education Act of 1965, as amended (“Title IV Programs”), which are administered by the DOE. For the year ended December 31, 2013, approximately 80% (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. Student financial aid funds are generally made available to students at prescribed intervals throughout their predetermined expected length of study. Students typically use the funds received from the federal financial aid programs to pay their tuition and fees and, in some cases, for living expenses or other costs of attendance.

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.

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. Some states have sought to assert jurisdiction over online educational institutions that offer educational services to residents in the state or to institutions that advertise or recruit in the state, notwithstanding the lack of a physical location in that state. State regulatory requirements for online education vary among the states, are not well developed in many states, are imprecise or unclear in some states, and are subject to change. 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

material adverse effect 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 \$16.9 million.

The DOE published new regulations that took effect on July 1, 2011 (the “2011 DOE Rules”), and that expand 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 will require 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.

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In addition, the 2011 DOE Rules also required institutions offering postsecondary education through distance education, such as online programs, to students in a state in which the institution is not physically located or in which it is otherwise subject to state jurisdiction as determined by the state to meet any state requirements for it to be legally offering postsecondary distance education in that state. The regulations required an institution to document upon request by the DOE that it has the applicable state approval.

In June 2012, the United States Court of Appeals for the District of Columbia vacated the 2011 DOE Rules with respect to state authorization of distance education. The DOE issued a Dear Colleague Letter acknowledging the decision of the Court of Appeals and stating that the DOE would not enforce the requirements of the regulation and commenting that institutions continue to be responsible for complying with all state laws as they relate to distance education. However, the DOE has announced its intent to consider new regulations regarding state authorization for programs offered through distance education beginning with a negotiated rulemaking committee convening in February 2014. See “– Regulatory Environment – DOE Development of New Regulations.”

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, that school and its related main campus and/or additional locations would lose their eligibility to participate in Title IV Programs, be unable to offer their programs and we could be forced to close those 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 material adverse effect 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, 2013, 17 of our campuses are accredited by the Accrediting Commission of Career Schools and Colleges, or ACCSC; 19 of our campuses are accredited by the Accrediting Council for Independent Colleges and Schools, or ACICS; one of our campuses is accredited by the New England Association of Schools and Colleges of Technology, or NEASC; and one of our campuses is accredited by the Accrediting Bureau of Health Education Schools, or ABHES. All of these accrediting commissions are recognized by the DOE. 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