

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

**Form 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2020

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 000-51371

**LINCOLN EDUCATIONAL SERVICES CORPORATION**

(Exact name of registrant as specified in its charter)

New Jersey

(State or other jurisdiction of incorporation or organization)

57-1150621

(IRS Employer Identification No.)

200 Executive Drive, Suite 340  
West Orange, NJ

(Address of principal executive offices)

07052

(Zip Code)

(973) 736-9340

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No   
Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value per share	LINC	The NASDAQ Stock Market LLC

As of August 11, 2020, there were 26,400,782 shares of the registrant's common stock outstanding.

## INDEX TO FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2020

<b>PART I.</b>	<b>FINANCIAL INFORMATION</b>	
Item 1.	<a href="#">Financial Statements (Unaudited)</a>	1
	<a href="#">Condensed Consolidated Balance Sheets at June 30, 2020 and December 31, 2019</a>	1
	<a href="#">Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2020 and 2019</a>	3
	<a href="#">Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended June 30, 2020 and 2019</a>	4
	<a href="#">Condensed Consolidated Statements of Changes in Convertible Preferred Stock and Stockholders' Equity for the three and six months ended June 30, 2020 and 2019</a>	5
	<a href="#">Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2020 and 2019</a>	6
	<a href="#">Notes to Unaudited Condensed Consolidated Financial Statements</a>	8
Item 2.	<a href="#">Management's Discussion and Analysis of Financial Condition and Results of Operations</a>	25
Item 4.	<a href="#">Controls and Procedures</a>	40
<b>PART II.</b>	<b>OTHER INFORMATION</b>	40
Item 1.	<a href="#">Legal Proceedings</a>	40
Item 1A.	<a href="#">Risk Factors</a>	40
Item 6.	<a href="#">Exhibits</a>	41
	<a href="#">SIGNATURES</a>	42

---

**PART I – FINANCIAL INFORMATION**

## Item 1. Financial Statements

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share amounts)  
(Unaudited)

	<u>June 30,</u> <u>2020</u>	<u>December 31,</u> <u>2019</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 23,342	\$ 23,644
Restricted cash	2,626	-
Accounts receivable, less allowance of \$20,661 and \$18,107 at June 30, 2020 and December 31, 2019, respectively	27,906	20,652
Inventories	3,107	1,608
Prepaid income taxes and income taxes receivable	277	383
Prepaid expenses and other current assets	3,748	4,190
Total current assets	<u>61,006</u>	<u>50,477</u>
<b>PROPERTY, EQUIPMENT AND FACILITIES - At cost, net of accumulated depreciation and amortization of \$175,183 and \$172,408 at June 30, 2020 and December 31, 2019, respectively</b>	<u>49,172</u>	<u>49,345</u>
<b>OTHER ASSETS:</b>		
Noncurrent restricted cash	-	15,000
Noncurrent receivables, less allowance of \$2,932 and \$2,260 at June 30, 2020 and December 31, 2019, respectively	15,787	15,337
Operating lease right-of-use assets	53,397	49,065
Goodwill	14,536	14,536
Other assets, net	1,003	1,003
Total other assets	<u>84,723</u>	<u>94,941</u>
<b>TOTAL ASSETS</b>	<u>\$ 194,901</u>	<u>\$ 194,763</u>

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share amounts)  
(Unaudited)  
(Continued)

	<u>June 30,</u> <u>2020</u>	<u>December 31,</u> <u>2019</u>
<b>LIABILITIES, SERIES A CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current portion of credit agreement	\$ 2,000	\$ 2,000
Unearned tuition	17,573	23,411
Accounts payable	14,058	14,584
Accrued expenses	12,162	7,869
CARES Act student funds liability	2,626	-
CARES Act institutional funds liability	11,837	-
Current portion of operating lease liabilities	8,222	9,142
Other short-term liabilities	93	199
<b>Total current liabilities</b>	<b>68,571</b>	<b>57,205</b>
<b>NONCURRENT LIABILITIES:</b>		
Long-term credit agreement and term loan	16,121	32,028
Pension plan liabilities	3,850	4,015
Deferred income taxes, net	153	153
Long-term portion of operating lease liabilities	51,148	46,018
Other long-term liabilities	1,014	214
<b>Total liabilities</b>	<b>140,857</b>	<b>139,633</b>
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>SERIES A CONVERTIBLE PREFERRED STOCK</b>		
Preferred stock, no par value - 10,000,000 shares authorized, Series A convertible preferred shares, 12,700 shares issued and outstanding at June 30, 2020 and December 31, 2019	11,982	11,982
<b>STOCKHOLDERS' EQUITY:</b>		
Common stock, no par value - authorized: 100,000,000 shares at June 30, 2020 and December 31, 2019; issued and outstanding: 32,386,438 shares at June 30, 2020 and 31,142,251 shares at December 31, 2019	141,377	141,377
Additional paid-in capital	30,589	30,145
Treasury stock at cost - 5,910,541 shares at June 30, 2020 and December 31, 2019	(82,860)	(82,860)
Accumulated deficit	(43,025)	(42,058)
Accumulated other comprehensive loss	(4,019)	(3,456)
<b>Total stockholders' equity</b>	<b>42,062</b>	<b>43,148</b>
<b>TOTAL LIABILITIES, SERIES A CONVERTIBLE PREFERRED STOCK AND EQUITY</b>	<b>\$ 194,901</b>	<b>\$ 194,763</b>

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share amounts)  
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
REVENUE	\$ 62,470	\$ 63,569	\$ 132,511	\$ 126,833
COSTS AND EXPENSES:				
Educational services and facilities	26,245	29,749	56,482	59,728
Selling, general and administrative	35,162	35,913	76,310	74,062
(Gain) loss on disposition of assets	(97)	-	(96)	1
Total costs & expenses	61,310	65,662	132,696	133,791
OPERATING INCOME (LOSS)	1,160	(2,093)	(185)	(6,958)
OTHER:				
Interest income	-	2	-	7
Interest expense	(327)	(829)	(682)	(1,386)
INCOME (LOSS) BEFORE INCOME TAXES	833	(2,920)	(867)	(8,337)
PROVISION FOR INCOME TAXES	50	144	100	194
NET INCOME (LOSS)	\$ 783	\$ (3,064)	\$ (967)	\$ (8,531)
Basic				
Net income (loss) per common share	\$ 0.02	\$ (0.12)	\$ (0.06)	\$ (0.35)
Diluted				
Net income (loss) per common share	\$ 0.02	\$ (0.12)	\$ (0.06)	\$ (0.35)
Weighted average number of common shares outstanding:				
Basic	24,741	24,555	24,670	24,545
Diluted	24,741	24,555	24,670	24,545

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
**(In thousands)**  
**(Unaudited)**

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2020	2019	2020	2019
Net income (loss)	\$ 783	\$ (3,064)	\$ (967)	\$ (8,531)
Other comprehensive income				
Derivative qualifying as a cash flow hedge, net of taxes (nil)	(95)	-	(843)	-
Employee pension plan adjustments, net of taxes (nil)	140	154	280	308
Comprehensive income (loss)	<u>\$ 828</u>	<u>\$ (2,910)</u>	<u>\$ (1,530)</u>	<u>\$ (8,223)</u>

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN CONVERTIBLE PREFERRED STOCK AND**  
**STOCKHOLDERS' EQUITY**  
(In thousands, except share amounts)  
(Unaudited)

	Stockholders' Equity							Series A Convertible Preferred Stock		
	Common Stock		Additional Paid-in Capital	Treasury Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss				Total
	Shares	Amount				Loss	Total			
BALANCE - January 1, 2020	31,142,251	\$ 141,377	\$ 30,145	\$ (82,860)	\$ (42,058)	\$ (3,456)	\$ 43,148	12,700	\$ 11,982	
Net loss	-	-	-	-	(1,750)	-	(1,750)	-	-	
Employee pension plan adjustments	-	-	-	-	-	140	140	-	-	
Derivative qualifying as cash flow hedge	-	-	-	-	-	(748)	(748)	-	-	
Stock-based compensation expense										
Restricted stock	1,191,262	-	291	-	-	-	291	-	-	
Net share settlement for equity-based compensation	(58,451)	-	(172)	-	-	-	(172)	-	-	
BALANCE - March 31, 2020	<u>32,275,062</u>	<u>141,377</u>	<u>30,264</u>	<u>(82,860)</u>	<u>(43,808)</u>	<u>(4,064)</u>	<u>40,909</u>	<u>12,700</u>	<u>11,982</u>	
Net income	-	-	-	-	783	-	783	-	-	
Employee pension plan adjustments	-	-	-	-	-	140	140	-	-	
Derivative qualifying as cash flow hedge	-	-	-	-	-	(95)	(95)	-	-	
Stock-based compensation expense										
Restricted stock	111,376	-	325	-	-	-	325	-	-	
Net share settlement for equity-based compensation	-	-	-	-	-	-	-	-	-	
BALANCE - June 30, 2020	<u>32,386,438</u>	<u>\$ 141,377</u>	<u>\$ 30,589</u>	<u>\$ (82,860)</u>	<u>\$ (43,025)</u>	<u>\$ (4,019)</u>	<u>\$ 42,062</u>	<u>12,700</u>	<u>\$ 11,982</u>	

	Stockholders' Equity							Series A Convertible Preferred Stock		
	Common Stock		Additional Paid-in Capital	Treasury Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss				Total
	Shares	Amount				Loss	Total			
BALANCE - January 1, 2019	30,552,333	\$ 141,377	\$ 29,484	\$ (82,860)	\$ (44,073)	\$ (4,062)	\$ 39,866	-	\$ -	
Net loss	-	-	-	-	(5,467)	-	(5,467)	-	-	
Employee pension plan adjustments	-	-	-	-	-	154	154	-	-	
Stock-based compensation expense										
Restricted stock	478,853	-	52	-	-	-	52	-	-	
Net share settlement for equity-based compensation	(5,518)	-	(18)	-	-	-	(18)	-	-	
BALANCE - March 31, 2019	<u>31,025,668</u>	<u>141,377</u>	<u>29,518</u>	<u>(82,860)</u>	<u>(49,540)</u>	<u>(3,908)</u>	<u>34,587</u>	<u>-</u>	<u>-</u>	
Net loss	-	-	-	-	(3,064)	-	(3,064)	-	-	
Employee pension plan adjustments	-	-	-	-	-	154	154	-	-	
Stock-based compensation expense										
Restricted stock	116,583	-	191	-	-	-	191	-	-	
Net share settlement for equity-based compensation	-	-	-	-	-	-	-	-	-	
BALANCE - June 30, 2019	<u>31,142,251</u>	<u>\$ 141,377</u>	<u>\$ 29,709</u>	<u>\$ (82,860)</u>	<u>\$ (52,604)</u>	<u>\$ (3,754)</u>	<u>\$ 31,868</u>	<u>-</u>	<u>\$ -</u>	

See notes to unaudited condensed consolidated financial statements.

LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)  
(Unaudited)

	Six Months Ended June 30,	
	2020	2019
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (967)	\$ (8,531)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,763	3,989
Amortization of deferred finance charges	90	194
Deferred income taxes	-	424
(Gain) loss on disposition of assets	(96)	1
Fixed asset donations	(334)	(893)
Provision for doubtful accounts	12,618	8,923
Stock-based compensation expense	616	242
(Increase) decrease in assets:		
Accounts receivable	(20,322)	(13,818)
Inventories	(1,499)	(635)
Prepaid income taxes and income taxes receivable	106	(211)
Prepaid expenses and current assets	346	177
Other assets, net	(122)	(649)
Increase (decrease) in liabilities:		
Accounts payable	(615)	4,271
Accrued expenses	4,293	(470)
CARES Act student funds liability	2,626	-
CARES Act institutional funds liability	11,837	-
Unearned tuition	(5,838)	(2,829)
Deferred income taxes	-	93
Other liabilities	(34)	(1,060)
Total adjustments	<u>7,435</u>	<u>(2,251)</u>
Net cash provided by (used in) operating activities	<u>6,468</u>	<u>(10,782)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	(3,072)	(1,212)
Proceeds from insurance	97	-
Net cash used in investing activities	<u>(2,975)</u>	<u>(1,212)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payments on borrowings	(27,000)	(26,600)
Proceeds from borrowings	11,000	3,750
Credit (payment) of deferred finance fees	3	(98)
Net share settlement for equity-based compensation	(172)	(18)
Net cash used in financing activities	<u>(16,169)</u>	<u>(22,966)</u>
NET DECREASE IN CASH, CASH EQUIVALENTS AND RESTRICTED CASH	(12,676)	(34,960)
CASH, CASH EQUIVALENTS AND RESTRICTED CASH—Beginning of period	38,644	45,946
CASH, CASH EQUIVALENTS AND RESTRICTED CASH—End of period	<u>\$ 25,968</u>	<u>\$ 10,986</u>

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(In thousands)**  
**(Unaudited)**  
**(Continued)**

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2020</b>	<b>2019</b>
	<u>          </u>	<u>          </u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Cash paid for:		
Interest	\$ 589	\$ 1,073
Income taxes	\$ 14	\$ 99
<b>SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:</b>		
Liabilities accrued for or noncash purchases of fixed assets	\$ 614	\$ 1,030

See notes to unaudited condensed consolidated financial statements.

**LINCOLN EDUCATIONAL SERVICES CORPORATION AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**THREE AND SIX MONTHS ENDED JUNE 30, 2020 AND 2019**  
**(In thousands, except share and per share amounts and unless otherwise stated)**  
**(Unaudited)**

**1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION**

**Business Activities**— Lincoln Educational Services Corporation and its subsidiaries (collectively, the “Company”, “we”, “our” and “us”, as applicable) provide diversified career-oriented post-secondary education to recent high school graduates and working adults. The Company, which currently operates 22 schools in 14 states, offers programs in automotive technology, skilled trades (which include HVAC, welding and computerized numerical control and electronic systems technology, among other programs), healthcare services (which include nursing, dental assistant and medical administrative assistant, among other programs), hospitality services (which include culinary, therapeutic massage, cosmetology and aesthetics) and information technology. The schools operate under Lincoln Technical Institute, Lincoln College of Technology, Lincoln Culinary Institute, and Euphoria Institute of Beauty Arts and Sciences and associated brand names. Most of the campuses serve major metropolitan markets and each typically offers courses in multiple areas of study. Five of the campuses are destination schools, which attract students from across the United States and, in some cases, from abroad. The Company’s other campuses primarily attract students from their local communities and surrounding areas. All of the campuses are nationally or regionally accredited and are eligible to participate in federal financial aid programs by the U.S. Department of Education (the “DOE”) and applicable state education agencies and accrediting commissions which allow students to apply for and access federal student loans as well as other forms of financial aid.

The Company’s business is organized into three reportable business segments: (a) Transportation and Skilled Trades, (b) Healthcare and Other Professions (“HOPS”), and (c) Transitional, which refers to our campus operations which have been closed.

**COVID-19 Pandemic**— During the first quarter of 2020, the coronavirus disease (“COVID-19”) began to spread worldwide and has caused significant disruptions to the U.S. and world economies. In early March 2020, the Company began seeing the impact of the COVID-19 pandemic on our business. The impact was primarily related to transitioning classes from in-person, hands-on learning to online, remote learning. As part of this transition, the Company has incurred additional expenses. In addition, some students have been placed on leave of absence as they could not complete their externships and some students chose not to participate in online learning. Additionally, certain programs were extended due to restricted access to externship sites and classroom labs. Due to phased re-opening on a state-by-state basis, our schools have been reopening since May 2020 and, currently, all of our schools have re-opened and we expect the majority of the students who were placed on leave or otherwise deferred their programs to finish their programs now. As COVID-19 continues to affect many states and its course is unpredictable, the full impact on the Company’s consolidated financial statements remains uncertain.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”) was signed into law. The Company has and will continue to evaluate the impact of the CARES Act on the results of operations and cash flows. See Note 12 – *COVID-19 Pandemic and Cares Act* included elsewhere in this Quarterly Report on Form 10-Q for additional discussion about the CARES Act.

**Liquidity**— As of June 30, 2020, the Company had a net cash balance of \$7.8 million calculated as cash, cash equivalents and restricted cash less both the short-term and long-term portion of the Company’s Credit Facility (defined below). Excluding cash in the bank from the Cares Act of \$14.5 million, as of June 30, 2020, the Company had a net debt balance of \$6.6 million. At June 30, 2020, the Company’s sources of cash primarily included cash, cash equivalents and restricted cash of \$26.0 million including cash received under the Cares Act of \$14.5 million. In addition, the Company has availability to borrow additional funds under its Credit Facility for an additional \$21.0 million. As of December 31, 2019, the Company had a net cash balance of \$4.6 million. The Company believes that its likely sources of cash should be sufficient to fund operations for the next twelve months and thereafter for the foreseeable future. However, the circumstances relating to COVID-19 and its evolution make any prediction impossible and, if circumstances surrounding COVID-19 should evolve in a significantly adverse manner it is possible our liquidity could be materially and adversely affected.

**Basis of Presentation** – The accompanying unaudited condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial statements. Certain information and footnote disclosures normally included in annual financial statements have been omitted or condensed pursuant to such regulations. These statements, which should be read in conjunction with the December 31, 2019 consolidated financial statements and related disclosures of the Company included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2019, reflect all adjustments, consisting of normal recurring adjustments necessary to present fairly the consolidated financial position, results of operations and cash flows for such periods. The results of operations for the three and six months ended June 30, 2020 are not necessarily indicative of the results that may be expected for the full fiscal year ending December 31, 2020.

The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

**Use of Estimates in the Preparation of Financial Statements** – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. On an ongoing basis, the Company evaluates the estimates and assumptions, including those used to determine the incremental borrowing rate to calculate lease liabilities and right-of-use (“ROU”) assets, lease term to calculate lease cost, revenue recognition, bad debts, impairments, useful lives of fixed assets, income taxes, benefit plans and certain accruals. Actual results could differ from those estimates.

**New Accounting Pronouncements** – In March 2020, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2020-03, “*Codification Improvements to Financial Instruments*” (“ASU 2020-03”). ASU 2020-03 improves and clarifies various financial instruments topics. ASU 2020-03 includes seven different issues that describe the areas of improvement and the related amendments to GAAP. The Company adopted ASU 2020-03 upon issuance, which did not have a material effect on the Company’s condensed consolidated financial statements and related disclosures.

In December 2019, the FASB issued ASU 2019-12, “*Simplifying the Accounting for Income Taxes*”, which simplifies the accounting for income taxes by removing certain exceptions to the general principles of ASC 740, “*Income Taxes*”. The amendments also improve consistent application of and simplify GAAP for other areas of Topic 740 by clarifying and amending existing guidance. This ASU is effective for fiscal years beginning after December 15, 2020 and early adoption is permitted. Depending on the amendment, adoption may be applied on a retrospective, modified retrospective or prospective basis. The Company is currently assessing the effect that this ASU will have on its condensed consolidated financial statements and related disclosures.

In August 2018, the FASB issued ASU 2018-14, “*Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*”. This ASU adds, modifies and clarifies several disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance is effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The Company is currently assessing the effect that this ASU will have on its condensed consolidated financial statements and related disclosures.

In June 2016, the FASB issued ASU 2016-13, “*Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*” and subsequently issued additional guidance that modified ASU 2016-13. ASU 2016-13 and the subsequent modifications are identified as Accounting Standards Codification (“ASC”) 326. The standard requires an entity to change its accounting approach in determining impairment of certain financial instruments, including trade receivables, from an “incurred loss” to a “current expected credit loss” model. Further, the FASB issued ASU No. 2019-04, ASU No. 2019-05 and ASU 2019-11 to provide additional guidance on the credit losses standard. In November 2019, FASB issued ASU No. 2019-10, “*Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*”. This ASU defers the effective date of ASU 2016-13 for public companies that are considered smaller reporting companies as defined by the SEC to fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. Additionally, in February and March 2020, the FASB issued ASU 2020-02, “*Financial Instruments—Credit Losses (Topic 326) and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, Leases (Topic 842)*” ASU 2020-02 adds a SEC paragraph pursuant to the issuance of SEC Staff Accounting Bulletin No. 119 on loan losses to FASB Codification Topic 326 and also updates the SEC section of the Codification for the change in the effective date of Topic 842. Early adoption is permitted. We are currently assessing the effect that this ASC will have on our condensed consolidated financial statements and related disclosures.

**Income Taxes** – The Company accounts for income taxes in accordance with ASC Topic 740, “*Income Taxes*”. This statement requires an asset and a liability approach for measuring deferred taxes based on temporary differences between the financial statement and tax bases of assets and liabilities existing at each balance sheet date using enacted tax rates for years in which taxes are expected to be paid or recovered.

In accordance with ASC 740, the Company assesses our deferred tax asset to determine whether all or any portion of the asset is more likely than not unrealizable. A valuation allowance is required to be established or maintained when, based on currently available information, it is more likely than not that all or a portion of a deferred tax asset will not be realized. In accordance with ASC 740, our assessment considers whether there has been sufficient income in recent years and whether sufficient income is expected in future years in order to utilize the deferred tax asset. In evaluating the realizability of deferred income tax assets, the Company considered, among other things, historical levels of income, expected future income, the expected timing of the reversals of existing temporary reporting differences, and the expected impact of tax planning strategies that may be implemented to prevent the potential loss of future income tax benefits. Significant judgment is required in determining the future tax consequences of events that have been recognized in our consolidated financial statements and/or tax returns. Differences between anticipated and actual outcomes of these future tax consequences could have a material impact on the Company’s consolidated financial position or results of operations. Changes in, among other things, income tax legislation, statutory income tax rates, or future income levels could materially impact the Company’s valuation of income tax assets and liabilities and could cause our income tax provision to vary significantly among financial reporting periods.

During the three and six months ended June 30, 2020 and 2019, the Company did not recognize any interest and penalties expense associated with uncertain tax positions.

See Note 12 – *COVID-19 Pandemic and Cares Act* included in this Quarterly Report on Form 10-Q for additional discussion about the CARES Act impact on taxes.

**Derivative Instruments**—The Company records the fair value of derivative instruments as either assets or liabilities on the balance sheet. The accounting for gains and losses resulting from changes in fair value is dependent on the use of the derivative and whether it is designated and qualifies for hedge accounting.

All qualifying hedging activities are documented at the inception of the hedge and must meet the definition of highly effective in offsetting changes to future cash. The Company utilizes the change in variable cash flows method to evaluate hedge effectiveness quarterly. We record the fair value of the qualifying hedges in other long-term liabilities (for derivative liabilities) and other assets (for derivative assets). All unrealized gains and losses on derivatives that are designated and qualify for hedge accounting are reported in other comprehensive income (loss) and recognized when the underlying hedged transaction affects earnings. Changes in the fair value of these derivatives are recognized in other comprehensive income (loss). The Company classifies the cash flows from a cash flow hedge within the same category as the cash flows from the items being hedged.

The Company adopted ASU 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, on January 1, 2019, which changes the recognition and presentation requirements of hedge accounting, including eliminating the requirement to separately measure and report hedge ineffectiveness and presenting all items that affect earnings in the same income statement line item as the hedged item. The ASU also provides new alternatives for applying hedge accounting to additional hedging strategies, measuring the hedged item in fair value hedges of interest rate risk, reducing the cost and complexity of applying hedge accounting by easing the requirements for effectiveness testing, hedge documentation and application of the critical terms match method and reducing the risk of a material error correction if a company applies the shortcut method inappropriately. The adoption of ASU 2017-12 had no impact on the Company's consolidated financial statements.

## 2. EARNINGS PER SHARE

The Company presents basic and diluted earnings (loss) per common share using the two-class method which requires all outstanding Series A Preferred Stock and unvested restricted stock that contain rights to non-forfeitable dividends and therefore participate in undistributed earnings with common shareholders be included in computing earnings per share. Under the two-class method, net income is reduced by the amount of dividends declared in the period for each class of common stock and participating security. The remaining undistributed earnings are then allocated to common stock and participating securities, based on their respective rights to receive dividends. Series A Preferred Stock and unvested restricted stock contain non-forfeitable rights to dividends on an if-converted basis and on the same basis as common shares, respectively, and are considered participating securities. The Series A Preferred Stock and unvested restricted stock are not included in the computation of basic earnings (loss) per common share in periods in which we have a net loss, as the Series A Preferred Stock and unvested restricted stock are not contractually obligated to share in our net losses. However, the cumulative dividends on preferred stock for the period decreases the income or increases the net loss allocated to common shareholders. Basic earnings (loss) per common share has been computed by dividing net income (loss) allocated to common shareholders by the weighted-average number of common shares outstanding.

The basic and diluted net loss amounts are the same for the six months ended June 30, 2020 and 2019 as a result of the net loss and anti-dilutive impact of the potentially dilutive securities. The basic and diluted net loss amounts are the same for the three months ended June 30, 2019 as a result of the net loss and anti-dilutive impact of the potentially dilutive securities. For the three and six months ended June 30, 2019 earnings (loss) per share was calculated using the treasury stock method. Dilutive potential common shares include outstanding stock options, unvested restricted stock and Series A Preferred Stock. The Company uses the more dilutive method of calculating the diluted earnings per share by applying the more dilutive of either (a) the treasury stock method, if-converted method, or (b) the two-class method in its diluted EPS calculation. Potentially dilutive shares are determined by applying the treasury stock method to the assumed exercise of outstanding stock options and the assumed vesting of restricted stock. Potentially dilutive shares issuable upon conversion of the Series A Preferred Stock are calculated using the if-converted method.

The following is a reconciliation of the numerator and denominator of the diluted net income (loss) per share computations for the periods presented below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
<i>(in thousands, except share data)</i>				
<b>Numerator:</b>				
Net income (loss)	\$ 783	\$ (3,064)	\$ (967)	\$ (8,531)
Less: preferred stock dividend	(305)	-	(610)	-
Less: allocation to preferred stockholders	(83)	-	-	-
Less: allocation to restricted stockholders	(23)	-	-	-
Net income (loss) allocated to common stockholders	<u>\$ 372</u>	<u>\$ (3,064)</u>	<u>\$ (1,577)</u>	<u>\$ (8,531)</u>
<b>Basic loss per share:</b>				
<b>Denominator:</b>				
Weighted average common shares outstanding	24,741,331	24,555,435	24,669,838	24,544,879
Basic income (loss) per share	<u>\$ 0.02</u>	<u>\$ (0.12)</u>	<u>\$ (0.06)</u>	<u>\$ (0.35)</u>
<b>Diluted loss per share:</b>				
<b>Denominator:</b>				
Weighted average number of:				
Common shares outstanding	24,741,331	24,555,435	24,669,838	24,544,879
Dilutive potential common shares outstanding:				
Series A Preferred Stock	-	-	-	-
Unvested restricted stock	-	-	-	-
Stock options	-	-	-	-
Dilutive shares outstanding	<u>24,741,331</u>	<u>24,555,435</u>	<u>24,669,838</u>	<u>24,544,879</u>
Diluted income (loss) per share	<u>\$ 0.02</u>	<u>\$ (0.12)</u>	<u>\$ (0.06)</u>	<u>\$ (0.35)</u>

The following table summarizes the potential weighted average shares of common stock that were excluded from the determination of our diluted shares outstanding as they were anti-dilutive:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
<i>(in thousands, except share data)</i>				
Series A Preferred Stock	5,577,955	-	5,513,379	-
Unvested restricted stock	319,461	61,138	466,581	118,348
	<u>5,897,416</u>	<u>61,138</u>	<u>5,979,960</u>	<u>118,348</u>

### 3. REVENUE RECOGNITION

Substantially all of our revenues are considered to be revenues from contracts with students. The related accounts receivable balances are recorded in our balance sheets as student accounts receivable. We do not have significant revenue recognized from performance obligations that were satisfied in prior periods, and we do not have any transaction price allocated to unsatisfied performance obligations other than in our unearned tuition. We record revenue for students who withdraw from our schools only to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur. Unearned tuition represents contract liabilities primarily related to our tuition revenue. We have elected not to provide disclosure about transaction prices allocated to unsatisfied performance obligations if original contract durations are less than one-year, or if we have the right to consideration from a student in an amount that corresponds directly with the value provided to the student for performance obligations completed to date in accordance with ASC 606. We have assessed the costs incurred to obtain a contract with a student and determined them to be immaterial.

Unearned tuition in the amount of \$17.6 million and \$23.4 million is recorded in the current liabilities section of the accompanying condensed consolidated balance sheets as of June 30, 2020 and December 31, 2019, respectively. The change in this contract liability balance during the six-month period ended June 30, 2020 is the result of payments received in advance of satisfying performance obligations, offset by revenue recognized during that period. Revenue recognized for the six-month period ended June 30, 2020 that was included in the contract liability balance at the beginning of the year was \$22.2 million.

The following table depicts the timing of revenue recognition:

	Three months ended June 30, 2020			Six months ended June 30, 2020		
	Transportation and Skilled Trades Segment	Healthcare and Other Professions Segment	Consolidated	Transportation and Skilled Trades Segment	Healthcare and Other Professions Segment	Consolidated
<b>Timing of Revenue Recognition</b>						
Services transferred at a point in time	\$ 2,038	\$ 939	\$ 2,977	\$ 4,536	\$ 2,013	\$ 6,549
Services transferred over time	40,877	18,616	59,493	87,435	38,527	125,962
Total revenues	<u>\$ 42,915</u>	<u>\$ 19,555</u>	<u>\$ 62,470</u>	<u>\$ 91,971</u>	<u>\$ 40,540</u>	<u>\$ 132,511</u>

	Three months ended June 30, 2019			Six months ended June 30, 2019		
	Transportation and Skilled Trades Segment	Healthcare and Other Professions Segment	Consolidated	Transportation and Skilled Trades Segment	Healthcare and Other Professions Segment	Consolidated
<b>Timing of Revenue Recognition</b>						
Services transferred at a point in time	\$ 2,487	\$ 1,159	\$ 3,646	\$ 4,568	\$ 2,233	\$ 6,801
Services transferred over time	41,541	18,382	59,923	83,786	36,246	120,032
Total revenues	<u>\$ 44,028</u>	<u>\$ 19,541</u>	<u>\$ 63,569</u>	<u>\$ 88,354</u>	<u>\$ 38,479</u>	<u>\$ 126,833</u>

#### 4. LEASES

The Company determines if an arrangement is a lease at inception. The Company considers any contract where there is an identified asset and that it has the right to control the use of such asset in determining whether the contract contains a lease. An operating lease ROU asset represents the Company's right to use an underlying asset for the lease term and lease liabilities represent its obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are to be recognized at commencement date based on the present value of lease payments over the lease term. As all of the Company's operating leases do not provide an implicit rate, the Company uses an incremental borrowing rate based on the information available on the adoption date in determining the present value of lease payments. We estimate the incremental borrowing rate based on a yield curve analysis, utilizing the interest rate derived from the fair value analysis of our credit facility and adjusting it for factors that appropriately reflect the profile of secured borrowing over the expected term of the lease. The operating lease ROU assets include any lease payments made prior to the rent commencement date and exclude lease incentives. Our leases have remaining lease terms of one year to 11 years. Lease terms may include options to extend the lease term used in determining the lease obligation when it is reasonably certain that the Company will exercise that option. Lease expense for lease payments are recognized on a straight-line basis over the lease term for operating leases.

Our operating lease cost for the three months ended June 30, 2020 and 2019, was \$3.7 and \$3.6 million, respectively. Our operating lease cost for the six months ended June 30, 2020 and 2019, was \$7.4 and \$7.3 million, respectively. Our variable lease cost for the three and six months ended June 30, 2020 was \$0.5 million. The net change in the ROU asset and lease liability are included in other assets in the condensed consolidated cash flows for the six months ended June 30, 2020 and 2019.

During the three months ended June 30, 2020, the Company has withheld portions of and/or delayed payments to certain of its landlords as the Company sought to renegotiate payment terms, in order to further maintain liquidity given the temporary closures of its facilities. In some instances, the negotiations with landlords have already led to agreements with landlords for rent abatements or rental deferrals, while, in other cases, negotiations are ongoing. Total payments withheld or deferred as of June 30, 2020 were approximately \$1.2 million and are included in current liabilities.

In accordance with the FASB's recent Staff Q&A regarding rent concessions related to the effects of the COVID-19 pandemic, the Company has elected to account for agreed concessions by landlords that do not result in a substantial increase in the rights of the landlord or the obligations of the Company, as lessee, as though enforceable rights and obligations for those concessions existed in the original lease agreements and the Company has elected not to re-measure the related lease liabilities and right-of-use assets. For qualifying rent abatement concessions, the Company has recorded negative lease expense for the amount of the concession during the period of relief, and for qualifying deferrals of rental payments, the Company has recognized a payable in lieu of recognizing a decrease in cash for the lease payment that would have been made based on the original terms of the lease agreement, which will be reduced when the deferred payment is made in the future. During the three months ended June 30, 2020, the Company recognized \$0.5 million of negative lease expense related to rent abatement concessions.

Supplemental cash flow information and non-cash activity related to our operating leases are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
<b>Operating cash flow information:</b>				
Cash paid for amounts included in the measurement of operating lease liabilities	\$ 3,802	\$ 3,821	\$ 7,643	\$ 7,603
<b>Non-cash activity:</b>				
Lease liabilities arising from obtaining right-of-use assets	\$ 8,731	\$ 657	\$ 8,781	\$ 48,634

As of June 30, 2020 there were lease re-measurements of \$8.7 million.

Weighted-average remaining lease term and discount rate for our operating leases is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Weighted-average remaining lease term	6.39 years	5.63 years	6.39 years	5.63 years
Weighted-average discount rate	11.94%	14.43%	11.94%	14.43%

Maturities of lease liabilities by fiscal year for our operating leases as of June 30, 2020 are as follows:

Year ending December 31.

2020 (excluding the six months ended June 30, 2020)	\$ 7,691
2021	14,045
2022	13,553
2023	11,926
2024	10,689
2025	9,116
Thereafter	17,196
Total lease payments	84,216
Less: imputed interest	(24,846)
Present value of lease liabilities	\$ 59,370

## 5. GOODWILL AND LONG-LIVED ASSETS

The Company reviews long-lived assets for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. There were no long-lived asset impairments during the six months ended June 30, 2020 and 2019.

The Company reviews goodwill for impairment when indicators of impairment exist. Annually, or more frequently if necessary, the Company evaluates goodwill for impairment, with any resulting impairment reflected as an operating expense. The Company has concluded that, as of June 30, 2020, there were no indicators of potential impairment and, accordingly, the Company did not test goodwill for impairment.

The carrying amount of goodwill at June 30, 2020 and 2019 is as follows:

	Gross Goodwill Balance	Accumulated Impairment Losses	Net Goodwill Balance
Balance as of January 1, 2020	\$ 117,176	\$ (102,640)	\$ 14,536
Adjustments	-	-	-
Balance as of June 30, 2020	<u>\$ 117,176</u>	<u>\$ (102,640)</u>	<u>\$ 14,536</u>

	Gross Goodwill Balance	Accumulated Impairment Losses	Net Goodwill Balance
Balance as of January 1, 2019	\$ 117,176	\$ (102,640)	\$ 14,536
Adjustments	-	-	-
Balance as of June 30, 2019	<u>\$ 117,176</u>	<u>\$ (102,640)</u>	<u>\$ 14,536</u>

As of June 30, 2020 and 2019, the goodwill balance is related to the Transportation and Skilled Trades segment.

## 6. LONG-TERM DEBT

Long-term debt consists of the following:

	June 30, 2020	December 31, 2019
Credit agreement	\$ 18,833	\$ 34,833
Deferred Financing Fees	(712)	(805)
	18,121	34,028
Less current maturities	(2,000)	(2,000)
	<u>\$ 16,121</u>	<u>\$ 32,028</u>

### ***Credit Facility with Sterling National Bank***

On November 14, 2019, the Company entered into a new senior secured credit agreement (the “Credit Agreement”) with its lender, Sterling National Bank (the “Lender”), pursuant to which the Company obtained a new credit facility in the aggregate principal amount of up to \$60 million (the “Credit Facility”).

The Credit Facility is comprised of four facilities: a \$20 million senior secured term loan maturing on December 1, 2024 (the “Term Loan”), with monthly interest and principal payments based on 120-month amortization with the outstanding balance due on the maturity date; a \$10 million senior secured delayed draw term loan maturing on December 1, 2024 (the “Delayed Draw Term Loan”), with monthly interest payments for the first 18 months and thereafter monthly payments of interest and principal based on 120-month amortization and all balances due on the maturity date; a \$15 million senior secured committed revolving line of credit providing a sublimit of up to \$10 million for standby letters of credit maturing on November 13, 2022 (the “Revolving Loan”), with monthly payments of interest only; and a \$15 million senior secured non-restoring line of credit maturing on January 31, 2021 (the “Line of Credit Loan”). The Credit Agreement gives the Company the right to permanently terminate, in its entirety, the Revolving Loan or the Line of Credit Loan or permanently reduce the amount available for borrowing under the Revolving Loan or the Line of Credit Loan. In April 2020, the Company terminated the Line of Credit Loan.

The Credit Facility is secured by a first priority lien in favor of the Lender on substantially all of the personal property owned by the Company, as well as a pledge of the stock and other equity in the Company’s subsidiaries and mortgages on parcels of real property owned by the Company in Colorado, Tennessee and Texas, at which three of the Company’s schools are located, as well as a former school property owned by the Company located in Connecticut.

At the closing of the Credit Facility, the Lender advanced the Term Loan to the Company, the net proceeds of which was \$19.7 million after deduction of the Lender’s origination fee in the amount of \$0.3 million and other Lender fees and reimbursements to the Lender that are customary for facilities of this type. The Company used the net proceeds of the Term Loan, together with cash on hand, to repay the existing credit facility and transaction expenses.

Pursuant to the terms of the Credit Agreement, letters of credit issued under the Revolving Loan reduce dollar for dollar the availability of borrowings under the Revolving Loan. Borrowings under the Line of Credit Loan are to be secured by cash collateral.

Borrowing under the Delayed Draw Term Loan is available during the period commencing on the closing date of the Credit Facility and ending on May 31, 2021.

Accrued interest on each loan under the Credit Facility will be payable monthly in arrears. The Term Loan and the Delayed Draw Term Loan will bear interest at a floating interest rate based on the then one month London Interbank Offered Rate ("LIBOR") plus 3.50%. At the closing of the Credit Facility, the Company entered into a swap transaction with the Lender for 100% of the principal balance of the Term Loan, which matures on the same date as the Term Loan, pursuant to a swap agreement between the Company and the Lender. At the end of the borrowing availability period for the Delayed Draw Term Loan, the Company is required to enter into a swap transaction with the Lender for 100% of the principal balance of the Delayed Draw Term Loan, which will mature on the same date as the Delayed Draw Term Loan, pursuant to a swap agreement between the Company and the Lender or the Lender's affiliate. The Term Loan and Delayed Draw Term Loan are subject to a LIBOR interest rate floor of .25% if there is no swap agreement.

Revolving Loans bear interest at a floating interest rate based on the then LIBOR plus an indicative spread determined by the Company's leverage as defined in the Credit Agreement or, if the borrowing of a Revolving Loan is to be repaid within 30 days of such borrowing, the Revolving Loan will accrue interest at the Lender's prime rate plus .50% with a floor of 4.0%. Line of Credit Loans will bear interest at a floating interest rate based on the Lender's prime rate of interest. Revolving Loans are subject to a LIBOR interest rate floor of .00%.

Letters of credit will be charged an annual fee equal to (i) an applicable margin determined by the leverage ratio of the Company less (ii) .25%, paid quarterly in arrears, in addition to the Lender's customary fees for issuance, amendment and other standard fees. Letters of credit totaling \$4 million that were outstanding under the existing credit facility are treated as letters of credit under the Revolving Loan.

Under the terms of the Credit Agreement, the Company may prepay the Term Loan and/or the Delayed Draw Term Loan in full or in part without penalty except for any amount required to compensate the Lender for any swap breakage or other costs incurred in connection with such prepayment. The Lender receives an unused facility fee of 0.50% per annum payable quarterly in arrears on the unused portions of the Revolving Loan and the Line of Credit Loan.

In addition to the foregoing, the Credit Agreement contains customary representations, warranties and affirmative and negative covenants (including financial covenants that (i) restrict capital expenditures, (ii) restrict leverage, (iii) require maintaining minimum tangible net worth, (iv) require maintaining a minimum fixed charge coverage ratio and (v) require the maintenance of a minimum of \$5 million in quarterly average aggregate balances on deposit with the Lender, which, if not maintained, will result in the assessment of a quarterly fee of \$12,500), as well as events of default customary for facilities of this type. As of June 30, 2020, the Company was in compliance with all debt covenants.

As of June 30, 2020 and December 31, 2019, the Company had \$18.8 million and \$34.8 million, respectively, outstanding under the Credit Facility; offset by \$0.7 million and \$0.8 million of deferred finance fees, respectively. In January 2020, the Company repaid the \$15.0 million outstanding on the Line of Credit Loan. As of June 30, 2020 and December 31, 2019, letters of credit in the aggregate outstanding principal amount of \$4.0 million and \$4.0 million, respectively, were outstanding under the Credit Facility.

Scheduled maturities of long-term debt at June 30, 2020 are as follows:

<u>Year ending December 31,</u>	
2020	\$ 1,000
2021	2,000
2022	2,000
2023	2,000
2024	11,833
	<u>\$ 18,833</u>

## 7. STOCKHOLDERS' EQUITY

### **Common Stock**

Holders of our common stock are entitled to receive dividends when and as declared by our Board of Directors and have the right to one vote per share on all matters requiring shareholder approval. The Company has not declared or paid any cash dividends on our common stock since the Company's Board of Directors discontinued our quarterly cash dividend program in February 2015. The Company has no current intentions to resume the payment of cash dividends to holders of common stock in the foreseeable future.

### **Preferred Stock**

On November 14, 2019, the Company raised gross proceeds of \$12.7 million from the sale of 12,700 shares of its newly designated Series A 9.6% Convertible Preferred Stock, no par value per share (the "Series A Preferred Stock"). The Series A Preferred Stock was designated by the Company's Board of Directors pursuant to a certificate of amendment to the Company's amended and restated certificate of incorporation. The liquidation preference associated with the Series A Preferred Stock was \$1,000 per share at December 31, 2019. The Company incurred issuance cost of \$0.7 million as part of this transaction.

The description below provides a summary of certain material terms of the Series A Preferred Stock pursuant to the Securities Purchase Agreement and set forth in the Certificate of Amendment (the "Charter Amendment") affecting the Series A Preferred Stock:

#### **Securities Purchase Agreement.**

The Series A Preferred Stock was sold by the Company pursuant to a Securities Purchase Agreements dated as of November 14, 2019 (the "SPA") among the Company, Juniper Targeted Opportunity Fund, L.P. and Juniper Targeted Opportunities, L.P. (together, "Juniper Purchasers") and Talanta Investment, Inc. ("Talanta", together with Juniper Purchasers, the "Investors"). Among other things, the SPA includes covenants relating to the appointment of a director to the Company's Board of Directors to be selected solely by the holders of the Series A Preferred Stock.

**Dividends.** Dividends on the Series A Preferred Stock ("Series A Dividends"), at the initial annual rate of 9.6% is to be paid, in advance, from the date of issuance quarterly on each December 31, March 31, June 30 and September 30 with September 30, 2020 as the first dividend payment date. The Company, at its option, may pay dividends in cash or dividends will accrue and thereby increase the number of shares issuable upon conversion of the Series A Preferred Stock. The dividend rate is subject to increase (a) 2.4% per annum on the fifth anniversary of the issuance of the Series A Preferred Stock (b) by 2% per annum but in no event above 14% per annum should the Company fail to perform certain obligations under the Charter Amendment. The Series A Preferred Stock is not currently redeemable and it is not probable it will become redeemable in the future. As a result, the Company is not required to re-measure the Series A Preferred Stock and does not accrete changes in the redemption value. As of June 30, 2020, undeclared cumulative dividends are approximately \$0.8 million.

**Series A Preferred Stock Holders Right to Convert into Common Stock.** Each share of Series A Preferred Stock, at any time, is convertible into a number of shares of common stock equal to ("Convertible Formula") the quotient of (i) the sum of (A) \$1,000 (subject to adjustment as provided in the Charter Amendment) plus (B) the dollar amount of any declared Series A Dividends not paid in cash divided by (ii) the Series A Conversion Price (as defined and adjusted in the Charter Amendment) as of the applicable Conversion Date (as defined in the Charter Amendment). The initial Conversion Price is \$2.36. At all times, however, the number of Conversion Shares that can be issued to any Series A Preferred Stock Holder may not result in such holder and its affiliates owning more than 19.99% of the total number of shares of common stock outstanding after giving effect to the conversion (the "Hard Cap"), unless prior shareholder approval is obtained or no longer required by the rules of the principal stock exchange on which the Company's common stock trade.

**Mandatory Conversion.** If, at any time following November 14, 2022 the volume weighted average price of the Company's common stock equals or exceeds 2.25 times the Conversion Price for a period of 20 consecutive trading days and on each such trading day at least 20,000 shares of common stock was traded, the Company may, at its option and subject to the Hard Cap, require that any or all of the then outstanding shares of Series A Preferred Stock be automatically converted into shares of common stock at the then applicable convertible Formula at the Company's discretion.

**Redemption.** Beginning November 14, 2024, the Company may redeem all or any of the Series A Preferred Stock for a cash price equal to the greater of ("Liquidation Preference") (i) the sum of \$1,000 (subject to adjustment as provided in the Charter Amendment) plus the dollar amount of any declared Series A Dividends not paid in cash and (ii) the value of the Conversion Shares were such Series A Preferred Stock converted (as determined in the Charter Amendment) without regard to the Hard Cap.

**Change of Control.** In the event of certain changes of control, some of which are not in the Company's control, as defined in the Charter Amendment as a "Fundamental Change" or a "Liquidation" (as defined in the Charter Amendment), the Series A Preferred Stockholders shall be entitled to receive the Liquidation Preference, unless such Fundamental Change is a stock merger in which certain value and volume requirements are met, in which case the Series A Preferred Stock will be converted into common stock in connection with such stock merger. The Company has classified the Series A Preferred Stock as mezzanine equity on the Consolidated Balance Sheet based upon the terms of a change of control which could be outside the Company's control.

**Voting.** Holders of shares of Series A Preferred Stock will be entitled to vote with the holders of shares of common stock and not as a separate class, at any annual or special meeting of shareholders of the Company, on an as-converted basis, in all cases subject to the Hard Cap. In addition, a majority of the voting power of the Series A Preferred Stock must approve certain significant actions of the Company, including (i) declaring a dividend or otherwise redeeming or repurchasing any shares of common stock and other junior securities, if any, subject to certain exceptions, (ii) incurring indebtedness, except for certain permitted indebtedness and (iii) creating a subsidiary other than a wholly-owned subsidiary.

**Additional Provisions.** The Series A Preferred Stock is perpetual and therefore does not have a maturity date. The conversion price of the Series A Preferred Stock is subject to anti-dilution protections if the Company affects a stock split, stock dividend, subdivision, reclassification or combination of its common stock and certain other economically dilutive events.

**Registration Rights Agreement.** The Company also is a party to a Registration Rights Agreement ("RRA") with the investors of the Series A Preferred Stock. The RRA provides for unlimited demand registration rights, of which there can be two underwritten offerings each for at least \$5 million in gross proceeds, and piggyback registration rights, with respect to the Conversion Shares.

### **Restricted Stock**

The Company currently has three stock incentive plans: a Long-Term Incentive Plan (the "LTIP"), a Non-Employee Directors Restricted Stock Plan (the "Non-Employee Directors Plan") and the Lincoln Educational Services Corporation 2020 Incentive Compensation Plan (the "2020 Plan").

#### 2020 Plan

On March 26, 2020, the Board adopted, subject to shareholder approval, the 2020 Plan to provide an incentive to certain directors, officers, employees and consultants of the Company and its Subsidiaries to increase their interest in the Company's success by offering them an opportunity to obtain a proprietary interest in the Company through the grant of equity-based awards. On June 16, 2020, the shareholders of the Company approved the 2020 Plan. The 2020 Plan is administered by the Compensation Committee of the Board, or such other qualified committee appointed by the Board, who will, among other duties, have full power and authority to take all actions and to make all determinations required or provided for under the 2020 Plan. Pursuant to the 2020 Plan, the Company may grant options, share appreciation rights, restricted shares, restricted share units, incentive stock options and nonqualified stock options. The Plan has a duration of 10 years.

Subject to adjustment as described in the 2020 Plan, the aggregate number of common shares ("Shares") available for issuance under the 2020 Plan is Two Million (2,000,000) Shares. As of June 30, 2020, 111,376 restricted shares have been issued to the Non-Employee Directors which vest on the first anniversary of the grant date.

#### LTIP

Under the LTIP, certain employees have received awards of restricted shares of common stock based on service and performance. The number of shares granted to each employee is based on the amount of the award and the fair market value of a share of common stock on the date of grant. The 2020 Plan makes it clear that there will be no new grants under the LTIP effective as of the date of shareholder approval, June 16, 2020. The 2020 Plan also states that the shares available under the 2020 Plan will be two million shares plus the number of shares remaining available under the LTIP. As no shares remain available under the LTIP there can be no additional grants under the LTIP. Grants under the LTIP remain in effect according to their terms. Therefore, those grants are subject to the particular award agreement relating thereto and to the LTIP to the extent that the prior plan provides rules relating to those grants. The LTIP remains in effect only to that extent.

On February 20, 2020, performance-based restricted shares were granted to certain employees of the Company. The shares vest 20%, 30% and 50% on the first, second and third anniversary dates, respectively, based upon the attainment of a financial target during each fiscal year ending December 31, 2020, 2021 and 2022, respectively. There is no restriction on the right to vote or the right to receive dividends with respect to any of such restricted shares. As of June 30, 2020, the Company recorded expense of \$0.2 million as the expectation of attainment of the target is expected.

On February 28, 2019, restricted shares were granted to certain employees of the Company, which shares ratably vest over three years. There is no restriction on the right to vote or the right to receive dividends with respect to any of such restricted shares.

### Non-Employee Directors Plan

Pursuant to the Non-Employee Directors Plan, each non-employee director of the Company receives an annual award of restricted shares of common stock on the date of the Company's annual meeting of shareholders. The number of shares granted to each non-employee director is based on the fair market value of a share of common stock on that date. The restricted shares vest on the first anniversary of the grant date. There is no restriction on the right to vote or the right to receive dividends with respect to any of such restricted shares.

For the six months ended June 30, 2020 and 2019, the Company completed a net share settlement for 58,451 and 5,518 restricted shares, respectively, on behalf of certain employees that participate in the LTIP upon the vesting of the restricted shares pursuant to the terms of the LTIP. The net share settlement was in connection with income taxes incurred on restricted shares that vested and were transferred to the employees during 2019 and/or 2018, creating taxable income for the employees. At the employees' request, the Company will pay these taxes on behalf of the employees in exchange for the employees returning an equivalent value of restricted shares to the Company. These transactions resulted in a decrease of \$0.2 million and less than \$0.1 million for each of the three and six months ended June 30, 2020 and 2019, respectively, to equity on the condensed consolidated balance sheets as the cash payment of the taxes effectively was a repurchase of the restricted shares granted in previous years.

The following is a summary of transactions pertaining to restricted stock:

	<u>Shares</u>	<u>Weighted Average Grant Date Fair Value Per Share</u>
Nonvested restricted stock outstanding at December 31, 2019	595,436	\$ 3.15
Granted	1,302,638	2.65
Canceled	-	-
Vested	<u>(278,987)</u>	3.13
Nonvested restricted stock outstanding at June 30, 2020	<u><u>1,619,087</u></u>	2.75

The restricted stock expense for the three months ended June 30, 2020 and 2019 was \$0.3 million and \$0.2 million, respectively. The restricted stock expense for the six months ended June 30, 2020 and 2019 was \$0.6 million and \$0.2 million, respectively. The unrecognized restricted stock expense as of June 30, 2020 and December 31, 2019 was \$4.0 million and \$1.2 million, respectively. As of June 30, 2020, outstanding restricted shares under the LTIP had aggregate intrinsic value of \$6.3 million.

## Stock Options

The fair value of the stock options used to compute stock-based compensation is the estimated present value at the date of grant using the Black-Scholes option pricing model. The following is a summary of transactions pertaining to stock options:

	Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2019	116,000	\$ 10.56	1.83 years	\$ -
Granted/Canceled/Vested	-	-		-
Outstanding at June 30, 2020	<u>116,000</u>	10.56	1.33 years	-
Vested as of June 30, 2020	<u>116,000</u>	10.56	1.33 years	-
Exercisable as of June 30, 2020	<u>116,000</u>	10.56	1.33 years	-

As of June 30, 2020, there was no unrecognized pre-tax compensation expense.

The following table presents a summary of stock options outstanding:

At June 30, 2020					
Stock Options Outstanding				Stock Options Exercisable	
Exercise Prices	Shares	Contractual Weighted Average Life (years)	Weighted Average Price	Shares	Weighted Average Exercise Price
\$ 7.79	91,000	1.67	\$ 7.79	91,000	\$ 7.79
\$ 20.62	25,000	0.10	20.62	25,999	20.62
	<u>116,000</u>	1.33	10.56	<u>116,999</u>	10.56

## 8. INCOME TAXES

The provision for income taxes for the three months ended June 30, 2020 and 2019 was less than \$0.1 million, or 6.0% of pretax income, and \$0.1 million, or 4.9% of pretax loss, respectively. The provision for income taxes for the six months ended June 30, 2020 and 2019 was \$0.1 million, or 11.5% of pretax loss, and \$0.2 million, or 2.3% of pretax loss, respectively.

The Company assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to recover the existing deferred tax assets. In this regard, a significant objective negative evidence was the cumulative losses incurred by the Company in recent years. On the basis of this evaluation, the realization of the Company's deferred tax assets was not deemed to be more likely than not and, thus, the Company maintained a full valuation allowance on its net deferred tax assets as of June 30, 2020.

See Note 12 – COVID-19 Pandemic and Cares Act to the Unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for additional discussion about the CARES Act for impact on taxes.

## 9. COMMITMENTS AND CONTINGENCIES

In the ordinary conduct of its business, the Company is subject to certain lawsuits, investigations and claims, including, but not limited to, claims involving students or graduates and routine employment matters. Although the Company cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against it, the Company does not believe that any currently pending legal proceedings to which it is a party will have a material adverse effect on the Company's business, financial condition, and results of operations or cash flows.

Information regarding certain specific legal proceedings in which the Company is involved is contained in Part I, Item 3, and in Note 15 to the Notes to the Condensed Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2019. Unless otherwise indicated in this report, all proceedings discussed in the earlier report which are not indicated therein as having been concluded, remain outstanding as of June 30, 2020.

## 10. SEGMENTS

We operate our business in three reportable segments: (a) the Transportation and Skilled Trades segment; (b) the Healthcare and Other Professions segment; and (c) the Transitional segment. Our reportable segments have been determined based on a method by which we now evaluate performance and allocate resources. Each reportable segment represents a group of post-secondary education providers that offer a variety of degree and non-degree academic programs. These segments are organized by key market segments to enhance operational alignment within each segment to more effectively execute our strategic plan. Each of the Company's schools is a reporting unit and an operating segment. Our operating segments are described below.

**Transportation and Skilled Trades** – The Transportation and Skilled Trades segment offers academic programs mainly in the career-oriented disciplines of transportation and skilled trades (e.g. automotive, diesel, HVAC, welding and manufacturing).

**Healthcare and Other Professions** – The Healthcare and Other Professions segment offers academic programs in the career-oriented disciplines of health sciences, hospitality and business and information technology (e.g. dental assistant, medical assistant, practical nursing, culinary arts and cosmetology).

**Transitional** – The Transitional segment refers to our campus operations which have been closed. The schools in the Transitional segment employed a gradual teach-out process that enabled the schools to continue to operate to allow their current students to complete their course of study.

The Company continually evaluates each campus for profitability, earning potential, and customer satisfaction. This evaluation takes several factors into consideration, including the campus's geographic location and program offerings, as well as skillsets required of our students by their potential employers. The purpose of this evaluation is to ensure that our programs provide our students with the best possible opportunity to succeed in the marketplace with the goals of attracting more students to our programs and, ultimately, to provide our shareholders with the maximum return on their investment. Campuses classified in the Transitional segment have been subject to this process and have been strategically identified for closure. As of June 30, 2020 and 2019 and December 31, 2019, no campuses have been categorized in the Transitional segment.

We evaluate segment performance based on operating results. Adjustments to reconcile segment results to consolidated results are included under the caption "Corporate," which primarily includes unallocated corporate activity.

Summary financial information by reporting segment is as follows:

	For the Three Months Ended June 30,					
	Revenue				Operating Income (Loss)	
	2020	% of Total	2019	% of Total	2020	2019
Transportation and Skilled Trades	\$ 42,915	68.7%	\$ 44,028	69.3%	\$ 4,870	\$ 2,484
Healthcare and Other Professions	19,555	31.3%	19,541	30.7%	2,731	1,839
Corporate	-		-		(6,441)	(6,416)
Total	<u>\$ 62,470</u>	100.0%	<u>\$ 63,569</u>	100.0%	<u>\$ 1,160</u>	<u>\$ (2,093)</u>

	For the Six Months Ended June 30,					
	Revenue				Operating Income (Loss)	
	2020	% of Total	2019	% of Total	2020	2019
Transportation and Skilled Trades	\$ 91,971	69.4%	\$ 88,354	69.7%	\$ 9,708	\$ 4,300
Healthcare and Other Professions	40,540	30.6%	38,479	30.3%	4,733	2,811
Corporate	-		-		(14,626)	(14,069)
Total	<u>\$ 132,511</u>	100.0%	<u>\$ 126,833</u>	100.0%	<u>\$ (185)</u>	<u>\$ (6,958)</u>

	Total Assets	
	June 30, 2020	December 31, 2019
Transportation and Skilled Trades	\$ 135,140	\$ 121,611
Healthcare and Other Professions	29,184	27,945
Corporate	30,577	45,207
Total	<u>\$ 194,901</u>	<u>\$ 194,763</u>

## 11. FAIR VALUE

The carrying amount and estimated fair value of the Company's financial instrument assets and liabilities, which are not measured at fair value on the Condensed Consolidated Balance Sheet, are listed in the table below:

	June 30, 2020				
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
<b>Financial Assets:</b>					
Cash and cash equivalents	\$ 23,342	\$ 23,342	\$ -	\$ -	\$ 23,342
Restricted cash	2,626	2,626	-	-	2,626
Prepaid expenses and other current assets	3,748	-	3,748	-	3,748
<b>Financial Liabilities:</b>					
Accrued expenses	\$ 12,163	\$ -	\$ 12,163	\$ -	\$ 12,163
Other short term liabilities	93	-	93	-	93
Derivative qualifying cash flow hedge	1,017	-	1,017	-	1,017
Credit facility	18,121	-	14,943	-	14,943
<b>December 31, 2019</b>					
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
<b>Financial Assets:</b>					
Cash and cash equivalents	\$ 23,644	\$ 23,644	\$ -	\$ -	\$ 23,644
Restricted cash	15,000	15,000	-	-	15,000
Prepaid expenses and other current assets	4,190	-	4,190	-	4,190
<b>Financial Liabilities:</b>					
Accrued expenses	\$ 7,869	\$ -	\$ 7,869	\$ -	\$ 7,869
Other short term liabilities	199	-	199	-	199
Derivative qualifying cash flow hedge	174	-	174	-	174
Credit facility	34,028	-	34,028	-	34,028

As of June 30, 2020, we estimated the fair value of the Credit Facility based on a present value analysis utilizing aggregate market yields obtained from independent pricing sources for similar financial instruments. As of December 31, 2019, we estimated that the carrying value of the Credit Facility approximates the fair value due to the fact that the Credit Facility was entered into in close proximity.

The carrying amounts reported on the Consolidated Balance Sheets for Cash and cash equivalents, Restricted cash and Noncurrent restricted cash approximate fair value because they are highly liquid.

The carrying amounts reported on the Consolidated Balance Sheets for Prepaid expenses and other current assets, Accrued expenses and Other short term liabilities approximate fair value due to the short-term nature of these items.

### Qualifying Hedge Derivative

On November 14, 2019, the Company entered into an interest rate swap for the Term Loan with a notional amount of \$20M which expires on December 1, 2024. The loan has a 10-year straight line amortization. A principal amount of \$0.2 million is paid monthly. This interest rate swap converts the floating interest rate Term Loan to a fixed rate, plus a borrowing spread. The interest rate is variable based on LIBOR plus 3.50% and the Company's fixed rate is 5.36%. The Company designated this interest rate swap as a cash flow hedge.

The Company entered into this interest rate swap to hedge exposure resulting from the interest rate risk. The purpose of this hedge is to reduce the variability of the interest rate based on LIBOR. The Company manages these exposures within specified guidelines through the use of derivatives. All of our derivative instruments are utilized for risk management purposes, and the Company does not use derivatives for speculative trading purposes.

The following summarizes the fair value of the outstanding derivative:

	<u>June 30, 2020</u>		<u>December 31, 2019</u>	
	<u>Liability<sup>(1)</sup></u>		<u>Liability<sup>(1)</sup></u>	
	<u>Notional</u>	<u>Fair Value</u>	<u>Notional</u>	<u>Fair Value</u>
Derivative derived as a hedging instrument:				
Interest Rate Swap	\$ 18.8	\$ 1.0	\$ 19.8	\$ 0.1

- (1) The Company's derivative liability is measured at fair value using observable market inputs such as interest rates and our own credit risk as well as an evaluation of our counterparty's credit risk. Based on these inputs the derivative liability is classified within Level 2 of the valuation hierarchy. The liability is included in other long-term liabilities in the condensed consolidated balance sheets.

The following summarizes the financial statement classification and amount of interest expense recognized on hedging instruments:

	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
	<u>June 30, 2020</u>			
	<u>Interest expense</u>			
Interest Rate Swap	\$ 0.1	\$ 0.1	\$ 0.1	\$ 0.1

The following summarizes the effect of derivative instruments designated as hedging instruments in Other Comprehensive Income/(Loss):

	<u>June 30, 2020</u>	
	<u>Three Months Ended</u>	<u>Six Months Ended</u>
	<u>Interest expense</u>	<u>Interest expense</u>
Derivative qualifying as cash flow hedge		
Interest rate swap loss	\$ 0.1	\$ 0.8

## 12. COVID-19 PANDEMIC AND CARES ACT

The Company began seeing the impact of the global COVID-19 pandemic on its business in early March and such effects of the pandemic have continued. The spread of COVID-19 has had an unprecedented impact on higher educational institutions across the country, including our schools, and has led to the closure of campuses and the transition of academic programs from on-ground to online delivery. The impact for the Company was primarily related to transitioning classes from in-person, hands-on learning to online, remote learning. As part of this transition, the Company has incurred additional expenses. In addition, some students have been placed on leave of absence as they could not complete their externships and some students chose not to participate in online learning. Additionally, certain programs were extended due to restricted access to externship sites and classroom labs. In accordance with phased re-opening as applied on a state-by-state basis, all of our schools have now re-opened and we expect the majority of the students who have been on leave of absence or have deferred their programs to finish their programs. The Company expects to continue to be impacted by COVID-19 as the situation remains dynamic and evolving and subject to rapid and possibly material change. Additional impacts may arise of which the Company is not currently aware. The nature and extent of such impacts will depend on future developments, which are highly uncertain and cannot be predicted.

On March 27, 2020, the CARES Act was signed into law, which includes a \$2 trillion federal economic relief package providing financial assistance and other relief to individuals and business impacted by the spread of COVID-19. The CARES Act includes provisions for financial assistance and other regulatory relief benefitting students and their postsecondary institutions.

Among other things, the CARES Act includes a \$14 billion higher education emergency relief fund (“HEERF”) for the DOE to distribute directly to institutions of higher education. Institutions are required to use at least half of the HEERF funds for emergency grants to students for expenses related to disruptions in campus operations (e.g., food, housing, etc.). Institutions are permitted to use the remainder of the funds for additional emergency grants to students or to cover institutional costs associated with significant changes to the delivery of instruction due to the COVID-19 emergency, provided that those costs do not include payment to contractors for the provision of pre-enrollment recruitment activities, endowments, or capital outlays associated with facilities related to athletics, sectarian instruction, or religious worship. The law requires institutions receiving funds to continue to the greatest extent practicable to pay its employees and contractors during the period of any disruptions or closures related to the COVID-19 emergency.

The DOE has allocated funds to each institution of higher education based on a formula contained in the CARES Act. The formula is heavily weighted toward institutions with large numbers of Pell Grant recipients. The DOE allocated \$27.4 million to our schools to be distributed in two equal installments. The Company received \$13.7 million in the first installment which was intended for emergency grants to students. The Company has distributed \$11.1 million to the students and expects to distribute the remainder over the next few months. The \$2.6 million remaining to be distributed is included in restricted cash on the Company's Condensed Consolidated Balance Sheets. As of June 30, 2020, the Company had received \$13.2 million of the \$13.7 million from the second installment which is intended for institutional costs and additional emergency grants to students with the remaining \$0.5 million received in August 2020. The Company has reimbursed itself for \$1.3 million of permitted expenses as of June 30, 2020 which was netted against the original expenses included in selling, general and administrative on the Condensed Consolidated Statement of Operations. The DOE also has published guidance regarding permitted and prohibited use of these funds and requirements for reporting the use of these funds. If the funds are not spent or accounted for in accordance with applicable requirements, we could be required to return funds or be subject to other sanctions.

The CARES Act also contains separate educational provisions that relieve both institutions and students from complying with the requirement to repay Title IV funds following a student's withdrawal as a result of the COVID-19 emergency. Ordinarily, when a student withdraws, the institution (and, in some cases, the student) may be required to return unearned portions of the Title IV grant and loan funds awarded for the period. Institutions will be required to report to the DOE the total amount of grant and loan funds the institution has not returned due to the waiver. For federal loan borrowers, the CARES Act also directs the DOE to cancel the borrower's obligation to repay any Direct Loan associated with the relevant period. The law also expands the options to avoid student withdrawals due to a cessation of attendance by placing students on an approved leave of absence and waives certain requirements normally applicable to a leave of absence. The CARES Act also allows institutions to exclude from the calculation of a student's satisfactory academic progress any attempted credits not completed due to the COVID-19 emergency.

The Company is also permitted to delay payment of FICA payroll taxes until January 1, 2021. The Company will have to repay 50 percent of the deferred payments by December 31, 2021, and the remaining 50 percent by December 31, 2022. As of June 30, 2020, the Company had deferred payments of \$1.5 million.

**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

All references in this Quarterly Report on Form 10-Q to "we," "our," "us" and the "Company," refer to Lincoln Educational Services Corporation and its subsidiaries unless the context indicates otherwise.

The following discussion may contain forward-looking statements regarding the Company, our business, prospects and our results of operations that are subject to certain risks and uncertainties posed by many factors and events that could cause our actual business, prospects and results of operations to differ materially from those that may be anticipated by such forward-looking statements. Such statements may be identified by the use of words such as "expect," "estimate," "assume," "believe," "anticipate," "may," "will," "forecast," "outlook," "plan," "project," or similar words, and include, without limitation, statements relating to future enrollment, revenues, revenues per student, earnings growth, operating expenses, capital expenditures and the ultimate effect of the COVID-19 pandemic on the Company's business and results. These statements are based on the Company's current expectations and are subject to a number of assumptions, risks and uncertainties. Additional factors that could cause or contribute to differences between our actual results and those anticipated include, but are not limited to, those described in the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2019, as filed with the SEC and in our other filings with the SEC. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. We undertake no obligation to revise any forward-looking statements in order to reflect events or circumstances that may subsequently arise. Readers are urged to carefully review and consider the various disclosures made by us in this Quarterly Report and in our other reports filed with the SEC that advise interested parties of the risks and factors that may affect our business.

The interim financial statements and related notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q and the discussions contained herein should be read in conjunction with the annual financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2019, as filed with the SEC, which includes audited consolidated financial statements for our three fiscal years ended December 31, 2019.

**General**

The Company provides diversified career-oriented post-secondary education to recent high school graduates and working adults. The Company offers programs in automotive technology, skilled trades (which include HVAC, welding and computerized numerical control and electrical and electronic systems technology, among other programs), healthcare services (which include nursing, dental assistant and medical administrative assistant, among other programs), hospitality services (which include culinary, therapeutic massage, cosmetology and aesthetics) and information technology programs. The schools, currently consisting of 22 schools in 14 states, operate under Lincoln Technical Institute, Lincoln College of Technology, Lincoln Culinary Institute, and Euphoria Institute of Beauty Arts and Sciences and associated brand names. Most of the campuses serve major metropolitan markets and each typically offers courses in multiple areas of study. Five of the campuses are destination schools, which attract students from across the United States and, in some cases, from abroad. The Company's other campuses primarily attract students from their local communities and surrounding areas. All of the campuses are nationally or regionally accredited and are eligible to participate in federal financial aid programs by the 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.

Our business is organized into three reportable business segments: (a) Transportation and Skilled Trades, (b) Healthcare and Other Professions or "HOPS", and (c) Transitional, which refers to businesses that have been taught out.

**Impact of COVID-19 on the Company**

During the first quarter of 2020, COVID-19 began to spread worldwide and has caused significant disruptions to the U.S. and world economies. In early March 2020, the Company began seeing the impact of the COVID-19 pandemic on our business. Beginning on March 15, 2020, many businesses closed or reduced hours throughout the U.S. to combat the spread of COVID-19. On March 11, 2020, the World Health Organization declared the COVID-19 outbreak to be a pandemic. On March 13, 2020, a national emergency was declared, which made federal funds available to respond to the crisis. All 50 states have reported cases of COVID-19 and the states have implemented various containment efforts, including lockdowns on non-essential businesses. Economists expect that the impact of COVID-19 on the U.S. economy will be significant during the remainder of 2020. The circumstances related to COVID-19 are unprecedented, dynamic and evolving and currently unpredictable. As the economic impact of the COVID-19 pandemic becomes clearer as the year progresses, we could see significant changes to our operations.

The impact of COVID-19 was primarily related to transitioning classes from in-person, hands-on learning to online, remote learning. As part of this transition, the Company has incurred additional expenses. In addition, some students have been placed on leave of absence as they could not complete their externships and some students chose not to participate in online learning. Additionally, certain programs were extended due to restricted access to externship sites and classroom labs. In response to COVID-19, we have also implemented initiatives to safeguard our students and our employees in this time of crisis. Due to phased re-opening on a state-by-state basis, our schools have been reopening since May 2020 and, currently, all of our schools have re-opened and we expect the majority of the students who were placed on leave or otherwise deferred their programs to finish their programs now. As COVID-19 continues to affect many states and its course is unpredictable, the full impact on the Company's consolidated financial statements remains uncertain.

The following discussion highlights how we are responding and the expected impacts of COVID-19 on our business. Due to the evolving landscape relating to COVID-19 and the unpredictability of the circumstances, the information below should be read in conjunction with our COVID-19 Pandemic risk factor. See Part II, Item 1A. "Risk Factors — COVID-19 Pandemic" in this Quarterly Report on Form 10-Q for risks to our business arising as a consequence of COVID-19. See also Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2019 (the "2019 Form 10-K") for additional risk factors relating to our Company and the industry. In addition, see the forward-looking and cautionary statements discussion above. Forward-looking statements are subject to risks, uncertainties, assumptions, and other factors that may cause actual results to be materially different from those reflected in such forward-looking statements. These factors include, among others, the risks and uncertainties set forth in Item 1A. "Risk Factors" and elsewhere in the 2019 Form 10-K and this Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2020.

### Transition to Distance Learning

In the first and second quarters, the Company quickly transitioned all of its programs from in-person, hands-on learning to online, remote learning. The Company obtained approvals from the DOE, certain states and agencies to transition to distance learning. The Company worked with its book vendors to obtain e-books for the students. The Company has ensured that all students have either received laptops, tablets or already owned a device. The Company has enhanced its education platform for online learning through a software program. As schools have reopened, we are adhering to social distancing protocols which may differ from school-to-school depending on physical circumstances as well as other factors and we are limiting the number of students on campus at one time. The schools continue to teach a portion of each program through distance learning and labs are generally taught in-person.

### Employees

Our employees have been affected by COVID-19 in many ways, including disruptions due to unexpected school and day-care closings, family underemployment or unemployment, and learning how to work remotely and, in some cases, with new tools and technology to learn and to support that work. Our goal has been to support our people during the present uncertainty while remaining focused on meeting the needs of our students and business continuity. Early in the crisis, we provided employees with information about best practices to prevent the spread of COVID-19 and other viruses and illnesses. We recommended that non-student interfacing employees work from home and we reduced the density and provided physical space for us to implement social distancing protocols for the employees who were required to work in our offices. Later, we enabled substantially all of our workforce to work remotely. In addition, we have limited in-person meetings, non-employee visits to our locations, and non-essential business travel.

To further protect the health and welfare of our employees we have also encouraged employees who potentially have been exposed to COVID-19 to self-quarantine for 14 days while we continue to pay them. To ease access to medical assistance, we are waiving co-payments for COVID-19 testing and telemedicine for those employees enrolled in our health insurance plans. The Company's vacation policy was enhanced in the second quarter of 2020 to include up to two weeks of payments for unused vacation days for instructors.

### Community

We understand that the communities in which our employees live, work, and serve are also suffering distress as a result of COVID-19. Due to the growing needs of our neighbors, healthcare providers and many of the organizations in place to provide assistance are overburdened. In March 2020, several campuses in the Tri-State (NY, NJ & CT) area have donated medical supplies and personal protective equipment to major medical facilities throughout the region.

### Operations

We have robust pandemic and business continuity plans that include our business units and technology environments. When COVID-19 advanced to a pandemic, we activated our business continuity plan (the "Continuity Plan"). As an element of the Continuity Plan, we activated our Health Communications Response Team ("HCRT"), a group of the corporate senior managers, who directed a series of activities to address the health and safety of our workforce, to assist students, to sustain business operations, to coordinate communication and to address our management of other ongoing pandemic activities.

In response to a growing infected population across the United States, as noted above, we executed plans for social-distancing in our facilities and implemented work-from-home contingencies. As the virus spread, we created remote-working capabilities for our employees. We also completed a series of additional steps to appropriately ensure compliance with our telecommuting policy. The policy is designed to create a secure at-home work environment that protects our students' information and transactions while also providing the necessary technology capabilities to enable effective remote-working for our staff.

There has been a modest decline in productivity for certain departments as our personnel have been adjusting to this significant change in work environment. We currently believe our technology infrastructure is sufficient to maintain a remote-working environment for the vast majority of our workforce for the foreseeable future and that productivity should improve as our people adjust to this significant change in work environment. The level and ability of our employees to continue working from home could change, however, as conditions surrounding COVID-19 evolve and infections increase, or if there are interruptions in the internet infrastructure where our employees live or if our internet service providers are otherwise adversely affected.

### Return to In-Person Operations

Due to the phase-in of reopening which has been addressed on a state-by-state basis, we have been reopening our schools. Currently, all of our schools have re-opened and we continue to follow the guidelines released by each state and city in which our schools are located. The HCRT is continuing to closely monitor the guidelines released by each state and city in which our school are located for any change. As part of reopening our schools, we purchased personal protective equipment, are limiting the number of students in classrooms, have separated students by at least 6 feet, have closed/limited all common areas, require everyone at the schools to wear a cloth face mask and maintain a daily log of anyone at the school and monitor body temperatures of those at the school through non-contact thermometers. In a similar way, we are also rotating employees schedules to limit/control the number of employees in spaces.

### Student Population and Financial Results

As of June 30, 2020, the Company had 696 students on leave of absence due to COVID-19. The majority of these students were at the end of their programs and were on externship which they were not able to complete. A smaller portion of these students on leave had chosen not to undertake their programs through distance learning. The Company expects a majority of these students will return to school or an externship by the end of the year.

The Company has extended the length and graduation dates of four programs as there is only a small percentage of these four programs that can be taught through distance learning.

The Company has campuses where students live in dorms that are operated by either the Company itself, Collegiate Housing or other housing options. The majority of the students had returned home and their dorm charges have been reversed. In addition, at campuses where students have meal plans, the Company's cafeterias have been closed and all charges for meal plans have been reversed. For students that remain in dorms, the Company has given the students gift cards to assist in replacing their meal plans. As the students are returning to campus the dorms have reopened and the schools have limited the number of students in dorms to adhere to social distancing.

### Institutional Student Loans

COVID-19 is having far reaching, negative impact on individuals, businesses, and, consequently, the overall economy. Specifically, COVID-19 has materially disrupted business operations resulting in significantly higher levels of unemployment or underemployment. As a consequence, we expect many of our individual students will experience financial hardship, making it difficult, if not impossible, to meet their payment obligations to us without temporary assistance.

As a result of the negative impact on employment from COVID-19, we are observing higher levels of financial hardship for our students, which we expect will lead to higher levels of forbearance, delinquency and defaults. We expect that, left unabated, this deterioration in forbearance, delinquency and default rates will persist until such time as the economy and employment return to relatively normal levels.

We expect that, as the economic impact of COVID-19 evolves, we will continue to evaluate the measures we have put in place to assist our students during this unprecedented challenge. We continue to adapt and evolve our collections practices to meet the needs of our students.

### Liquidity

As previously reported, over the course of 2019, we significantly increased our overall liquidity position. As a result of these efforts, we currently believe our liquidity position is stable and we expect to be able to fund our business operations for the remainder of 2020 and we believe that we have sufficient capital to withstand the potential downturn in our business. If circumstances surrounding COVID-19 continue to change in a significantly adverse way, however, it is possible our liquidity could be materially and adversely affected, which could materially and adversely impact our business operations and our overall financial condition.

Regulatory agencies have also provided regulatory capital relief to institutions as a result of the crisis as discussed below.

### Regulatory

On March 27, 2020, the CARES Act was signed into law, which includes a \$2 trillion federal economic relief package providing financial assistance and other relief to individuals and business impacted by the spread of COVID-19. The spread of COVID-19 has had an unprecedented impact on higher educational institutions across the country, including our schools, and has led to the closure of campuses and the transition of academic programs from on-ground to online delivery. The CARES Act includes provisions for financial assistance and other regulatory relief benefitting students and their postsecondary institutions.

Among other things, the CARES Act includes a \$14 billion higher education emergency relief fund (“HEERF”) for the DOE to distribute directly to institutions of higher education. Institutions are required to use at least half of the HEERF funds for emergency grants to students for expenses related to disruptions in campus operations (e.g., food, housing, etc.). Institutions are permitted to use the remainder of the funds for additional emergency grants to students or to cover institutional costs associated with significant changes to the delivery of instruction due to the COVID-19 emergency, provided that those costs do not include payment to contractors for the provision of pre-enrollment recruitment activities, endowments, or capital outlays associated with facilities related to athletics, sectarian instruction, or religious worship. The law requires institutions receiving funds to continue to the greatest extent practicable to pay its employees and contractors during the period of any disruptions or closures related to the COVID-19 emergency.

The DOE has allocated funds to each institution of higher education based on a formula contained in the CARES Act. The formula is heavily weighted toward institutions with large numbers of Pell Grant recipients. The DOE allocated \$27.4 million to our schools to be distributed in two equal installments. The Company received \$13.7 million in the first installment which was intended for emergency grants to students. The Company has distributed \$11.1 million to the students and expects to distribute the remainder over the next few months. The \$2.6 million remaining to be distributed is included in restricted cash on the Company's Condensed Consolidated Balance Sheets. As of June 30, 2020, the Company had received \$13.2 million of the \$13.7 million from the second installment which is intended for institutional costs and additional emergency grants to students with the remaining \$0.5 million received in August 2020. The Company has reimbursed itself for \$1.3 million of permitted expenses as of June 30, 2020. The DOE also has published guidance regarding permitted and prohibited use of these funds and requirements for reporting the use of these funds. If the funds are not spent or accounted for in accordance with applicable requirements, we could be required to return funds or be subject to other sanctions.

The CARES Act also contains separate educational provisions that relieve both institutions and students from complying with the requirement to repay Title IV funds following a student's withdrawal as a result of the COVID-19 emergency. Ordinarily, when a student withdraws, the institution (and, in some cases, the student) may be required to return unearned portions of the Title IV grant and loan funds awarded for the period. Institutions will be required to report to the DOE the total amount of grant and loan funds the institution has not returned due to the waiver. For federal loan borrowers, the CARES Act also directs the DOE to cancel the borrower's obligation to repay any Direct Loan associated with the relevant period. The law also expands the options to avoid student withdrawals due to a cessation of attendance by placing students on an approved leave of absence and waives certain requirements normally applicable to a leave of absence. The CARES Act also allows institutions to exclude from the calculation of a student's satisfactory academic progress any attempted credits not completed due to the COVID-19 emergency.

The Company is also permitted to delay payment of FICA payroll taxes until January 1, 2021. The Company will have to repay 50 percent of the deferred payments by December 31, 2021, and the remaining 50 percent by December 31, 2022. As of June 30, 2020, the Company had deferred payments of \$1.5 million.

### Other

Based on analysis of ASC 350 and ASC 360, during the three and six months ended June 30, 2020, we are currently not aware of any material impairments of our goodwill, indefinite-lived intangible assets or finite-lived assets. The Company will continue to assess the relevant criteria on a quarterly basis based on updated cash flow and market assumptions. Unfavorable changes in cash flow or market assumptions could result in impairment of these assets in future periods.

## Critical Accounting Policies and Estimates

For a description of our critical accounting policies and estimates, refer to “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates” and Note 1 to the Condensed Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019 and Note 1 to the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for the quarter ended June 30, 2020.

In addition, due to outbreak of COVID-19, we have reassessed those of our accounting policies whose application places the most significant demands on management’s judgment, for instance, revenue recognition, allowance for doubtful account, goodwill, and long-lived assets, stock-based compensation, derivative instruments and hedging activity, borrowings, assumptions related to ROU assets, lease cost, income taxes and assets and obligations related to employee benefit plans. Such reassessments did not have a significant impact on our results of operations and cash flows for the periods presented.

## Effect of Inflation

Inflation has not had a material effect on our operations.

## Results of Continuing Operations for the Three and Six Months Ended June 30, 2020

The following table sets forth selected consolidated statements of operations data as a percentage of revenues for each of the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Revenue	100.0%	100.0%	100.0%	100.0%
Costs and expenses:				
Educational services and facilities	42.0%	46.8%	42.6%	47.1%
Selling, general and administrative	56.3%	56.5%	57.6%	58.4%
(Gain) loss on sale of assets	-0.2%	0.0%	-0.1%	0.0%
Total costs and expenses	98.1%	103.3%	100.1%	105.5%
Operating income (loss)	1.9%	-3.3%	-0.1%	-5.5%
Interest expense, net	-0.5%	-1.3%	-0.5%	-1.1%
Income (loss) from operations before income taxes	1.4%	-4.6%	-0.6%	-6.6%
Provision for income taxes	0.1%	0.2%	0.1%	0.2%
Net income (loss)	1.3%	-4.8%	-0.7%	-6.8%

## Three Months Ended June 30, 2020 Compared to Three Months Ended June 30, 2019

### Consolidated Results of Operations

**Revenue.** Revenue was \$62.5 million for the three months ended June 30, 2020, down 1.7% from \$63.6 in the prior year comparable quarter despite the 11.0% increase in average student population. The impact of COVID-19 has extended graduation dates for certain programs due to restricted access to externships sites and classroom labs. These restrictions have deferred \$0.9 million in revenue to the second half of the year. In addition, non-tuition revenue was reduced \$0.8 million due to credits issued to students for dorm and meal fees resulting from campus closures caused by COVID-19. The dorms are owned and operated by the Company. We received funds under the Cares Act which may be used to reimburse the Company for the student credits issued, but at this time we are awaiting further guidance from the DOE on the appropriate application of such funds.

Partially offsetting the increase in revenue was the impact of COVID-19, which has extended graduation dates for certain programs due to restricted access to externship sites and classroom labs. These restrictions have deferred \$0.9 million in revenue to the second half of the year. In addition, non-tuition revenue was reduced \$0.8 million due to credits issued to students for dorm and meal fees resulting from campus closures caused by COVID-19. The dorms are owned and operated by the Company. We received funds under the Cares Act which may be used to reimburse the Company for the student credits issued, but at this time we are awaiting further guidance from the DOE on the appropriate application of such funds.

For a general discussion of trends in our student enrollment, see “Seasonality and Outlook” below.

**Educational services and facilities expense.** Our educational services and facilities expense decreased \$3.5 million, or 11.8%, to \$26.2 million for the three months ended June 30, 2020 from \$29.8 million in the prior year comparable period. Reduced costs were a result of several factors including facilities cost savings due to facility closure during the quarter as a result of actions taken to control transmission of COVID-19; renegotiation of lease terms at certain campuses reducing rent expense; and the reduction in instructional and books and tools expenses as a result of students completing their course remotely.

Educational services and facilities expense, as a percentage of revenue, decreased to 42.0% from 46.8% for the three months ended June 30, 2020 and 2019, respectively.

**Selling, general and administrative expense.** Our selling, general and administrative expense decreased \$0.7 million, or 2.1% to \$35.2 million for the three months ended June 30, 2020 from \$35.9 million in the prior year comparable period. The decrease was primarily driven by cost reductions in sales, student services, and marketing investments, partially offset by an increase in bad debt expense and salaries and benefits expense.

Reductions in sales expense was the result of travel restrictions imposed by the COVID-19 pandemic, while lower student services expense was the result of suspended busing and transportation services for students. Reduced marketing investments were due to the timing of marketing spend.

Bad debt expense increased mainly due to a higher reserve amount for doubtful accounts due to lower historical repayment rates coupled with higher accounts receivable.

Selling, general and administrative expenses, as a percentage of revenue, decreased to 56.3% for the three months ended June 30, 2020 from 56.5% in the prior year comparable period.

**Net interest expense.** Net interest expense for the three months ended June 30, 2020 decreased by \$0.5 million, or 60.5%, to \$0.3 million from \$0.8 million in the prior year comparable period. The reduction in expense quarter over quarter is due to favorable terms from the refinance of our credit facility as well as a lower loan balance outstanding in the current year.

**Income taxes.** Our provision for income taxes was essentially flat at approximately \$0.1 million the three months ended June 30, 2020 and 2019. No federal or state income tax benefit was recognized for either period loss due to the recognition of a full valuation allowance. Income tax expense resulted from various minimum state taxes.

## **Six Months Ended June 30, 2020 Compared to Six Months Ended June 30, 2019**

### **Consolidated Results of Operations**

**Revenue.** Revenue increased \$5.7 million, or 4.5% to \$132.5 million for the six months ended June 30, 2020 from \$126.8 million in the prior year comparable period. The increase was the result of an 8.8% increase in average student population in part driven by starting the year with approximately 760 more students than in the prior year comparable period. As a result, our ending population as of June 30, 2020 grew 14.0% compared to prior year. Excluding students on leave of absence as a result of COVID-19, ending population grew 7.5% or approximately 800 students. The majority of these students were near the end of their programs and are expected to resume their program during the third quarter as all of our schools are now open and more externship sites reopen. We do not recognize revenue during a students’ leave of absence period, therefore, we anticipate earning revenue starting in the third quarter upon the students’ return.

Partially offsetting the increase in revenue was the impact of COVID-19, which has extended graduation dates for certain programs due to restricted access to externship sites and classroom labs. These restrictions have deferred \$0.9 million in revenue to the second half of the year. In addition, non-tuition revenue was reduced \$0.8 million due to credits issued to students for dorm and meal fees resulting from campus closures caused by COVID-19. The dorms are owned and operated by the Company. We received funds under the Cares Act which may be used to reimburse the Company for the student credits issued, but at this time we are awaiting further guidance from the DOE on the appropriate application of such funds.

Total student starts increased 5.3% for the six months ended June 30, 2020 as compared to the prior year comparable period.

For a general discussion of trends in our student enrollment, see “Seasonality and Outlook” below.

**Educational services and facilities expense.** Our educational services and facilities expense decreased \$3.2 million, or 5.4% to \$56.5 million for the six months ended June 30, 2020 from \$59.7 million in the prior year comparable period. Reduced costs were a result of several factors including facilities cost savings due to facility closures during the first and second quarter as a result of actions taken to control transmission of COVID-19; renegotiation of lease terms at certain campuses reducing rent expense; and the reduction in instructional and books and tools expenses as a result of students completing their course remotely.

Educational services and facilities expense, as a percentage of revenue, decreased to 42.6% from 47.1% for the six months ended June 30, 2020 and 2019, respectively.

**Selling, general and administrative expense.** Our selling general and administrative expense increased \$2.2 million, or 3.0% to \$76.3 million for the six months ended June 30, 2020 from \$74.1 million in the prior year comparable period. The additional costs were driven by several factors including additional bad debt expense and increased salaries and benefits expense, partially offset by cost savings in sales expense, student services expense and marketing investments.

Bad debt expense increased mainly due to a higher reserve amount for doubtful accounts due to lower historical repayment rates coupled with higher accounts receivable.

Reductions in sales expense was a result of travel restrictions imposed by the COVID-19 pandemic, while lower student services expense was a result of suspended busing and transportation services for students. Reduced marketing investments were due to the timing of marketing spend.

Selling, general and administrative expenses, as a percentage of revenue, decreased slightly to 57.6% for the six months ended June 30, 2020 from 58.4% in the prior year comparable period.

**Net interest expense.** Net interest expense for the six months ended June 30, 2020 decreased by \$0.7 million, or 50.5%, to \$0.7 million from \$1.4 million in the prior year comparable period. The reduction in expense year over year is due to favorable terms from the refinance of our credit facility as well as a lower loan balance outstanding in the current year.

**Income taxes.** Our provision for income taxes was \$0.1 million and \$0.2 million for the six months ended June 30, 2020 and 2019, respectively. No federal or state income tax benefit was recognized for either period loss due to the recognition of a full valuation allowance. Income tax expense resulted from various minimal state tax expenses.

## **Segment Results of Operations**

We operate our business in three reportable segments: (a) the Transportation and Skilled Trades segment; (b) the Healthcare and Other Professions (“HOPS”) segment; and (c) the Transitional segment. Our reportable segments have been determined based on a method by which we now evaluate performance and allocate resources. Each reportable segment represents a group of post-secondary education providers that offer a variety of degree and non-degree academic programs. These segments are organized by key market segments to enhance operational alignment within each segment to more effectively execute our strategic plan. Each of the Company’s schools is a reporting unit and an operating segment. Our operating segments are described below.

**Transportation and Skilled Trades** – The Transportation and Skilled Trades segment offers academic programs mainly in the career-oriented disciplines of transportation and skilled trades (e.g. automotive, diesel, HVAC, welding and manufacturing).

**Healthcare and Other Professions** – The Healthcare and Other Professions segment offers academic programs in the career-oriented disciplines of health sciences, hospitality and business and information technology (e.g. dental assistant, medical assistant, practical nursing, culinary arts and cosmetology).

**Transitional** – The Transitional segment refers to campus operations which have been closed.

The Company continually evaluates each campus for profitability, earning potential, and customer satisfaction. This evaluation takes several factors into consideration, including the campus’s geographic location and program offerings, as well as skillsets required of our students by their potential employers. The purpose of this evaluation is to ensure that our programs provide our students with the best possible opportunity to succeed in the marketplace with the goals of attracting more students to our programs and, ultimately, to provide our shareholders with the maximum return on their investment. As of June 30, 2020, no campuses have been categorized in the Transitional segment.

We evaluate segment performance based on operating results. Adjustments to reconcile segment results to consolidated results are included under the caption "Corporate," which primarily includes unallocated corporate activity.

The following table presents results for our two reportable segments (as no campuses have been categorized in the Transitional segment) for the three months ended June 30, 2020 and 2019:

	<b>Three Months Ended June 30,</b>		
	<b>2020</b>	<b>2019</b>	<b>% Change</b>
<b>Revenue:</b>			
Transportation and Skilled Trades	\$ 42,915	\$ 44,028	-2.5%
HOPS	19,555	19,541	0.1%
<b>Total</b>	<b>\$ 62,470</b>	<b>\$ 63,569</b>	<b>-1.7%</b>
<b>Operating Income (Loss):</b>			
Transportation and Skilled Trades	\$ 4,870	\$ 2,484	96.1%
Healthcare and Other Professions	2,731	1,839	48.5%
Corporate	(6,441)	(6,416)	-0.4%
<b>Total</b>	<b>\$ 1,160</b>	<b>\$ (2,093)</b>	<b>155.4%</b>
<b>Starts:</b>			
Transportation and Skilled Trades	2,302	2,028	13.5%
Healthcare and Other Professions	1,127	949	18.8%
<b>Total</b>	<b>3,429</b>	<b>2,977</b>	<b>15.2%</b>
<b>Average Population:</b>			
Transportation and Skilled Trades	7,298	6,827	6.9%
Leave of Absence - COVID-19	(424)	-	100.0%
Transportation and Skilled Trades Excluding Leave of Absence - COVID-19	6,874	6,827	0.7%
Healthcare and Other Professions	4,254	3,578	18.9%
Leave of Absence - COVID-19	(393)	-	100.0%
Healthcare and Other Professions Excluding Leave of Absence - COVID-19	3,861	3,578	7.9%
<b>Total</b>	<b>11,552</b>	<b>10,405</b>	<b>11.0%</b>
<b>Total Excluding Leave of Absence - COVID-19</b>	<b>10,735</b>	<b>10,405</b>	<b>3.2%</b>
<b>End of Period Population:</b>			
Transportation and Skilled Trades	7,826	7,195	8.8%
Leave of Absence - COVID-19	(463)	-	100.0%
Transportation and Skilled Trades Excluding Leave of Absence - COVID-19	7,363	7,195	2.3%
Healthcare and Other Professions	4,456	3,582	24.4%
Leave of Absence - COVID-19	(233)	-	100.0%
Healthcare and Other Professions Excluding Leave of Absence - COVID-19	4,223	3,582	17.9%
<b>Total</b>	<b>12,282</b>	<b>10,777</b>	<b>14.0%</b>
<b>Total Excluding Leave of Absence - COVID-19</b>	<b>11,586</b>	<b>10,777</b>	<b>7.5%</b>

## Three Months Ended June 30, 2020 Compared to the Three Months Ended June 30, 2019

### Transportation and Skilled Trades

Operating income increased \$2.4 million to \$4.9 million for the three months ended June 30, 2020 from \$2.5 million in the prior year comparable period. The increase quarter over quarter was mainly driven by the following factors:

- Revenue was \$42.9 million for the three months ended June 30, 2020, down 2.5% from \$44.0 in the prior year comparable period million despite the 6.9% increase in average student population. Student start growth increased 13.5% for the three months ended June 30, 2020 as compared to the prior year comparable period. As a result, the Company's ending population as of June 30, 2020 grew 8.8% compared to prior year. After excluding students who are on leave of absence as a result of the impact of COVID-19, the ending population grew 2.3% or approximately 170 students. Non-tuition revenue was reduced \$0.8 million due to credits issued to students for Company owned dorms and meal fees resulting from campus closures caused by COVID-19. In addition, as a result of the impact of COVID-19, graduation dates for certain programs have been extended due to restricted access to externships sites and classroom labs which resulted in \$0.1 million in revenue being deferred to the second half of the year.
- Educational services and facilities expense decreased \$2.8 million, or 14.0% to \$17.6 million for the three months ended June 30, 2020 from \$20.4 million in the prior year comparable period. Reduced costs were a result of several factors including facilities cost savings due to facility closure during the quarter as a result of actions taken to control transmission of COVID-19; renegotiation of lease terms at certain campuses reducing rent expense; and the reduction in instructional and books and tools expenses as a result of students completing their course remotely.
- Selling, general and administrative expense decreased \$0.5 million, or 2.5% to \$20.6 million for the three months ended June 30, 2020 from \$21.1 million in the prior year comparable period. The cost savings were primarily attributed to reductions in sales expense, student services and marketing expense partially offset by an increase in bad debt expense, which are all discussed above in the consolidated results from operations.

### Healthcare and Other Professions

Operating income increased \$0.9 million to \$2.7 million for the three months ended June 30, 2020 from \$1.8 million in the prior year comparable period. The increase quarter over quarter was mainly driven by the following factors:

- Revenue remained essentially flat at \$19.5 million for the three months ended June 30, 2020 and 2019, despite the 18.9% increases in average student population. Student start growth increased 18.8% for the three months ended June 30, 2020 as compared to the prior year comparable period. As a result, the Company's ending population as of June 30, 2020 grew 24.4% compared to prior year. After excluding students who are on leave of absence as a result of the impact of COVID-19, ending population grew 17.9% or approximately 640 students. Partially offsetting student start growth was the extension of graduation dates for certain programs which have been extended due to restricted access to externships sites and classroom labs due to COVID-19. These restrictions have resulted in \$0.8 million in revenue being deferred to the second half of the year.
- Educational services and facilities expense decreased \$0.6 million, or 6.8% to \$8.7 million for the three months ended June 30, 2020 from \$9.3 million in the prior year comparable period. Reduced costs were a result of several factors including facilities cost savings due to facility closure during the quarter as a result of actions taken to control transmission of COVID-19; renegotiation of lease terms at certain campuses reducing rent expense; and the reduction in instructional and books and tools expenses as a result of students completing their course remotely.
- Selling general and administrative expense decreased \$0.3 million, or 2.9% to \$8.1 million for the three months ended June 30, 2020 from \$8.4 million in the prior year comparable period. The cost savings were primarily attributed to reductions in sales expense, student services and marketing expense partially offset by an increase in bad debt expense, which are all discussed above in the consolidated results from operations.

### Transitional

No campuses have been classified in the Transitional segment for the three months ending June 30, 2020 and 2019, respectively.

**Corporate and Other**

This category includes unallocated expenses incurred on behalf of the entire Company. Corporate and other expenses remained essentially flat at \$6.4 million for the three months ended June 30, 2020 and 2019, respectively.

The following table present results for our two reportable segments for the six months ended June 30, 2020 and 2019:

	<b>Six Months Ended June 30,</b>		
	<b>2020</b>	<b>2019</b>	<b>% Change</b>
<b>Revenue:</b>			
Transportation and Skilled Trades	\$ 91,971	\$ 88,354	4.1%
HOPS	40,540	38,479	5.4%
Total	<u>\$ 132,511</u>	<u>\$ 126,833</u>	<u>4.5%</u>
<b>Operating Income (Loss):</b>			
Transportation and Skilled Trades	\$ 9,708	\$ 4,300	125.8%
Healthcare and Other Professions	4,733	2,811	68.4%
Corporate	(14,626)	(14,069)	-4.0%
Total	<u>\$ (185)</u>	<u>\$ (6,958)</u>	<u>97.3%</u>
<b>Starts:</b>			
Transportation and Skilled Trades	4,022	3,849	4.5%
Healthcare and Other Professions	2,123	1,987	6.8%
Total	<u>6,145</u>	<u>5,836</u>	<u>5.3%</u>
<b>Average Population:</b>			
Transportation and Skilled Trades	7,302	6,935	5.3%
Leave of Absense - COVID-19	(223)	-	100.0%
Transportation and Skilled Trades Excluding Leave of Absense - COVID-19	<u>7,079</u>	<u>6,935</u>	<u>2.1%</u>
Healthcare and Other Professions	4,120	3,561	15.7%
Leave of Absense - COVID-19	(213)	-	100.0%
Healthcare and Other Professions Excluding Leave of Absense - COVID-19	<u>3,907</u>	<u>3,561</u>	<u>9.7%</u>
Total	<u>11,422</u>	<u>10,496</u>	<u>8.8%</u>
Total Excluding Leave of Absense - COVID-19	<u>10,986</u>	<u>10,496</u>	<u>4.7%</u>
<b>End of Period Population:</b>			
Transportation and Skilled Trades	7,826	7,195	8.8%
Leave of Absense - COVID-19	(463)	-	100.0%
Transportation and Skilled Trades Excluding Leave of Absense - COVID-19	<u>7,363</u>	<u>7,195</u>	<u>2.3%</u>
Healthcare and Other Professions	4,456	3,582	24.4%
Leave of Absense - COVID-19	(233)	-	100.0%
Healthcare and Other Professions Excluding Leave of Absense - COVID-19	<u>4,223</u>	<u>3,582</u>	<u>17.9%</u>
Total	<u>12,282</u>	<u>10,777</u>	<u>14.0%</u>
Total Excluding Leave of Absense - COVID-19	<u>11,586</u>	<u>10,777</u>	<u>7.5%</u>

## Six Months Ended June 30, 2020 Compared to the Six Months Ended June 30, 2019

### Transportation and Skilled Trades

Operating income increased \$5.4 million to \$9.7 million for the six months ended June 30, 2020 from \$4.3 million in the prior year comparable period. The increase year over year was mainly driven by the following factors:

- Revenue increased \$3.6 million, or 4.1% to \$92.0 million for the six months ended June 30, 2020 from \$88.4 million in the prior year comparable period. The increase was the result of a 2.1% increase in average population excluding the students on leave of absence due to COVID-19 driven by starting the year with approximately 360 more students than in the prior year comparable period. As a result, our ending population grew 8.8% compared to prior year. Excluding students on leave of absence as a result of COVID-19, ending population grew 2.3% or approximately 170 students. The majority of these students were near the end of their programs and are expected to resume their program during the third quarter as all of our schools are now open and more externship sites reopen. We do not recognize revenue during a students' leave of absence period, therefore, we anticipate earning revenue starting in the third quarter upon the students' return. Partially offsetting the increase in revenue was the impact of COVID-19, which has extended graduation dates for certain programs due to restricted access to externship sites and classroom labs. These restrictions have deferred \$0.1 million in revenue to the second half of the year. In addition, non-tuition revenue was reduced \$0.8 million due to credits issues to students for dorm and meal fees resulting from campus closures caused by COVID-19. The dorms are owned and operated by the Company. We received funds under the Cares Act which may be used to reimburse the Company for the student credits issued, but at this time we are awaiting further guidance from the DOE on the appropriate application of such funds.
- Educational services and facilities expense decreased \$2.9 million, or 7.1% to \$38.1 million for the six months ended June 30, 2020 from \$41.0 million in the prior year comparable period. Reduced costs were a result of several factors including facilities cost savings due to facility closures during the first and second quarter as a result of actions taken to control transmission of COVID-19; renegotiation of lease terms at certain campuses reducing rent expense; and the reduction in instructional and books and tools expenses as a result of students completing their course remotely.
- Selling general and administrative expenses increased \$1.2 million, or 2.8% to \$44.2 million for the six months ended June 30, 2020 from \$43.0 million in the prior year comparable period. The increase was primarily the result of an increase in bad debt expense, partially offset by cost savings realized in sales expense and student services expense discussed above in the consolidated results of operations.

### Healthcare and Other Professions

Operating income increased \$1.9 million to \$4.7 million for the six months ended June 30, 2020 from \$2.8 million in the prior year comparable period. The increase was mainly driven by the following factors:

- Revenue increased \$2.0 million, or 5.4% to \$40.5 million for the six months ended June 30, 2020 from \$38.5 million in the prior year comparable period. The increase was the result of a 9.7% increase in average population excluding the students on leave of absence due to COVID-19 driven by starting the year with approximately 400 more students than in the prior year comparable period. As a result, our ending population as of June 30, 2020 grew 24.4% compared to prior year. Excluding students on leave of absence as a result of COVID-19, ending population grew 17.9% or approximately 640 students. The majority of these students were near the end of their programs and are expected to resume their program during the third quarter as all of our schools are now open and more externship sites reopen. We do not recognize revenue during a students' leave of absence period, therefore, we anticipate earning revenue starting in the third quarter upon the students' return. Partially offsetting the increase in revenue was the impact of COVID-19 that resulted in a decrease of \$0.8 million of revenue which is being deferred to the second half of the year. The deferral resulted from certain programs that were extended due to restricted access to externship sites and classroom labs.
- Educational services and facilities expense decreased \$0.3 million, or 1.8% to \$18.4 million for the six months ended June 30, 2020 from \$18.7 million in the prior year comparable period. Reduced costs were a result of facilities cost savings due to facility closures during the first and second quarter as a result of actions taken to control transmission of COVID-19 and renegotiation of lease terms at certain campuses reducing rent expense. Partially offsetting the savings were increases in instructional expense as a result of starting the year with approximately 400 more students than prior year in correlation with an increased average student population that was up 12.5% in the first quarter of 2020 compared to the prior year comparable period. The additional costs incurred in the first quarter of 2020 were partially offset by savings realized in the second quarter of 2020.

- Selling, general and administrative expense increased \$0.5 million, or 2.8% to \$17.5 million for the six months ended June 30, 2020 from \$17.0 million in the prior year comparable period. The increase was primarily the result of an increase in bad debt expense, partially offset by cost savings realized in marketing expense, both of which are discussed above in the consolidated results of operations.

### **Transitional**

No campuses have been classified in the Transitional segment for the six months ending June 30, 2020 and 2019, respectively.

### **Corporate and Other**

This category includes unallocated expenses incurred on behalf of the entire Company. Corporate and other expenses were \$14.6 million and \$14.1 million for the six months ended June 30, 2020 and 2019, respectively.

### **LIQUIDITY AND CAPITAL RESOURCES**

Our primary capital requirements are for maintenance and expansion of our facilities and the development of new programs. Our principal sources of liquidity have been cash provided by operating activities and borrowings under our credit facility. The following chart summarizes the principal elements of our cash flow for each of the six months ended June 30, 2020 and 2019, respectively:

	Six Months Ended	
	June 30,	
	2020	2019
Net cash provided by (used in) operating activities	\$ 6,468	\$ (10,782)
Net cash used in investing activities	(2,975)	(1,212)
Net cash used in financing activities	(16,169)	(22,966)

As of June 30, 2020, the Company had a net cash balance of \$7.8 million compared to \$4.6 million at December 31, 2019. The net debt/cash balance is calculated as our cash and cash equivalents and restricted cash less both short and long-term portion of the credit agreement. Included in cash and cash equivalents and restricted cash as of June 30, 2020 is \$14.5 million received from the Cares Act. Excluding cash received under the Cares Act of \$14.5 million, as of June 30, 2020, the Company had a net debt balance of \$6.6 million. The decrease in cash position can mainly be attributed to the repayments of \$16.0 million in borrowings under our credit facility and seasonality of our business.

To fund our business plans, including any anticipated future losses, purchase commitments, capital expenditures and principal and interest payments on borrowings, we leveraged our owned real estate. We are also continuing to take actions to improve cash flow by aligning our cost structure to our student population, in addition to our current sources of capital that provide short term liquidity.

Our primary source of cash is tuition collected from our students. The majority of students enrolled at our schools rely on funds received under various government-sponsored student financial aid programs to pay a substantial portion of their tuition and other education-related expenses. The most significant source of student financing is Title IV Programs, which represented approximately 78% of our cash receipts relating to revenues in 2019. Pursuant to applicable regulations, students must apply for a new loan for each academic period. Federal regulations dictate the timing of disbursements of funds under Title IV Programs and loan funds are generally provided by lenders in two disbursements for each academic year. The first disbursement is usually received approximately 31 days after the start of a student's academic year and the second disbursement is typically received at the beginning of the sixteenth week from the start of the student's academic year. Certain types of grants and other funding are not subject to a 31-day delay. In certain instances, if a student withdraws from a program prior to a specified date, any paid but unearned tuition or prorated Title IV Program financial aid is refunded according to federal, state and accrediting agency standards.

As a result of the significant amount of Title IV Program funds received by our students, we are highly dependent on these funds to operate our business. Any reduction in the level of Title IV Program funds that our students are eligible to receive or any restriction on our eligibility to receive Title IV Program funds would have a significant impact on our operations and our financial condition. See "Risk Factors" in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2019.

## **Operating Activities**

Net cash provided by operating activities was \$6.5 million for the six months ended June 30, 2020 compared to net cash used in operating activities of \$10.8 million in the prior year comparable period. Included in the June 30, 2020 net cash balance is \$14.5 million in federal funds received under the Cares Act intended for reimbursement to students for expenses related to disruptions in campus operations (e.g., food, housing, etc.) and as permitted to use the funds to cover institutional costs associated with significant changes to the delivery of instruction due to the COVID-19 emergency, provided that those costs do not include payment to contractors for the provision of pre-enrollment recruitment activities, endowments, or capital outlays associated with facilities related to athletics, sectarian instruction, or religious worship. Excluding the federal funds received, we would have a net cash used in operating activities balance of \$8.0 million. The decrease in net cash used in operating activities for the six months ended June 30, 2020 as compared to the six months ended June 30, 2019 is primarily due to operating losses and changes in working capital such as accounts receivable, accounts payable, accrued expenses and unearned tuition year over year.

## **Investing Activities**

Net cash used in investing activities increased \$1.8 million to \$3.0 million for the six months ended June 30, 2020 compared to the six months ended June 30, 2019.

One of our primary uses of cash in investing activities was capital expenditures associated with investments in training technology, classroom furniture, and new program buildouts.

We currently lease a majority of our campuses. We own our real property in Grand Prairie, Texas; Nashville, Tennessee; and Denver, Colorado and our former school property located in Suffield, Connecticut.

Capital expenditures were 2% of revenues in 2019 and are expected to approximate 2% of revenues in 2020. We expect to fund future capital expenditures with cash generated from operating activities and borrowings under our credit facility.

## **Financing Activities**

Net cash used in financing activities was \$16.2 million for the six months ended June 30, 2020 compared to \$23.0 million in the prior year comparable period. The decrease of \$6.8 million was primarily due to decreased net payments on borrowings of \$16.0 million for the six months ended June 30, 2020 as compared to \$22.9 million in the prior year comparable period.

Net payments on borrowings consisted of: (a) total borrowing to date under our secured credit facility of \$11.0 million; and (b) \$27.0 million in total repayments made by the Company. See Part II, Item 1A. "Risk Factors — COVID-19 Pandemic" in this Quarterly Report on Form 10-Q for risks associated with COVID-19.

## **Credit Facility with Sterling National Bank**

On November 14, 2019, the Company entered into a new senior secured credit agreement (the "Credit Agreement") with its lender, Sterling National Bank (the "Lender"), pursuant to which the Company obtained a new credit facility in the aggregate principal amount of up to \$60 million (the "Credit Facility").

The Credit Facility is comprised of four facilities: a \$20 million senior secured term loan maturing on December 1, 2024 (the "Term Loan"), with monthly interest and principal payments based on 120-month amortization with the outstanding balance due on the maturity date; a \$10 million senior secured delayed draw term loan maturing on December 1, 2024 (the "Delayed Draw Term Loan"), with monthly interest payments for the first 18 months and thereafter monthly payments of interest and principal based on 120-month amortization and all balances due on the maturity date; a \$15 million senior secured committed revolving line of credit providing a sublimit of up to \$10 million for standby letters of credit maturing on November 13, 2022 (the "Revolving Loan"), with monthly payments of interest only; and a \$15 million senior secured non-restoring line of credit maturing on January 31, 2021 (the "Line of Credit Loan"). The Credit Agreement gives the Company the right to permanently terminate, in its entirety, the Revolving Loan or the Line of Credit Loan or permanently reduce the amount available for borrowing under the Revolving Loan or the Line of Credit Loan. In April 2020, the Company terminated the Line of Credit Loan.

The Credit Facility is secured by a first priority lien in favor of the Lender on substantially all of the personal property owned by the Company, as well as a pledge of the stock and other equity in the Company's subsidiaries and mortgages on parcels of real property owned by the Company in Colorado, Tennessee and Texas, at which three of the Company's schools are located, as well as a former school property owned by the Company located in Connecticut.

At the closing of the Credit Facility, the Lender advanced the Term Loan to the Company, the net proceeds of which was \$19.7 million after deduction of the Lender's origination fee in the amount of \$0.3 million and other Lender fees and reimbursements to the Lender that are customary for facilities of this type. The Company used the net proceeds of the Term Loan, together with cash on hand, to repay the existing credit facility and transaction expenses.

Pursuant to the terms of the Credit Agreement, letters of credit issued under the Revolving Loan reduce dollar for dollar the availability of borrowings under the Revolving Loan. Borrowings under the Line of Credit Loan are to be secured by cash collateral.

Borrowing under the Delayed Draw Term Loan is available during the period commencing on the closing date of the Credit Facility and ending on May 31, 2021.

Accrued interest on each loan under the Credit Facility will be payable monthly in arrears. The Term Loan and the Delayed Draw Term Loan will bear interest at a floating interest rate based on the then one month London Interbank Offered Rate ("LIBOR") plus 3.50%. At the closing of the Credit Facility, the Company entered into a swap transaction with the Lender for 100% of the principal balance of the Term Loan, which matures on the same date as the Term Loan, pursuant to a swap agreement between the Company and the Lender. At the end of the borrowing availability period for the Delayed Draw Term Loan, the Company is required to enter into a swap transaction with the Lender for 100% of the principal balance of the Delayed Draw Term Loan, which will mature on the same date as the Delayed Draw Term Loan, pursuant to a swap agreement between the Company and the Lender or the Lender's affiliate. The Term Loan and Delayed Draw Term Loan are subject to a LIBOR interest rate floor of .25% if there is no swap agreement.

Revolving Loans bear interest at a floating interest rate based on the then LIBOR plus an indicative spread determined by the Company's leverage as defined in the Credit Agreement or, if the borrowing of a Revolving Loan is to be repaid within 30 days of such borrowing, the Revolving Loan will accrue interest at the Lender's prime rate plus .50% with a floor of 4.0%. Line of Credit Loans will bear interest at a floating interest rate based on the Lender's prime rate of interest. Revolving Loans are subject to a LIBOR interest rate floor of .00%.

Letters of credit will be charged an annual fee equal to (i) an applicable margin determined by the leverage ratio of the Company less (ii) .25%, paid quarterly in arrears, in addition to the Lender's customary fees for issuance, amendment and other standard fees. Letters of credit totaling \$4 million that were outstanding under the existing credit facility are treated as letters of credit under the Revolving Loan.

Under the terms of the Credit Agreement, the Company may prepay the Term Loan and/or the Delayed Draw Term Loan in full or in part without penalty except for any amount required to compensate the Lender for any swap breakage or other costs incurred in connection with such prepayment. The Lender receives an unused facility fee of 0.50% per annum payable quarterly in arrears on the unused portions of the Revolving Loan and the Line of Credit Loan.

In addition to the foregoing, the Credit Agreement contains customary representations, warranties and affirmative and negative covenants (including financial covenants that (i) restrict capital expenditures, (ii) restrict leverage, (iii) require maintaining minimum tangible net worth, (iv) require maintaining a minimum fixed charge coverage ratio and (v) require the maintenance of a minimum of \$5 million in quarterly average aggregate balances on deposit with the Lender, which, if not maintained, will result in the assessment of a quarterly fee of \$12,500), as well as events of default customary for facilities of this type. As of June 30, 2020 the Company was in compliance with all debt covenants. As of June 30, 2020 and December 31, 2019, the Company had \$18.8 million and \$34.8 million, respectively, outstanding under the Credit Facility; offset by \$0.7 million and \$0.8 million of deferred finance fees, respectively. In January 2020, the Company repaid the \$15.0 million outstanding on the Line of Credit Loan. As of June 30, 2020 and December 31, 2019, letters of credit in the aggregate outstanding principal amount of \$4.0 million and \$4.0 million, respectively, were outstanding under the Credit Facility.

The following table sets forth our long-term debt (in thousands):

	June 30, 2020	December 31, 2019
Credit agreement	\$ 18,833	\$ 34,833
Deferred Financing Fees	(712)	(805)
	18,121	34,028
Less current maturities	(2,000)	(2,000)
	<u>\$ 16,121</u>	<u>\$ 32,028</u>

As of June 30, 2020, we had outstanding loan commitments to our students of \$71.6 million, as compared to \$75.5 million at December 31, 2019.

## Contractual Obligations

**Current portion of Long-Term Debt, Long-Term Debt and Lease Commitments.** As of June 30., 2020, our current portion of long-term debt and long-term debt consisted of borrowings under our Credit Facility. We lease offices, educational facilities and various items of equipment for varying periods through the year 2031 at basic annual rentals (excluding taxes, insurance, and other expenses under certain leases).

The following table contains supplemental information regarding our total contractual obligations as of June 30, 2020 (in thousands):

	Payments Due by Period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Credit facility*	\$ 18,833	\$ 2,000	\$ 4,000	\$ 12,833	\$ -
Operating leases	85,965	14,978	27,277	21,599	22,111
Interest on term loan**	3,528	974	1,621	933	-
Total contractual cash obligations	<u>\$ 108,326</u>	<u>\$ 17,952</u>	<u>\$ 32,898</u>	<u>\$ 35,365</u>	<u>\$ 22,111</u>

\* Excludes deferred finance fees of \$0.7 million.

\*\* Includes fixed rate interest payment resulting from the cash flow hedge.

## Off-Balance Sheet Arrangements

We had no off-balance sheet arrangements as of June 30, 2020, except for surety bonds. As of June 30, 2020, we posted surety bonds in the total amount of approximately \$11.8 million. We are required to post surety bonds on behalf of our campuses and education representatives with multiple states to maintain authorization to conduct our business. These off-balance sheet arrangements do not adversely impact our liquidity or capital resources.

## Seasonality

Our revenue and operating results normally fluctuate as a result of seasonal variations in our business, principally due to changes in total student population. Student population varies as a result of new student enrollments, graduations and student attrition. Historically, our schools have had lower student populations in our first and second quarters and we have experienced larger class starts in the third quarter and higher student attrition in the first half of the year. Our second half growth is largely dependent on a successful high school recruiting season. We recruit our high school students several months ahead of their scheduled start dates and, thus, while we have visibility on the number of students who have expressed interest in attending our schools, we cannot predict with certainty the actual number of new student enrollments and the related impact on revenue. Our expenses, however, typically do not vary significantly over the course of the year with changes in our student population and revenue. This year, due to COVID-19, it has not been a typical year and expenses have varied more significantly. During the first half of the year, we make significant investments in marketing, staff, programs and facilities to meet our second half of the year targets and, as a result, such expenses do not fluctuate significantly on a quarterly basis. To the extent new student enrollments, and related revenue, in the second half of the year fall short of our estimates, our operating results could be negatively impacted. We expect quarterly fluctuations in operating results to continue as a result of seasonal enrollment patterns. Such patterns may change as a result of new school openings, new program introductions, and increased enrollments of adult students and/or acquisitions.

## Regulations Update – Negotiated Rulemaking

On April 2, 2020, the DOE published proposed regulations related primarily to distance education and to topics addressed during negotiated rulemaking committee meetings that took place in early 2019. See the Company's disclosures in its Annual Report on Form 10-K for the fiscal year ended December 31, 2019 under the caption "Regulatory Environment – Negotiated Rulemaking." The proposed regulations address topics including, among other things, correspondence courses, direct assessment programs, foreign institutions, written arrangements with ineligible institutions or organizations to provide a portion of an educational program, requirements for prompt action by the DOE on certain Title IV eligibility applications, requirements related to the length of educational programs and entry level requirements for the occupation, the clock to credit hour conversion formula, the requirements for returning unearned Title IV Program funds received for students who withdraw before completing their educational programs, and the requirements for measuring a student's satisfactory academic progress. The proposed regulations are subject to change by the DOE in response to public comments that were received through May 4, 2020. If the DOE publishes regulations by November 1, 2020, the regulations typically would take effect by July 1, 2021 although we cannot predict the ultimate publication date or effective date of any final regulations the DOE might publish. We are in the process of analyzing the proposed regulations and their potential impact on us and our institutions.

#### Item 4. CONTROLS AND PROCEDURES

(a) *Evaluation of disclosure controls and procedures.* Our Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Securities Exchange Act Rule 13a-15(e)) as of the end of the quarterly period covered by this report, have concluded that our disclosure controls and procedures are adequate and effective to reasonably ensure that material information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

(b) *Changes in Internal Control Over Financial Reporting.* There were no changes made during our most recently completed fiscal quarter in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

As a result of the COVID-19 pandemic, certain employees of the Company began working remotely in March 2020 but these changes to the working environment did not have a material effect on the Company's internal control over financial reporting. There was no other change in the Company's internal control over financial reporting that occurred during the six months ended June 30, 2020 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

#### Item 1. LEGAL PROCEEDINGS

In the ordinary conduct of our business, we are subject to periodic lawsuits, investigations and claims, including, but not limited to, claims involving students or graduates and routine employment matters. Although we cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against us, we do not believe that any currently pending legal proceeding to which we are a party will have a material adverse effect on our business, financial condition, results of operations or cash flows. Information regarding certain specific legal proceedings in which the Company is involved is contained in Part I, Item 3, and in Note 15 to the notes to the Condensed Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2019. Unless otherwise indicated in this report, all proceedings discussed in the earlier report which are not indicated therein as having been concluded, remain outstanding as of June 30, 2020.

#### Item 1 A. RISK FACTORS

Our business activities involve a variety of risks. In addition to the risk factor below, readers should carefully consider the risk factors disclosed in Part I, Item 1A. "Risk Factors" of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2020 which was filed with the SEC on May 15, 2020.

**The pandemic caused by COVID-19 could have a materially adverse impact on our business, results of operations, financial condition and/or cash flows. The extent of the impact of the COVID-19 pandemic will depend on future developments, which are highly uncertain and largely beyond our control, including, among others, the scope and duration of the pandemic; the number of our employees, students, and vendors adversely affected by the pandemic; the broader public health and economic dislocations resulting from the pandemic; any legislative or regulatory changes or other actions taken by governmental authorities to limit the public health, financial and economic impacts of the COVID-19 pandemic; any reputational damage related to the perception of our or our industry's response to the COVID-19 pandemic; and the impact of the pandemic on local and U.S. economies.**

The COVID-19 pandemic has caused significant disruption to the U.S. and world economies, including the closing of many schools and businesses for extended periods of time, significantly higher unemployment and underemployment, significantly lower interest rates and equity market valuations, and extreme volatility in the U.S. and world financial markets. We expect that the impact of the COVID-19 pandemic on the U.S. economy will be significant during the remainder of 2020 and that it could materially adversely affect our results of operations and financial condition, and/or our cash flows.

As described in Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations — Impact of COVID-19 on the Company" in this Quarterly Report on Form 10-Q, as of June 30, 2020, the Company had 696 students on leave of absence due to COVID-19. The majority of these students were at the end of their programs and were on externship which they were not able to complete. A smaller portion of these students chose not to undertake their programs through distance learning. The Company expects a majority of these students will be back at school or an externship by the end of the year.

The Company has extended the length and graduation dates of four programs as there is only a small percentage of these four programs that can be taught through distance learning.

The Company has campuses where students live in dorms that are operated by either the Company itself, Collegiate Housing or other housing options. The majority of the students had returned home and their dorm charges have been reversed. In addition, at campuses where students have meal plans, the Company's cafeterias have been closed and all charges for meal plans have been reversed. For students that remain in dorms, the Company has given the students gift cards to assist in replacing their meal plans. As the students are returning to campus the dorms have reopened and the school has limited the number of students in dorms to adhere to social distancing.

In addition, our employees moved to a work-from-home environment. We have never had to run our operations entirely remotely for an extended period of time, and it is possible we will encounter significant challenges to running our business. Unanticipated issues arising from handling personal, confidential and other information from a less efficient work-from-home environment could adversely impact our operations and lead to greater risk for us.

The extent to which the COVID-19 pandemic impacts our business, results of operations, financial condition and/or cash flows will depend on future developments, which are highly uncertain and largely beyond our control, including, among others: the scope and duration of the pandemic; the number of our employees, students, and vendors adversely affected by the pandemic; the broader public health and economic dislocations resulting from the pandemic; any legislative or regulatory changes or other actions taken by governmental authorities to limit the public health, financial and economic impacts of the COVID-19 pandemic; any reputational damage related to the public perception of our or our industry's response to the COVID-19 pandemic; and the impact of the COVID-19 pandemic on local, and U.S. economies. However, as with many other businesses, the impact of COVID-19 on our business could be material and adverse.

## Item 6. EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>
3.1	Amended and Restated Bylaws of Lincoln Educational Services Corporation (as amended through April 24, 2020) (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q filed with the SEC on May 15, 2020).
10.1	Lincoln Educational Services Corporation 2020 Long-Term Incentive Plan (as amended) (incorporated by reference to Exhibit 10.16 to the Company's Current Report on Form 8-K filed with the SEC on June 5, 2020).
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following financial statements from Lincoln Educational Services Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2020, formatted in XBRL: (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Operations, (iii) Condensed Consolidated Statements of Comprehensive (Loss) Income, (iv) Condensed Consolidated Statements of Changes in Stockholders' Equity, (v) Condensed Consolidated Statements of Cash Flows and (vi) the Notes to Condensed Consolidated Financial Statements, tagged as blocks of text and in detail.

---

\* As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

LINCOLN EDUCATIONAL SERVICES CORPORATION

Date: August 13, 2020

By: /s/ Brian Meyers  
Brian Meyers  
Executive Vice President, Chief Financial Officer and Treasurer

## Exhibit Index

<a href="#">3.1</a>	Amended and Restated Bylaws of Lincoln Educational Services Corporation (as amended through April 24, 2020) (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q filed with the SEC on May 15, 2020).
<a href="#">10.1</a>	Lincoln Educational Services Corporation 2020 Long-Term Incentive Plan (as amended) (incorporated by reference to Exhibit 10.16 to the Company's Current Report on Form 8-K filed with the SEC on June 5, 2020).
<a href="#">31.1</a>	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<a href="#">31.2</a>	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<a href="#">32</a>	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following financial statements from Lincoln Educational Services Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2020, formatted in XBRL: (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Operations, (iii) Condensed Consolidated Statements of Comprehensive (Loss) Income, (iv) Condensed Consolidated Statements of Changes in Stockholders' Equity, (v) Condensed Consolidated Statements of Cash Flows and (vi) the Notes to Condensed Consolidated Financial Statements, tagged as blocks of text and in detail.

---

\* As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

## CERTIFICATION

I, Scott Shaw, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lincoln Educational Services Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 13, 2020

/s/ Scott Shaw

\_\_\_\_\_  
Scott Shaw  
Chief Executive Officer

---

## CERTIFICATION

I, Brian Meyers, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lincoln Educational Services Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 13, 2020

/s/ Brian Meyers

Brian Meyers  
Chief Financial Officer

---

**CERTIFICATION****Pursuant to 18 U.S.C. 1350 as adopted by  
Section 906 of the Sarbanes-Oxley Act of 2002**

Each of the undersigned, Scott Shaw, Chief Executive Officer of Lincoln Educational Services Corporation (the “Company”), and Brian Meyers, Chief Financial Officer of the Company, has executed this certification in connection with the filing with the Securities and Exchange Commission of the Company’s Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2020 (the “Report”).

Each of the undersigned hereby certifies that, to his respective knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 13, 2020

/s/ Scott Shaw

\_\_\_\_\_  
Scott Shaw  
Chief Executive Officer

/s/ Brian Meyers

\_\_\_\_\_  
Brian Meyers  
Chief Financial Officer

---