Kaplan Higher Education LLC

(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)

Consolidated Financial Statements

December 31, 2017

Kaplan Higher Education LLC and Subsidiaries
(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)
Index
December 31, 2017

K&A
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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Kaplan Higher Education LLC

We have audited the accompanying consolidated financial statements of Kaplan Higher Education LLC and its subsidiaries, which comprise the consolidated balance sheet as of December 31, 2017, and the related consolidated statement of operations, consolidated statement of stockholder's equity and statement of cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on this consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements is free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Kaplan Higher Education LLC and its subsidiaries as of December 31, 2017, and the results of its operations and its cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying Appendix A on Kaplan University Condensed Balance Sheet and Appendix B on Kaplan University Condensed Statement of Operations are required by The Higher Learning Commission of the North Central Association of Colleges and Schools and are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. Such information is not intended to be a complete presentation of financial position and results of operations of Kaplan University and has not been subjected to stand-alone audit procedures performed in conjunction with the audit of the consolidated financial statements. If Kaplan University was subject to audit procedures performed on a standalone basis, actual results may vary from those presented in the accompanying Appendix A and Appendix B. The information has been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and in our opinion, is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Knutte & Associates, P.C.

Darien, Illinois
June 27, 2018

Kaplan Higher Education LLC and Subsidiaries
(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)
Consolidated Balance Sheet

(in thousands, except share amounts)		As of December 31, 2017
Assets		
Current assets		
Cash and cash equivalents	$	127,382
Accounts and notes receivable, less allowance for doubtful accounts of $9,960		16,931
Prepaid expenses and other current assets		7,956
Total current assets		152,269
Property and equipment		23,506
Goodwill		182,596
Intangible assets		5,268
Other assets		823
Total assets	$	364,462
Liabilities and Stockholder's Equity		
Current liabilities		
Accounts payable and accrued expenses	$	16,923
Accrued compensation and benefits		14,897
Deferred revenue		52,833
Other current liabilities		15,519
Total current liabilities		100,172
Due to related parties		19,422
Deferred income taxes		13,133
Other liabilities		11,809
Total liabilities		144,536
Stockholder's equity		
Common stock, $ .01 par value-authorized 100 shares; 100 shares issued and outstanding		10
Additional paid-in capital		159,664
Retained earnings		60,252
Total stockholder's equity		219,926
Total liabilities and stockholder's equity	$	364,462

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

Kaplan Higher Education LLC and Subsidiaries
(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)
Consolidated Statement of Operations

(in thousands)	Year Ended December 31, 2017
Revenues	$ 546,495
School operating expenses	
Educational services	105,697
Marketing and advertising	94,044
Admissions	70,663
General and administrative expenses	232,165
Amortization of intangible assets	1,033
Total operating expenses	503,602
Income from continuing operations before income taxes	42,893
Provision for income taxes	11,430
Net income	$ 31,463

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

Kaplan Higher Education LLC and Subsidiaries
(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)
Consolidated Statement of Stockholder's Equity

(in thousands, except per share amounts)

	Common Stock		Additional Paid-in	Retained	
	Shares	Amount	Capital	Earnings	Total
As of December 31, 2016	100	$ 10	$ 249,664	$ 28,789	$ 278,463
Net income for the year				31,463	31,463
Dividends			(90,000)		(90,000)
As of December 31, 2017	100	$ 10	$ 159,664	$ 60,252	$ 219,926

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

Kaplan Higher Education LLC and Subsidiaries

(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)

Consolidated Statement of Cash Flows

(in thousands)	Year Ended December 31, 2017
Operating activities	
Net income	$ 31,463
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities	
Depreciation and amortization	12,158
Amortization of other intangible assets	1,033
Provision for losses on accounts receivable and notes receivable	25,151
Deferred income taxes	(5,097)
Changes in operating assets and liabilities, net of assets acquired and liabilities assumed	
Accounts and notes receivable	(22,475)
Prepaid expenses and other current assets	(1,018)
Other assets	739
Accounts payable and accrued expenses	(4,508)
Deferred revenue	9,061
Other liabilities	7,648
Net cash and cash equivalents provided by operating activities	54,155
Cash flow from investing activities	
Purchase of property and equipment	(4,711)
Net cash and cash equivalents used in investing activities	(4,711)
Cash flow from financing activities	
Dividends	(90,000)
Kaplan intercompany - changes during year	(1,196)
Net cash and cash equivalents used in financing activities	(91,196)
Net decrease in cash and cash equivalents	(41,752)
Cash and cash equivalents at beginning of year	169,134
Cash and cash equivalents at end of year	$ 127,382
Supplemental disclosure of cash flow information	
Cash paid during the year for	
Income taxes paid	$ 46

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

1. Organization and Nature of Business

Kaplan Higher Education LLC ("Kaplan Higher Education", "KHE" or the "Company") through its wholly owned subsidiaries operates diversified career-oriented postsecondary education schools and online programs from high school diplomas to graduate and professional degrees, professional licenses, designations and certifications. This includes solutions for insurance, securities, real estate, mortgage and appraisal licensing exams and for advanced designations, such as CFA and CPA exams, along with industry-recognized certifications such as Microsoft, Oracle, Novell and Cisco. As of December 31, 2017, the Company offers degree and, in certain locations, diploma programs through their 19 campuses located in 8 states as well as online throughout the United States. The Company's college and graduate level programs offer students the knowledge and skills necessary for employment in a range of fields, including healthcare, business, information technology, legal, and fashion and design.

The Company derived less than 74% of its receipts for the year ended December 31, 2017, from Title IV programs as provided for by the Higher Education Act of 1965, as amended.

2. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation
The accompanying Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States and include the assets, liabilities, results of operations and cash flows of its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates
The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Management bases its estimates and assumptions on historical experience and on various other factors that are believed to be reasonable under the circumstances. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be affected by changes in those estimates. On an ongoing basis, the Company evaluates its estimates and assumptions.

Business Combinations
The purchase price of an acquisition is allocated to the assets acquired, including intangible assets and liabilities assumed, based on their respective fair values at the acquisition date. Acquisition-related costs are expensed as incurred. The excess of the cost of an acquired entity over the net of the amounts assigned to the assets acquired and liabilities assumed is recognized as goodwill. The net assets and results of operations of an acquired entity are included in the Company's Consolidated Financial Statements from the acquisition date.

Cash and Cash Equivalents
Cash and cash equivalents consist of cash on hand, short-term investments with original maturities of three months or less, investments in money market funds with weighted average maturities of three months or less and restricted cash balances, held for students that were received from U.S. Federal and state governments under various aid grant and loan programs, such as Title IV of the U.S. Federal Higher Education Act of 1965, as amended, that the Company is required to maintain pursuant to U.S. Department of Education and other regulations.

At December 31, 2017, the Company held $2.5 million in cash balances at certain financial institutions which amounts were in excess of the $250,000 federally insured amounts and $123.1 million in money market funds. The Company monitors the financial condition of these institutions since the Company is exposed to credit risk for such excess amounts; however, at this time the Company does not believe any of these institutions present such risk and has not experienced any losses from these arrangements.

Fair Value Measurements

Fair value measurements are determined based on the assumptions that a market participant would use in pricing an asset or liability based on a three-tiered hierarchy that draws a distinction between market participant assumptions based on (i) observable inputs, such as quoted prices in active markets (Level 1); (ii) inputs other than quoted prices in active markets that are observable either directly or indirectly (Level 2) and (iii) unobservable inputs that require the Company to use present value and other valuation techniques in the determination of fair value (Level 3). Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measure. The Company's assessment of the significance of a particular input to the fair value measurements requires judgment and may affect the valuation of the assets and liabilities being measured and their placement within the fair value hierarchy.

The Company's financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2017 were as follows:

	Fair Value Measurements			
(in thousands)	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable (Level 2)	Unobservable Inputs (Level 3)	Fair Value
Assets				
Money market investments	$ -	$ 123,128	$ -	$ 123,128
Total financial assets	$ -	$ 123,128	$ -	$ 123,128

Assets and liabilities that are measured using significant other observable inputs are primarily valued by reference to quoted prices of similar assets or liabilities in active markets, adjusted for any terms specific to that asset or liability.

The Company measures certain assets - including goodwill; intangible assets; property, plant and equipment; cost method investments - at fair value on a nonrecurring basis when they are deemed to be impaired. The fair value of these assets is determined with valuation techniques using the best information available and may include quoted market prices, market comparables and discounted cash flow models.

Fair Value of Financial Instruments

The carrying amounts reported in the Company's Consolidated Financial Statements for cash and cash equivalents including restricted cash; accounts receivable; prepaid and other current assets; accounts payable and accrued liabilities; and the current portion of deferred revenue approximate fair value because of the short-term nature of these financial instruments.

Allowance for Doubtful Accounts
Accounts and notes receivable have been reduced by an allowance for amounts that may be uncollectible in the future. This estimated allowance is based primarily on the aging category, historical collection experience and management's evaluation of the financial condition of the customer. The Company generally considers an account past due or delinquent when a student or customer misses a scheduled payment. The Company writes off accounts and notes receivable balances deemed uncollectible against the allowance for doubtful accounts following the passage of a certain period of time, or generally when the account is turned over for collection to an outside collection agency.

Property and Equipment
Property and equipment are recorded at cost. Replacements and major improvements are capitalized; maintenance and repairs are expensed as incurred. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the related assets or the remaining lease terms for leasehold improvements, if shorter. Estimated useful lives for financial reporting purposes are as follows:

Buildings and building improvements	7–40 years
Equipment, furniture and fixtures	3–10 years
Leasehold improvements	1–15 years
Computer software	3–7 years

Costs incurred to develop computer software for internal use are accounted for in accordance with Financial Accounting Standards Boards ("FASB") guidance, Accounting Standards Codification ("ASC") Topic 350-40, "Internal-Use Software". As required, the Company capitalizes the costs incurred during the application development stage, which include costs to design the software configuration and interfaces, coding, installation and testing. Costs incurred during the preliminary project along with post-implementation stages of internal use computer software are expensed as incurred. Capitalized development costs are amortized over three to seven years and amortization begins when the computer software is ready for use. Costs incurred to maintain existing software are expensed as incurred. The capitalization and ongoing assessment of recoverability of development costs requires judgment by management with respect to certain external factors, including, but not limited to, technological and economic feasibility, and estimated economic life.

Evaluation of Long-Lived Assets
The recoverability of long-lived assets and finite-lived intangible assets is assessed whenever adverse events or changes in circumstances indicate that recorded values may not be recoverable. A long-lived asset is considered to not be recoverable when the undiscounted estimated future cash flows are less than the asset's recorded value. An impairment charge is measured based on estimated fair market value, determined primarily using estimated future cash flows on a discounted basis. Losses on long-lived assets to be disposed of are determined in a similar manner, but the fair market value would be reduced for estimated costs to dispose.

Goodwill and Other Intangible Assets
Goodwill arises in the course of purchasing schools and consists of the excess of purchase price over the fair value of identified net assets of businesses acquired. Goodwill is reviewed at least annually for impairment. The Company reviews the carrying value of goodwill utilizing a discounted cash flow model. The Company must make assumptions regarding estimated future cash flows and market values to determine a reporting unit's estimated fair value. If these estimates or related

assumptions change in the future, the Company may be required to record an impairment charge. The Company performed an impairment test of goodwill as of December 31, 2017, in accordance with ASC Topic 350, “Goodwill and Other”, and concluded that no impairment of goodwill exists.

Other intangible assets arise in the course of purchasing schools and development of specialized curriculum and consist primarily of the value of acquired student and customer relationships, trademarks, product development and content of developed curriculum, and non-compete covenants with management of the acquired schools, which are all amortized on a straight-line basis over three to ten years; and also include the value of Title IV financial aid eligibility and accreditations, which are not amortized but are reviewed at least annually for impairment.

Cost Method Investment
The Company uses the cost method of accounting for its minority investment in a nonpublic company where it does not have significant influence over the operations and management of the investee. Investments are recorded at the lower of cost or fair value as estimated by management.

Revenue Recognition
Revenue is recognized when persuasive evidence of an arrangement exists, the fees are fixed or determinable, the product or service has been delivered and collectability is reasonably assured. The Company considers the terms of each arrangement to determine the appropriate accounting treatment. Revenue consists primarily of tuition, fees and course materials derived from courses and offerings taught in the Company’s schools and online, net of discounts, drops and rebates. Tuition and fee revenues are recognized on a proportionate daily basis over the course delivery period or the length of student access to the online course. If a student withdraws from a course or program, the paid but unearned portion of the student tuition is refunded.

Deferred revenue is the portion of payments received but not earned and is reflected as a current or long term liability in the accompanying consolidated balance sheet based on the timeframe in which the deferred revenue will be earned.

Educational Services Expense
Educational services expense includes direct operating expenses of the schools consisting primarily of payroll and payroll related occupancy and supplies costs.

Marketing and Advertising Expense
Marketing and advertising expense consists primarily of payroll and payroll related, direct response and other advertising, promotional materials and other related marketing costs. Marketing and advertising costs are expensed as incurred.

Admissions Expense
Admissions expense consists primarily of payroll and payroll related costs for admissions staff at schools.

Income Taxes
The Company uses the liability method of accounting for income taxes. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and the tax bases of assets and liabilities measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Such amounts are computed based on a separate income tax return basis.

3. Regulatory Matters

Title IV Eligibility and Compliance with Title IV Program Requirements. To maintain eligibility to participate in Title IV programs ("Title IV Program") administered by the United States Department of Education ("ED") pursuant to the Federal Higher Education Act of 1965 as amended ("HEA"), a school must comply with extensive statutory and regulatory requirements relating to its financial aid management, educational programs, financial strength, administrative capability, compensation practices, facilities, recruiting practices, representations made to current and prospective students and various other matters. In addition, the school must be licensed, or otherwise legally authorized, to offer postsecondary educational programs by the appropriate governmental body in the state or states in which it is physically located or is otherwise subject to state authorization requirements, be accredited by an accrediting agency recognized by the ED and be certified to participate in the Title IV programs by the ED. Schools are required periodically to apply for renewal of their authorization, accreditation or certification with the applicable state governmental bodies, accrediting agencies and the ED. In accordance with ED regulations, KHE campuses are grouped into a main campus and additional campus locations. KHE is assigned its own identification number, known as an OPEID number, for the purpose of determining compliance with certain Title IV requirements. No assurance can be given that KHE or its individual programs will maintain their Title IV eligibility, accreditation and state authorization in the future or that the ED might not successfully assert that KHE has previously failed to comply with Title IV requirements.

The Company derives a substantial portion of its net revenues from financial aid received by its students under Title IV programs. In order to continue to participate in Title IV Programs, the Company must comply with complex standards set forth in the HEA and the regulations promulgated there under ("Regulations"). Among other things, these Regulations require the Company's schools to exercise due diligence in approving and disbursing funds and servicing loans, limit the proportion of cash receipts of its schools derived from Title IV Programs to no more than 90% of the total net revenue derived from the school's students in its Title IV eligible educational programs, and to exercise financial responsibility related to maintaining certain financial covenants. All of the Company's schools participate in Title IV Programs and management believes they are in compliance with the Regulations (See Appendix B).

The failure of any of the Company's schools to comply with the requirements of the HEA or the Regulations could result in the restriction or loss by the Company or such school of its ability to participate in Title IV Programs. If the Department determines that any of its schools is not financially responsible, the Department may require that the Company or such school post an irrevocable letter of credit in an amount equal to not less than one-half of Title IV Program funds received by the relevant school during the last complete award year or, at the Department's discretion, require some other less onerous demonstration of financial responsibility. One-half of Title IV funds received by an individual school for the year ended December 31, 2017, ranged from $1 million to $151.4 million and one-half of the aggregate Title IV funds received by all of the Company's schools equaled $187 million.

Department regulations also cover financial responsibility. There are three financial responsibility tests as follows: an equity ratio, a primary reserve ratio and a net income ratio. The equity ratio measures the institution's capital resources, ability to borrow and financial viability. The primary reserve ratio measures the institution's ability to support current operations from expendable resources. The net income ratio measures the ability to operate at a profit. The results of each ratio are assigned a strength factor on a scale from negative 1.0 to positive 3.0, with negative 1.0 reflecting financial weakness and 3.0 reflecting financial strength. An institution's strength factors are then weighted based on an assigned weighting percentage for each ratio. The weighted scores for the three ratios are then added together to produce a composite score for the institution. The composite score must be at least 1.5 for the institution to be deemed financially responsible by the Department without the need for further financial oversight. If the institution's composite score is less than 1.5, but equal to or greater than 1.0, the institution may continue in the Title IV Program for a maximum period of three years, subject to more rigorous financial aid disbursement and financial monitoring requirements of the Department. The Company's calculated consolidated composite score for the year ended December 31, 2017, totaled 1.7.

In instances where an institution has made Title IV refunds to students in the previous two years later than the prescribed guidelines, the institution is required to post a letter of credit for the benefit of the Department. As of December 31, 2017, the Company has no outstanding letters of credit due to late refunds.

As a result of the Company's participation in the Title IV program, the Company's schools are subject to periodic program reviews and audits by regulating bodies.

On February 23, 2015, the Department began a review of Kaplan University. The review will assess Kaplan's administration of its Title IV, HEA programs and will initially focus on the 2013 to 2014 and 2014 to 2015 award years. On December 17, 2015, Kaplan University received a notice from the ED that it had been placed on provisional certification status until September 30, 2018, in connection with the open and ongoing ED program review. The ED has not notified Kaplan University of any negative findings. However, at this time, Kaplan cannot predict the outcome of this review, when it will be completed or any liability or other limitations that the ED may place on Kaplan University as a result of this review. During the period of provisional certification, Kaplan University must obtain prior ED approval to open a new location, add an educational program, acquire another school or make any other significant change.

There are four remaining outstanding program reviews at campuses that were part of the Company and were sold to ECA in 2015. The Company retains responsibility for any financial obligation resulting from the program reviews at the KHE Campuses business that were open at the time of sale of the campuses to ECA.

The Company does not expect the open program reviews to have a material impact on KHE; however, the results of open program reviews and their impact on Kaplan's operations are uncertain.

Borrower Defense to Repayment Regulations. On November 1, 2016, the ED issued final rules that would have become effective on July 1, 2017, but were subsequently delayed, that expand the bases on which borrowers may obtain a discharge of their federal financial aid loans and that establish a process for the ED to commence a separate proceeding against the institution to recover the discharged amounts. Prior to the effective date, on June 14, 2017, the ED delayed implementation of a large portion of the rule. Multiple state attorneys general have sued the ED to force reinstatement of the rules.

The final rules amend existing procedures and standards for borrowers seeking the discharge of certain Title IV loans first disbursed prior to July 1, 2017, based on certain acts or omissions of the institution. The final rules also expand the bases for borrowers to obtain discharges of certain Title IV loans first disbursed on or after July 1, 2017, including any substantial misrepresentations by the school or any of its representatives or individuals or entities with whom the institution has an agreement, certain breaches of contract and certain judgments against the school. The final rules include procedures for borrowers to assert discharge claims as a group rather than individually and create extended and, in some cases, unlimited statutes of limitation for the submission of discharge claims. The final rules also establish procedures for the evaluation of claims, for minimal school participation in the process and for the ED to consolidate and present borrower claims during the process. If the borrower discharge claims are approved, the ED may discharge some or all of the loans and initiate a separate proceeding to recover any discharged loans from the institution.

On October 24, 2017, the ED published an interim final rule that delayed until at least July 1, 2018, the effective date of the majority of these regulations. On the same date, the ED also published a notice of proposed rulemaking that proposed to further delay, until July 1, 2019, the effective date of the majority of the regulations to ensure that there is adequate time to conduct negotiated rulemaking and, as necessary, develop revised regulations. Comments on the proposal were due by November 24, 2017. The ED convened the first meeting of negotiated rulemaking in November 2017 and convened additional meetings in early 2018. The ED intends to issue proposed regulations for public comment during the first half of 2018, but the ED has not established a final schedule. Any regulations published in final form by November 1, 2018, typically would take effect on July 1, 2019, but there is no assurance as to the timing or content of any such regulations. On February 14, 2018, the ED issued a final regulation delaying the effective date of most of the provisions with respect to borrower defense to repayment until November 1, 2019. The ED has indicated that, in the meantime, it will continue to accept claims with respect to borrower defense to repayment and process them under pre-2016 policies and practices.

We cannot predict how the ED would interpret and enforce the new borrower defense to repayment rules if they take effect after the delay or how these rules, or any rules that may arise out of the negotiated rulemaking process, may impact KHE's participation in the Title IV programs; however, the new rules could have a material adverse effect on Kaplan's business and results of operations, and the broad sweep of the rules may, in the future, require Kaplan to submit a letter of credit as indicated above.

Gainful Employment. Under the Higher Education Act, certain education programs, including all programs offered by proprietary institutions such as KHE, are required to lead to gainful employment in a recognized occupation in order to be eligible to participate in the Title IV programs. The ED has defined the phrase "gainful employment" to mean employment with earnings high enough to meet specific student debt-to-income ratios. The ED tied an education program's Title IV eligibility to whether the program meets that definition. These regulations are known as the "Gainful Employment" regulation or "GE" rules. A final Gainful Employment regulation was released on October 31, 2014. The final rule went into effect on July 1, 2015, and Kaplan timely submitted the required Gainful Employment data to the ED.

As noted previously, the final rule maintained the debt-to-earnings thresholds requiring that each GE program show that its graduates' debt payment on loans taken out to attend the program are no more than a certain percentage of their earnings. If a program fails this metric multiple years in a row, it will become ineligible for Title IV aid. Under the debt-to-earnings rates, a program passes the test if its annual debt-to-earnings rate does not exceed 8% or its discretionary debt-to-earnings rate does not exceed 20%. A program fails the test if its annual debt-to-earnings rate exceeds 12% and its discretionary debt to earnings rate exceeds 30%. A program is in a regulatory status called the "warning zone" if it does not pass or fail the test (i.e., either its annual debt-to-earnings rate is greater than 8%, but less than 12%, or its discretionary debt-to-earnings rate is greater than 20%, but less than 30%). If a program fails the test two times within three years, it will become ineligible to participate in the Title IV programs for a period of three years. If a program is either in the warning zone or fails the test for four consecutive years, it will also become ineligible to participate in Title IV programs for a period of three years. In addition, the regulation requires an institution to provide to current and prospective students prescribed warnings of potential ineligibility of the program in any year for which the program could become ineligible based on the prior-year GE rates. Institutions with such programs also must wait to enroll prospective students into the failing program until three days after providing the warning to students. Such institutions also may be required to submit a letter of credit or other financial protection to the ED under the new borrower defense to repayment regulations noted in this disclosure, although the effective date of these regulations has been delayed.

The rules also included revised requirements for program approval, public disclosures on certain outcomes (graduation, placement, repayment rates and other consumer information) and a “certification” requirement that each program is included in the school’s accreditation grant and has programmatic-level accreditation if required for licensure in the occupation. This “certification” requirement has a material negative impact on KHE’s Concord Law School’s Juris Doctor program, which accounted for less than 1% of KHE’s 2017 revenue. Because it is completely online, that program does not have the accreditation necessary to allow graduates to become licensed to practice law upon graduation and qualify to take the bar exam in any state other than California. Accordingly, because the ED has not provided guidance that narrows the rule as written, in 2015, Concord Law School was required to cease enrollments in multiple states.

KHE implemented actions to mitigate the potential impact of the GE regulations on certain programs that may fail the GE debt-to-income ratio by discontinuing likely failing programs and placing tuition caps on certain other programs. New programs have replaced a significant portion of the intake loss of the discontinued programs (isolating for general declines in all programs). Kaplan believes that the new programs are not “substantially similar” under the GE rules to any other current or past programs. However, if the ED determines that these new programs are substantially similar and combines the new programs with programs that are currently in the warning zone or that failed the GE test, eligibility of the new programs to participate in Title IV programs and revenues from such programs would be materially adversely affected. The GE rules do not apply to degree programs (Graduate degrees, Associate’s and Bachelor’s) at non-profit or public institutions such as the new university.

In October 2016, the ED issued draft debt-to-earnings rates. KHE had five programs in which the draft rates failed the GE test; however, two of these five programs are not active and the remaining three are not currently accepting enrollments. KHE has 16 programs in which the draft rates put them in warning zone status. Four of these programs are active and accounted for $71 million and $51.1 million in revenue for 2015 and 2016, respectively. For 2017, these four programs accounted for $44.5 million in revenue. KHE continues to employ mitigation actions to minimize the financial impact of GE and secure GE compliance. Of the remaining 12 programs, five were suspended several years ago and have no active students and seven of these programs are not currently accepting enrollments.

On January 9, 2017, the ED released the final first-year debt-to-earnings rates, which did not change from the draft rates issued in October 2016. Under the GE regulations, KHE has the ability to challenge the underlying data used in the debt-to-earnings calculations. KHE has appealed the underlying earnings data in certain programs that fell into the fail or warning zone category. If successful, the appeals could shift the number of programs in each category favorably.
On June 30, 2017, the ED announced the extension of the compliance date for certain gainful employment disclosure requirements from July 1, 2017, to July 1, 2018, and subsequently relaxed the documentation requirements for alternate earnings appeals. On August 18, 2017, the ED extended to February 1, 2018, the deadline for all programs to file supporting documents for their alternate earnings appeals. The ED has not announced a delay or suspension in the enforcement of any other GE regulations. However, on August 8, 2017, ED officials announced that the ED did not have a timetable for the issuance of lists of students who completed programs, which is the first step toward generating the data for calculating new gainful employment rates. Consequently, we cannot predict when the ED will begin the process of calculating and issuing new draft or final

gainful employment rates in the future. We also cannot predict whether the announcement of the intent to initiate gainful employment rulemaking, discussed below, or the extension of certain gainful employment deadlines may result in the ED delaying the issuance of new draft or final gainful employment rates in the future.

On June 15, 2017, the ED announced its intention to convene a negotiated rulemaking committee to develop proposed regulations to revise the GE rules. The committee convened in December 2017, will continue to meet in early 2018, and may issue proposed regulations for public comment during the first half of 2018, but the ED has not established a final schedule for publication of proposed or final regulations. Any regulations published in final form by November 1, 2018, typically would take effect on July 1, 2019, but we cannot provide any assurances as to the timing or content of any such regulations.

Some of the data needed to compute debt-to-earnings rates and project their impact on Title IV program eligibility under the GE regulations are not accessible to the Company, including specific graduate earnings information that will be compiled by the Social Security Administration. In addition, the continuing eligibility of programs for Title IV funding may be affected by factors beyond Kaplan's control, such as changes in the actual or deemed earnings level of its graduates, changes in student borrowing levels, increases in interest rates, changes in the U.S. Federal poverty income level relevant for calculating one of the proposed debt-to-earnings rates and other factors. As a result, the ultimate outcome of future GE rates and their impact on Kaplan's operations are still uncertain. Kaplan is continuing efforts to mitigate any current and potential negative impact of the GE rules. These efforts include increasing career services support, implementing financial literacy counseling, creating program-specific tuition reductions and scholarships and revising the pricing model to implement a tuition cap for at-risk programs. Although Kaplan is taking these and other steps to address compliance with GE regulations, there is no assurance that these measures will be adequate to prevent a material number of programs from receiving debt-to-earnings rates that fail or are in the warning zone and to prevent a loss of Title IV eligibility. This has caused Kaplan to eliminate or limit enrollments in certain educational programs at some of its schools; may result in the loss of student access to Title IV programs; and has had and may continue to have a material adverse effect on KHE's revenues, operating income and cash flows.

The 90/10 Rule. Under regulations referred to as the 90/10 rule, an institution would lose its eligibility to participate in Title IV programs for a period of at least two fiscal years if the institution derives more than 90% of its receipts from Title IV programs, as calculated on a cash basis in accordance with the Higher Education Act and applicable ED regulations, in each of two consecutive fiscal years. An institution with Title IV receipts exceeding 90% for a single fiscal year would be placed on provisional certification and may be subject to other enforcement measures, including a potential requirement to submit to the ED a letter of credit under the borrower defense to repayment regulations that were scheduled to take effect on July 1, 2017, but were subsequently delayed. KHE derived less than 74% of its receipts from Title IV programs in 2017.

KHE is taking various measures to reduce the percentage of its receipts attributable to Title IV funds, including modifying student payment options; emphasizing direct-pay and employer-paid education programs; encouraging students to evaluate carefully the amount of their Title IV borrowing; eliminating some programs; cash-matching; and developing and offering additional non-Title IV-eligible certificate preparation, professional development and continuing education programs. Kaplan has taken steps to ensure that revenue from programs acquired by KHE is eligible to be counted in that campus's 90/10 calculation. However, there can be no guarantee that the ED will not challenge the inclusion of revenue from any acquired program in KHE's 90/10 calculations or will not issue an interpretation of the 90/10 rule that would exclude such revenue from the calculation. There can be no guarantee that these measures will be adequate to prevent the 90/10 ratio at KHE from exceeding 90% in the future. In addition, certain legislators have proposed amendments to the Higher Education Act that would lower the threshold percentage in the 90/10 rule to 85%, treat non-Title IV federal funds as Title IV funds in the 90/10 calculation and make other refinements to the calculation. If these proposals or similar laws or regulations are adopted, they would make it more difficult for KHE's institutions to comply with the 90/10 rule.

Change of Control. If an institution experiences a change of control, such as the proposed transfer of KHE, under the standards of applicable state agencies, accrediting agencies or the ED, the institution must seek the approval of the relevant agencies. An institution that undergoes a change of control, which may include a change of control of the institution's parent corporation or other owners, must be reviewed and recertified by the ED and obtain approvals from certain state agencies and accrediting bodies, in some cases prior to the change of control. The standards pertaining to a change of control are not uniform and are subject to interpretation by the respective agencies. Certifications obtained from the ED following a change of control are granted on a provisional basis that permits the institution to continue participating in Title IV programs, but provides fewer procedural protections than full certifications. As a result, the ED may withdraw an institution's provisional certification more easily than if it is fully certified. In addition, the ED may subject an institution on provisional certification status to greater scrutiny in some instances, for example, when it applies for approval to add a new location or program or makes another substantive change. As noted above, the proposed transfer of KHE is subject to regulatory approval by the ED, HLC, and certain other agencies.

State Authorization. Kaplan's institutions and programs are subject to state-level regulation and oversight by state licensing agencies, whose approval is necessary to allow an institution to operate and grant degrees or diplomas in the state. State laws may establish standards for instruction, qualifications of faculty, location and nature of facilities, financial policies and responsibility and other operational matters. Institutions that participate in Title IV programs must be legally authorized to operate in the state in which the institution is physically located or is otherwise subject to state authorization requirements.

Some states have sought to assert jurisdiction over online educational institutions that offer education services to residents in the state or to institutions that advertise or recruit in the state, notwithstanding the lack of a physical location in the state. State regulatory requirements for online education vary among the states, are not well developed in many states, are imprecise or unclear in some states and are subject to change. If KHE is found not to be in compliance with an applicable state regulation and a state seeks to restrict one or more of KHE's business activities within its boundaries, KHE may not be able to recruit or enroll students in that state and may have to cease providing services in that state. If a state's requirements are found not to be in compliance with ED regulations or if KHE's institutions do not receive state approvals where necessary, the institutions could be deemed to lack the state authorization necessary to participate in the Title IV programs and be subject to loss of Title IV eligibility, repayment obligations and other sanctions. Due to an exemption, KHE's home state of Iowa does not require KHE to be registered in Iowa. However, to comply with the law, KHE was granted affirmative registration in Iowa. Kaplan believes that all of KHE's campuses currently meet the ED requirements to be considered legally authorized to provide the programs they offer in the states in which the campuses are located. The ED has stated that it will not publish a list of states that meet, or fail to meet, the state authorization requirements, and it is uncertain how the ED will interpret these requirements in each state.

On December 19, 2016, the ED issued final regulations regarding distance-education state authorization requirements that may require KHE to be authorized in additional states, as well as regulations applicable to institutions with Title IV participating locations in a foreign country. These regulations, however, recognize state authorization reciprocity agreements, in which KHE participates, as a means of satisfying the Title IV requirement. An institution must be able to document its approval under a state authorization reciprocity agreement, upon the ED's request, if it does not have a separate authorization in a state where it enrolls distance-education students. The regulations are not scheduled to take effect until July 1, 2018.

Specifically, the regulations will require an institution that offers postsecondary education through distance education in a state in which the institution is not physically located, or in which the state determines that the institution is otherwise subject to the state's jurisdiction, to meet the state's authorization requirements for offering postsecondary distance education in that state or show that it is authorized through a reciprocity agreement. The regulations also will require the institution to document that there is a state process for review and appropriate action on complaints from enrolled students in each such state. In addition, the regulations will require the institution to provide public disclosures regarding various matters relating to its state authorization and to provide individualized disclosures to each prospective student regarding certain matters, including whether the student's program fails to meet licensure or certification prerequisites in the state in which the student resides.

If Kaplan is unable to obtain the required approvals for distance-education programs by the effective date of the new regulations, then Kaplan students residing in the state for which approval was not obtained may be unable to receive Title IV funds, which could have a material adverse effect on Kaplan's business and operations. The implementation of this rule may further limit Concord's ability to enroll students in its Juris Doctor program outside of California and may materially impact Concord's revenue.

Congressional Reauthorization of Title IV Programs. All of the Title IV programs are subject to periodic legislative review and reauthorization. In addition, while Congress historically has not limited the amount of funding available for the various Title IV student loan programs, the availability of funding for the Title IV programs that provide for the payment of grants is primarily contingent upon the outcome of the annual U.S. Federal appropriations process. Congress also can make changes in the laws affecting Title IV programs in those annual appropriations bills and in other laws it enacts between Higher Education Act reauthorizations. The Higher Education Act was reauthorized through September 2014 and has continued to receive annual appropriations. The House Education and the Workforce Committee approved a reauthorization bill on December 13, 2017. The Senate Health, Education, Labor and Pensions (HELP) Committee has indicated it plans to develop its own reauthorization bill. It is not known if or when Congress will pass final legislation that amends the Higher Education Act or other laws affecting U.S. Federal student aid. Whether as a result of changes in the laws and regulations governing Title IV programs, a reduction in Title IV program funding levels or a failure of KHE to maintain eligibility to participate in Title IV programs, a material reduction in the amount of Title IV financial assistance available to the students attending those schools could have a material adverse effect on Kaplan's business and operations. In addition, any development that has the effect of making the terms on which Title IV financial assistance is made available materially less attractive could also have a material adverse effect on Kaplan's business and operations.

Program Reviews, Audits and Investigations. Kaplan's schools are subject to audits and program compliance reviews by various external agencies, including the ED; its Office of the Inspector General; other federal agencies, including the Department of Defense and the Department of Veterans Affairs; and state and accrediting agencies. While program reviews may be undertaken for a variety of reasons, they are performed routinely as part of regulatory oversight of institutions that participate in Title IV or federal or state student funding programs. If the ED or another regulatory agency determines that an institution has improperly disbursed Title IV or other federal or state program funds or violated a provision of the Higher Education Act or other federal or state law or regulations, the affected institution may be required to repay funds to the ED or the appropriate federal or state agency or lender and may be assessed an administrative fine and be subject to other sanctions. Although Kaplan endeavors to comply with all U.S. Federal and state laws and regulations, Kaplan cannot guarantee that its interpretation of the relevant rules will be upheld by the ED or other agencies or upon judicial review.

On February 23, 2015, the ED began a review of KHE. The review will assess Kaplan's administration of its Title IV and Higher Education Act programs and will initially focus on the 2013 to 2014 and 2014 to 2015 award years. On December 17, 2015, KHE received a notice from the ED that it had been placed on provisional certification status until September 30, 2018, in connection with the open and ongoing ED program review. The ED has not notified KHE of any negative findings. However, at this time, Kaplan cannot predict the outcome of this review, when it will be completed or any liability or other limitations that the ED may place on KHE as a result of this review. During the period of provisional certification, KHE must obtain prior ED approval to open a new location, add an educational program, acquire another school or make any other significant change.

In addition, there are two open program reviews at campuses that were part of the KHE Campuses business prior to its sale in 2015 to Education Corporation of America (ECA), and the ED's final reports on the program reviews at former KHE Broomall, PA, and Pittsburgh, PA, locations are pending. Kaplan retains responsibility for any financial obligation resulting from the ED program reviews at the KHE Campuses business that were open at the time of sale.

Return of Title IV Funds. ED regulations require schools participating in Title IV programs to calculate correctly and return on a timely basis unearned Title IV funds disbursed to students who withdraw from a program of study prior to completion. These funds must be returned in a timely manner, generally within 45 days of the date the school determines that the student has withdrawn. Under ED regulations, failure to make timely returns of Title IV program funds for 5% or more of students sampled in a school's annual compliance audit, or in a program review or Office of the Inspector General (OIG) audit could result in a requirement that the school post a letter of credit in an amount equal to 25% of its prior-year returns of Title IV program funds. Currently, KHE is not required to post a letter of credit. If unearned funds are not properly calculated and returned in a timely manner, an institution is subject to monetary liabilities, fines or other sanctions.

Kaplan recently determined that a procedural change that was implemented with respect to student financial aid refunds may not have been in accordance with the regulation governing return of financial aid for students who withdraw from a program prior to completion. Consequently, $8.4 million in estimated unreturned funds from prior periods was recorded in Kaplan's fourth quarter 2017 results; this estimated refund liability is included in current liabilities on the Company's consolidated balance sheet at December 31, 2017. No restatement of prior period financial statements and no change in previously reported financial results was required due to the immateriality of the adjustment for the periods presented. Kaplan has self-reported this matter to the ED. Kaplan is in the process of implementing remediation measures, including improvements to the review and approval process for changes to Title IV financial aid refund policies and procedures.

4. Property and Equipment

Property and equipment consisted of the following at December 31, 2017:

(in thousands)		
Land and land improvements	$	380
Buildings and building improvements		9,724
Leasehold improvements		51,563
Equipment, furniture and fixtures		16,516
Computer software		56,605
Construction in progress		1,279
		136,067
Less: Accumulated depreciation and amortization		(112,561)
	$	23,506

Depreciation and amortization expense for 2017 totaled $13.2 million.

5. Goodwill and Other Intangible Assets.

Goodwill balances and changes during the year ended December 31, 2017 were as follows (in thousands):

Balance at December 31, 2016	$	182,596
Change in Goodwill		-
Balance at December 31, 2017	$	182,596

Other intangible assets, subject to amortization and those not subject to amortization, consisted of the following at December 31, 2017:

	Definite-Lived					Indefinite-Lived
Estimated Useful Lives	Non Compete 5 years	Student and Customer Relationships 5 - 10 years	Trademarks 5 - 7 years	Product Development and Content 3 years	Total	Title IV Financial Aid Eligibility & Accreditation Unamortized
(in thousands)						
Gross carrying amounts	$ 50	$ 4,225	$ 1,978	$ 242	$ 6,495	$ 500
Accumulated amortization	(37)	(912)	(603)	(175)	(1,727)	-
Net carrying amounts	$ 13	$ 3,313	$ 1,375	$ 67	$ 4,768	$ 500
Aggregate amortization expense for the year					$ 1,033	$ -

At December 31, 2017, aggregate amortization expense of other intangible assets for each of the five succeeding years ended December 31, are estimated as follows:

(in thousands)	Total
2018	$ 872
2019	724
2020	657
2021	657
2022	657
Thereafter	1,201
	$ 4,768

6. Income Taxes

The Company files its federal tax return as part of a federal consolidated group with Graham Holdings Company (GHC). In addition, the Company files combined or consolidated state returns with either GHC or Kaplan, Inc. in 29 states. The aggregate current tax expense, deferred tax benefit and tax balance due from related parties at December 31, 2017 were $16.5 million, ($5.1) million and $0, respectively. Deferred income taxes reflect the net income tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant temporary differences as of December 31, 2017 consisted primarily of a $30.3 million deferred tax liability for amortized goodwill and other intangible assets offset partially by a $8.7 million deferred tax asset related to the write-off of the ECA investment occurring in 2016.

The Company endeavors to comply with tax laws and regulations where it does business, but cannot guarantee that, if challenged, the Company's interpretation of all relevant tax laws and regulations will prevail and that all tax benefits recorded in the financial statements will ultimately be recognized in full. The Company has taken reasonable efforts to address uncertain tax positions, and has determined that there are no material transactions or material tax positions taken by the Company that would fail to meet the more-likely-than-not threshold for recognizing transactions or tax positions in the financial statements. Accordingly, the Company has not recorded a reserve for uncertain tax positions in the financial statements, and the Company does not expect any significant tax increase or decrease to occur within the next 12 months with respect to any transactions or tax positions taken and reflected in the financial statements. In making these determinations, the Company presumes that taxing authorities pursuing examinations of the Company's compliance with tax law filing requirements will have full knowledge of all relevant information, and, if necessary, the Company will pursue resolution of disputed tax positions by appeals or litigation.

7. Leases

The Company leases most of its education and administrative space under various operating lease arrangements expiring on dates through 2024. Most lease arrangements contain lease incentives including tenant improvement allowances and/or rent holidays. In accordance with ASC Topic 840, "Leases", when such incentives are included in the lease arrangement, a deferred rent liability is recorded on the consolidated balance sheet and the rent expense is recorded evenly over the term of the lease. The Company is also required to make additional payments under certain facility operating leases for taxes, insurance and other operating expenses incurred during the operating lease period. Certain leases contain renewal options ranging from one to five years. Rent expense totaled $10.5 million and sublease income was $5.5 million for the year ended December 31, 2017.

Future minimum lease payments under noncancelable operating leases in effect at December 31, 2017 were as follows:

(in thousands)	
2018	$ 17,918
2019	16,981
2020	14,316
2021	13,724
2022	5,956
Thereafter	6,089
	$ 74,984

As of December 31, 2017, the Company has outstanding letters of credit totaling $2.5 million as required by a lease agreement, which expire in 2024.

8. Related Party

Kaplan Higher Education Corporation participates in the Student Financial Aid (SFA) under the Title IV programs administered by the U.S. Department of Education pursuant to the Higher Education Act of 1965, as amended (HEA). The Company must comply with the regulations promulgated under the HEA. Those regulations require that all related party transactions be disclosed, regardless of their materiality to the financial statements. The amounts below reflect all of the related party transactions that the Company entered into in fiscal year 2017.

At December 31, 2017, the net balance of Due from related parties related to inter-company was $19.4 million. Such balances consist of cash advances to the Company’s parent, Kaplan, Inc., and to Kapan, Inc.’s parent, Graham Holdings Company (“GHC”) offset by expenses paid by them on behalf of the Company. Kaplan, Inc., provides shared service functions for the Company and sweeps excess cash in order to fund payments made on behalf of the Company to vendors and employees, which includes certain funds that are ultimately settled with GHC. These uncollateralized balances are due on demand and are non-interest bearing.

During 2017, the following inter-company and related party transactions occurred, respectively:

(in thousands)		Amount	Primary Related Party	Location
Included in Net Revenues				
Educational Services	$	79	Kaplan, Inc.	Singapore
Educational Services		158	Kaplan, Inc.	Hong Kong
Educational Services		1,189	Kaplan, Inc.	UK
Educational Services		73	Kaplan, Inc.	Dubai, UAE
Educational Services		145	Kaplan, Inc.	Australia
Classroom and facility space rental		1,157	Kaplan, Inc.	United States
Management services provided to ECA	$	8,396	Education Corporation of America	United States
Included in Costs and Expenses				
Test preparation material	$	582	Kaplan, Inc.	United States
Corporate insurance expenses		2,619	Graham Holdings Company	United States
Management services provided by KHE on behalf of ECA		8,388	Kaplan, Inc.	United States
Contributions to employee retirement and restricted stock plans		10,009	Graham Holdings Company	United States
Employee medical and life insurances		17,990	Graham Holdings Company	United States
Administrative, legal and real estate services	$	3,384	Kaplan, Inc.	United States
Other - Cash Transactions				
Taxes paid	$	46	Kaplan, Inc.	United States

9. Commitments and Contingencies

The Company is party to routine litigation incidental to its business, including ordinary course employment litigation. Management does not believe that the resolution of any or all of such routine litigation is likely to have a material adverse effect on the Company's financial condition or results of operations.

The following reflects a summary of the Company's purchase commitments as of December 31, 2017:

(in thousands)		Total
2018	$	3,410
2019		2,361
2020		2,105
2021		916
2022		579
Thereafter		-
	$	9,371

10. New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued comprehensive new guidance that supersedes all existing revenue recognition guidance. In August 2015, the FASB issued an amendment to the guidance that defers the effective date by one year. The new guidance requires revenue to be recognized when the Company transfers promised goods or services to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services. The new guidance also significantly expands the disclosure requirements for revenue recognition. The guidance is effective for interim and fiscal years beginning after December 15, 2017. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016. The Company does not expect the guidance to have a material impact on its financial statements. The Company will adopt the new guidance on January 1, 2018.

In January 2016, the FASB issued new guidance that substantially revises the recognition, measurement and presentation of financial assets and financial liabilities. The new guidance, among other things, requires (i) equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, with some exceptions; (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (iii) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (iv) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements; and (v) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. The guidance is effective for interim and fiscal years beginning after December 15, 2017. Early adoption is not permitted. The Company does not expect the guidance to have a material impact on its financial statements.

In February 2016, the FASB issued new guidance that requires, among other things, a lessee to recognize a right-of-use asset representing an entity's right to use the underlying asset for the lease term and a liability for lease payments on its balance sheet, regardless of classification of a lease as operating or financing. For leases with a term of twelve months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and liabilities and account for the lease similar to existing guidance for operating leases today. This new guidance supersedes all prior guidance. The guidance is effective for interim and fiscal years beginning after December 15, 2018. Early adoption is permitted. The standard requires lessees and lessors to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is in the process of evaluating the impact of this new guidance on its Consolidated Financial Statements; however, the recognition of right-of-use assets and lease liabilities is expected to have a material effect on its Consolidated Balance Sheet.

In March 2016, the FASB issued new guidance that simplifies the accounting for stock-based compensation. The new guidance (i) requires all excess tax benefits and tax deficiencies to be recognized in the income statement with the tax effects of vested or exercised awards treated as discrete items. Additionally, excess tax benefits will be recognized regardless of whether the benefit reduces taxes payable in the current period, effectively eliminating the APIC pool, (ii) concludes excess tax benefits should be classified as an operating activity in the statement of cash flows, (iii) requires an entity to make an entity-wide accounting policy election to either estimate a forfeiture rate for awards or account for forfeitures as they occur, (iv) changes the threshold for equity classification for cash settlements of awards for withholding requirements to the maximum statutory tax rate in the applicable jurisdiction and (v) concludes cash paid by an employer when directly withholding shares for tax-withholding purposes should be classified as a financing activity in the statement of cash flows. The guidance is effective for interim and fiscal years beginning after December 15, 2016. Additionally, the Company elected to account for forfeitures of stock awards as they occur and not estimate a forfeiture rate. The Company does not expect the forfeiture rate election to have a material impact on its financial statements.

In January 2017, the FASB issued new guidance which simplifies the subsequent measurement of goodwill. The new guidance eliminates Step 2 from the goodwill impairment test, which required entities to determine the implied fair value of goodwill as of the test date to measure a goodwill impairment charge. Instead, an entity should continue to test goodwill for impairment by comparing the fair value of a reporting unit with its carrying amount (Step 1), and an impairment charge will be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. The guidance is effective for interim and fiscal years beginning after December 15, 2019, with early adoption permitted. The Company early adopted this guidance in the second quarter of 2017.

In March 2017, the FASB issued new guidance that changes the presentation of net periodic pension cost and net periodic postretirement benefit cost for defined benefit plans. The guidance requires an issuer to disaggregate the service cost component of net periodic pension and postretirement benefit cost from other components. Under the new guidance, service cost will be included in the same line item(s) as other compensation costs arising from services rendered by employees during the period, while the other components will be recognized after income from operations. The guidance is effective for interim and fiscal years beginning after December 15, 2017. The guidance must be applied retrospectively; however, a practical expedient is available which permits an employer to use amounts previously disclosed in its pension and postretirement plans footnote for the prior comparative periods. The Company will adopt the new standard in the first quarter of 2018.

In February 2018, the FASB issued new guidance that allows an entity to elect to reclassify stranded tax effects resulting from the Tax Cuts and Jobs Act (the Tax Act) from accumulated other comprehensive income to retained earnings. If elected, the amount of the reclassification shall include the effect of the change in the U.S. federal corporate income tax rate on the gross deferred tax amount and related valuation allowances at the date of enactment of the Tax Act as well as other income tax effects of the Tax Act on items remaining in accumulated other comprehensive income. The guidance is effective for interim and fiscal years beginning after December 15, 2018, with early adoption permitted.

Other new pronouncements issued but not effective until after December 31, 2018, are not expected to have a material impact on the Company's Consolidated Financial Statements.

11. Subsequent Events

In preparing the financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through the date the financial statements were issued. As such, management has evaluated events occurring between January 1, 2018 and June 29, 2018 for proper recording or disclosure in these financial statements.

On April 27, 2017, certain subsidiaries of Kaplan entered into a Contribution and Transfer Agreement to contribute the institutional assets and operations of Kaplan University to an Indiana non-profit, public-benefit corporation that is a subsidiary affiliated with Purdue University. The closing of the transactions contemplated by the Transfer Agreement occurred on March 22, 2018. At the same time, the parties entered into a Transition and Operations Support Agreement (TOSA) pursuant to which Kaplan will provide key non-academic operations support to the new university.

The new university will operate almost exclusively online as a new Indiana public university affiliated with Purdue under the name Purdue University Global. As part of the transfer to Purdue University Global, KU transferred students, academic personnel, faculty and operations, property leases for KU's campuses and learning centers, Kaplan-owned academic curricula and content related to KU courses. The operations support activities that Kaplan will provide to Purdue University Global will include technology support, help-desk functions, human resources support for transferred faculty and employees, admissions support, financial aid administration, marketing and advertising, back-office business functions, certain test preparation and domestic and international student recruiting services.

The transfer of KU does not include any of the assets of the KU School of Professional and Continuing Education, which provides professional training and exam preparation for professional certifications and licensures, nor does it include the transfer of other Kaplan businesses such as Kaplan Test Preparation and Kaplan International. Those entities, programs and business lines will remain part of Kaplan. Kaplan received nominal cash consideration upon transfer of the institutional assets.

Pursuant to the TOSA, Kaplan is not entitled to receive any reimbursement of costs incurred in providing support functions, or any fee, unless and until Purdue University Global has first covered all of its operating costs (subject to a cap). If Purdue University Global achieves cost efficiencies in its operations, then Purdue University Global may be entitled to an additional payment equal to 20 percent of such cost efficiencies (Purdue Efficiency Payment). In addition, during each of Purdue University Global’s first five years, prior to any payment to Kaplan, Purdue University Global is entitled to a priority payment of $10 million per year beyond costs. To the extent Purdue University Global’s revenue is insufficient to pay the $10 million per year priority payment, Kaplan is required to advance an amount to Purdue University Global to cover such insufficiency. At closing, Kaplan paid to Purdue University Global an advance in the amount of $20 million, representing, and in lieu of, priority payments for Purdue University Global’s fiscal years ending June 30, 2019 and June 30, 2020.

To the extent that there are sufficient revenues to pay the Purdue Efficiency Payment, Purdue University Global is reimbursed for its operating costs (subject to a cap) and the priority payment to Purdue University Global is paid. To the extent there is remaining revenue, Kaplan will then receive reimbursement for its operating costs (subject to a cap) of providing the support activities. If Kaplan achieves cost efficiencies in its operations, then Kaplan may be entitled to an additional payment equal to 20 percent of such cost efficiencies (Kaplan Efficiency Payment). If there are sufficient revenues, Kaplan may also receive a fee equal to 12.5 percent of Purdue University Global’s revenue. The fee will increase to 13 percent beginning with Purdue University Global’s fiscal year ending June 30, 2023 and continuing through Purdue University Global’s fiscal year ending June 30, 2027, and then the fee will return to 12.5 percent thereafter. Subject to certain limitations, a portion of the fee that is earned by Kaplan in one year may be carried over and instead paid to Kaplan in subsequent years.

After the first five years of the TOSA, Kaplan and Purdue University Global will be entitled to payments in a manner consistent with the structure described above, except that (i) Purdue University Global will no longer be entitled to a priority payment and (ii) to the extent that there are sufficient revenues after payment of the Kaplan Efficiency Payment (if any), Purdue University Global will be entitled to an annual payment equal to 10 percent of the remaining revenue after the Kaplan Efficiency Payment (if any) is paid and subject to certain other adjustments. The TOSA has a 30-year initial term, which will automatically renew for five-year periods unless terminated. After the sixth year, Purdue University Global has the right to terminate the agreement upon payment of a termination fee equal to 1.25 times Purdue University Global’s revenue for the preceding 12-month period, which payment would be made pursuant to a 10-year note, and at the election of Purdue University Global, it may receive for no additional consideration certain assets used by Kaplan to provide the support activities pursuant to the TOSA. At the end of the 30-year term, if Purdue University Global does not renew the TOSA, Purdue University Global will be obligated to make a final payment of 75% of its total revenue earned during the preceding 12-month period, which payment will be made pursuant to a 10-year note, and at the election of Purdue University Global, it may receive for no additional consideration certain assets used by Kaplan to provide the support activities pursuant to the TOSA.

Either party may terminate the TOSA at any time if Purdue University Global generates (i) $25 million in cash operating losses for three consecutive years or (ii) aggregate cash operating losses greater than $75 million at any point during the initial term. Operating loss is defined as the amount of revenue Purdue University Global generates minus the sum of (1) Purdue University Global's and Kaplan's respective costs in performing academic and support functions and (2) the $10 million priority payment to Purdue University Global in each of the first five years. Upon termination for any reason, Purdue University Global will retain the assets that Kaplan contributed pursuant to the Transfer Agreement. Each party also has certain termination rights in connection with a material default or material breach of the TOSA by the other party.

Pursuant to the U.S. Department of Education (ED) requirements, Purdue assumes responsibility for any liability arising from the operation of the institution. This assumption will not limit Kaplan's obligation to indemnify Purdue for pre-closing liabilities under the Transfer Agreement. As a result of the transfer of KU, Kaplan will no longer own or operate KU or any other institution participating in student financial aid programs that have been created under Title IV of the U.S. Federal Higher Education Act of 1965, as amended. Consequently, Kaplan is no longer responsible for operating KU. However, pursuant to the TOSA, Kaplan will be performing functions that fall within the ED's definition of a third-party servicer and will, therefore, assume certain regulatory responsibilities that require approval by the ED. The third-party servicer arrangement between Kaplan and Purdue University Global is also subject to information security requirements established by the Federal Trade Commission as well as all aspects of the Family Educational Rights and Privacy Act. As a third-party servicer, Kaplan may be required to undergo an annual compliance audit of its administration of the Title IV functions or services that it performs.

On March 22, 2018, Kaplan completed the sale of the institutional assets and operations of Kaplan University (KU) to an Indiana non-profit, public-benefit corporation that is a subsidiary affiliated with Purdue University (Purdue).

As a result of the transaction, Kaplan reorganized its higher education operations into the following two operating segments for the purpose of making operating decisions and assessing performance: Higher Education and Professional (U.S.) for 2018. The Higher Education segment comprises the historical KU for-profit postsecondary education business and the future non-academic operations support services provided to the new university, Purdue University Global. The Professional (U.S.) segment comprises the KU School of Professional and Continuing Education, which provides professional training and exam preparation for professional certifications and licensures.

Kaplan Higher Education LLC and Subsidiaries

(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)

Appendix A: Kaplan University Consolidated Balance Sheet

(in thousands, except share amounts)		As of December 31, 2017
Assets		
Current assets		
Cash and cash equivalents	$	125,138
Accounts and notes receivable, less allowance for doubtful accounts		12,814
Prepaid expenses and other current assets		4,120
Total current assets		142,072
Property and equipment		16,914
Goodwill		76,173
Intangible assets		500
Due from related parties		27,878
Other assets		580
Total assets	$	264,117
Liabilities and Stockholder's Equity		
Current liabilities		
Accounts payable and accrued expenses	$	4,633
Accrued compensation and benefits		10,918
Deferred revenue		48,559
Other current liabilities		14,671
Total current liabilities		78,781
Deferred income taxes		3,862
Other liabilities		10,079
Total liabilities		92,722
Stockholder's equity		
Common stock, $ .01 par value-authorized 100 shares;		
100 shares issued and outstanding		10
Additional paid-in capital		58,966
Retained earnings		112,419
Total stockholder's equity		171,395
Total liabilities and stockholder's equity	$	264,117

Kaplan Higher Education LLC and Subsidiaries

(A wholly owned subsidiary of Kaplan, Inc., a subsidiary of Graham Holdings Company)

Appendix B: Kaplan University Consolidated Statement of Operations

(in thousands)	Year Ended December 31, 2017
Revenues	$ 516,044
School operating expenses	
Educational services	96,277
Marketing and advertising	96,862
Admissions	68,306
General and administrative expenses	213,811
Total operating expenses	475,256
Income from continuing operations before income taxes	40,788
Provision for income taxes	13,837
Net income	$ 26,951