

AMERICAN PUBLIC EDUCATION INC
Form 10-Q
May 08, 2018

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 March 31, 2018

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: - 001-33810

AMERICAN PUBLIC EDUCATION, INC.
(Exact name of registrant as specified in its charter)
Delaware 01-0724376
(State or other jurisdiction of (I.R.S. Employer
Incorporation or organization) Identification No.)

111 West Congress Street
Charles Town, West Virginia 25414
(Address, including zip code, of principal executive offices)

(304) 724-3700
(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 Smaller reporting company

Edgar Filing: AMERICAN PUBLIC EDUCATION INC - Form 10-Q

(Do not check if a 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

The total number of shares of common stock outstanding as of May 4, 2018 was 16,399,199.

Index

AMERICAN PUBLIC EDUCATION, INC.
FORM 10-Q
INDEX

	Page
<u>PART I – FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	<u>3</u>
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>17</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>26</u>
<u>Item 4. Controls and Procedures</u>	<u>27</u>
<u>PART II – OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	<u>27</u>
<u>Item 1A. Risk Factors</u>	<u>27</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>31</u>
<u>Item 3. Defaults Upon Senior Securities</u>	<u>31</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>31</u>
<u>Item 5. Other Information</u>	<u>31</u>
<u>Item 6. Exhibits</u>	<u>32</u>
<u>SIGNATURES</u>	<u>33</u>

Index

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

AMERICAN PUBLIC EDUCATION, INC.

Consolidated Balance Sheets (Current Period Unaudited)

(In thousands)

	As of March 31, 2018 (Unaudited)	As of December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents (Note 2)	\$ 186,168	\$ 179,205
Accounts receivable, net of allowance of \$6,181 in 2018 and \$6,276 in 2017	7,924	7,136
Prepaid expenses	7,409	4,792
Total current assets	201,501	191,133
Property and equipment, net	90,247	92,374
Investments	12,280	12,481
Goodwill	33,899	33,899
Other assets, net	8,304	9,151
Total assets	\$ 346,231	\$ 339,038
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 4,952	\$ 8,844
Accrued liabilities	15,744	13,423
Deferred revenue	21,957	19,374
Income tax payable	2,668	1,710
Total current liabilities	45,321	43,351
Deferred income taxes	7,131	6,281
Total liabilities	52,452	49,632
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock, \$.01 par value; Authorized shares - 10,000; no shares issued or outstanding	—	—
Common stock, \$.01 par value; Authorized shares - 100,000; 16,399 issued and outstanding in 2018; 16,268 issued and outstanding in 2017	164	163
Additional paid-in capital	180,735	180,674
Retained earnings	112,880	108,569
Total stockholders' equity	293,779	289,406
Total liabilities and stockholders' equity	\$ 346,231	\$ 339,038

The accompanying notes are an integral part of these Consolidated Financial Statements.

Index

AMERICAN PUBLIC EDUCATION, INC.
 Consolidated Statements of Income (Unaudited)
 (In thousands, except share and per share amounts)

	Three Months Ended March 31,	
	2018	2017
	(Unaudited)	
Revenue	\$74,967	\$ 75,688
Costs and expenses:		
Instructional costs and services	29,686	28,956
Selling and promotional	15,581	15,435
General and administrative	18,888	17,756
Loss on disposals of long-lived assets	128	490
Depreciation and amortization	4,522	4,744
Total costs and expenses	68,805	67,381
Income from operations before interest income and income taxes	6,162	8,307
Interest income	493	11
Income before income taxes	6,655	8,318
Income tax expense	1,865	3,849
Equity investment (loss) income	(201) 40
Net income	\$4,589	\$ 4,509
Net Income per common share:		
Basic	\$0.28	\$ 0.28
Diluted	\$0.28	\$ 0.28
Weighted average number of common shares:		
Basic	16,359,792	16,190,061
Diluted	16,534,053	16,320,858

The accompanying notes are an integral part of these Consolidated Financial Statements.

Index

AMERICAN PUBLIC EDUCATION, INC.
 Consolidated Statements of Cash Flows (Unaudited)
 (In thousands)

	Three Months Ended March 31, 2018 (Unaudited)	2017	
Operating activities			
Net income	\$ 4,589	\$ 4,509	
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	4,522	4,744	
Stock-based compensation	1,843	1,246	
Equity investment loss (income)	201	(40)
Deferred income taxes	850	2,588	
Loss on disposals of long-lived assets	128	490	
Other	38	20	
Changes in operating assets and liabilities:			
Accounts receivable, net of allowance for bad debt	(788	749)
Prepaid expenses and other assets	(2,380	(2,196)
Income tax receivable	—	(4,233)
Accounts payable	(3,892	(2,016)
Accrued liabilities	1,870	(2,783)
Income taxes payable	958	(559)
Deferred revenue	2,305	2,535	
Net cash provided by operating activities	10,244	5,054	
Investing activities			
Capital expenditures	(1,427	(1,670)
Capitalized program development costs and other assets	(239	(627)
Net cash used in investing activities	(1,666	(2,297)
Financing activities			
Cash paid for repurchase of common stock	(1,615	(1,402)

Cash received from issuance of common stock	—		98	
Net cash used in financing activities	(1,615)	(1,304)
Net increase in cash and cash equivalents	6,963		1,453	
Cash and cash equivalents at beginning of period	179,205		146,351	
Cash and cash equivalents at end of period	\$	186,168	\$	147,804
Supplemental disclosure of cash flow information				
Income taxes paid	\$	—	\$	6,052

The accompanying notes are an integral part of these Consolidated Financial Statements

Index

AMERICAN PUBLIC EDUCATION, INC.
Notes to Consolidated Financial Statements

Note 1. Nature of the Business

American Public Education, Inc., or APEI, which together with its subsidiaries is referred to as the “Company,” is a provider of online and campus-based postsecondary education to approximately 84,700 students through two subsidiary institutions:

American Public University System, Inc., or APUS, provides online postsecondary education directed primarily at the needs of the military, military-affiliated, and public service communities through American Military University, or AMU, and American Public University, or APU. APUS is regionally accredited by the Higher Learning Commission.

National Education Seminars, Inc., which is referred to herein as Hondros College of Nursing, or HCN, provides nursing education to students at five campuses in Ohio, as well as online, to serve the needs of the nursing and healthcare communities. HCN is nationally accredited by the Accrediting Council of Independent Colleges and Schools, or ACICS, and the RN-to-BSN Program is accredited by the Commission on Collegiate Nursing Education.

The Company’s institutions are licensed or otherwise authorized, or are in the process of obtaining such licenses or authorizations, to offer postsecondary education programs by state authorities to the extent the institutions believe such licenses or authorizations are required, and are certified by the United States Department of Education, or ED, to participate in student financial aid programs authorized under Title IV of the Higher Education Act of 1965, as amended, or Title IV programs.

The Company’s operations are organized into two reportable segments:

American Public Education Segment, or APEI Segment. This segment reflects the operational activities at APUS, other corporate activities, and minority investments.

Hondros College of Nursing Segment, or HCN Segment. This segment reflects the operational activities of HCN.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation and Accounting

The accompanying unaudited interim Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP.

Principles of Consolidation

The accompanying unaudited interim Consolidated Financial Statements include accounts of APEI and its wholly owned subsidiaries. All material intercompany transactions and balances have been eliminated in consolidation.

Unaudited Interim Financial Information

The unaudited interim Consolidated Financial Statements do not include all of the information and notes required by GAAP for audited annual financial statement presentations. In the opinion of management, these statements include all adjustments (consisting of normal recurring adjustments) considered necessary to present a fair statement of the Company’s consolidated results of operations, financial position, and cash flows. Operating results for any interim

period are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. This Quarterly Report on Form 10-Q should be read in conjunction with the Company's Consolidated Financial Statements and accompanying notes in its audited financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2017, or the Annual Report.

Index

Use of Estimates

The preparation of the Consolidated Financial Statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts in these unaudited interim Consolidated Financial Statements and accompanying notes. Actual results could differ from those estimates.

Restricted Cash

Cash and cash equivalents includes funds held for students for unbilled educational services that were received from Title IV programs. As a trustee of these Title IV program funds, the Company is required to maintain and restrict these funds pursuant to the terms of each subsidiary institution's program participation agreement with ED. Restricted cash on the Company's Consolidated Balance Sheets was approximately \$2.0 million at March 31, 2018 and \$2.3 million at December 31, 2017. Changes in restricted cash that represent funds held for students as described above are included in cash flows from operating activities on the Company's Consolidated Statements of Cash Flows because these restricted funds are related to a core activity of its operations.

Revenue

The Company adopted Financial Accounting Standards Board, or FASB, Accounting Standards Codification, or ASC, 606, Revenue from Contracts with Customers, with a date of initial application of January 1, 2018. As a result, the Company has changed its accounting policy for revenue recognition.

The Company applied ASC 606 using the modified retrospective approach. The cumulative effect of initially applying ASC 606 was recognized as an adjustment to retained earnings at January 1, 2018. Prior periods have not been adjusted, and therefore comparative information continues to be reported under Topic 605, Revenue Recognition. The adoption of ASC 606 had the following impacts on the Company's Consolidated Balance Sheet (unaudited):

Balance at December 31, 2017 (In thousands)	Adjustments from adoption of ASC 606	Balance at January 1, 2018
------------------------------------------------------------	-----------------------------------------------	-------------------------------------

Consolidated Balance Sheet

Deferred revenue	\$19,374	\$ 379	\$19,753
Deferred income taxes	6,281	(101)	6,180
Retained earnings	108,569	(278)	108,291

In accordance with the new revenue standard's requirements, the impact of adoption on the Company's Consolidated Balance Sheet at March 31, 2018 and its Consolidated Statement of Income of the three months ended March 31, 2018 were as follows (unaudited):

As of March 31, 2018		Balance without adoption
As Reported	Adjustment	

Consolidated Balance Sheet (In thousands)

Liabilities			
Deferred revenue	\$21,957	\$ (423)	\$22,380
Deferred income taxes	7,131	113	7,244
Equity			
Retained earnings	112,880	310	113,190

Index

	Three Months Ended March 31, 2018		
	As Reported	Adjustment	Balance without adoption
Consolidated Statement of Income (In thousands)			
Revenue	\$74,967	\$ (44)	\$ 75,011
Income tax expense	1,865	12	1,877

Recent Accounting Pronouncements

In January 2016, the FASB issued Accounting Standards Update, or ASU, No. 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The standard addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. These changes will require an entity to measure, at fair value, investments in equity securities and other ownership interests in an entity and to recognize the changes in fair value within net income. ASU 2016-01 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, and early adoption was not permitted. The Company adopted this standard effective January 1, 2018. The Company accounts for its investment in RallyPoint Networks, Inc., or RallyPoint, in accordance with ASU 2016-01 and ASC 321, Investments - Equity Securities. For each reporting period, the Company completes a qualitative assessment considering impairment indicators to evaluate whether the investment is impaired. During the three months ended March 31, 2018, the Company determined that impairment indicators existed and utilized an independent valuation firm to assess the fair value of the investment. The interim assessment concluded that the fair value of its investment was less than the carrying amount resulting in a non-cash pre-tax impairment charge of \$0.5 million. This impairment charge is included in equity investment loss in the interim Consolidated Statements of Income.

The Company considers the applicability and impact of all ASUs issued by the FASB. ASUs issued subsequent to the filing of the Annual Report on February 27, 2018 were assessed and determined to be either inapplicable or expected to have minimal impact on the Company's consolidated financial position and/or results of operations.

Note 3. Revenue

On January 1, 2018, the Company adopted ASC 606, Revenue from Contracts with Customers, using the modified retrospective approach. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported in accordance with previous accounting under ASC 605, Revenue Recognition.

The following is a description of principal activities from which the Company generates its revenue.

Instructional services. Instructional services revenue includes tuition, technology, and laboratory fees. The Company generally recognizes revenue as instructional services are provided over the period or term, which is, for APUS, either an eight- or sixteen-week period, and for HCN, a quarterly term. Tuition is charged by course or term, technology fees are charged to APUS students on a per course basis, and laboratory fees are charged to HCN students on a per term basis, when applicable. Generally, instructional services are billed when a course or term begins, and paid within thirty days of the bill date.

Graduation fees. APUS graduation fee revenue represents a one-time, non-refundable \$100 fee per degree, charged to students upon submission of a program graduation application. The fee covers administrative costs associated with completing a review of the student's academic and financial standing prior to graduation. The Company recognizes

revenue once graduation review services are completed. Generally, graduation fees are billed and paid when the student submits the graduation application.

Textbook and other course material fees. Textbook and other course materials revenue represent fees related to the sale of textbooks and other course materials to HCN students. Revenue is recognized at the beginning of the term when the textbooks and other course materials fees are billed. Payment is generally received within thirty days of the bill date. Sales tax collected from students on the sale of textbooks and other course materials is excluded from revenue.

Other fees. Other fees revenue represent one-time, non-refundable fees such as: application, enrollment, transcript, and other miscellaneous fees. Generally other fees revenue is recognized when the fee is charged to the student which coincides with the specific obligation to the student.

Index

Disaggregation of Revenue

In the following table, revenue, shown net of grants and scholarships, is disaggregated by type of service provided. The table also includes a reconciliation of the disaggregated revenue with the reportable segments (unaudited).

	Three Months Ended March 31, 2018 (In thousands)		
	APEI	HCN	Consolidated
Instructional services, net of grants and scholarships	\$65,206	\$8,061	\$ 73,267
Graduation fees	276	—	276
Textbook and other course materials	—	1,122	1,122
Other fees	186	116	302
Total Revenue	\$65,668	\$9,299	\$ 74,967

APUS provides a tuition grant to support students who are U.S. Military active-duty service members, National Guard, reservists, military spouses and dependents, and veterans as well as a grant to cover the technology fee for students using DoD tuition assistance programs. APUS and HCN also provide scholarships to certain students to assist them financially with their educational goals.

The statement of retained earnings at January 1, 2018 was adjusted by \$278,000 to reflect the after tax impact related to the adoption of ASC 606, related to the recognition of graduation fees revenue at APUS. There were no adjustments to any other revenue type as a result of the adoption of ASC 606.

Contract Balances and Performance Obligations

The Company has no contract assets or deferred contract costs as of March 31, 2018 and December 31, 2017. The Company recognizes a contract liability, or deferred revenue, when a student begins an online course, in the case of APUS, or starts a term, in the case of HCN, and revenue is recognized as described earlier in this footnote. Deferred revenue at March 31, 2018 was \$22.0 million and includes \$13.0 million in future revenue that has not yet been earned for courses and terms that are in progress as well as \$9.0 million in advanced consideration received for future courses or terms, or student deposits, and represents the Company's performance obligation to transfer future instructional services to students. The Company's remaining performance obligations represent the transaction price allocated to future reporting periods.

The Company has elected, as a practical expedient, to not disclose the value of unsatisfied performance obligations for contracts with customers that have an expected duration of one year or less.

When the Company begins providing the performance obligation, a contract receivable is created, resulting in accounts receivable on the Company's Consolidated Balance Sheets. The Company accounts for receivables in accordance with ASC 310, Receivables. The Company uses the portfolio approach, a practical expedient, to evaluate if a contract exists and to assess collectability at the time of contract inception based on historical experience. Contracts are subsequently reviewed for collectability if significant events or circumstances indicate a change. The allowance for doubtful accounts is based on management's evaluation of the status of existing accounts receivable. Among other factors, management considers the age of the receivable, the anticipated source of payment and the historical allowance considerations. Consideration is also given to any specific known risk areas among the existing accounts receivable balances. Recoveries of receivables previously written off are recorded when received. The Company does not charge interest on past due receivables.

Refund Policies

The Company provides a stated period of time during which students may withdraw from a class, for APUS, or a term, for HCN, without further financial obligation resulting in a refund liability. The refund policy for each company

is as follows:

American Public University System

9

Index

APUS's tuition revenue varies from period to period based on the number of net course registrations and the volume of undergraduate versus graduate registrations. Students may remit tuition payments through the online registration process at any time or they may elect various payment options, including payments by sponsors, alternative loans, financial aid, or the DoD tuition assistance program which remits payments directly to APUS. If one of the various other payment options is confirmed as secured, the student is allowed to start the course. These other payment options can delay the receipt of payment up until the course starts or longer, resulting in the recording of an account receivable at the beginning of each session. Tuition revenue for sessions in progress that have not been earned by APUS is presented as deferred revenue in the accompanying Consolidated Balance Sheets.

APUS refunds 100% of tuition for courses that are dropped before the conclusion of the first seven days of a course. The Company does not recognize revenue for dropped courses. After a course begins, APUS uses the following refund policy:

8-Week Course- Tuition
Refund Schedule

Withdrawal Date	Tuition Refund Percentage
Before or During Week 1	100%
During Week 2	75%
During Weeks 3 and 4	50%
During Weeks 5 through 8	No Refund

16-Week Course- Tuition
Refund Schedule

Withdrawal Date	Tuition Refund Percentage
Before or During Week 1	100%
During Week 2	100%
During Weeks 3 and 4	75%
During Weeks 5 through 8	50%
During Weeks 9 through 16	No Refund

Students affiliated with certain organizations may have an alternate refund policy.

If a student withdraws during the academic term, APUS calculates the portion of instructional services and other fees that are non-refundable based on the tuition refund policy and recognizes it as revenue in the period the withdrawal occurs.

Hondros College of Nursing.

HCN's tuition revenue varies from period to period based on the number of students enrolled and the programs they are enrolled in. Students may remit tuition payments at any time, or they may elect various payment options that can delay receipt of payment up until the term starts or longer. These other payment options include payments by sponsors, financial aid, alternative loans, or payment plan options. If a payment option is confirmed, the student is allowed to start the term. Generally, financial aid is awarded prior to the start of the term and requests for authorization of disbursement begin in the first week of the term. Tuition revenue for the term in progress that has not yet been earned by HCN is presented as deferred revenue in the accompanying Consolidated Balance Sheets.

HCN's refund policy complies with the rules of the Ohio State Board of Career Colleges and Schools and is applicable to each term. For a course with an on-campus or other in-person component, the date of withdrawal is determined by a student's last attended day of clinical offering, laboratory session, or lecture. For an online course, the date of withdrawal is determined by a student's last submitted assignment in the course. HCN uses the following refund policy:

Index

Quarterly Term