SOUTH UNIVERSITY

AUDIT OF COMPLIANCE FOR EACH MAJOR STATE PROJECT IN ACCORDANCE WITH CHAPTER 10.650, RULES OF THE AUDITOR GENERAL

Year Ended June 30, 2016

R.D. HOAG & ASSOCIATES, PC
Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR STATE PROJECT AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH CHAPTER 10.650, RULES OF THE AUDITOR GENERAL

To the Board of Directors
South University

Report on Compliance for Each Major State Project

We have audited South University's compliance with the types of compliance requirements described in the Department of Financial Services' *State Projects Compliance Supplement* that could have a direct and material effect on each of South University's major State projects for the year ended June 30, 2016. South University's major State projects are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with State statutes, regulations, and the terms and conditions applicable to its State projects.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of South University's major State projects based on our audit of the types of compliance requirements referred to above.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Chapter 10.650, *Rules of the Auditor General*. Those standards and Chapter 10.650, *Rules of the Auditor General* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major State project occurred. An audit includes examining, on a test basis, evidence about South University's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major State project. However, our audit does not provide a legal determination of South University's compliance.

Opinion on Each Major State Project

In our opinion, South University complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major State projects for the year ended June 30, 2016.

Report on Internal Control Over Compliance

Management of South University is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered South University's internal control over compliance with the types of requirements that could have a direct and material effect on each major State project to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major State project and to test and report on internal control over compliance in accordance with Chapter 10.650, *Rules of the Auditor General* but not for the purpose of expressing an opinion on the effectiveness of South University's internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of South University's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a State project on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a State project will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a State project that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of Chapter 10.650, *Rules of the Auditor General*. Accordingly, this report is not suitable for any other purpose.

R.D. Hong + Associates, P.C.

March 28, 2017

SOUTH UNIVERSITY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - STATE PROJECTS

Year Ended June 30, 2016

A. SUMMARY OF AUDITORS' RESULTS

1. The consolidated financial statements of South University, LLC and Subsidiaries were audited by another independent registered public accounting firm whose report dated September 28, 2016 expressed an unmodified opinion.

2. The consolidated financial statements of South University, LLC and Subsidiaries were audited by another independent registered public accounting firm whose "Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*" dated September 28, 2016 identified no instances of noncompliance material to the financial statements and no findings related to the financial statements which would be required to be reported in accordance with *Government Auditing Standards*.

3. The independent auditor's report on compliance for each major State project for South University expresses an unmodified opinion.

4. The audit of the major state projects of South University disclosed no findings or questioned costs required to be disclosed under Chapter 10.650, *Rules of the Auditor General*.

5. The programs tested as major state projects included:

   Florida Department of Education Student Financial Assistance Programs:

   a. Florida Access to Better Learning and Education Grant - CSFA #48.017

6. The dollar threshold for distinguishing between Type A and Type B projects was $300,000 for major State projects.

7. No management letter is required because there were no matters related to major State projects required to be reported in the management letter.

8. No Summary Schedule of Prior Audit Findings is required because there were no prior audit findings related to major State projects.

9. No Corrective Action Plan is required because there were no findings required to be reported under Chapter 10.650, *Rules of the Auditor General*.

Consolidated Financial Statements and Supplemental Information

South University, LLC and Subsidiaries
Fiscal Years Ended June 30, 2016 and 2015
With Report of Independent Auditors

South University, LLC and Subsidiaries

Consolidated Financial Statements
and Supplemental Information

Fiscal Years Ended June 30, 2016 and 2015

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Report of Independent Auditors

The Member and Board of Trustees of
South University, LLC and Subsidiaries

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of South University, LLC and Subsidiaries, which comprise the consolidated balance sheets as of June 30, 2016 and 2015, and the related consolidated statements of operations, member's equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of South University, LLC and Subsidiaries at June 30, 2016 and 2015, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating balance sheets, statements of operations, 90/10 ratios, and composite scores, and supplemental schedule of expenditures of state financial assistance are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with Government Auditing Standards, we have also issued our report dated September 28, 2016 on our consideration of South University, LLC and Subsidiaries' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering South University, LLC and Subsidiaries' internal control over financial reporting and compliance.

Ernst + Young LLP

Ernst & Young LLP
September 28, 2016

South University, LLC and Subsidiaries
Consolidated Balance Sheets
(In thousands)

	June 30,	
	2016	**2015**
Assets		
Current assets:		
Cash and cash equivalents	$ 46,151	$ 47,991
Restricted cash	50,655	49,232
Student accounts receivable, net of allowance of $17,034 and $28,779	42,027	45,871
Notes, advances, and other receivables	2,128	4,093
Deferred income taxes	—	2,895
Other current assets	1,180	2,997
Total current assets	142,141	153,079
Property and equipment, net	33,081	38,598
Other long-term assets	10,227	7,548
Intangible assets, net	1,191	2,355
Goodwill	44,295	44,295
Total assets	$ 230,935	$ 245,875
Liabilities and member's equity		
Current liabilities:		
Accounts payable	$ 2,893	$ 4,074
Accrued liabilities	11,704	7,470
Unearned tuition	54,038	49,794
Advance payments	23,339	23,907
Total current liabilities	91,974	85,245
Deferred income taxes	17,250	19,426
Deferred rent	29,943	31,072
Member's equity:		
Net investment of EDMC (Note 2)	(34,200)	(5,525)
Accumulated earnings	125,968	115,657
Total member's equity	91,768	110,132
Total liabilities and member's equity	$ 230,935	$ 245,875

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

South University, LLC and Subsidiaries
Consolidated Statements of Operations
(In thousands)

	For the Fiscal Year ended June 30,	
	2016	**2015**
Net revenues	$ 359,053	$ 378,138
Costs and expenses:		
Educational services	193,749	201,757
General and administrative	130,323	135,433
Long-lived asset impairments	1,345	10,107
Depreciation and amortization	10,996	14,662
Total costs and expenses	336,413	361,959
Income before income taxes	22,640	16,179
Income tax expense	12,329	20,046
Net income (loss)	$ 10,311	$ (3,867)

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

South University, LLC and Subsidiaries
Consolidated Statements of Member's Equity
(In thousands)

	Net Investment of EDMC	Accumulated Earnings	Total Member's Equity
Balance, June 30, 2014	$ 6,492	$ 119,524	$ 126,016
Decrease in net investment of EDMC	(12,017)	—	(12,017)
Net loss	—	(3,867)	(3,867)
Balance, June 30, 2015	(5,525)	115,657	110,132
Decrease in net investment of EDMC	(28,675)	—	(28,675)
Net income	—	10,311	10,311
Balance, June 30, 2016	$ (34,200)	$ 125,968	$ 91,768

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

South University, LLC and Subsidiaries
Consolidated Statements of Cash Flows
(In thousands)

	For the Fiscal Year Ended June 30,	
Cash flows from operating activities:	**2016**	**2015**
Net income (loss)	$ 10,311	$ (3,867)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	10,996	14,662
Bad debt expense	19,318	24,539
Long-lived asset impairments	1,345	10,107
Non-cash adjustments related to deferred rent	(2,061)	(1,153)
Deferred income taxes	719	11,047
Changes in assets and liabilities:		
Restricted cash	(1,423)	(9,037)
Receivables	(16,207)	8,727
Reimbursements for tenant improvements	1,460	286
Other assets	376	(2,030)
Accounts payable	(967)	(166)
Accrued liabilities	5,479	(783)
Unearned tuition and advance payments	3,676	1,077
Total adjustments	22,711	57,276
Net cash flows provided by operating activities	33,022	53,409
Cash flows from investing activities:		
Expenditures for long-lived assets	(3,189)	(11,107)
Reimbursements for tenant improvements	(1,460)	(286)
Net cash flows used in investing activities	(4,649)	(11,393)
Cash flows from financing activities:		
Decrease in net investment of EDMC	(30,213)	(13,996)
Net cash flows used in financing activities	(30,213)	(13,996)
Net (decrease) increase in cash and cash equivalents	(1,840)	28,020
Cash and cash equivalents, beginning of year	47,991	19,971
Cash and cash equivalents, end of year	$ 46,151	$ 47,991

	As of June 30,	
Supplemental disclosure of cash flow information	**2016**	**2015**
Capital expenditures in current liabilities	$ 560	$ 1,088

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

1. OWNERSHIP, OPERATIONS, AND GOVERNANCE

South University, LLC and Subsidiaries ("South University" or the "University") is a nonsectarian, coeducational institution of higher education with campuses in the following cities:

- Savannah, Georgia
- West Palm Beach, Florida
- Montgomery, Alabama
- Tampa, Florida
- Columbia, South Carolina
- Richmond, Virginia
- Virginia Beach, Virginia
- Novi, Michigan
- Cleveland, Ohio
- High Point, North Carolina
- Austin, Texas
- Orlando, Florida (a learning site)

Additionally, the University's consolidated financial statements include campuses of The Art Institutes in the following cities:

- Dallas, Texas
- Fort Worth, Texas
- Charlotte, North Carolina
- Raleigh-Durham, North Carolina

The University is a wholly-owned subsidiary of Education Management Corporation ("EDMC") and South University is accredited by the Commission on Colleges of the Southern Association of Colleges and Schools Commission on Colleges ("SACSCOC") to award Associate's, Bachelor's, Master's, and Doctoral degrees. Additionally, South University offers degree programs fully-online through South University-Savannah or through a flexible combination of both online and campus-based instruction.

On June 1, 2006, EDMC was acquired by a consortium of private equity investment funds led by Providence Equity Partners, Goldman Sachs Capital Partners and Leeds Equity Partners (collectively, the "Sponsors"). The acquisition was accomplished through the merger of an acquisition company into EDMC, with EDMC surviving the merger (the "Transaction"). The Transaction was accounted for as a purchase; however, the impact of the purchase accounting related to the Transaction was not allocated to the University's financial statements. The University's assets and liabilities, where applicable, continue to be recognized on a historical basis.

In November 2014, EDMC voluntarily delisted its common stock from The Nasdaq Global Select Market and subsequently deregistered its common stock under the Securities Exchange Act of 1934, as amended.

On January 5, 2015, EDMC issued shares of Series A-1 optionally convertible preferred stock and Series A-2 mandatorily convertible preferred stock (together with the Series A-1 preferred stock, the "Preferred Stock") in connection with a restructuring of its outstanding indebtedness (the "Debt Restructuring"). On April 13, 2015, EDMC received final regulatory approval for the Debt Restructuring, transferring control of EDMC to creditors who participated in the Debt Restructuring.

Revisions and Reclassifications

Certain reclassifications of prior year data have been made to conform to the fiscal 2016 presentation, with no effect on previously reported net income (loss) or member's equity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation and Presentation (Including EDMC Debt Restructuring)

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. All significant intercompany transactions and balances have been eliminated in combination. Unless otherwise specified, any reference to a “year” is to a fiscal year ended June 30.

In order to address financial covenant compliance and maturity issues with respect to EDMC's outstanding indebtedness at June 30, 2014, EDMC entered into a Restructuring Support Agreement (the “RSA”) in September 2014 pursuant to which the holders of substantially all of EDMC's term loan facilities and 100% of the revolving credit facility, holders of a majority of the Cash Pay/PIK Interest Notes due 2018, certain of EDMC's interest rate swap counter-parties and holders of in excess of 72% of EDMC's outstanding common stock agreed to support the Debt Restructuring. On January 5, 2015, EDMC entered into the following transaction in connection with the closing of the initial step of the Debt Restructuring:

- $150.0 million of revolving loans under EDMC's existing revolving credit facility were repaid in cash at par, with such amount available for re-borrowing under a new revolving credit facility which matures March 31, 2019;
- Except for $15.8 million of Senior Cash Pay/PIK Notes due 2018, the remaining portion of EDMC's outstanding indebtedness was exchanged for two first lien senior secured term loans due July 2, 2020 in the aggregate principal amount of $400.0 million, mandatorily convertible Series A-2 preferred stock of EDMC, optionally convertible Series A-1 preferred stock of EDMC and warrants to purchase common stock of EDMC; and
- $106.4 million of existing letters of credit were rolled into the new senior secured credit facility.

EDMC received the final regulatory approval for the Debt Restructuring on April 13, 2015 and the mandatorily convertible shares of Series A-2 preferred stock were converted into 2,345,804,755 shares of EDMC common stock. After conversion of the Series A-2 preferred stock, there were 2,472,963,157 shares of EDMC common stock outstanding on June 30, 2015. EDMC’s shareholders prior to the Debt Restructuring now own 4% of the outstanding common stock along with warrants to purchase 5% of EDMC’s common stock after giving effect to the conversion of all of the preferred stock and subject to further dilution by warrants awarded pursuant to the Debt Restructuring. EDMC recorded a gain on the Debt Restructuring of $165.2 million during the quarter ended March 31, 2015 due to the excess of the carrying value of EDMC's prior indebtedness over the recorded value of the new indebtedness.

The University’s financial statements for the year ended June 30, 2016 were prepared on the basis of the University continuing as a going concern. As a result, the University’s financial statements do not reflect any adjustments that might result if the University was not a going concern. A company is considered a going concern when there is not substantial doubt about its ability to meet its obligations as they become due over the subsequent twelve month period.

Management of the University believes that the cash flow from operations and available cash on hand will provide adequate funds for ongoing operations and obligations as they become due during the next twelve months ending June 30, 2017. To the extent the University’s level of cash from operations and available cash on hand is not sufficient to meet its obligations as they become due, EDMC will provide the appropriate level of liquidity to enable the University to meet its obligations as they become due over the next year. As of June 30, 2016, EDMC's available liquidity was $355.2 million, which consists of $315.3 million of cash and cash equivalents and $39.9 million available for borrowing under a $150.0 million revolving credit facility.

EDMC experienced deteriorating financial results from operations during fiscal 2016 due primarily to declining student enrollment, including the impact of the announced teach-out of a number of school locations. Results during fiscal 2017 may continue to decline primarily due to declining student enrollment and may further be impacted by the gainful employment regulation promulgated by the U.S. Department of Education. In the event that the U.S. Department of Education publishes rates from fiscal 2015 as it has announced it intends to do in early 2017, the gainful employment regulation will require certain disclosures to prospective and current students enrolled in programs which do not satisfy the debt to income thresholds set forth in the regulation, which may adversely impact enrollment in these programs. The gainful employment regulation will not result in any programs, which do not meet the minimum thresholds, from qualifying for Title IV financial aid programs during fiscal 2017 under the Higher Education Act of 1965, as amended.

Management of EDMC continues to implement cost reduction actions to reduce cash outflows in order to maintain sufficient liquidity to allow EDMC to meet its obligations as they become due through June 30, 2017. While no assurance can be given that management's cost reduction actions will continue to reduce cash outflows at a level sufficient to offset the projected declines in cash inflows, based on management's projected cash flows for fiscal 2017, management believes that cash flow from operations and available cash on hand will provide adequate funds for ongoing operations, required debt service, and other obligations as they become due during the next twelve months ending June 30, 2017. To the extent the level of cash flow from operations and available cash on hand is not sufficient to support the required debt service and other obligations as they become due, EDMC has the ability to supplement its cash flow with borrowings under the $150.0 million revolving credit facility. The ability to draw on the revolving credit facility is at the discretion of EDMC subject to the terms of the Credit and Guaranty Agreement entered into between EDMC and its lenders including, among other requirements, that more than 50% of the lenders have not notified EDMC that a material adverse effect, excluding any adverse effect from the gainful employment regulations, has occurred to EDMC's business. The occurrence of material adverse effect other than due to the gainful employment regulation may impact the EDMC's ability to draw on the revolving credit facility and therefore limit its liquidity.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management bases these estimates on assumptions that it believes to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Cash and Cash Equivalents and Restricted Cash

The University considers all highly liquid instruments purchased with a maturity of three months or less to be cash equivalents. These investments are stated at cost, which, based upon the scheduled maturities, approximates fair value.

The University holds funds from the United States government under various student aid grants and loan programs in separate bank accounts. The University also serves as trustee for the U.S. Department of Education or respective lender, guaranty agency or student borrower, as applicable. The funds held in these bank accounts are not shown as cash or restricted cash on the consolidated balance sheets until the authorization and disbursement process has occurred. Once the authorization and disbursement process to the student has been completed, the funds are transferred to unrestricted cash accounts and become available for use in current operations, except as noted in footnote two to the table below. This transfer generally occurs for the period of the academic term for which such funds were authorized, with no term being more than 16 weeks in length.

Restricted cash was as follows at June 30 (in thousands):

	2016	2015
Cash secured letters of credit (1)	$ 43,955	$ 43,955
Title IV funds in excess of charges applied (2)	6,700	5,277
Total restricted cash	$ 50,655	$ 49,232

(1) Includes amounts related to two cash secured letter of credit facilities entered into by EDMC pursuant to which the lenders agreed to issue letters of credit to the U.S. Department of Education. Such cash is not available for any purpose other than to reimburse drawings under the letters of credit or to pay related fees and obligations. Refer to Note 3, "Governmental Regulations," for more information.

(2) U.S. Department of Education regulations require Title IV Program funds received by the University in excess of the charges applied to the relevant students at that time to be, with these students' permission, maintained and classified as restricted cash. In addition, some states have similar requirements. Such funds received for courses that have not yet begun are recorded as restricted cash due to legal restrictions on the use of the funds and as advance payments on the University's consolidated balance sheet. Funds transferred through electronic funds transfer programs are held in a separate cash account and released when certain conditions are satisfied. These restrictions have not significantly affected the University's ability to fund daily operations.

Revenue Recognition

The University's revenues are recorded net of student refunds and scholarships and consist primarily of tuition and fees, student housing fees, bookstore sales, restaurant sales in connection with culinary programs, workshop fees and sales of related study materials. The University derived approximately 98% and 96% of its net revenues from tuition and fees in the fiscal years ended June 30, 2016 and 2015, respectively. The University bills tuition and housing revenues at the beginning of an academic term and recognizes the revenue on a pro rata basis over the term of instruction or occupancy. Advance payments represent that portion of payments received but not earned and are recorded as a current liability in the accompanying consolidated balance sheet.

If a student withdraws from the University, a student's obligation for tuition and fees is limited depending on when a student withdraws during an academic term. Student refunds are regulated by the standards of the U.S. Department of Education, various state education authorities that regulate the University's schools, the Southern Association of Colleges and Schools Commission on Colleges (“SACSCOC”) and the University's institutional policies (collectively, “Refund Policies”). In the vast majority of situations, if a student withdrew from one of the University's schools after attending class for a portion of a term of instruction (ranging from approximately 40% to 70%), he or she would not be eligible for any reduction in tuition under the University's Refund Policies. Accordingly, the student would have to pay the University the balance of tuition and fees that has not been received already either in the form of financial aid or payments from the student. However, if a student withdraws from one of the University's schools prior to attending the full term of instruction (ranging from approximately 40% to 70%), the University may reduce the amount of a student's obligation for tuition and fees based on a tiered approach under which, in general, the greater the portion of the academic term that has elapsed at the time the student withdraws, the greater the student’s obligation is to the University for the tuition and fees related to that academic term.

Based on the application of its Refund Policies, the University may be entitled to incremental revenue on the day the student withdraws from one of its schools. The University reassesses collectability when a student withdraws from the institution (i.e., is no longer enrolled) and records this incremental revenue based on cash received.

Student Receivables

The University records student receivables at cost less an estimated allowance for doubtful accounts, which is determined on a quarterly basis based on the likelihood of collection considering students' enrollment status and historical payment experience. Historical collection experience is analyzed by disaggregating the student receivable balances based on predominant risk characteristics, such as whether the student is currently in-school, recently withdrew from school, or has not made a payment for a longer period of time. This level of disaggregation of student receivables results in individual pools of receivables which management believes appropriately differentiates credit risk in the portfolio and provides a reasonable basis to compute the estimate of loss. When certain criteria are met, which is generally when receivables age past the due date by more than four months, and internal collection measures have been taken without success, the accounts of former students are placed with a collection agency. Student accounts that have been placed with a collection agency are almost fully reserved and are written off after collection attempts have been unsuccessful.

Leases

The University leases certain classroom, dormitory, and office space, as well as equipment under operating leases. Before entering into a lease, an analysis is performed to determine whether a lease should be classified as a capital or an operating lease.

Certain of the University's lease agreements include tenant improvement allowances. Once the lease agreement is signed, these tenant improvement allowances are recorded as other current assets with the offset to deferred rent liabilities on the consolidated balance sheet. Concurrent with the expenditures for lease improvements, the University records increases to leasehold improvement assets in property and equipment. Other current assets are reduced once the landlord reimburses the University. The deferred rent liabilities related to tenant improvements are amortized over the term of the lease as a reduction to rent expense upon possession of the lease space.

Most of the University's lease agreements contain escalation clauses under which, if fixed and determinable, rent expense is recognized on a straight-line basis over the lives of the leases, which generally range from approximately five to 15 years with one or more renewal options. For leases with renewal options, the University records rent expense and amortizes the leasehold improvements on a straight-line basis over the original lease term, exclusive of the renewal period. When a renewal occurs, the University records rent expense over the new lease term.

Property and Equipment

Property and equipment is recorded at cost less accumulated depreciation. The University's property and equipment is depreciated over estimated useful lives ranging from three to 15 years using the straight-line method, depending on the asset. Leasehold improvements are amortized using the straight-line method over the shorter of the remaining lease term, exclusive of any renewal periods, or their estimated useful lives. Accelerated depreciation methods are generally used for income tax purposes. The University evaluates the recoverability of property and equipment whenever events or changes in circumstances indicate the carrying amount of such assets may not be fully recoverable and when events and circumstances indicate that the undiscounted cash flows estimated to be generated by those assets or asset groups are less than their carrying amounts. Events and circumstances that could trigger an impairment review include changes in the regulatory environment, deteriorating economic conditions or poor operating performance at individual campus locations. Any resulting impairment loss is measured as the difference between the fair value of the assets or asset groups and their carrying value with the loss recorded as an operating expense in the consolidated statement of operations in the period incurred. Refer to Note 4, "Property and Equipment," for more information.

Goodwill and Intangible Assets

On June 1, 2006, in connection with the Transaction, property, equipment, intangible assets other than goodwill, and other assets and liabilities were recorded at fair value. The excess of the amount paid to acquire the University at the time of the Transaction over the fair values of these net assets represented the intrinsic value of the University beyond its tangible and identifiable intangible net assets and was assigned to goodwill.

The University formally evaluates the carrying amount of goodwill for each of its locations on April 1 of each fiscal year. In addition, the University performs an evaluation on an interim basis if it determines that recent events or prevailing conditions indicate a potential impairment of goodwill. A significant amount of judgment is involved in determining whether an indicator of impairment has occurred between annual impairment tests. These indicators include, but are not limited to, overall financial performance such as adverse changes in recent forecasts of operating results, industry and market considerations, updated business plans, and regulatory and legal developments.

Goodwill is impaired when the carrying amount of a location's goodwill exceeds its implied fair value, as determined under a two-step approach. In the first step, the University determines the fair value of each reporting unit and compares that fair value to each location's carrying value. The University estimates the fair value of its locations using a combination of the discounted cash flow method (income approach) and the guideline public company method (market approach), which takes into account the invested capital and associated earnings multiples of publicly-traded peer companies. If the results of the first step indicate the carrying amount of a reporting unit is higher than its fair value, a second step must be performed, which requires the University to determine the implied fair value of goodwill in the same manner as if it had acquired the location in an arm's length transaction as of the testing date. This second step is performed by deducting the estimated fair value of all tangible and identifiable intangible net assets of the reporting unit from the estimated fair value of the location. If the recorded amount of goodwill exceeds this implied fair value, an impairment charge is recorded for the difference as an operating expense in the period incurred.

Indefinite-lived intangible assets, consisting of the licensing, accreditation and Title IV program participation assets for the University are also evaluated annually on April 1 for impairment and on an interim basis if events or changes in circumstances between annual tests indicate that the asset might be impaired. The University uses a combination of the cost and income approaches to establish the asset value of licenses, accreditation, and Title IV program participation assets. On the impairment testing date, if the fair value of the intangible asset is less than its carrying value, an impairment loss is recognized for an amount equal to the difference. The intangible asset is then carried at its new fair value.

Refer to Note 5, "Goodwill and Intangible Assets," for more information.

Unearned Tuition

Due to the fact that the University has academic terms with starting and ending dates that differ throughout the period, there may be tuition from these academic terms for which the associated revenue has not been earned. Such amounts are recorded as unearned tuition as a current liability in the accompanying consolidated balance sheet.

Art Grant

The Art Institutes introduced a new grant program in fiscal 2015 which provides a tuition discount for students who successfully complete 12 credits towards an associates or bachelor degree, enroll in and satisfy a minimum attendance period for the next term. The University records the discount on tuition for students who have enrolled in the Art Grant program on a proportional basis starting with the first credit earned, net of estimated breakage. If the student becomes ineligible, the University recognizes deferred revenue in the period in which ineligibility occurs. During fiscal year 2016,the University recognized $3.1 million in grants awarded to students participating in the Art Grant program. As of June 30, 2016 and 2015, a liability of $2.8 million and $1.2 million was recorded related to these grants, respectively, which is presented within unearned tuition.

Net Investment of EDMC

The University participates in a cash management program operated by EDMC that allows EDMC to consolidate most cash from all its locations in order to maximize investment income. In addition, EDMC funds checks written on the University's disbursement bank account as they clear the disbursing bank. The difference between the cash provided to EDMC by the University and the day-to-day funding provided by EDMC to the University has been classified in member's equity as part of the net investment of EDMC in the consolidated balance sheets as there is no formal repayment schedule related to this amount. The net investment of EDMC balance also includes contributed capital.

The EDMC Board of Directors approved a resolution directing the Chief Financial Officer of EDMC to provide sufficient cash at the end of each fiscal year to the University in order to have a composite score of at least 1.5 calculated pursuant to the financial responsibility standards promulgated by the U.S. Department of Education as outlined in Note 3, "Governmental Regulations".

Income Taxes

The University accounts for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities result from (i) temporary differences in the recognition of income and expense for financial and income tax reporting requirements, and (ii) differences between the recorded value of assets acquired in business combinations accounted for as purchases for financial reporting purposes and their corresponding tax bases. Deferred income tax assets are reduced by a valuation allowance if it is more-likely-than-not that some portion of the deferred income tax asset will not be realized.

The University is included in the federal consolidated tax return filed by EDMC. The University and EDMC do not have a formal tax-sharing agreement. The provision for income taxes in the accompanying consolidated statement of income is calculated on a carve-out basis, giving recognition to the impact of filing in a consolidated group. The effective tax rate differs from the consolidated federal and state statutory rates primarily due to valuation allowances, the impact of the Debt Restructuring, and expenses that are not deductible for tax purposes. State taxes are accrued and reported in the states where the University provides services.

Contingencies

The University accrues for contingent obligations when it is probable that a liability has been incurred and the amount is reasonably estimable. As facts concerning contingencies become known, management reassesses its position and makes appropriate adjustments to its consolidated financial statements.

Costs and Expenses

Educational services expense consists primarily of costs related to the development, delivery and administration of the University's education programs. Major cost components are faculty compensation, salaries of administrative and student services staff, facility occupancy costs, bad debt expense, costs of educational materials, information systems costs and support services provided by The Center as described in Note 9, "Related-Party Transactions." These costs are expensed as services are provided to the University or as incurred.

General and administrative expense primarily consists of marketing and student admissions expenses and departmental costs such as executive management, finance and accounting, legal, corporate development, and other departments that do not provide direct services to the University's students. These costs are expensed as services are provided to the University or as incurred.

Marketing costs, which are expensed as incurred and classified as general and administrative expense in the consolidated statements of operations, were \$55.7 million and \$60.4 million in the fiscal years ended June 30, 2016 and 2015, respectively.

Recent Accounting Pronouncements

In June 2016, the Financial Accounting Standards Board (the “FASB”) issued an Accounting Standards Update (“ASU”) No. 2016-13 that will require entities to use a new forward-looking “expected loss” model on trade and other receivables, held-to-maturity debt securities, loans, and other instruments that generally will result in the earlier recognition of allowances for credit losses. Entities will have to disclose significantly more information, including information they use to track credit quality by year of origination for most financing receivables. The standard is effective for the University for the fiscal years beginning after December 15, 2020, and interim periods therein. Early adoption is permitted for annual periods beginning after December 15, 2018, and interim periods therein. The University is currently evaluating the impact that the standard will have on its financial condition, results of operations, and disclosures.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842),” replacing the existing guidance in ASC 840, “Leases.” The new guidance establishes a right-of-use (ROU) model which requires the lessee to record a ROU asset and corresponding lease liability on the balance sheet for all leases with terms exceeding twelve months. Leases will be classified as either financing or operating, with the classification affecting the pattern of expense recognition on the income statement. The standard is effective for the Company beginning in fiscal year 2021, with early adoption permitted. The new guidance must be applied on a modified retrospective basis at the beginning of the earliest comparative period presented in the financial statements. The University is currently evaluating the impact that the standard will have on its financial condition, results of operations, and disclosures.

In July 2015, the FASB issued ASU No. 2015-17 “Income Taxes (Topic 740).” The new guidance requires an entity to classify deferred tax liabilities and assets as noncurrent within a classified statement of financial position. The standard is effective for the University beginning fiscal year 2018, with early adoption permitted, and may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The University has decided to implement the guidance early, beginning with the fiscal year 2016 financial statements presented herein on a prospective basis.

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, “Revenue from Contracts with Customers." The standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. In July 2015, the FASB voted to defer the effective date of ASU 2014-09. Accordingly, this guidance is effective for interim and annual periods beginning after December 15, 2017 with early adoption permitted for interim and annual periods beginning after December 15, 2016. This accounting standard, as amended, is effective for the University beginning in the first quarter of fiscal year 2019. The University is currently evaluating the impact that the standard will have on its financial condition, results of operations, and disclosures.

3. GOVERNMENTAL REGULATIONS

Most of the students at the University's campuses rely, at least in part, on financial assistance to pay for the cost of their education. In the United States, the largest sources of such support are the federal student aid programs under Title IV of the Higher Education Act of 1965, as amended ("HEA"). Additional sources of funds include other federal grant programs, state grant and loan programs, private loan programs and institutional grants and scholarships. To provide students access to financial assistance resources available through Title IV programs, a school must be (i) authorized to offer its programs of instruction by the relevant agency of the states in which it is physically located and comply with applicable state requirements regarding fully-online programs, (ii) institutionally accredited by an agency recognized by the U.S. Department of Education, and (iii) certified as an eligible institution by the U.S. Department of Education. In addition, the university must ensure that Title IV program funds are properly accounted for and disbursed in the correct amounts to eligible students and remain in compliance generally with the Title IV program regulations. Most of the U.S. Department of Education's requirements, such as the financial responsibility standards and the 90/10 Rule, which are described in greater detail below, are applied on an institutional basis, with an institution defined as a main campus and its additional locations, if any.

Financial Responsibility Standards. Education institutions participating in Title IV programs must satisfy a series of specific standards of financial responsibility. The U.S. Department of Education has adopted standards to determine an institution’s financial responsibility to participate in Title IV programs. The regulations establish three ratios: (i) the equity ratio, intended to measure an institution’s capital resources, ability to borrow and financial viability; (ii) the primary reserve ratio, intended to measure an institution’s ability to support current operations from expendable resources; and (iii) the net income ratio, intended to measure an institution’s profitability. Each ratio is calculated separately, based on the figures in the institution’s most recent annual audited financial statements, and then weighted and consolidated to arrive at a single composite score. The composite score must be at least 1.5 in order for the institution to be deemed financially responsible without conditions or additional oversight. If an institution fails to meet any of these requirements, the U.S. Department of Education may set restrictions on the institution’s eligibility to participate in Title IV programs. Institutions are evaluated for compliance with these requirements as part of the U.S. Department of Education’s renewal of certification process and also annually as each institution submits its audited financial statements to the U.S. Department of Education. As of June 30, 2016 and 2015, the University satisfied the financial responsibility standards.

As of June 30, 2016, EDMC did not meet the required quantitative measures of financial responsibility on a consolidated basis due to the amount of indebtedness incurred and goodwill it recorded in connection with the Transaction. Accordingly, EDMC is required by the U.S. Department of Education to post a letter of credit and is subject to provisional certification and additional financial and cash monitoring of its disbursements of Title IV funds. In May 2016, the U.S. Department of Education decreased the amount of the required letter of credit from $271.5 million to $240.6 million, which equals 15 percent of the total Title IV aid received by students attending EDMC’s institutions during the fiscal year ended June 30, 2015.

The “90/10 Rule.” Under a provision of the HEA commonly referred to as the “90/10 Rule,” an institution will cease to be eligible to participate in Title IV programs if, on a cash accounting basis, more than 90% of its revenues for each of two consecutive fiscal years were derived from Title IV programs as calculated under the applicable regulations. If an institution loses its Title IV eligibility under the 90/10

Rule, it may not reapply for eligibility until the end of two fiscal years. Institutions that fail to satisfy the 90/10 Rule for one fiscal year are placed on provisional certification. The University was in compliance with the 90/10 Rule for the fiscal years ended June 30, 2016 and 2015.

4. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following as of June 30 (in thousands):

Asset Class	2016	2015
Leasehold improvements	$ 74,021	$ 71,706
Furniture and equipment	21,525	20,428
Technology and other equipment	24,450	27,779
Library books	6,995	6,707
Construction in progress	423	755
Total	127,414	127,375
Less accumulated depreciation	(94,333)	(88,777)
Property and equipment, net	$ 33,081	$ 38,598

The University's depreciation and amortization expense related to property and equipment was $11.0 million and $14.7 million in the fiscal years ended June 30, 2016 and 2015, respectively. Included in depreciation expense was approximately $1.5 million and $2.0 million for the fiscal years ended June 30, 2016 and 2015, respectively, that has been allocated from EDMC for assets which are not recorded in the University's consolidated financial statements but are utilized by the University.

Impairments

During fiscal 2016, the University recorded long-lived asset impairment charges of $1.3 million at one of The Art Institutes locations where estimated cash flows are projected to be insufficient to support the carrying value of the related property and equipment.

During fiscal 2015, the University announced that it will no longer enroll new students at The Art Institute of Fort Worth and teach-out students currently enrolled at this location. In connection with the teach-out, the University recorded long-lived asset impairment charges of $1.0 million in the consolidated statements of operations.

Also during fiscal 2015, the University also recorded long-lived asset impairment charges of $8.5 million at two of its other locations where estimated cash flows are projected to be insufficient to support the carrying value of the related property and equipment. The University estimated fair value of assets at these locations using a combination of the discounted cash flow method (income approach) and orderly liquidation value in-use (cost approach) on a non-recurring basis using unobservable Level Three inputs including the following key assumptions:

- a discount rate ranging from 18.0% to 23.5%; and
- an orderly liquidation value factor (expressed as a percentage of original cost) ranging from 2.0% to 7.5%.

Impairment losses are allocated to the assets and recorded through accumulated depreciation.

5. GOODWILL AND INTANGIBLE ASSETS

The University was acquired by EDMC in fiscal 2004. As part of this business combination, goodwill was recorded, which consists of the cost in excess of the fair value of the identifiable net assets acquired. A roll forward of the University's goodwill balance from June 30, 2014 to June 30, 2016 is as follows (in thousands):

	Total
Balance Sheet as of June 30, 2014:	
Gross	$ 44,902
Accumulated impairments	—
Goodwill	44,902
Statement of Operations for the Fiscal Year Ended June 30, 2015:	
Impairment charge	(607)
Balance Sheet as of June 30, 2015:	
Gross	44,902
Accumulated impairments	(607)
Goodwill	44,295
Statement of Operations for the Fiscal Year Ended June 30, 2016:	
Impairment charge	—
Balance Sheet as of June 30, 2016:	
Gross	44,902
Accumulated impairments	(607)
Goodwill	$ 44,295

Goodwill Impairment Charges

The University formally evaluates the carrying amount of goodwill for each of its reporting units on April 1 of each fiscal year. In addition, the University performs an evaluation on an interim basis if it determines that recent events or prevailing conditions indicate a potential impairment of goodwill. A significant amount of judgment is involved in determining whether an indicator of impairment has occurred between annual impairment tests. These indicators include, but are not limited to, overall financial performance such as adverse changes in recent forecasts of operating results, industry and market considerations, updated business plans, and regulatory and legal developments.

A two step process is used to determine the amount to be recorded for an impairment. In the first step, the University determines the fair value of each location and compares that value to the location's carrying value. If the results of this first step indicate the carrying amount of a location is in excess of its fair value, the second step must be performed, which requires that the University determine the implied fair value of goodwill in the same manner as if it had acquired those locations as of the testing date. Under the second step, an impairment is recognized if the carrying amount of a location's goodwill exceeds its implied fair value. If an impairment charge is required to be recorded, it is presented as an operating expense in the period in which the goodwill's carrying value exceeds its new implied fair value.

Consistent with prior years, management performed its annual goodwill impairment testing as of April 1, 2016. The results indicated that the South University locations had fair values in excess of its carrying value as of March 31, 2016. Additionally during the fourth quarter, a change in market considerations indicated potential impairment to the Company's goodwill. The results indicated that the South University's locations had fair value in excess of its carrying value as of June 30, 2016.

The valuation of the University's locations under the traditional discounted cash flow method requires the use of internal business plans that are based on judgments and estimates, which account for expected future economic conditions, demand and pricing for the University's educational services, costs, inflation and discount rates, and other factors. The use of judgments and estimates involves inherent uncertainties. The University's measurement of the fair values of its locations is dependent on the accuracy of the assumptions used and how the University's estimates compare to future operating performance. The key assumptions include the following:

- Future cash flow assumptions — The University's projections are based on organic growth and are derived from historical experience and assumptions regarding future growth and profitability trends. These projections also take into account the current economic climate and the extent to which the regulatory environment is expected to impact future growth opportunities. The University's analysis incorporated an assumed period of cash flows of ten years with a terminal value determined using the Gordon Growth Model.
- Discount rate — The discount rate is based on each location's weighted average cost of capital ("WACC"). The three components of WACC are the cost of equity, cost of debt and capital structure, each of which requires judgment by management to estimate. The University develops its cost of equity estimate using the Capital Asset Pricing Model based on perceived risks and predictability of each reporting unit's future cash flows. The cost of debt component represents a market participant's estimated cost of borrowing, which the University estimates using the average return on corporate bonds as of the valuation date, adjusted for taxes. At March 31, and June 30, 2016, the WACC used to estimate the fair value of the University was 22% and 30%, respectively.

Intangible Assets

Intangible assets consisted of the following at June 30 (in thousands):

	2016		2015	
	Gross Carrying Amount	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Curriculum	$ 8,044	$ (6,919)	$ 8,069	$ (5,801)
Other intangibles	350	(284)	350	(263)
Total intangible assets	$ 8,394	$ (7,203)	$ 8,419	$ (6,064)

The University's amortization expense related to intangible assets was approximately $1.5 million and $1.6 million in the fiscal years ended June 30, 2016 and 2015, respectively. Estimated annual amortization expense for each of the years ending June 30, 2017 through 2021 is as follows at June 30, 2016 (in thousands):

Fiscal Year:	**Amortization Expense**
2017	$ 676
2018	365
2019	128
2020	22
2021	—

6. STUDENT RECEIVABLES

The University offers four types of financing arrangements to its students to assist with the obligation associated with tuition and fees: retail installment contracts; commitment agreements; paid in full amounts; and lines of credit. These financing arrangements help students fund the difference between total tuition and fees and the amount covered by various sources of financial aid, including amounts awarded under Title IV programs, private loans, and cash payments. Paid in full amounts are short-term extensions of credit for typically small balances which are repayable upon demand by the University. Retail installment contracts, commitment agreements, and lines of credit are extensions of credit which include a monthly minimum payment amount, permit students to repay amounts borrowed over a specified period of time, and incur interest charges that accrue each month on unpaid balances when the accounts reach an out-of-school enrollment status.

Student receivables include $10.1 million (net of $10.2 million allowance) and $7.4 million (net of $7.9 million allowance) recorded in other long-term assets on the accompanying balance sheet related to retail installment contracts, commitment agreements, and lines of credit to students for amounts due beyond one year during the fiscal years ended June 30, 2016 and 2015, respectively.

The University monitors its student receivables based on enrollment status. Receivables from former students who are in collections are almost fully reserved for. Receivables for out-of-school students are reserved for at a higher rate than receivables from students that are in-school. The gross current and noncurrent student receivables by student status were as follows at June 30 (in thousands):

	2016	2015
In-school	$ 55,565	$ 47,563
Out-of-school	3,393	17,669
Collections	20,357	24,717
Gross student receivables	$ 79,315	$ 89,949

A roll forward of the University's total allowance for doubtful accounts from June 30, 2014 to June 30, 2016 is as follows (in thousands):

Balance, June 30, 2014	$ 37,547
Bad debt expense	24,539
Amounts written off	(25,404)
Balance, June 30, 2015	36,682
Bad debt expense	19,318
Amounts written off	(28,806)
Balance, June 30, 2016	$ 27,194

The amounts set forth above are recorded within student receivables, net and other long-term assets on the consolidated balance sheets. Recoveries of amounts previously written off were not significant in any period presented. Refer to Note 2, "Summary of Significant Accounting Policies," for more information.

7. ACCRUED LIABILITIES

Accrued liabilities consisted of the following as of June 30 (in thousands):

	2016	2015
Employee compensation	$ 5,487	$ 4,903
Advertising	3,757	—
Student support services	1,298	1,223
Capital expenditures	323	481
Taxes	494	430
Student refunds	255	387
Other	90	46
Total accrued liabilities	$ 11,704	$ 7,470

8. FAIR VALUE OF FINANCIAL INSTRUMENTS

The University determines the fair value of assets and liabilities based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. The fair values are based on assumptions that market participants would use when pricing an asset or liability, including assumptions about risk and the risks inherent in valuation techniques and the inputs to valuations. The fair value hierarchy is based on whether the inputs to valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the University's own assumptions of what market participants would use. The fair value hierarchy includes three levels of inputs that may be used to measure fair value as described below.

Level One - Quoted prices for identical instruments in active markets.

Level Two - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations for which all significant inputs are observable market data.

Level Three - Unobservable inputs significant to the fair value measurement supported by little or no market activity.

In some cases, the inputs used to measure fair value may meet the definition of more than one level of fair value hierarchy. The lowest level input that is significant to the fair value measurement in its totality determines the applicable level in the fair value hierarchy.

As described in Note 4, "Property and Equipment" and Note 5, "Goodwill and Intangible Assets," the University recorded asset impairments during fiscal 2015 resulting in certain long-lived assets being measured at fair value on a non-recurring basis using Level Three inputs.

9. RELATED-PARTY TRANSACTIONS

Coordinating and Support Services

The University receives coordinating and support services from EDMC, such as legal, insurance, and information technology-related services. EDMC allocates costs to the University based upon certain factors including the University's revenues and student enrollment, which estimate the amount that the University would pay an unaffiliated entity for these services. In addition, during fiscal 2014, EDMC created "The Center," which has been providing support services to its campuses through the centralization and automation of certain non-student facing activities, including financial aid packaging, the qualification and transfer of prospective students to school admissions teams, student billing services, certain registrar services, and support call center services for students and employees. The Center allocates costs to each campus based primarily based on the level of transaction volume.

Total costs allocated by The Center and EDMC to the University were approximately $43.7 million and $41.1 million, which are included in general and administrative expense and educational services expense in the consolidated statements of operations in the fiscal years ended June 30, 2016 and 2015, respectively.

Employee Scholarships

The University records revenues and expenses related to its internal tuition grant policy on a gross basis. The University received $2.4 million and $2.8 million in fiscal 2016 and 2015, respectively, relating to employees of other EDMC wholly-owned entities attending the University. In addition, the University paid $1.6 million and $0.9 million in fiscal 2016 and 2015, respectively, to other EDMC wholly-owned entities relating to its employees attending other EDMC wholly-owned institutions.

Leases

The University's Tampa campus shares its physical location with the Art Institute of Tampa, which is also wholly-owned by EDMC. Certain building costs, primarily rent expense, are allocated by EDMC between South University of Tampa and the Art Institute of Tampa. Total rent expense for this shared location was $2.5 million and $2.3 million in fiscal years ended June 30, 2016 and 2015, respectively. Included in this amount was approximately $1.3 million and $1.2 million that was allocated to South University of Tampa in the fiscal years ended June 30, 2016 and 2015, respectively, and is included in the accompanying consolidated statements of operations within educational services expense.

EDMC guarantees all of the University's lease agreements, under which EDMC assumes all obligations, liabilities, and duties of the University in the event of default. The guarantees are in place through the full terms of the leases, including any extensions or renewals. Refer to Note 11, "Commitments and Contingencies," for the University's remaining lease obligations.

Cash Management

Refer to Note 2, "Summary of Significant Accounting Policies," under "Net Investment of EDMC" for information regarding the University's cash management program.

10. INCOME TAXES

The provision for income taxes includes current and deferred taxes, as reflected below for the fiscal year ended June 30 (in thousands):

	2016	2015
Current taxes:		
Federal	$ 12,858	$ 8,602
State	867	402
Total current tax provision	13,725	9,004
Deferred tax expense	(1,396)	11,042
Total income tax expense	$ 12,329	$ 20,046

As a result of the EDMC consolidated group being in a historical cumulative loss position, it was concluded that the group may not fully recognize the benefit of its deferred tax assets. As such, valuation allowances have been recorded against the federal and state deferred tax assets of the EDMC consolidated group. The deferred tax assets presented in the accompanying balance sheet reflect the impact of the recording of such valuation allowances against the University's deferred tax assets.

In November 2015, the FASB issued ASU 2015-17, Balance Sheet Classification of Deferred Taxes. This ASU simplifies the presentation of deferred income taxes by requiring that all deferred tax assets and liabilities, along with any related valuation allowance, be classified as noncurrent in the balance sheet. The Company elected to adopt this ASU on a prospective basis during the fourth quarter of 2016. The adoption of this ASU did not have a material impact on the Company's financial position and it had no impact on its results of operations or cash flows. Deferred income taxes are presented in the consolidated balance sheet for all significant temporary difference between tax and financial reporting, which consist primarily of the allowances for doubtful accounts, property and equipment, intangible assets, deferred rent and the impact of the Debt Restructuring. Net deferred income tax assets and liabilities consisted of the following at June 30 (in thousands):

	2016	2015
Gross current deferred tax assets	$ —	$ 13,534
Valuation allowance	—	(10,639)
Total current deferred tax assets	$ —	$ 2,895
Total noncurrent deferred tax assets	$ 18,384	$ 9,375
Valuation allowance	(12,330)	(6,457)
Total noncurrent deferred tax assets	6,054	2,918
Noncurrent deferred tax liabilities	23,304	22,344
Total net noncurrent deferred tax liabilities	$ 17,250	$ 19,426

At June 30, 2016 and 2015, South University of North Carolina had net operating loss carry forwards of approximately \$3.8 million and \$4.9 million, respectively, which are available to offset future taxable income and related deferred tax assets of \$0.0 million and \$0.2 million, respectively. These carry forwards begin to expire in fiscal 2028.

11. COMMITMENTS AND CONTINGENCIES

Debt Restructuring Litigation

In October 2014, a complaint captioned Marblegate Asset Management, et al v. Education Management Corporation, et al. was filed in federal district court in the Southern District of New York seeking, among other things, a preliminary injunction to block the Debt Restructuring. The plaintiffs, holders of Notes, alleged that the Debt Restructuring would force them either to convert their debt to equity or to risk the elimination of their practical ability to recover their principal and remaining interest payments in violation of the Trust Indenture Act of 1939 because substantially all of the Company's assets would be foreclosed and sold in an asset sale to an affiliate and EDMC would release its guaranty of the Cash Pay/PIK Notes due 2018. In December 2014, the Court denied the plaintiffs' request for a preliminary injunction enjoining the Debt Restructuring but indicated that the plaintiffs were likely to win on the merits of their claim that the Debt Restructuring as constituted violated the Trust Indenture Act of 1939. The Company and the debt holders who agreed to participate in the Debt Restructuring subsequently amended the restructuring in response to the Court's ruling and the initial step of the transaction, including the foreclosure and asset sale and the exchange of debt for equity, was completed in January 2015. Secured creditors also released EDMC of its guarantee of the secured debt in connection with the transaction but the Company did not take steps required to effectuate the release of EDMC from its guarantee of outstanding Cash Pay/PIK Notes due 2018. In addition, the subsidiary to which the Company's assets were transferred issued its own guarantee of the Cash Pay/PIK Notes due 2018, which will remain in place so long as EDMC's guarantee of the Cash Pay/PIK Notes due 2018 is not released. EDMC then brought a counterclaim seeking a declaration that it was permitted to effectuate the release of its guarantee. The Company also reached an agreement with all the plaintiffs in the case other than Marblegate prior to completing the first step of the Debt Restructuring.

In June 2015, the Court ruled that EDMC's release of its guaranty of the Cash PIK/Pay Notes due 2018 would violate the Trust Indenture Act of 1939. The Company appealed the decision to the Second Circuit Court of Appeals in order to protect the interests of the overwhelming majority of its creditors who participated in the Debt Restructuring. The Second Circuit Court of Appeals heard oral arguments from the parties to the case on May 12, 2016. The Cash PIK/Pay Notes due 2018 held by Marblegate had an outstanding principal balance of $16.7 million at June 30, 2016. The Company will continue making interest payments on the notes while the appeal is pending and will be obligated to pay the debt in full in the event that it does not prevail on the appeal or successfully appeal an adverse decision to the United States Supreme Court.

Other Matters

EDMC is a defendant in certain other legal proceedings arising out of the conduct of its business. Additionally, EDMC is subject to compliance reviews by various state and federal agencies which provide student financial aid programs, with respect to which noncompliance may result in liability for educational benefits paid as well as fines and other corrective action. In the opinion of management, based upon an investigation of these matters and discussion with legal counsel, the ultimate outcome of such other legal proceedings and compliance reviews, individually and in the aggregate, is not expected to have a material adverse effect on EDMC's consolidated financial position, results of operations or liquidity. At June 30, 2016, the School was not subject to any legal proceedings that are expected to have a material adverse effect on its consolidated financial position, results of operations or liquidity.

Lease Commitments

The University leases its facilities under various operating leases, some of which are with related parties (see Note 9, "Related-Party Transactions"), that expire on various dates through 2029. Rent expense under these leases was approximately $22.5 million and $23.8 million in the fiscal years ended June 30, 2016 and 2015, respectively.

The annual minimum future cash commitments for the fiscal years ending June 30 under the University's noncancelable, long-term operating leases are as follows at June 30, 2016 (in thousands):

Fiscal Year:	
2017	$ 20,994
2018	19,906
2019	20,022
2020	19,955
2021	19,101
Thereafter	82,644

Surety Bonds

At June 30, 2016, the University has provided $11.3 million of surety bonds primarily to state regulatory agencies through four different surety providers.

12. EMPLOYEE BENEFIT PLANS

Through September 20, 2014, EDMC sponsored a 401(k) plan that covered substantially all employees under which EDMC matched employee contributions to the retirement plan dollar for dollar up to 6%. All participants in the plan vested in EDMC's matching contributions immediately. The University recorded expense related to the retirement plan of approximately $0.7 million for the fiscal year ended June 30, 2015. Effective September 20, 2014, EDMC suspended its matching program indefinitely. The Company did not make any contributions to the retirement plan during fiscal 2016.

13. SUBSEQUENT EVENTS

The University has evaluated subsequent events through September 28, 2016, the date through which these financial statements were available to be issued.

Supplemental Information

South University, LLC and Subsidiaries

Consolidating Balance Sheet

(Dollars in thousands)

June 30, 2016

	South University-Savannah	South University-Tampa	South University-West Palm Beach	South University-Montgomery	South University-Richmond	South University-Columbia	South University Virginia Beach	South University-Novi	South University - Austin	South University - Cleveland	South University - Highpoint	South University - Orlando	The Art Institute of Dallas	The Art Institute of Fort Worth	The Art Institute of Charlotte	The Art Institute of Raleigh - Durham	Reclass-ifications & Eliminations	South University, LLC and Subsidiaries
Cash and cash equivalents	$ 646	$ 2,745	$ 3,540	$ 2,301	$ 3,357	$ 3,516	$ 2,562	$ 2,529	$ 4,946	$ 1,872	$ 3,286	$ 860	$ 6,163	$ 1,983	$ 2,020	$ 3,825	$ —	$ 46,151
Restricted cash	34,823	—	4,188	155	200	200	—	1,400	1,100	2,510	2,500	—	3,441	5	96	37	—	50,655
Total cash	35,469	2,745	7,728	2,456	3,557	3,716	2,562	3,929	6,046	4,382	5,786	860	9,604	1,988	2,116	3,862	—	96,806
Receivables:																		
Trade	21,715	3,000	2,646	2,218	3,639	5,567	2,161	1,846	1,523	1,850	1,859	54	2,969	528	5,387	2,099	—	59,061
Allowance for doubtful accounts	(6,374)	(107)	112	(616)	(1,268)	(857)	(359)	(248)	(128)	(577)	(236)	7	(1,432)	(251)	(3,506)	(1,194)	—	(17,034)
Notes, advances, and other receivables	2,039	11	1	1	—	54	1	1	1	17	1	(37)	3	4	30	1	—	2,128
Other current assets	144	146	4	(3)	598	61	26	(7)	(1)	17	40	—	57	—	52	46	—	1,180
Total current assets	52,993	5,795	10,491	4,056	6,526	8,541	4,391	5,521	7,441	5,689	7,450	884	11,201	2,269	4,079	4,814	—	142,141
Property and equipment, net	1,487	1,417	3,768	1,285	2,992	4,156	3,523	2,276	3,858	2,776	3,174	746	857	9	331	426	—	33,081
Investment in subsidiaries	55,640	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(55,640)	—
Deferred income taxes	—	—	175	—	—	—	—	—	—	—	—	—	—	—	—	—	(175)	—
Other long-term assets	1,000	586	501	641	1,146	2,020	491	709	302	594	566	—	371	26	865	409	—	10,227
Intangible assets, net of amortization	1,052	—	67	45	—	27	—	—	—	—	—	—	—	—	—	—	—	1,191
Goodwill	44,295	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	44,295
Total assets	$ 156,467	$ 7,798	$ 15,002	$ 6,027	$ 10,664	$ 14,744	$ 8,405	$ 8,506	$ 11,601	$ 9,059	$ 11,190	$ 1,630	$ 12,429	$ 2,304	$ 5,275	$ 5,649	$ (55,815)	$ 230,935
Current liabilities:																		
Accounts payable	$ 1,702	$ 152	$ 98	$ 45	$ 61	$ 178	$ 139	$ 80	$ 63	$ 93	$ 96	$ 11	$ 54	$ 9	$ 57	$ 55	$ —	$ 2,893
Accrued liabilities	6,005	414	375	340	672	710	253	323	302	325	333	42	727	83	437	363	—	11,704
Unearned tuition	18,952	4,447	4,725	2,197	2,988	6,259	2,830	2,633	1,974	1,917	1,959	330	999	199	955	674	—	54,038
Advance payments	19,389	545	363	249	183	408	403	404	107	137	105	16	574	57	224	175	—	23,339
Total current liabilities	46,048	5,558	5,561	2,831	3,904	7,555	3,625	3,440	2,446	2,472	2,493	399	2,354	348	1,673	1,267	—	91,974
Deferred income taxes	17,425	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(175)	17,250
Deferred rent	1,226	942	3,791	1,537	2,558	2,506	1,340	1,821	2,828	2,152	2,274	199	3,504	467	748	2,050	—	29,943
Member's equity:																		
Net investment of EDMC	11,706	(9,684)	(22,412)	(8,857)	5,324	(43,492)	2,297	9,638	20,323	14,552	13,528	1,712	(32,851)	3,325	(8,315)	6,645	2,361	(34,200)
Accumulated earnings (deficit)	80,062	10,982	28,062	10,516	(1,122)	48,175	1,143	(6,393)	(13,996)	(10,117)	(7,105)	(680)	39,422	(1,836)	11,169	(4,313)	(58,001)	125,968
Total member's equity	91,768	1,298	5,650	1,659	4,202	4,683	3,440	3,245	6,327	4,435	6,423	1,032	6,571	1,489	2,854	2,332	(55,640)	91,768
Total liabilities and member's equity	$ 156,467	$ 7,798	$ 15,002	$ 6,027	$ 10,664	$ 14,744	$ 8,405	$ 8,506	$ 11,601	$ 9,059	$ 11,190	$ 1,630	$ 12,429	$ 2,304	$ 5,275	$ 5,649	$ (55,815)	$ 230,935

South University, LLC and Subsidiaries

Consolidating Balance Sheet

(Dollars in thousands)

June 30, 2015

	South University-Savannah	South University-Tampa	South University-West Palm Beach	South University-Montgomery	South University-Richmond	South University-Columbia	South University Virginia Beach	South University-Novi	South University - Austin
Cash and cash equivalents	$ 7,525	$ 2,940	$ 3,045	$ 3,320	$ 2,752	$ 3,757	$ 3,611	$ 3,015	$ 4,135
Restricted cash	33,481	—	4,296	155	200	46	—	1,400	1,100
Total cash	41,006	2,940	7,341	3,475	2,952	3,803	3,611	4,415	5,235
Receivables:									
Trade	25,321	4,150	2,640	2,917	4,377	6,399	2,803	2,951	1,504
Allowance for doubtful accounts	(9,423)	(1,018)	(356)	(1,100)	(1,341)	(1,520)	(966)	(679)	(412)
Notes, advances, and other receivables	3,896	8	—	20	24	25	42	—	—
Deferred income taxes	861	105	9	87	113	188	112	66	38
Other current assets	142	1,454	85	86	59	195	223	71	84
Total current assets	61,803	7,639	9,719	5,485	6,184	9,090	5,825	6,824	6,449
Property and equipment, net	1,763	1,895	4,809	1,537	3,432	4,755	2,283	2,799	4,253
Investment in subsidiaries	58,128	—	—	—	—	—	—	—	—
Deferred income taxes	—	355	—	—	—	—	—	—	—
Other long-term assets	813	404	44	522	963	1,371	372	488	55
Intangible assets, net of amortization	2,171	—	89	59	—	36	—	—	—
Goodwill	44,295	—	—	—	—	—	—	—	—
Total assets	$ 168,973	$ 10,293	$ 14,661	$ 7,603	$ 10,579	$ 15,252	$ 8,480	$ 10,111	$ 10,757
Current liabilities:									
Accounts payable	$ 2,184	$ 224	$ 126	$ 93	$ 101	$ 287	$ 74	$ 117	$ 266
Accrued liabilities	3,758	237	227	175	215	437	580	189	242
Unearned tuition	18,541	4,038	4,221	2,035	3,069	6,444	2,698	2,857	1,161
Advance payments	20,112	637	633	191	118	467	474	223	66
Total current liabilities	44,595	5,136	5,207	2,494	3,503	7,635	3,826	3,386	1,735
Deferred income taxes	13,042	—	1,154	40	908	769	77	189	713
Deferred rent	1,200	1,139	4,203	1,714	2,190	2,512	1,099	2,040	2,784
Member's equity:									
Net investment of EDMC	40,385	(4,759)	(21,383)	(8,098)	5,359	(40,100)	2,980	11,028	18,698
Accumulated earnings (deficit)	69,751	8,777	25,480	11,453	(1,381)	44,436	498	(6,532)	(13,173)
Total member's equity	110,136	4,018	4,097	3,355	3,978	4,336	3,478	4,496	5,525
Total liabilities and member's equity	$ 168,973	$ 10,293	$ 14,661	$ 7,603	$ 10,579	$ 15,252	$ 8,480	$ 10,111	$ 10,757

	South University - Cleveland	South University - Highpoint	South University - Orlando	The Art Institute of Dallas	The Art Institute of Fort Worth	The Art Institute of Charlotte	The Art Institute of Raleigh - Durham	Reclass-ifications & Eliminations	South University, LLC and Subsidiaries
Cash and cash equivalents	$ 2,614	$ 2,471	$ 1,296	$ 611	$ 2,314	$ 55	$ 4,530	$ —	$ 47,991
Restricted cash	2,505	2,500	—	3,449	3	76	21	—	49,232
Total cash	5,119	4,971	1,296	4,060	2,317	131	4,551	—	97,223
Receivables:									
Trade	1,963	2,415	25	4,067	983	8,404	3,731	—	74,650
Allowance for doubtful accounts	(633)	(585)	(2)	(2,490)	(399)	(5,167)	(2,688)	—	(28,779)
Notes, advances, and other receivables	—	—	—	(13)	5	44	42	—	4,093
Deferred income taxes	56	15	—	362	24	496	363	—	2,895
Other current assets	152	119	—	99	38	109	81	—	2,997
Total current assets	6,657	6,935	1,319	6,085	2,968	4,017	6,080	—	153,079
Property and equipment, net	3,293	3,718	859	983	22	1,701	496	—	38,598
Investment in subsidiaries	—	—	—	—	—	—	—	(58,128)	—
Deferred income taxes	—	—	5	—	—	417	—	(777)	—
Other long-term assets	352	161	—	213	73	1,180	537	—	7,548
Intangible assets, net of amortization	—	—	—	—	—	—	—	—	2,355
Goodwill	—	—	—	—	—	—	—	—	44,295
Total assets	$ 10,302	$ 10,814	$ 2,183	$ 7,281	$ 3,063	$ 7,315	$ 7,113	$ (58,905)	$ 245,875
Current liabilities:									
Accounts payable	$ 147	$ 138	$ 9	$ 67	$ 30	$ 157	$ 54	$ —	$ 4,074
Accrued liabilities	166	239	7	276	85	320	317	—	7,470
Unearned tuition	1,730	1,782	19	439	159	270	331	—	49,794
Advance payments	128	67	—	431	101	133	126	—	23,907
Total current liabilities	2,171	2,226	35	1,213	375	880	828	—	85,245
Deferred income taxes	1	990	—	686	577	—	1,057	(777)	19,426
Deferred rent	2,346	2,437	220	3,620	563	793	2,212	—	31,072
Member's equity:									
Net investment of EDMC	14,552	11,472	2,193	(38,175)	3,670	(7,820)	8,131	(3,658)	(5,525)
Accumulated earnings (deficit)	(8,768)	(6,311)	(265)	39,937	(2,122)	13,462	(5,115)	(54,470)	115,657
Total member's equity	5,784	5,161	1,928	1,762	1,548	5,642	3,016	(58,128)	110,132
Total liabilities and member's equity	$ 10,302	$ 10,814	$ 2,183	$ 7,281	$ 3,063	$ 7,315	$ 7,113	$ (58,905)	$ 245,875

South University, LLC and Subsidiaries

Consolidating Statement of Operations

(Dollars in thousands)

For the Fiscal Year Ended June 30, 2016

	South University-Savannah	South University-Tampa	South University-West Palm Beach	South University-Montgomery	South University-Richmond	South University-Columbia	South University Virginia Beach	South University-Novi	South University - Austin	South University - Cleveland	South University - Highpoint	South University - Orlando	The Art Institute of Dallas	The Art Institute of Fort Worth	The Art Institute of Charlotte	The Art Institute of Raleigh - Durham	Reclass-ifications & Eliminations	South University, LLC and Subsidiaries
Net revenues	$ 158,870	$ 21,132	$ 22,845	$ 11,317	$ 14,283	$ 30,422	$ 13,877	$ 12,608	$ 7,122	$ 8,655	$ 8,580	$ 873	$ 17,909	$ 2,978	$ 16,465	$ 11,117	$ —	$ 359,053
Costs and expenses:																		
Educational services	66,418	10,550	11,807	6,728	9,391	16,066	8,120	7,910	5,689	6,574	6,539	462	13,213	2,894	13,557	7,831	—	193,749
General and administrative	71,355	6,005	6,135	3,745	3,745	7,395	4,693	4,015	3,056	3,227	2,837	783	6,108	56	4,254	2,914	—	130,323
Long-lived asset impairments	—	—	—	—	—	—	—	—	—	—	—	—	—	31	1,314	—	—	1,345
Depreciation and amortization	3,556	506	1,102	419	904	916	598	572	513	588	565	178	215	6	257	101	—	10,996
Total costs and expenses	141,329	17,061	19,044	10,892	14,040	24,377	13,411	12,497	9,258	10,389	9,941	1,423	19,536	2,987	19,382	10,846	—	336,413
Earnings in investment in subsidiaries	3,531	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(3,531)	—
Income (loss) before income taxes	21,072	4,071	3,801	425	243	6,045	466	111	(2,136)	(1,734)	(1,361)	(550)	(1,627)	(9)	(2,917)	271	(3,531)	22,640
Income tax expense (benefit)	10,761	1,866	1,219	1,362	(16)	2,306	(179)	(28)	(1,313)	(385)	(567)	(135)	(1,112)	(295)	(624)	(531)	—	12,329
Net income (loss)	$ 10,311	$ 2,205	$ 2,582	$ (937)	$ 259	$ 3,739	$ 645	$ 139	$ (823)	$ (1,349)	$ (794)	$ (415)	$ (515)	$ 286	$ (2,293)	$ 802	$ (3,531)	$ 10,311
University "90/10" Ratio																		
Numerator																		$ 276,660
Denominator																		$ 349,728
Rate																		79.1%
Composite Score	2.8	1.3	2.4	1.5	1.9	1.8	1.6	1.8	1.8	1.8	1.8	1.8	1.8	2.4	1.7	2.4	—	1.7

South University, LLC and Subsidiaries

Consolidating Statement of Operations

(Dollars in thousands)

For the Fiscal Year Ended June 30, 2015

	South University-Savannah	South University-Tampa	South University-West Palm Beach	South University-Montgomery	South University-Richmond	South University-Columbia	South University-Virginia Beach	South University-Novi	South University-Austin	South University-Cleveland	South University-High Point	South University - Orlando	The Art Institute of Dallas	The Art Institute of Fort Worth	The Art Institute of Charlotte	The Art Institute of Raleigh - Durham	Reclass-ifications & Eliminations	South University, LLC and Subsidiaries
Net revenues	$ 161,383	$ 20,469	$ 22,186	$ 11,503	$ 14,741	$ 31,776	$ 16,265	$ 12,381	$ 5,223	$ 7,450	$ 7,328	$ 29	$ 23,721	$ 6,462	$ 23,669	$ 13,552	$ —	$ 378,138
Costs and expenses:																		
Educational services	67,229	10,448	11,188	6,874	9,035	16,113	8,649	7,334	5,640	5,844	5,390	183	15,153	3,648	18,308	10,721	—	201,757
General and administrative	72,525	6,308	5,989	3,657	4,119	7,546	5,070	4,226	3,021	3,333	2,723	182	6,293	2,289	4,789	3,363	—	135,433
Long-lived asset impairments	—	—	—	—	—	—	—	—	—	—	—	—	4,266	997	607	4,237	—	10,107
Depreciation and amortization	4,238	508	1,152	495	958	1,521	594	631	417	598	541	54	1,140	281	570	964	—	14,662
Total costs and expenses	143,992	17,264	18,329	11,026	14,112	25,180	14,313	12,191	9,078	9,775	8,654	419	26,852	7,215	24,274	19,285	—	361,959
Earnings in investment in subsidiaries	(15,142)	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	15,142	—
Income (loss) before income taxes	2,249	3,205	3,857	477	629	6,596	1,952	190	(3,855)	(2,325)	(1,326)	(390)	(3,131)	(753)	(605)	(5,733)	15,142	16,179
Income tax expense (benefit)	6,116	908	2,943	553	1,544	3,863	877	380	(339)	(592)	925	(125)	1,635	897	(349)	810	—	20,046
Net (loss) income	$ (3,867)	$ 2,297	$ 914	$ (76)	$ (915)	$ 2,733	$ 1,075	$ (190)	$ (3,516)	$ (1,733)	$ (2,251)	$ (265)	$ (4,766)	$ (1,650)	$ (256)	$ (6,543)	$ 15,142	$ (3,867)
University "90/10" Ratio																		
Numerator																		$ 303,868
Denominator																		$ 380,603
Rate																		79.8%
Composite Score	2.5	2.5	1.3	2.7	1.8	1.4	2.3	2.3	1.7	1.8	1.7	1.8	0.4	1.8	2.1	1.5		1.9

South University, LLC and Subsidiaries

Supplemental Schedule of Expenditures of State Financial Assistance

For the Fiscal Year Ended June 30, 2016

	CSFA No.	Grant No.	Expenditures	Transfers to Subrecipients
FLORIDA DEPARTMENT OF EDUCATION				
Direct Projects:				
Florida Student Assistance Grant	48.054	N/A	$ 263,500	$ —
Florida Access to Better Learning and Education Grant		N/A	849,000	—
Florida Children and Spouses of Deceased or Disabled Veterans and Service Members Scholarship	48.055	N/A	3,290	—
Florida Bright Futures Scholarship	48.059	N/A	35,088	—
TOTAL DIRECT PROJECTS			$ 1,150,878	$ —
Indirect Projects:			$ —	$ —
Passed Through:			$ —	$ —
TOTAL FLORIDA DEPARTMENT OF EDUCATION			$ 1,150,878	$ —
TOTAL EXPENDITURES OF STATE FINANCIAL ASSISTANCE			$ 1,150,878	$ —

NOTE TO SCHEDULE OF EXPENDITURES OF STATE FINANCIAL ASSISTANCE

BASIS OF PRESENTATION

The information in this schedule is prepared on the accrual basis of accounting and is presented in accordance with Chapter 69I-5, Rules of the Florida Department of Financial Services, Florida Administrative Code, *Schedule of Expenditures of State Financial Assistance.*

South University, LLC and Subsidiaries

Supplemental Schedule of Expenditures of State Financial Assistance

For the Fiscal Year Ended June 30, 2015

	CSFA No.	Grant No.	Expenditures	Transfers to Subrecipients
FLORIDA DEPARTMENT OF EDUCATION				
Direct Projects:				
Florida Student Assistance Grant	48.054	N/A	$ 286,250	$ —
Florida Access to Better Learning and Education Grant	—	N/A	785,500	—
Florida Children and Spouses of Deceased or Disabled Veterans and Service Members Scholarship	48.055	N/A	6,536	—
Florida Bright Futures Scholarship	48.059	N/A	53,973	—
TOTAL DIRECT PROJECTS			$ 1,132,259	$ —
Indirect Projects:			$ —	$ —
Passed Through:			$ —	$ —
TOTAL FLORIDA DEPARTMENT OF EDUCATION			$ 1,132,259	$ —
TOTAL EXPENDITURES OF STATE FINANCIAL ASSISTANCE			$ 1,132,259	$ —

NOTE TO SCHEDULE OF EXPENDITURES OF STATE FINANCIAL ASSISTANCE

BASIS OF PRESENTATION

The information in this schedule is prepared on the accrual basis of accounting and is presented in accordance with Chapter 69I-5, Rules of the Florida Department of Financial Services, Florida Administrative Code, *Schedule of Expenditures of State Financial Assistance.*

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Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

The Member and Board of Trustees of
South University, LLC and Subsidiaries

We have audited, in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of South University, LLC and Subsidiaries, which comprise the consolidated balance sheets as of June 30, 2016 and 2015, and the related consolidated statements of operations, member's equity and cash flows for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated September 28, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered South University, LLC and Subsidiaries' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of South University, LLC and Subsidiaries' internal control. Accordingly, we do not express an opinion on the effectiveness of South University, LLC and Subsidiaries' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control described in the accompanying Schedule of Findings and Responses that we consider to be a material weakness (2016-001).

Compliance and Other Matters

As part of obtaining reasonable assurance about whether South University, LLC and Subsidiaries' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

South University, LLC and Subsidiaries' to Findings

South University, LLC and Subsidiaries' response to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. South University, LLC and Subsidiaries' response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Ernst + Young LLP

Ernst & Young LLP
September 28, 2016

South University, LLC and Subsidiaries
Schedule of Findings and Responses
Year Ended June 30, 2016

2016-001

Criteria:	The South University, LLC and Subsidiaries' (the "University") financial statements are prepared in accordance with U.S. generally accepted accounting principles (GAAP).
Condition:	The University has not maintained effective controls to ensure the proper selection of its revenue recognition policy. Specifically, the process for analyzing the collectibility criterion for revenue recognition was not designed to assess collectibility, on a student-by-student basis, prior to enrollment in the University. This condition also existed at June 30, 2015, as previously reported. **This material weakness was remediated by June 30, 2016.**
Cause:	The University's lack of adequate internal controls over the selection of the revenue recognition policy did not appropriately address the assertion of collectability being reasonably assured on a student-by-student basis prior to enrollment.
Effect:	The lack of adequately designed controls over the proper selection of its revenue recognition policy could result in errors within the University's financial statements that could be material.
Recommendation:	We recommend that the University implement controls over the selection of the revenue recognition policy to appropriately assess collectibility, on a student-by-student basis, prior to enrollment in the University.
Views of responsible officials planned corrective actions:	In fiscal 2016, the School remediated a historical material weakness on internal controls surrounding in its revenue recognition policy by developing a suite of controls that operate together to mitigate the collectability risk associated with day one revenue recognition. **The controls were implemented and fully operational at June 30, 2016, remediating the material weakness.**