WHITNEY INFORMATION NETWORK INC
Form 10-Q
January 15, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2007

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

For the transition period from to

Commission file number: 0-27403

WHITNEY INFORMATION NETWORK, INC.

(Exact name of registrant as specified in its charter)

Colorado	**84-1475486**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1612 East Cape Coral Parkway, Cape Coral, Florida	**33904**
(Address of principal executive offices)	(Zip Code)

(239) 542-0643

(Registrant s telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

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

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date:

There were 11,738,587 shares of common stock outstanding as of December 15, 2008.

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PART I. FINANCIAL INFORMATION

Explanatory Note

In this Quarterly Report on Form 10-Q for the three and six months ended June 30, 2007 (Quarterly Report), Whitney Information Network, Inc. (Company, we, us or our) has restated its Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) and Condensed Consolidated Statement of Cash Flows for the three and six month period ended June 30, 2006 for the effects of a restatement of our financial statements for the years ended December 31, 2006, 2005, 2004, 2003 and 2002. This restatement was filed in our Annual Report on Form 10-K/A for the year ended December 31, 2006 (2006 Annual Report on Form 10-K/A), which was filed with the Securities and Exchange Commission (SEC) on January 15, 2009. The restatement corrected errors relating to: (i) disclosures of related party transactions; (ii) the method and disclosure of certain acquisitions; and (iii) depreciable lives of intangible assets and property and equipment. The restatement also includes certain other corrections and conforming changes and had minimal effect on the Company s cash flows, liquidity or our financial position for the respective restated periods. See Part I, Item I - Financial Statements and Note 4 -*Restatement of the Consolidated Financial Statements* in the Notes to the Condensed Consolidated Financial Statements.

Background

On November 14, 2006, the Company was notified that the SEC was conducting a formal investigation to determine whether the Company complied with securities laws in connection with (i) the claimed efficacy or trading success of its stock market educational programs and (ii) its acquisition of certain other companies. On December 11, 2006, the Company received a subpoena requesting documents in connection with the commencement of a grand jury investigation by the United States Attorney s Office for the Eastern District of Virginia (DOJ). This investigation is related to the Company s marketing activities from January 1, 2002 to the present.

In December 2006, our Board of Directors established a Special Committee of independent directors to conduct an internal investigation of the activities that are the subject of the government investigations, and the Special Committee engaged the law firm of Wilmer Cutler Pickering Hale and Dorr LLP (Wilmer Hale) to assist with this investigation. The Special Committee reported its findings and made recommendations to the Board of Directors, as reported in the Company s Current Report on Form 8-K filed with the SEC on November 9, 2007, and such recommendations have either been implemented or are being implemented as discussed herein.

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ITEM 1 FINANCIAL STATEMENTS

WHITNEY INFORMATION NETWORK, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited, in thousands, except share data)

	June 30, 2007	December 31, 2006 (restated)
Assets		
Current assets:		
Cash and cash equivalents	$ 28,090	$ 33,221
Restricted cash	11,936	7,525
Accounts receivable, net	463	3,373
Notes receivable, current portion	3,123	84
Deferred course expenses, current portion	16,100	14,559
Prepaid advertising and other prepaid expenses	2,228	2,519
Inventory	1,371	1,061
Assets held for sale		4,719
Total current assets	63,311	67,061
Notes receivable, net of current portion	7,042	7,087
Property and equipment, net	12,037	11,745
Investment and development costs in real estate	2,098	5,061
Intangible assets, net	464	496
Deferred course expenses, net of current portion	6	171
Other assets	223	66
Total assets	$ 85,181	$ 91,687
Liabilities and Stockholders Deficit		
Current liabilities:		
Accounts payable	$ 11,779	$ 6,936
Income taxes payable	494	545
Accrued course expenses	2,324	1,250
Accrued salaries, wages and benefits	3,932	3,965
Other accrued expenses	6,329	5,820
Long-term debt, current portion	190	3,139
Deferred rental incentives, current portion	105	71
Deferred revenue, current portion	115,722	114,922
Total current liabilities	140,875	136,648
Long-term debt, net of current portion	2,968	3,015
Deferred rental incentives, net of current portion	419	394
Deferred revenue, net of current portion	49	486
Total liabilities	144,311	140,543
Commitments and contingencies		
Stockholders deficit:		
Preferred stock, no par value, 10,000,000 shares authorized, no shares issued and outstanding		

Common stock, no par value, 25,000,000 shares authorized, 11,738,587 shares issued and outstanding, as of June 30, 2007 and December 31, 2006		2,591		2,591
Paid-in capital		1,624		1,089
Foreign currency translation adjustment		(1,473)		(1,160)
Accumulated deficit		(61,872)		(51,376)
Total stockholders deficit		(59,130)		(48,856)
Total liabilities and stockholders deficit	$	85,181	$	91,687

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

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WHITNEY INFORMATION NETWORK, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)
(Unaudited, in thousands, except per share data)

	Three months ended June 30, 2007	Three months ended June 30, 2006 (restated)	Six months ended June 30, 2007	Six months ended June 30, 2006 (restated)
Revenue	$ 46,937	$ 48,013	$ 103,198	$ 92,902
Operating costs and expenses:				
Direct course expenses	28,510	27,502	53,939	53,957
Advertising and sales expenses	17,821	16,661	34,245	30,863
General and administrative expenses	9,276	8,362	19,292	16,622
Special items	3,503	189	6,789	459
Total operating costs and expenses	59,110	52,714	114,265	101,901
Loss from operations	(12,173)	(4,701)	(11,067)	(8,999)
Other income (expense):				
Other income (expense), net	117	(100)	201	(321)
Interest income	445	572	885	980
Interest expense	(70)	(136)	(172)	(218)
Equity (loss) income from related parties	(154)	(8)	(331)	22
Gain on sale of assets	43		37	
Total other income	381	328	620	463
Loss before income taxes	(11,792)	(4,373)	(10,447)	(8,536)
Income tax (benefit) provision	12	(39)	(49)	(39)
Net loss	$ (11,780)	$ (4,412)	$ (10,496)	$ (8,575)
Net loss per share:				
Basic	$ (1.00)	$ (0.40)	$ (0.89)	$ (0.79)
Diluted	$ (1.00)	$ (0.40)	$ (0.89)	$ (0.79)
Weighted average common shares outstanding:				
Basic	11,739	10,924	11,739	10,852
Diluted	11,739	10,924	11,739	10,852
Comprehensive loss:				
Net loss	$ (11,780)	$ (4,412)	$ (10,496)	$ (8,575)
Foreign currency translation adjustments	(296)	(99)	(313)	258
Comprehensive loss	$ (12,076)	$ (4,511)	$ (10,809)	$ (8,317)

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

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WHITNEY INFORMATION NETWORK, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Unaudited, in thousands)

	Six months ended June 30,	
	2007	2006 (restated)
Cash flows from operating activities:		
Net loss	$ (10,496)	$ (8,575)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	797	634
Stock-based compensation costs	535	497
Stock gift		937
Deferred rental incentive	59	
Gain on sale of assets	(37)	
Minority interest and equity loss (income) from related parties	331	(22)
Changes in operating assets and liabilities:		
Restricted cash	(4,411)	(882)
Accounts receivable, net	2,910	(2,397)
Prepaid advertising and other prepaid expenses	291	(375)
Inventory	(310)	70
Deferred course expenses	(1,376)	(2,118)
Other assets	(157)	17
Accounts payable	4,843	1,579
Accrued course expenses	1,074	(265)
Deferred revenue	363	24,516
Accrued salaries, wages and benefits	(33)	2,201
Other accrued expenses	506	(1,817)
Income taxes payable	(51)	(221)
Net cash (used in) provided by operations	(5,162)	13,779
Cash flows from investing activities:		
Purchase of property and equipment	(1,170)	(878)
Proceeds received on notes receivable	36	1,740
Advances on notes receivables	(270)	
Proceeds from sale of assets	5,039	
Investments in and advances to related parties, net	(125)	(59)
Distributions to minority interest		(44)
Net cash provided by investing activities	3,510	759
Cash flows from financing activities:		
Payments to stockholders from sale of common stock		(5,110)
Proceeds from the issuance of long-term debt	56	
Principal payments on long-term debt	(3,222)	(79)
Proceeds from the exercise of stock options and warrants		1,010
Stock offering and registration costs		(627)
Net cash used in financing activities	(3,166)	(4,806)
Effect of foreign currency translation	(313)	258
Net (decrease) increase in cash and cash equivalents	(5,131)	9,990
Cash and cash equivalents, at beginning of period	33,221	32,883
Cash and cash equivalents, at end of period	$ 28,090	$ 42,873
Supplemental Cash Flow Information of non-cash activities:		

Promissory note received from the sale of our 50% in Tranquility Bay of South West Florida, LLC, net of reserve of $1,438	$	3,030	$	
Long-term debt added for our acquisition of the 50% interest in SCB Building, LLC	$		$	3,600

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

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WHITNEY INFORMATION NETWORK, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 - Basis of Presentation

The interim Condensed Consolidated Financial Statements include the accounts of Whitney Information Network, Inc. and its wholly-owned subsidiaries (collectively referred to herein as the Company, we, us, or our). These unaudited Condensed Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and, in the opinion of management, contain all adjustments, consisting only of normal, recurring adjustments, necessary to fairly present the financial condition, results of operations and cash flows for the periods presented.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to those rules and regulations. The information in this interim report should be read in conjunction with our audited Consolidated Financial Statements and the Notes thereto included in the Company s Annual Report on Form 10-K/A filed with the SEC on January 15, 2009 (2006 Annual Report on Form 10-K/A).

In the opinion of management, all adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation have been included. The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect the reported amount of assets and liabilities and the disclosure of contingent liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period.

The results for the three and six months ended June 30, 2007 are not necessarily indicative of the results expected for the year ending December 31, 2007.

Reclassifications

Certain reclassifications have been made in our 2006 Condensed Consolidated Financial Statements as necessary for comparability with our 2007 presentation.

Note 2 Summary of Significant Accounting Policies

Please refer to the Company s 2006 Annual Report on Form 10-K/A for the year ended December 31, 2006, filed with the SEC on January 15, 2009, for additional discussion of the Company s significant accounting policies.

Principles of consolidation

The accompanying Condensed Consolidated Financial Statements have been prepared in accordance with GAAP and include the accounts and balances of the Company and its subsidiaries. All significant intercompany balances and transactions have been eliminated.

Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect the reported amount of assets and liabilities and the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The more significant estimates the Company makes include, but are not limited to, course breakage, deferred income tax assets, realizability of long-lived assets and provisions for litigation-related matters. Actual results could differ from these estimates.

Financial instruments

Financial instruments consist primarily of cash and cash equivalents, short-term investments, receivables, deferred seminar expense, accounts payable, accrued expenses, deferred educational revenues, and notes payable. Statements of Financial

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Accounting Standards (SFAS) No. 107, *Disclosure about Fair Value of Financial Instruments* (SFAS No. 107), requires the disclosure of the fair value of financial instruments, including assets and liabilities recognized on the balance sheets. Management estimates the aggregate fair value of the other financial instruments recognized at the balance sheet date (including receivables, payables and accrued liabilities) approximates their fair value; as such financial instruments are short-term in nature, bear interest at current market rates or are subject to frequent repricing if applicable.

Cash and cash equivalents

The Company classifies all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. The Company continually monitors and evaluates our investment positions and the creditworthiness of the financial institutions with which the Company invests and maintains deposit accounts. Our joint venture agreement with Rich Global, LLC requires us to segregate our cash balances between (i) funds received from RDE students; and (ii) funds received from the sale of our Proprietary Brands. The Company is restricted from using cash generated from the RDE Brand to pay for expenses incurred by our Proprietary Brands, except in the payment of license and management fees owed to us in accordance with our agreement with Rich Global, LLC as reimbursement for the fulfillment of advanced courses purchased by RDE students and partner distributions paid when cash balances exceed the cost to fulfill outstanding student contracts.

The amounts included in the Condensed Consolidated Financial Statements are stated at cost which approximates fair value at the balance sheet date. The Company maintains deposits in banks which may exceed the federal deposit insurance available. Management believes the potential risk of loss on these accounts to be minimal.

Restricted cash

The Company uses merchant service providers to process credit card transactions. Under the terms of these agreements, the merchant has the right to withhold credit card funds to cover chargebacks in the event the Company is unable to honor its commitments. Additionally, the Company is required to maintain letters of credit in certain states in which it operates its business. At June 30, 2007 and December 31, 2006, the Company had $1.1 million and $1.6 million, respectively, in letters of credit outstanding with various states and agencies. The Company considers restricted cash as a current asset in the Condensed Consolidated Balance Sheets as merchant service providers typically hold such reserve funds for one year. As of June 30, 2007, and December 31, 2006, the Company had restricted cash balances of $11.9 million and $7.5 million, respectively.

Receivables from clearing brokers

Receivables from clearing brokers consist of cash deposits and receivables from revenue earned, net of expenses incurred, from customer transactions conducted through the clearing brokers.

Inventory

Inventory consists primarily of books, videos and training materials held for sale to students enrolled in our educational programs. Inventories are stated at the lower of cost using the first-in, first-out method or market.

Property and equipment, net

Property and equipment is stated at cost net of accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets as presented in the following table:

Buildings	40 years
Furniture fixtures and equipment	7 years
Other assets	5 years
Purchased software	3 years

Upon the sale or retirement of assets, the costs accumulated depreciation are removed from the accounts and any gain or loss is recognized. Maintenance and repairs are charged to expense when incurred.

Depreciation expense was approximately $0.4 million and $0.2 million for the three months ended June 30, 2007 and 2006, respectively, and $0.8 million and $0.5 million for the six months ended June 30, 2007 and 2006, respectively.

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Intangible assets and goodwill

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long Lived Assets* (SFAS No. 144), the Company evaluates the carrying amount of our long-lived assets such as property and equipment, and definite-lived intangible assets subject to amortization for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets held and used is measured by the comparison of the carrying amount with the future net cash flows the assets are expected to generate. The Company looks primarily to the undiscounted future cash flows in the assessment of whether or not long-lived assets have been impaired. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the estimated fair value of the assets.

Intangible assets include customer lists and trademarks which are recorded at cost. Customer lists and trademarks are amortized over their estimated useful lives of three and fifteen years, respectively. The Company performs impairment tests for our intangible assets annually. At December 31, 2006, based on our evaluations the Company recorded an impairment expense of $3.6 million.

Advertising and sales expense and prepaid advertising

The Company expenses advertising and sales costs as incurred. Advertising and sales expenses reported on the Condensed Consolidated Statements of Operations were $17.8 million and $16.7 million for the quarters ended June 30, 2007 and 2006, respectively, and $34.2 million and $30.9 million for the six months ended June 30, 2007 and 2006, respectively. The Company expenses advertising costs, training room rentals and direct sales expenses as incurred. Advertising paid in advance is recorded as prepaid until such time as the advertisement is published.

Deferred course expenses

The Company defers commissions and fees paid to our speakers until the corresponding revenue is earned. Our speakers, who are typically independent contractors, earn commissions on the cash receipts received at our educational events and are paid approximately 45 days after the educational event. The deferred course expenses are tracked individually by student and are recognized in the Condensed Consolidated Statements of Operations as the student attends the course, at which time, the associated revenues and expenses are recognized.

Income taxes

The Company adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN No. 48), *Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109*, on January 1, 2007. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in a company s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*, and prescribes a recognition threshold of more likely than not and a measurement process for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In making this assessment, a company must determine whether it is more likely than not that a tax position will be sustained upon examination, based solely on the technical merits of the position and must assume that the tax

position will be examined by taxing authorities. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transition. The Company recognizes interest and penalties accrued related to unrecognized tax benefits as components of its income tax provision. The Company did not have any interest and penalties accrued upon the adoption of FIN No. 48, and as of June 30, 2007, the Company does not have any interest and penalties accrued related to unrecognized tax benefits.

As of January 1, 2007, and June 30, 2007, the Company believes that no reserves for uncertain income tax positions need to be recorded pursuant to FIN No. 48. As a result, there was no cumulative effect adjustment related to adoption. The adoption of FIN No. 48 did not have an impact on the Company s Condensed Consolidated Financial Statements.

The provision for income taxes is based on the consolidated United States entities and the individual foreign companies estimated tax rates for the applicable year. Our income tax provision has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred income taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The income tax provision represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred income taxes result from differences between the financial and the tax basis of our assets and liabilities and are measured using the enacted tax rates and

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laws that will be in effect when the differences are expected to reverse. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. See Note 8 - *Income Taxes.*

Foreign currency translation

The Company accounts for foreign currency translation in accordance with SFAS No. 52, *Foreign Currency Translation* (SFAS No. 52). The functional currencies of the Company s foreign operations are the reported local currencies. Translation adjustments result from translating our foreign subsidiaries financial statements into United States dollars. The balance sheet accounts of our foreign subsidiaries are translated into United States dollars using the exchange rate in effect at the balance sheet date. Revenues and expenses are translated into United States dollars using average exchange rates during the period. The resulting translation gains or losses are recorded as a component of accumulated other comprehensive loss in stockholders deficit. Realized gains and losses resulting from foreign exchange transactions are included in total operating costs and expenses in the unaudited Condensed Consolidated Statements of Operations. During the three months ended June 30, 2007 and 2006, foreign currency transaction (gains)/losses totaled approximately $(30,000) and $11,000, respectively. Foreign currency transaction (gains)/losses totaled approximately $(24,000) and $375,000 during the six months ended June 30, 2007 and 2006, respectively, and are reported on our Condensed Consolidated Statements of Operations as a component of other income (expense), net.

Income (loss) per share

Basic and diluted income (loss) per share are calculated in accordance with SFAS No. 128*, Earnings Per Share*. During the second quarter of 2007 and 2006, the Company issued zero and 147,500 shares, respectively, of Common Stock on the exercise of stock options. During the six months ended June 30, 2007 and 2006, the Company issued zero and 471,450 shares, respectively, of Common Stock on the exercise of stock options. In the second quarter of 2007, potentially dilutive securities were comprised of stock options and warrants to purchase 150,204 shares of Common Stock that were not included in the calculation of diluted loss per share as their impact would be anti-dilutive. For the six months ended June 30, 2007, potentially dilutive securities were comprised of stock options and warrants to purchase 144,436 shares of Common Stock that were not included in the calculation of diluted loss per share as their impact would be anti-dilutive.

Revenue recognition

Revenue is recognized in accordance with Staff Accounting Bulletin No. 104, *Revenue Recognition* (SAB No. 104) and Emerging Issues Task Force No. 00-21, *Revenue Arrangements with Multiple Deliverables* (EITF No. 00-21). The Company recognizes revenue when: (i) persuasive evidence of an arrangement exists, (ii) delivery of product has occurred or services have been rendered, (iii) the price to the buyer is fixed or determinable, and (iv) collectibility is reasonable assured. For product sales, these conditions are generally met upon shipment of the product to the customer or completion of the sale transaction. For training and service sales, these conditions are generally met upon presentation of the training seminar or delivery of the service.

Some of our training and consulting contracts contain multiple deliverable elements that include training along with other products and services. In accordance with EITF No. 00-21, sales arrangements with multiple deliverables are divided into separate units of accounting if the deliverables in the sales contract meet the following criteria: (i) the delivered training or product has value to the client on a standalone basis; (ii) there is objective and reliable evidence of the fair value of undelivered items; and (iii) delivery of any undelivered item is probable. The fair

value of each element is generally determined by prices charged when sold separately. In certain arrangements, the Company offers these products bundled together at a discount. The discount is allocated on a pro-rata basis to each element based on the relative fair value of each element when fair value support exists for each element in the arrangement. The overall contract consideration is allocated among the separate units of accounting based upon their fair values, with the amount allocated to the delivered item being limited to the amount that is not contingent upon the delivery of additional items or meeting other specified performance conditions. If the fair value of all undelivered elements exists, but fair value does not exist for one or more delivered elements, the residual method is used. Under the residual method, the amount of consideration allocated to the delivered items equals the total consideration less the aggregate fair value of the undelivered items. Fair value of the undelivered items is based upon the normal pricing practice for the Company s existing training programs, consulting services, and other products, which are generally the prices of the items when sold separately.

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Each transaction is separated into its specific elements and revenue for each element is recognized according to the following policies:

Product	Recognition Policy
Seminars (camps)	Deferred and recognized as the seminar or camp is provided
Home study (DVDs)	Recognized upon delivery to customer
Online courses	Deferred and recognized as service is delivered
Coaching and mentoring sessions	Deferred and recognized as service is provided
Data subscriptions and renewals	Deferred and recognized on a straight-line basis over the subscription period

In the normal course of business, the Company recognizes revenue based on the students attendance of the course, event, mentoring training, coaching session or delivery of the software, data or course materials.

When the likelihood of attendance by the student is remote, course breakage is calculated on the historical percentage of (i) students who never attended a course; (ii) those students who never attended a course subsequent to expiration; and (iii) the highest number of days in which 95% of students who attended our courses did so subsequent to expiration.

The Company determines our course breakage rate based upon estimates developed from historical student attendance patterns. Typically, the Company uses a three year period to estimate student attendance patterns. Based on the historical information, the Company is able to determine the likelihood of an expired course remaining unattended. The Company has determined that the Company does not have a legal obligation to remit the value of expired courses to the relevant taxing jurisdictions.

To the extent new lines of business do not have adequate historical data subsequent to course expiration, the Company recognizes revenue based upon course attendance. Only at such time that the Company has developed verifiable and objective data from our historical data subsequent to course expiration will the Company apply course breakage based on the methodology described above.

Deferred revenue occurs from seminars, online courses, coaching sessions and website subscriptions and renewals when payment is received before the service has been performed. Deferred revenue is recognized into revenue over the period that the services are performed.

Stock based compensation

Effective January 1, 2006, we adopted SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123R), which requires us to measure the cost of employee services received in exchange for all equity awards granted including stock options based on the fair market value of the award as of the grant date. SFAS No. 123R supersedes SFAS No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123) and Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB No. 25). We adopted SFAS No. 123R using the modified prospective application method of adoption which requires us to record compensation cost related to unvested stock awards as of December 31, 2005, by recognizing the unamortized grant date fair value of these awards over the remaining service periods of those awards with no change in historical reported earnings. Awards granted after December 31, 2005, are valued at fair value in accordance with the provisions of SFAS No. 123R and recognized on the same basis as the vesting period. We estimated forfeiture rates for June 30, 2007 and 2006, based on historical

experience.

For each of the three months ended June 30, 2007 and 2006, the Company recorded approximately $0.2 million of share-based compensation expense. The Company recorded approximately $0.5 million for each of the six months ended June 30, 2007 and 2006. The Company considers all of its share-based compensation expense as a component of general and administrative expenses. The impact of adoption of SFAS No. 123R is that future share-based payment awards will be recorded as compensation expense over their requisite service period, and such expense is not expected to be material to future earnings.

Comprehensive loss

Comprehensive loss includes changes to equity accounts that were not the result of transactions with shareholders. Comprehensive loss is comprised of net income or loss and other comprehensive income and loss items. Our comprehensive

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loss consists of changes in the cumulative foreign currency translation adjustment. Our comprehensive losses for the three months ended June 30, 2007 and 2006 were $12.1 million and $4.5 million, respectively. For the six months ended June 30, 2007 and 2006, the Company s comprehensive losses were $10.8 million and $8.3 million, respectively.

Note 3 - Recently Issued Accounting Standards

In February 2007, the FASB issued SFAS No.159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159). SFAS No. 159 provides companies with an option to report selected financial assets and liabilities at fair value. SFAS No.159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities and to provide additional information that will help investors and other financial statement users to more easily understand the effect of a company s choice to use fair value on its earnings. Additionally, SFAS No.159 requires entities to display the fair value of those assets and liabilities for which a company has chosen to use fair value on the face of the balance sheet. SFAS No. 159 is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. SFAS No. 159 is not expected to have any material impact on the Company s financial position, results of operations, or cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157), which establishes a framework for measuring the fair value of assets and liabilities in accordance with GAAP and expands disclosures about fair value measurements. The FASB has issued a proposed interpretation that would defer the implementation of SFAS No. 157 for non-financial assets and liabilities until fiscal years beginning after November 15, 2008. The remaining provisions of SFAS No. 157 are effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. SFAS No. 157 is not expected to have any material impact on the Company s financial position, results of operations or cash flows.

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Note 4 - Restatement of the Consolidated Financial Statements

As reflected in our previously filed Form 10-K/A on January 15, 2009, our Consolidated Financial Statements and other financial information were restated for the years ended December 31, 2006, 2005, 2004, 2003, and 2002 and for each of the quarters in the periods ended 2006 and 2005. That restatement had minimal effect on our results of operations, cash flows and financial position for the respective restated periods. Certain of our material internal control weaknesses resulted in inaccurate financial reporting and restatements to our previously filed Consolidated Financial Statements from 2001 through 2006. The restated Consolidated Financial Statements reflect the following:

In December 2006, the Company s Board of Directors established a Special Committee of independent directors to conduct an internal investigation of the activities that are the subject of the government investigations and the Special Committee engaged the law firm of Wilmer Cutler Pickering Hale and Dorr LLP (WilmerHale) to assist with these investigations. The matters under investigation included (i) the claimed efficacy of the Company s stock market education programs, and (ii) the Company s acquisitions of certain other companies. Members of our management, including Mr. Whitney, were interviewed by WilmerHale, consistent with the Company s continued cooperation with the investigations by the SEC and Department of Justice (DOJ). The Special Committee reported its findings and made recommendations to the Board of Directors, as previously disclosed in the Form 10-K/A for the year ended December 31, 2006 and on the Company s Current Report on Form 8-K, filed with the SEC on November 9, 2007 and such recommendations have either been implemented or are being implemented.

With respect to the Company s acquisitions of certain other companies, among other findings, based upon the WilmerHale investigation, the Special Committee reported to the Board of Directors in September 2007 and delivered its final recommendations in November 2007, and reported such recommendations to the SEC in November 2007. The Special Committee found that certain of the Company s prior disclosures were incorrect. Such disclosures were corrected in the Form 10-K/A filed for the fiscal year ended December 31, 2006. The certain prior disclosures that were incorrect are as follows:

The Company previously disclosed that: (1) in July 2003 the Company acquired Whitney Leadership Group, Inc. (Whitney Leadership) from Mr. Whitney, our former Chairman and Chief Executive Officer and Ingrid Whitney for $1.2 million; (2) at the time, Whitney Leadership held all of the copyright and intellectual property rights associated with its educational materials and licensed those rights to the Company for payments; and (3) the Company entered into the acquisition agreement in order to eliminate those payments and to gain control of intellectual property rights that form the core of the Company s business. The Special Committee found that the Company did not disclose a provision in a document denominated as an exhibit to the agreement that afforded Mr. Whitney the right to terminate the Company s rights to the use of his name and likeness under certain circumstances, including if Mr. Whitney were no longer employed with the Company or no longer owned a controlling voting interest in the Company. The Special Committee found that the version of the exhibit containing this provision was created in May 2004. Mr. Whitney indicated that he believed that the subsequently created exhibit memorialized a prior oral agreement. In any event, Mr. Whitney never exercised his right to terminate the Company s rights and at the request of the Special Committee, Mr. Whitney voided that provision effective January 7, 2008.

The Company previously disclosed that as a result of a series of transactions among Russell Whitney, Ingrid Whitney and John Kane (1) in July 2003 the Company purchased Equity Corp. Holdings, Inc. (Equity Corp.) from Mr. Kane; (2) as part of the transaction, the Company agreed to assume and pay a $4.75 million promissory note issued to Mr. Whitney and his wife by Equity Corp. in June 2002; and (3) Equity Corp. incurred this obligation when it elected to redeem all of Russell and Ingrid Whitney s ownership in Equity Corp., 90% of the outstanding stock, as of June 1, 2002. The Special Committee concluded that the redemption did not occur, and no note was issued by Equity Corp. to Russell and Ingrid Whitney in June 2002. The Special Committee found that the redemption of Russell and Ingrid Whitney s Equity Corp. shares and Equity Corp. s incurring of this $4.75 million obligation in fact closed on May 31, 2003. The Special Committee concluded that Equity Corp. s redemption of Russell and Ingrid Whitney s Equity Corp. shares was not separate from the Company s acquisition of Mr. Kane s Equity Corp. shares, which resulted in a change in the accounting method for the acquisition of Equity Corp. from the acquisition method of accounting for a

business combination to the combination of entities under common control, similar to a pooling of interests. As previously reported by the Company in its Current Report on Form 8-K dated November 3, 2007 and filed with the SEC on November 8, 2007, the Board of Directors has determined that, with respect to the acquisition of Equity Corp., the Company incorrectly applied the acquisition method of accounting for a business combination and instead should have accounted for the transaction as a combination of entities under common control, similar to a pooling of interests. The Company previously disclosed that Mr. Kane received $62,500 in cash, $62,500 in a note and 62,500 shares valued at $125,000 for the purchase of his interest in Equity Corp. However, the 62,500 shares were revalued at $312,500 using the average of the quoted market prices a few days before and after the acquisition.

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As previously reported by the Company in a Current Report on Form 8-K dated November 9, 2007, the Company did not obtain a fairness opinion regarding the acquisition price of Equity Corp. and Whitney Leadership, but did obtain a business valuation report. A committee of independent members of the Board of Directors is reviewing the Equity Corp. and Whitney Leadership transactions regarding compliance with applicable governance and related party requirements.

The Company previously disclosed that: (1) the Company purchased all of the outstanding common stock of Precision Software Services, Inc. (Precision) from Mr. Whitney and Mr. Kane, who subsequently became an executive officer of the Company, in exchange for an aggregate of approximately 333,000 shares of Common Stock valued at $500,000 and $250,000 in notes; and (2) Mr. Whitney received $125,000 in notes payable. The Special Committee concluded that the Company did not disclose that (1) the $250,000 in notes payable (of which Mr. Whitney and Mr. Kane each received $125,000) were not for the purchase of Precision, but rather the purchase of software that Mr. Whitney and Mr. Kane had licensed to Precision; and (2) the Company also paid $250,000 in cash (of which Mr. Whitney and Mr. Kane each received $125,000) for that software. In researching the accounting treatment of this transaction, the Company discovered an error in the depreciation of the related intangible asset, as well as an inadvertent impairment in 2006. The asset was incorrectly named in the general ledger and, as a result, included in the impairment expense associated with a discontinued brand.

In addition to the disclosures related to specific transactions, we reviewed our related party transactions. The additional disclosures concerning related party transactions in Costa Rica are included in Note 7 - *Certain Relationships and Related Transactions*.

In addition to the findings of the Special Committee and certain other conforming changes, we determined that the following errors required correction:

- Certain intangible assets and property and equipment were assigned incorrect depreciable lives
- Inventory related to Star Trader® had not been recorded as impaired at December 31, 2006
- Various accounts payable invoices were recorded in the incorrect period

On January 15, 2009, the Company filed Amendment No. 1 to its Annual Report on Form 10-K for the fiscal year ended December 31, 2006, to amend and restate the financial statements and other financial information for the years 2006, 2005 and 2004, and financial information for the years 2003 and 2002, and for each of the quarters in the years 2005 and 2006. The restatement had minimal effect on the Company s cash flows, liquidity or on our financial position for the respective restated periods.

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Effects of the Restatement

The following table reflects the effect of the restatement on the Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2006 (in thousands, except per share amounts):

	Three months ended June 30, 2006			Six months ended June 30, 2006		
	As previously reported	Effect of restatement	Restated	As previously reported	Effect of restatement	Restated
Revenue	$ 47,525	$ 488	$ 48,013	$ 92,414	$ 488	$ 92,902
Operating costs and expenses:						
Direct course expense	27,022	480	27,502	53,476	481	53,957
Advertising and sales expense	16,661		16,661	30,863		30,863
General and administrative expense	8,677	(315)	8,362	17,281	(659)	16,622
Special items		189	189		459	459
Total operating costs and expense	52,360	354	52,714	101,620	281	101,901
Loss from operations	(4,835)	134	(4,701)	(9,206)	207	(8,999)
Other income (expense), net	(100)		(100)	68	(389)	(321)
Interest income	572		572	980		980
Interest expense	(136)		(136)	(218)		(218)
Equity (loss) income from related parties	(8)		(8)	22		22
Total other income (expense)	328		328	852	(389)	463
Loss before taxes	(4,507)	134	(4,373)	(8,354)	(182)	(8,536)
Income tax expense	(39)		(39)	(39)		(39)
Net (loss) income	(4,546)	134	(4,412)	(8,393)	(182)	(8,575)
Foreign currency translation adjustment	(99)		(99)	(132)	390	258
Comprehensive loss	$ (4,645)	$ 134	$ (4,511)	$ (8,525)	$ 208	$ (8,317)
Net loss per share						
Basic	$ (0.42)	$ 0.02	$ (0.40)	$ (0.77)	$ (0.02)	$ (0.79)
Diluted	$ (0.42)	$ 0.02	$ (0.40)	$ (0.77)	$ (0.02)	$ (0.79)
Weighted average common shares outstanding						
Basic	10,924		10,924	10,852		10,852
Diluted	10,924		10,924	10,852		10,852

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The following table reflects the effect of the restatement on the Condensed Consolidated Statement of Cash Flows (in thousands):

	For the six months ended June 30, 2006		
	As previously reported	Effect of restatement	Restated
Cash flows from operating activities:			
Net loss	$ (8,393)	$ (182)	$ (8,575)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation and amortization	897	(263)	634
Stock-based compensation costs	497		497
Stock gift	937		937
Minority interest and equity (loss) from related parties		(22)	(22)
Changes in operating assets and liabilities:			
Restricted cash	(1,255)	373	(882)
Accounts receivable, net	(2,397)		(2,397)
Prepaid advertising and other prepaid expenses	(375)		(375)
Inventory	70		70
Deferred course expenses	(2,118)		(2,118)
Other assets	17		17
Accounts payable	1,687	(108)	1,579
Accrued course expenses	(265)		(265