SYLVAN LEARNING SYSTEMS INC
Form 8-K
June 09, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 8-K

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

Date of Report (Date of earliest event reported): **June 9, 2003**

Sylvan Learning Systems, Inc.

(Exact Name of Registrant as Specified in Charter)

Maryland	**0-22844**	**52-1492296**
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1001 Fleet Street, Baltimore, Maryland 21202
(Address of Principal Executive Offices) (ZIP Code)

Registrant s telephone number, including area code: **(410) 843-8000**

Item 5. Other Events

On March 10, 2003, the Company and Educate, Inc., a company newly formed by Apollo Management, L.P., (Apollo) executed an Asset Purchase Agreement that provides for the acquisition by Educate, Inc. of substantially all of the Company s K-12 education business units, including eSylvan, Inc. and Connections Academy, Inc., which are investments held by Sylvan Ventures (collectively, the K-12 Disposal Group). The consolidated financial statements of Sylvan Learning Systems, Inc. for each of the three years in the period ended December 31, 2002 have been restated to reflect the results of the K-12 Disposal Group as discontinued operations. Also included is a revised Management s Discussion and Analysis of Financial Condition and Results of Operations based on the restated results of operations as described above.

Item 7. Selected Consolidated Financial Data and Exhibits

The selected consolidated financial data for the years ended December 31, 2002, 2001, 2000, 1999, and 1998 have been derived from Sylvan s consolidated financial statements. The financial data should be read in conjunction with the consolidated financial statements and notes thereto.

The Company consummated several significant purchase business combinations in the five-year period ended December 31, 2002. These business combinations affect the comparability of the amounts presented. Additionally, the accompanying financial data has been restated to reflect the net assets of the disposal groups of the K-12 education business units, Aspect, Prometric and PACE as the respective assets and liabilities related to discontinued operations. The following data should be read in conjunction with Notes 3 and 5 to the consolidated financial statements.

Exhibits

Exhibit Number	**Description**
23.01	Consent of Ernst & Young LLP with respect to consolidated financial statements of Sylvan Learning Systems, Inc.
23.02	Consent of PricewaterhouseCoopers LLP with respect to consolidated financial statements of Chancery Software Ltd.
99.1	Certification of Douglas L. Becker pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.2	Certification of Sean R. Creamer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.3	Report of Independent Accountants of PricewaterhouseCoopers LLP with respect to the consolidated financial statements of Chancery Software Ltd.

SIGNATURES

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on June 9, 2003.

SYLVAN LEARNING SYSTEMS, INC.
(Registrant)

By: /s/ Sean R. Creamer
Name: Sean R. Creamer
Title: Senior Vice President and
Chief Financial Officer

	Year ended December 31,				
	2002(1) (2) (3) (4)	2001(5)	2000(6) (7)	1999(8) (9) (10)	1998(11)
	(in thousands, except per share amounts)				
Statements of Operations Data:					
Revenues					
Core operating segments	$ 384,741	$ 300,266	$ 147,433	$ 119,937	$ 52,533
Sylvan Ventures	645				
Total Revenues	385,386	300,266	147,433	119,937	52,533
Costs and expenses					
Direct costs:					
Core operating segments	345,624	264,694	132,240	91,906	34,455
Sylvan Ventures	2,592				
General and administrative expenses:					
Core operating segments	21,318	22,003	20,306	26,855	15,530
Sylvan Ventures	4,804	9,211	5,473		
Loss on assets sold	20,244				
Transaction costs related to pooling of interests					3,245
Restructuring and asset impairment charges				899	
Total costs and expenses	394,582	295,908	158,019	119,660	53,230
Operating income (loss)	(9,196)	4,358	(10,586)	277	(697)
Other income (expense)					
Investment and other income	6,574	11,646	20,380	1,225	3,983
Interest expense	(8,382)	(9,177)	(6,919)	(3,707)	(237)
Sylvan Ventures investment income (losses)	(2,308)	22,131	(11,441)		
Loss on investments	(8,343)	(14,231)			
Equity in net income (loss) of affiliates:					
Sylvan Ventures	(5,595)	(52,374)	(21,222)		
Other	131	(501)	(981)	(2,356)	(3,402)
	(5,464)	(52,875)	(22,203)	(2,356)	(3,402)
Minority interest in consolidated subsidiaries:					
Sylvan Ventures	2,057	2,590	9,133		
Other	(6,881)	(7,599)	(1,674)	(319)	
	(4,824)	(5,009)	7,459	(319)	
Loss from continuing operations before income taxes and cumulative effect of change in accounting principle	(31,943)	(43,157)	(23,310)	(4,880)	(353)
Income tax benefit	15,040	18,798	15,736	5,127	3,943
Income (loss) from continuing operations before cumulative effect of change in	$ (16,903)	$ (24,359)	$ (7,574)	$ 247	$ 3,590

accounting principle										
Income (loss) from continuing operations per share, basic	$	(0.42)	$	(0.64)	$	(0.17)	$	0.00	$	0.07
Income (loss) from continuing operations per share, diluted	$	(0.42)	$	(0.64)	$	(0.17)	$	0.00	$	0.07
Balance Sheet Data:										
Cash and cash equivalents	$	98,618	$	95,353	$	112,482	$	16,073	$	27,606
Available-for-sale securities		22,546		60,091		202,077		10,890		6,108
Net working capital		106,328		156,520		190,688		284,311		24,485
Intangible assets and deferred costs, net		236,444		251,402		236,364		157,918		90,038
Net assets of discontinued operations		129,217		118,243		109,733		368,931		383,896
Total assets		965,374		909,191		1,016,963		764,625		602,410
Long-term debt, including current portion, due to shareholders and other long term liabilities		200,174		148,716		197,959		185,436		61,691
Stockholders equity		485,928		545,855		553,263		474,093		488,833

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(1) On March 10, 2003, the Company announced that it would sell the operations comprising its K-12 education business units which include the Learning Centers and Education Solutions which were formerly part of the K-12 business segment and the Connections Academy and eSylvan businesses which were formerly part of the Sylvan Ventures business segment. The Company s consolidated statements of operations were restated to reflect the results of operations of the K-12 business units as discontinued operations. Therefore, the operations of these disposal groups are not presented on this table.

(2) The following material acquisitions were completed during the year ended December 31, 2002. The Company s 2002 results of continuing operations include the results of the acquired companies from the effective date of the acquisitions through December 31, 2002.

On February 1, 2002, Sylvan Ventures exercised its option to acquire an additional 10% ownership of common stock in Walden E-Learning, Inc. (Walden) for $8.0 million, increasing its ownership percentage in Walden to 51%. Prior to the exercise of its option, Sylvan Ventures had acquired a 41% stake in Walden for $32.8 million in February 2001. The transactions have been accounted for as a step acquisition with a total purchase price of $39.9 million after subtracting previously recorded equity in net losses. The purchase price was allocated to acquired assets of $57.4 million and assumed liabilities of $17.5 million. The operating results of Walden are included as part of the Online operating segment.

On March 1, 2002, the Company acquired for cash all of the outstanding common stock of Hedleton, B.V., which owns all of the capital stock of Escuela Superior De Alta Gestion De Hotel, S.A. (Marbella), a private for-profit university located in Marbella, Spain. The purchase price for the outstanding common stock totaled approximately $6.7 million, including acquisition costs of $0.5 million. The purchase price was allocated to acquired assets of $9.3 and assumed liabilities of $2.6 million.

Effective August 1, 2002, the Company acquired all of the outstanding common stock of the Glion Group, S.A., the parent company of Glion Hotel School, S.A. (Glion), a leading hotel management school in Switzerland. The initial cash purchase price totaled approximately $16.9 million, including acquisition costs of $1.4 million. Additionally, the Company is required to make payments of $2.0 million and $3.4 million on August 30, 2003 and August 30, 2004, respectively. The purchase agreement includes a provision for a possible reduction in the purchase price of up to $1.5 million based on the working capital of Glion at the acquisition date. The purchase price was allocated to acquired assets of $58.3 and assumed liabilities of $41.4 million.

In November 2002, Sylvan Ventures completed its acquisition of substantially all the assets and certain liabilities of the National Technological University (NTU) and Stratys Learning Solutions, Inc. (the holding company of NTU) for cash payments of $7.5 million and a promissory note payable of $7.5 million due in 2007. The purchase price was allocated to acquired assets of $21.4 and assumed liabilities of $6.4 million. The operating results of NTU are included as part of the Online operating segment.

(3) The Company recognized a net realized investment loss of $10.6 million in 2002, comprised of $8.3 million of losses from investments unrelated to Sylvan Ventures and $2.3 million of investment losses from

investments by Sylvan Ventures. The most significant transaction giving rise to these losses is attributable to the Frontline Group investment. The Company recorded a loss of $7.4 million related to the write-off of its investment in and advances to the Frontline Group. This investment write-off was a result of challenges facing the corporate training industry in general, and Frontline Group specifically. The Company originally accepted shares of common stock in Frontline Group in 1999 as consideration for the sale of the PACE business unit.

(4) During 2002, the Company recorded a $3.5 million charge related to the write-off of previously deferred costs of a terminated initial public offering of the Campus Based operating segment and one terminated Campus Based acquisition. These charges are included in core operating costs. In addition, during 2002, the Company sold the portion of its English Language Instruction segment that is located in Spain (WSI Spain). As a result of the sale, the Company recognized a loss on assets sold of $20.2 million.

(5) The Company recognized a net realized investment gain of $7.9 million in 2001, comprised of $14.2 million of losses from investments unrelated to Sylvan Ventures and gains of $22.1 million resulting from Sylvan Ventures transactions. The most significant transactions giving rise to this net gain are described below.

On September 11, 2001 Sylvan Ventures recognized an investment gain of $24.7 million upon the sale of its 42% stake in Classwell Learning Group, Inc. for total cash proceeds of $31.8 million.

On June 15, 2001, Caliber Learning Network, Inc. (Caliber) filed for Chapter 11 bankruptcy protection. The Sylvan Ventures investment in Caliber of $2.9 million was reduced to $0 upon recording its allocable share of losses related to Caliber prior to the bankruptcy proceedings, which is included in equity in net loss of affiliates. Additionally, the Company recorded a loss on investment of $14.2 million. This loss consists of bad debt expense for notes receivable from and advances to Caliber of $7.5 million as well as the accrual of a $6.7 million estimated liability relating to the Company s guarantee of certain non-cancelable Caliber lease obligations and other Caliber related liabilities incurred by the Company.

(6) The following material acquisitions were completed during the year ended December 31, 2000. The Company s 2000 results of continuing operations include the results of the acquired companies from the effective date of the acquisitions through December 31, 2000.

Effective June 30, 2000, the Company acquired for cash the controlling interests in Gesthotel, S.A. which owns and operates Les Roches. The purchase price totaled $12.3 million and was allocated to acquired assets totaling $32.4 million and assumed liabilities totaling $20.1 million.

Effective November 24, 2000, the Company acquired for cash the controlling interests in Planeacion de Sistemas, S.A. which controls and operates Universidad del Valle de Mexico (UVM). The purchase price totaled $49.9 million and was allocated to acquired assets totaling $67.7 million and assumed liabilities totaling $17.8 million. Contingent consideration is also payable to the sellers if specified levels of earnings before interest and taxes are achieved in 2002. Consideration of $0.5 million based on the attainment of these earnings levels was paid to the sellers and recorded as additional goodwill in 2002.

Effective December 12, 2000, the Company acquired for cash the controlling interests in Desarollo del Conocimiento S.A., a holding company that controls and operates Universidad de Las Americas (UDLA). The purchase price totaled $26.0 million, including acquisition costs of $1.7 million, $13.0 million of which was paid in 2001 after finalization of UDLA s 2000 operating results. The purchase price was allocated to acquired assets totaling $34.8 million and assumed liabilities totaling $8.8 million.

(7) The Company recognized realized investment losses of $11.4 million in 2000. The most significant transactions giving rise to these losses are described below.

In 2000, Sylvan Ventures incurred a $3.0 million realized loss upon the disposal of its $4.9 million investment in the common stock of ZapMe! Corporation for cash proceeds of $1.9 million.

Sylvan Ventures also recorded realized investment losses of $8.4 million in 2000 based on an assessment that two investments were permanently impaired due to a significant deterioration in operating results and concerns regarding the ability of these companies to successfully implement their business plan.

(8) The following material acquisitions were completed during the year ended December 31, 1999. The Company s 1999 results of operations include the results of the acquired companies from the effective date of the acquisitions through December 31, 1999.

On April 1, 1999, the Company acquired a controlling interest in Universidad Europea de Madrid (UEM) for cash of $29.2 million.

The Company acquired 23 WSI franchise businesses for a total purchase price of $65.8 million.

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(9) During 1999, the Company recognized restructuring costs of $0.9 million related to continuing operations. Additionally, the Company recognized significant non-recurring operating charges related to continuing operations during the fourth quarter of 1999, which totaled $5.7 million, of which $2.7 million is included in direct costs and $3.0 million is included in core operating general and administrative expenses above. These charges were principally related to asset impairment charges, which resulted from management s focus on simplification of the business model and a return to the core business strengths.

(10) In 1999, $3.2 million of expenses were recognized related to a pooling-of-interest acquisition, such as legal, accounting and advisory fees.

(11) On January 1, 1998, the Company acquired Canter for an initial purchase price of $25.0 million. Additional consideration of $48.8 million has been paid upon Canter s achievement of certain targets. The acquisition was accounted for as a purchase. The Company s 1998 results of continuing operations include the results of Canter from January 1, 1998 through December 31, 1998.

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

The statements contained herein include forward-looking statements. Forward-looking statements include information about possible or assumed results of operations, business strategies, financing plans, competitive position and potential growth opportunities. Forward-looking statements include all statements that are not historical facts and are generally accompanied by words such as may, will, intend, anticipate, believe, estimate, expect, should or similar expressions. These statements also relate to the Company s contingent payment obligations relatin to acquisitions, future capital requirements, potential acquisitions and the Company s future development plans and are based on current expectations. Forward-looking statements involve various risks, uncertainties and assumptions. The Company s actual results may differ materially from those expressed in these forward-looking statements.

Future events and actual results could differ materially from those set forth in the forward-looking statements as a result of many factors. These factors may include, without limitation: the Company s ability to continue to make acquisitions and to successfully integrate and operate acquired businesses; changes in student enrollment; the development and expansion of the franchise system and the effect of new technology applications in the educational services industry; failure to maintain or renew required regulatory approvals, accreditations or authorizations; the Company s ability to effectively manage business growth; possible increased competition from other educational service providers; the effect on the business and results of operations of fluctuations in the value of foreign currencies; and the many risks associated with the operation of an increasingly global business, including complex legal structures, foreign currency, legal, tax and economic risks and the risk of changes in the business climates in the markets where the Company operates. These forward-looking statements are based on estimates, projections, beliefs and assumptions of management and speak only as of the date made and are not guarantees of future performance.

Overview

Pending Sale of Business Units

Sylvan Learning Systems, Inc. and subsidiaries (the Company or Sylvan) is a leading international provider of post-secondary educational services. On March 10, 2003 the Company announced that it would sell the operations comprising its K-12 education business units (K-12 segment) and committed to a plan to sell certain investments in Sylvan Ventures that are not strategic to its post-secondary education business in a transaction more fully described below. In connection with this announcement, the Company realigned its business segments. The Company provides educational services through three separate business segments: a campus-based university segment (Campus Based), an online university segment (Online), and Sylvan Ventures. The Campus Based segment owns or maintains controlling interests in six private universities located in Spain, Switzerland, Mexico, Chile and France and also includes the non-Spain operations of Wall Street Institute (WSI), a European-based franchiser and operator of learning centers that teach the English language in the post-secondary market. The Online segment provides professional development and graduate degree programs to teachers through Canter and Associates. Online also includes the operations of Walden E-Learning, Inc. (Walden) and National Technological University (NTU), which were previously reported as part of Sylvan Ventures. The Sylvan Ventures

segment includes investments in certain education technology companies and consolidates the operations of EdVerify (EdVerify), Inc. and Educational Satellite Services, Inc. (ESS), majority-owned subsidiaries. The Company plans to dispose of all remaining investments of the Sylvan Ventures segment, including EdVerify and ESS.

On March 10, 2003, the Company and Educate, Inc., a company newly formed by Apollo Management, L.P., (Apollo) executed an Asset Purchase Agreement that provides for the acquisition by Educate, Inc. of substantially all of the Company s K-12 education business units, including eSylvan, Inc. and Connections Academy, Inc., which are investments held by Sylvan Ventures. The consideration for the sale of the assets comprising the K-12 business units will consist of the following at closing:

Cash of $112.0 million to $117.0 million, plus an amount equal to the difference between $72.5 million and the conversion value of the convertible debentures issued by the Company and surrendered by Apollo at closing, less any accrued and unpaid interest on the debentures, plus deferred payments of approximately $3.0 million;

A subordinated note in the amount of $55.0 million, bearing interest at 12% per annum and maturing in 2009;

The surrender of convertible debentures issued by the Company with a conversion value of up to $72.5 million;

The assumption of trade accounts payable of the K-12 business units, and other specified liabilities of the K-12 business units;

Apollo s 25% preferred interest in Sylvan Ventures.

Additionally, the proceeds received by the Company are subject to post closing adjustments for specified changes in working capital from the date of the agreement to the closing date. The Company is also entitled to up to $10.0 million of additional consideration if certain operations of Connections Academy exceed specified levels of earnings prior to December 31, 2007. The transaction will result in the elimination of various consent and governance rights that had been held by Apollo. Apollo s representation on the Company s Board of Directors will be reduced from two board seats to one.

In a separate transaction, Sylvan acquired the remaining membership interests in Sylvan Ventures not owned by Sylvan or Apollo for consideration of 581,000 shares of Sylvan common stock, which is restricted from sale for three years. These membership interests were held by investment companies that are partially owned by certain executive management of the Company. Additionally, all membership profit interests in Sylvan Ventures have been eliminated. Upon completion of these acquisitions and the sale of the K-12 business units, the Company will own all of the membership interests of Sylvan Ventures LLC. The Sylvan Ventures investments that are non-strategic to the post-secondary business are now held for sale. The remaining investments of Sylvan Ventures will include the consolidated investments in Walden and NTU, which will be managed and reported within the Online segment, and a $2.4 million note receivable that will mature over the next two years.

The Company, after the sale of substantially all of its K-12 business units, will hold for sale its remaining K-12 assets, consisting of the Company s Sylvan Learning Center operations in the United Kingdom and France. The Company expects to sell these two operations, principally for contingent amounts of future consideration, by December 31, 2003.

The transactions were negotiated and approved by a committee of Sylvan s Board of Directors composed solely of independent directors. Credit Suisse First Boston LLC and U.S. Bancorp Piper Jaffray, Inc. were financial advisors to the committee of independent directors. The Apollo transaction is subject to legal and regulatory approvals and is expected to close on or before June 30, 2003.

As a result of these expected transactions, the Company estimates that it will record a yet to be determined gain from the disposition of its K-12 business units upon closing of the sale to Educate, Inc. (expected to be in the second quarter of 2003), representing the difference between the carrying value of the net assets sold (approximately $111 million at March 31, 2003) and net proceeds upon sale.

The operations of the Company s disposal groups comprising its K-12 business units have been classified as discontinued operations in the consolidated financial statements. Because the operations and cash flows of these groups will be eliminated from the ongoing operations of the Company as a result of the disposal transactions, and because the Company will not have any significant continuing involvement in the held for sale operations after the disposal transactions, the results of operations of these businesses are reported for all periods as a separate component of income, net of income taxes.

These transactions present a number of risks and uncertainties, including the possibility that the transactions will not be completed due to legal, regulatory or other reasons. If these transactions are completed, the Company s overall business will be significantly smaller and will consist exclusively of the Campus Based and Online university business. Following

completion of these transactions, most of the Company s business operations will be in foreign countries, which increases the potentially negative effects on the Company of the many risks of doing business in foreign countries.

Stock Option Modification in the Second Quarter of 2003

Certain employees of the Company s Campus Based University segment previously were granted options to acquire common stock of the holding company subsidiary comprising the Campus Based segment. Due to the restructuring of the Company s operations resulting from the sale of the K-12 business units and non-strategic Sylvan Ventures assets, the Company on April 1, 2003 negotiated an agreement with these employees holding stock options to acquire common stock of the subsidiary that provides for the exchange of these stock options for stock options to acquire common stock of Sylvan. The result of the exchange of options did not increase the aggregate intrinsic value of the options or reduce the ratio of the exercise price per share of the options to the per share fair value of common stock on the date of exchange, as determined by these independent members of the Board of Directors advised by independent valuation experts. The exchange was accounted for as a modification of granted stock options, and the Company will record a non-cash charge of $24.0 million over the remaining vesting period of the options.

In connection with the sale of the K-12 Education business, each unexpired and unexercised outstanding option to purchase shares of the Company s common stock held by employees who will be employed by Educate, Inc. will continue to vest for a period of twelve months following the closing of the transaction and will be exercisable for twenty-four months following the closing. This will be accounted for as a modification of granted stock options, resulting in a new measurement date. The modification will result in non-cash compensation expense in an amount equal to the intrinsic value of such options at the date of closing of the sale of Educate, Inc. This expense will be included in the Company s results from discontinued operations.

Critical Accounting Policies and Estimates

The Company s accounting policies are more fully described in Note 2 of Notes to Consolidated Financial Statements. As disclosed in Note 1 of Notes to Consolidated Financial Statements, the preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements. The Company believes the following key accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements and are critical to its business operations and the understanding of its results of operations.

Revenue Recognition. Revenue from the sale of educational products is generally recognized when shipped. Revenue from educational services are recognized in the period services are provided. As the Company continues to integrate educational product and service businesses, the resulting business structure may impact the revenue recognition of product sales to affiliated educational service providers.

Educational services provided by the Company include results-oriented English language instruction modules that are based on desired proficiency levels. The related revenue is recognized ratably over the estimated period required to complete the modules, which ranges from 8 months to 11 months, depending on the location that the services are provided. The Company estimates the period of instruction based on an analysis of actual historical activity by location. If the historical data the Company uses to calculate these estimates does not properly reflect future usage, revenue recognized by the Company may be negatively impacted. Additionally, if usage trends change over time, the Company may have significant fluctuations in recognized revenues in the future.

Goodwill and Other Intangible Assets. During each of the years presented, the Company acquired certain businesses accounted for using the purchase method of accounting. A portion of the purchase prices for these businesses was allocated to identifiable tangible and intangible assets and assumed liabilities based on estimated fair values at the dates of acquisitions. Any excess purchase price was allocated to goodwill. This goodwill and other indefinite-lived intangibles are evaluated at least annually for impairment by comparison of the carrying amounts of the respective reporting units to their implied fair value determined by discounting estimated future cash flows expected from the reporting units.

Other intangible assets include acquired student rosters, accreditation, non-competition agreements and curriculum. The assumptions used to calculate the fair value of these identified intangible assets included estimates of future operating results and cash flows, as well as discount rates based on specifically identified risks for each acquisition and assumptions about the weighted average cost of capital for each acquisition. The assigned useful lives, which range from 4 to 30 years, are based upon estimated matriculation rates and other factors.

If the Company used different assumptions and estimates in the calculation of the fair value of identified intangible assets and the estimation of the related useful lives, the amounts allocated to these assets, as well as the related amortization expense, could have been significantly different than the amounts recorded.

In assessing the recoverability of the Company s goodwill and other intangible assets, the Company must make assumptions regarding estimated future cash flows and other factors to determine the fair value of the respective assets. If these estimates or their related assumptions change in the future, the Company may be required to record impairment charges for these assets not previously recorded. In 2002, the Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets,* which required the Company to analyze its goodwill for impairment upon adoption. As a result, the Company recorded a non-cash charge of $78.6 million, net of income tax benefit of $7.7 million, which is included as a cumulative effect of a change in accounting principle in the consolidated statements of operations.

Investment in Affiliated Companies and Other Investments. The Company holds minority interests in companies having operations or technology in areas within its strategic focus, some of which are non-publicly traded companies whose value is difficult to determine. At December 31, 2002 these investments had a carrying value of approximately $21.1 million. The Company records an investment impairment charge when it believes an investment has experienced a decline in value that is other than temporary. Adverse changes in market conditions or poor operating results of underlying investments may require management to make subjective judgments about the recoverability of its investments. Due to the inherent subjectivity of the valuation of minority investments in companies without readily ascertainable fair values, it is reasonably possible that events or circumstances could change in the near term and thereby change management s estimates of the recoverability of its investments. On March 10, 2003, the Company announced its intention to sell assets non-strategic to its post-secondary business and recorded a loss on Sylvan Ventures investments held for sale of $8.3 million, primarily representing the book value of Sylvan Ventures cost basis investments in iLearning ($0.3 million) and ClubMom ($7.6 million). In addition in the first quarter of 2003, Sylvan Ventures wrote down the balance in its equity method investment in Chancery through a charge to equity in net loss of affiliates. Sylvan Ventures also recorded an operating loss of $0.2 million related to the write-off of the net assets of the consolidated investment in EdVerify. These investments are being marketed to a single buyer and are expected to be sold by June 30, 2003 for principally contingent consideration.

Income Taxes. The Company earns a significant portion of its income from subsidiaries located in countries outside of the United States. At December 31, 2002, undistributed earnings of foreign subsidiaries totaled approximately $337.3 million. Deferred tax liabilities have not been recognized for these undistributed earnings because it is management s intention to reinvest such undistributed earnings outside of the United States. APB Opinion No. 23, *Accounting for Income Taxes Special Areas*, requires that a company evaluate its circumstances to determine whether or not there is sufficient evidence to support the assertion that it has or will reinvest undistributed foreign earnings indefinitely.

The Company s assertion that earnings from its foreign operations will be permanently reinvested is supported by projected working capital and long-term capital needs in each subsidiary location in which the earnings are generated. Additionally, the Company believes that it has the ability to permanently reinvest foreign earnings based on a review of projected cash flows from domestic operations, projected working capital and liquidity for both short-term and long-term domestic needs, and the expected availability of debt or equity markets to provide funds for those domestic needs.

If circumstances change and it becomes apparent that some or all of the undistributed earnings of the Company s foreign subsidiaries will be remitted in the foreseeable future, the Company will be required to recognize deferred tax liabilities on those amounts. As of December 31, 2002, if all undistributed earnings had been remitted to the United States, the amount of incremental U.S. federal income tax liabilities, net of foreign tax credits, would have been approximately $104.6 million, of which $84.4 million related to discontinued operations.

The Company has generated significant deferred tax assets, primarily as a result of its equity in the net losses of affiliated companies. The Company records a valuation allowance to reduce its deferred tax assets to the amount that it believes is more likely than not to be realized. The primary factor used by the Company to determine the amount of

valuation allowance needed to offset deferred tax assets related to these losses is that when realized, these capital losses may be carried back to offset the Company s substantial prior year capital gains, subject to certain limitations. The Company also has considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the amount of valuation allowance needed. If the Company were to determine that it would not be able to realize all or part of its net deferred tax assets in the future, an adjustment to the deferred tax assets would be charged to income in the period such determination was made. Likewise, should the Company determine that it would be able to realize its deferred tax assets in the future in excess of its net recorded amount, an adjustment to the deferred tax assets would increase income in the period such determination was made.

Accounts and Notes Receivable. The Company s accounts receivable consist primarily of installment payments due from parents and students for tuition at Wall Street Institute centers and universities; related fees that are payable over the course of payment plans of up to nine months; and amounts due from franchisees for franchise fees, franchise royalties and didactic material purchases. Notes receivable consist primarily of loans to franchisees, which are generally collateralized. The Company routinely makes estimates of the collectibility of its accounts and notes receivable. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers and franchisees to make required payments. The Company estimates the amount of the required allowance by reviewing the status of past-due receivables and analyzing historical bad debt trends. Actual collection experience has not varied significantly from estimates, due primarily to credit policies, collection experience, and a lack of concentration of accounts receivable. If the financial condition of the Company s customers and franchisees were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Results of Operations

Revenues generated by Sylvan s three continuing business segments are described as follows:

Campus Based (formerly named International Universities) earns tuition and related fees paid by the students of Universidad Europea de Madrid (UEM), Universidad del Valle de Mexico (UVM), Universidad de Las Americas (UDLA), École Supérieure du Commerce Extérieur (ESCE) as well as students from Swiss Hotel Association Hotel Management School Les Roches (Les Roches), Escuela Superior De Alta Gestion De Hotel, S.A. (Marbella) and Glion Hotel School, S.A. (Glion) (collectively, The Hospitality Group), in addition to franchise royalties, Company-owned center revenues, didatic material sales and franchise sale fees related to WSI operations outside of Spain;

Online earns revenues from instructional services that are provided through an online format, as well as other forms of distance learning; and

Sylvan Ventures earns a small amount of revenues on satellite services provided to a number of universities.

The Campus Based and Online segments, when presenting aggregated statements of operations data, are referred to as core operating segments.

In connection with the Company s March 10, 2003 announcement that it would sell the operations comprising its K-12 education business units, the operations of the Company s disposal groups comprising its K-12 business units are classified as discontinued operations for all periods presented**.** Accordingly, the following discussion describes the results of the operations of only the Campus Based, Online and Sylvan Ventures business segments.

The following table sets forth the percentage relationships of the components of operating revenues for the Company s three segments as well as income statement line items expressed as a percentage of total revenues for the years ended December 31:

	2002	2001	2000
Revenues:			
Campus Based	79%	79%	58%
Online	19%	15%	25%
Sylvan Ventures			
Other(1)	2%	6%	17%
Total revenues	100%	100%	100%
Direct costs:			
Campus Based	70%	70%	56%
Online	17%	12%	20%
Sylvan Ventures	1%		
Other(1)	2%	6%	14%
Total direct costs	90%	88%	90%
Core operating general and administrative expenses	6%	7%	14%
Sylvan Ventures general and administrative expenses	1%	3%	4%
Loss on assets sold	5%		
Operating income	(2)%	1%	(7)%
Other non-operating income (loss)	(1)%	%	14%
Interest expense	(2)%	(3)%	(5)%
Sylvan Ventures investment income (losses)	(1)%	7%	(8)%
Equity in loss of affiliates	(2)%	(17)%	(15)%
Minority interest	(1)%	(2)%	5%
Loss from continuing operations before taxes	(9)%	(14)%	(16)%
Tax benefit	4%	6%	11%
Loss from continuing operations before cumulative effect of change in accounting principle	(5)%	(8)%	(5)%
Income from discontinued operations, net of tax	1%	2%	1%
Gain (loss) on disposal of discontinued operations, net of income tax expense (benefit)	(1)%		211%
Loss before cumulative effect of change in accounting principle	(5)%	(6)%	(207)%
Cumulative effect of change in accounting principle, net of income tax benefit	(20)%		
Net Loss	(25)%	(6)%	(207)%

(1) Other represents the results of operations of the English Language Instruction Spain business that was sold effective July 1, 2002.

The following comparisons of results of operations focus on the continuing operations of the Company.

Comparison of results for the year ended December 31, 2002 to results for the year ended December 31, 2001.

Revenues. Total revenues increased by $85.1 million, or 28%, to $385.4 million for the year ended December 31, 2002 (the 2002 fiscal year) from $300.3 million for the year ended December 31, 2001 (the 2001 fiscal year). This revenue increase was primarily driven by increases in tuition and enrollment at universities in the Campus Based segment.

Campus Based revenue for the 2002 fiscal year period increased by $67.1 million, or 28%, to $303.7 million compared to the 2001 fiscal year. This increase is primarily due to an increase in enrollments at UDLA, UVM, Les Roches and UEM. Additionally, revenue increased by $18.0 million due to the full year effect of the acquisition of the controlling interest in ESCE, which occurred in the fourth quarter of 2001 and the acquisitions of controlling interests in Marbella and Glion, which occurred in the first and third quarters of 2002, respectively. Non-Spain WSI revenues increased $6.0 million, primarily due to the full year effect of the acquisition of centers in Portugal in the third quarter of 2001 as well as an increase in revenues in Italy and Germany. Campus Based operating revenue represents 79% of total revenues of the Company for the 2002 fiscal year.

Online revenue increased by $29.8 million, or 67%, to $74.1 million for the 2002 fiscal year compared to the 2001 fiscal year. $21.7 million of the increase is due to the acquisitions of Walden in February 2002 and NTU in November 2002, respectively. Canter teacher-training revenue increased by $9.2 million, or 22%, to $51.5 million during the 2002 fiscal year compared to the 2001 fiscal year. Canter s revenue increase was due to greater demand for its products, particularly the distance learning masters programs, which saw enrollments for the Spring 2003 semester increased by 17% to 12,800 students. Sylvan Teacher Institute revenue decreased by $1.1 million, or 54%, to $0.9 million in the 2002 fiscal year compared to the 2001 fiscal year. The decrease was due to the planned decrease in professional development workshops performed in the 2002 fiscal year compared to the 2001 fiscal year. Online operating revenue represents 19% of total revenues of the Company for the year ended December 31, 2002.

Sylvan Ventures revenue increased to $0.7 million for the 2002 fiscal year. The increase was attributable to EdVerify, Inc. and ESS, Inc revenues due to the consolidation of these acquisitions over the past six months. Operating revenues for Sylvan Ventures represent less than 1% of the Company s total revenues for 2002.

Other- English Language Instruction Spain revenue decreased by $12.4 million, or 64%, to $7.0 million for the 2002 fiscal year compared to the 2001 fiscal year primarily due to the sale of WSI-Spain, effective July 1, 2002. Additional operational factors in the period of Sylvan ownership reflected the result of lower tuition revenues in existing Company-owned centers, as well as decreased royalties and didactic material sales to franchises due to market oversaturation by English language instruction providers in Spain.

Direct Costs. Total direct costs of revenues increased $83.5 million, or 32%, to $348.2 million for the 2002 fiscal year from $264.7 million for the 2001 fiscal year. Excluding the impact of goodwill amortization in the 2001 fiscal year of $9.5 million, direct costs increased $93.1 million, or 36%, for the 2002 fiscal year. Direct costs as a percentage of total revenues increased to 90% in the 2002 fiscal year from 88% in the 2001 fiscal year. Excluding the impact of goodwill amortization, direct costs as a percentage of revenues were 85% in the 2001 fiscal year.

Campus Based expenses increased by $59.4 million to $271.0 million, or 89% of Campus Based revenue for the 2002 fiscal year, compared to $211.6 million, or 89% of Campus Based revenue for the 2001 fiscal year. The increase in expenses reflects i) higher expenses, particularly labor and marketing expenses given the higher volume of enrollments and operating activities at the universities compared to the 2001 fiscal year, ii) the full year effect of the acquisition of the controlling interest in ESCE, which occurred in the fourth quarter of 2001 and the acquisitions of controlling interests in Marbella and Glion, which occurred in the first and third quarters of 2002, respectively, and iii) an increase in overhead costs, including staffing expenses, as a result of the increase in the university business. Included in the fiscal 2002 expenses was the write-off of $3.5 million of deferred costs related to the terminated initial public offering of the Campus Based segment and one terminated Campus Based university acquisition. Excluding these charges, Campus Based expenses represented 88% of Campus Based revenues for the 2002 fiscal year. The decrease in expenses as a percentage of revenue is primarily due to operating efficiencies achieved throughout the Campus Based segment, particularly at UDLA, UEM and UVM.

Online expenses increased by $30.1 million to $65.3 million, or 88% of Online revenue for the 2002 fiscal year, compared to $35.2 million, or 79% of Online revenue for the 2001 fiscal year. $27.3 million of this increase was due to the acquisitions of Walden in February 2002 and NTU in November 2002. Canter had a decrease in expenses as a percentage of revenue for the 2002 year primarily due to the adoption of Statement No. 142 in 2002, which discontinued the amortization of goodwill. The amortization of goodwill related to the Canter acquisition was $3.1 million in the 2001 fiscal year. This decrease in Canter s expenses as a percentage of its revenue was partially offset by an increase in expenses as a percentage of revenue due to the inclusion of the operating results of OnlineLearning.net in the 2002 fiscal year. The acquisitions of OnlineLearning.net, effective July 1, 2001, resulted in lower margin revenue for Canter in the fiscal 2002 year.

Sylvan Ventures operating expenses increased to $2.6 million in the 2002 fiscal year as a result of operating costs related to the acquisitions of EdVerify, Inc. and ESS, Inc.

Other - English Language Instruction-Spain expenses decreased by $8.5 million to $9.3 million for the 2002 fiscal year compared to $17.8 million for the 2001 fiscal year due to the sale of WSI Spain, effective July 1, 2002.

Other Expenses. Core operating segment general and administrative expenses decreased by $0.7 million in the 2002 fiscal year compared to the 2001 fiscal year. The decrease was primarily due to increased leveraging of centralized costs and effective cost control efforts. Core operating segment general and administrative expenses decreased to 6% of core operating segment revenues in the 2002 fiscal year, compared to 7% of revenues in the 2001 fiscal year, due to strong revenue expansion combined with cost controls.

Sylvan Ventures management costs decreased by $4.4 million to $4.8 million for the 2002 fiscal year compared to $9.2 million for the 2001 fiscal year. The decrease was due to significant reduction in labor, travel and consulting costs associated with the research, evaluation and acquisition of new investment opportunities as management shifted its focus towards managing and reinvesting solely in its current investment portfolio.

English Language Instruction Spain - Loss on assets sold of $20.2 million represents the impairment of assets related to WSI Spain due to the Company s decision to dispose of the business unit, and the lack of material consideration received upon sale. The asset write-offs included franchise receivables, fixed assets and working capital amounts that the Company transferred to the buyer effective July 1, 2002.

Sylvan Ventures equity in net losses of affiliates decreased to $5.6 million for the 2002 fiscal year from $52.4 million for the 2001 fiscal year. These losses relate to Sylvan Ventures share of operating losses generated by the early stage enterprises in the investment portfolio not under Sylvan Ventures control. This decrease was primarily due to Sylvan Ventures change in strategy to focus on managing its current investments rather than investing in new early stage enterprises, as well as the consolidation of Walden and EdVerify. The reduction in the number of early stage enterprises and the decision of certain portfolio companies to cease operations slowed the losses absorbed by Sylvan Ventures, as these companies initially generate significant losses. Additionally, a number of the enterprises in which Sylvan Ventures invested throughout 2000 and 2001 have matured, and thus are generating reduced losses, relative to their earlier stages in the 2001 fiscal year. The adoption of Statement No. 142 also resulted in Sylvan Ventures no longer amortizing goodwill associated with equity method investments. The amortization of goodwill related to the Sylvan Ventures equity investments in the 2001 fiscal year was $8.9 million.

Sylvan Ventures incurred an investment loss on portfolio investments of $2.3 million in the 2002 fiscal year compared to investment income of $22.1 million in the 2001 fiscal year. The gain in fiscal year 2001 of $24.7 million was generated by the sale of the Classwell investment in September 2001. Minority interests share of Sylvan Ventures losses totaled $2.1 million and $2.6 million for the 2002 and 2001 fiscal years, respectively.

Investment losses totaled $8.3 million in the 2002 fiscal year compared to $14.2 million in the 2001 fiscal year. The 2002 fiscal year loss is primarily due to $7.4 million related to the write-off of the Company s investment in and advances to the Frontline Group. This investment write-off was a result of challenges facing the corporate training industry in general, and Frontline Group specifically. The Company originally accepted shares of common stock in Frontline Group as consideration for the sale of the PACE business unit in 1999.

The 2001 loss on investment was related to the Company s investment in Caliber Learning Network, Inc. (Caliber). Caliber filed for Chapter 11 bankruptcy protection on June 15, 2001. The Sylvan Ventures investment in Caliber of $2.9 million was reduced to $0 upon recording its allocable share of losses related to Caliber prior to the bankruptcy proceedings, which is included in Sylvan Ventures equity in net loss of affiliates. Additionally, the Company recorded a loss on investment of $14.2 million in the 2001 fiscal year, consisting of bad debt expense for uncollected notes receivable and advances to Caliber of $7.5 million, as well as the accrual of a $6.7 million estimated liability relating to the Company s guarantee of certain non-cancelable Caliber lease obligations and other Caliber related liabilities incurred by the Company. In 2002, the Company recorded an additional $0.7 million of liabilities related to Caliber lease guarantees. Due to the uncertainties surrounding the bankruptcy proceedings and the ultimate settlement of Caliber s lease and other liabilities, it is possible that the Company s loss estimate may change prior to finalization.

Other non-operating items decreased by $2.9 million for the 2002 fiscal year compared to the 2001 fiscal year. This decrease was attributable in part to a decrease in interest income of $4.2 million resulting from lower investment balances

and a reduced interest rate environment, partially offset by a decrease in interest expense of $0.8 million and a decrease in equity in net loss of affiliates of $0.6 million.

Income Taxes. The Company s effective income tax rate was 47% and 44% for the 2002 and 2001 fiscal years, respectively. The effective income tax rate has increased from the 2001 fiscal year because the acquisition of profitable foreign subsidiaries has increased the net tax benefit on overall losses of the Company. This reported effective income tax rate differs from the U.S. federal statutory tax rate due to the impact of state income taxes, minority interests and foreign income taxed at lower rates.

Cumulative Effect of Change in Accounting Principle. As a result of adopting Statement No. 142 as of January 1, 2002 and performing the required transitional impairment tests, the Company recorded a non-cash charge of $78.6 million, net of income tax benefit of $7.7 million, which is included in cumulative effect of change in accounting principle in the consolidated statements of operations. The impairment charge relates solely to the English Language Instruction business and consists principally of the write-down of goodwill related to WSI Spain, WSI Italy and WSI Brazil.

Comparison of results for the year ended December 31, 2001 to results for the year ended December 31, 2000.

Revenues. Total revenues from continuing operations increased by $152.8 million, or 104% to $300.3 million for the year ended December 31, 2001 (2001 fiscal year) from $147.4 million for the year ended December 31, 2000 (2000 fiscal year). Included in total revenues for the 2001 fiscal year were $150.9 million of revenues from Les Roches, UVM and UDLA, which were acquired in the third and fourth quarters of 2000. Total revenues increased 14% excluding the increase due to the Les Roches, UVM and UDLA acquisitions. This revenue increase was primarily driven by growth in the Online segment and acquisitions of WSI centers in the Campus Based segment.

Campus Based revenue increased by $151.2 million, or 177%, to $236.6 million for the 2001 fiscal year compared to the 2000 fiscal year. Of this increase, $135.1 million was due to the full year effect of acquisitions of controlling interests of Les Roches, UVM and UDLA, which occurred in the third and fourth quarters of 2000 and the acquisition of the controlling interest in ESCE, which occurred in the fourth quarter of 2001. Revenue at UEM increased $4.2 million, or 10%, to $48.4 million for the 2001 fiscal year compared to the 2000 fiscal year primarily due to increased enrollment, new program offerings and tuition increases. Non-Spain WSI revenues increased $11.9 million, primarily due to the acquisition of centers in Italy, Portugal, Argentina and Brazil. Operating revenue for Campus Based represents 79% of total revenues of the Company for the 2001 fiscal year

Online revenue increased by $7.5 million, or 20%, to $44.3 million for the 2001 fiscal year compared to the 2000 fiscal year. Canter product license and service revenue increased $7.5 million, or 22%, to $42.2 million in the 2001 fiscal year from $34.7 million in the 2000 fiscal year. The Canter revenue increase is due to the increased demand for the distance learning masters programs offered by Canter s university customers. Sylvan Teacher Institute revenue

remained constant at $2.1 million for both the 2001 and the 2000 fiscal year. Operating revenue for Online represents 15% of total revenues of the Company for the 2001 fiscal year.

Other revenues from the English Language Instruction Spain business decreased by $5.9 million, or 23%, to $19.4 million for the 2001 fiscal year compared to the 2000 fiscal year. The decrease was primarily attributable to lower franchise sales and maturation of the market in Spain. Operating revenue for English Language Instruction-Spain represents 6% of total revenues of the Company for the 2001 fiscal year.

Direct Costs. Total direct costs of revenues increased by $132.5 million, or 100%, to $264.7 million for the 2001 fiscal year from $132.2 million for the 2000 fiscal year. Included in direct costs in the 2001 fiscal year were $126.6 million of costs of Les Roches, UVM and UDLA, which were acquired in the third and fourth quarters of 2000. Total direct costs increased $19.0 million, or 16%, excluding the costs related to Les Roches, UVM and UDLA. Direct costs as a percentage of total revenues decreased to 88% in the 2001 fiscal year from 90% in the 2000 fiscal year.

Campus Based expenses increased by $128.5 million to $211.6 million, or 89% of Campus Based revenue for the 2001 fiscal year, compared to $83.1 million, or 97% of Campus Based revenue for the 2000 fiscal year. Expenses increased $114.2 million due to the full year effect of acquisitions of controlling interests of Les Roches, UVM and UDLA, which occurred in the third and fourth quarters of 2000 and the acquisition of the controlling interest in ESCE, which occurred in the fourth quarter of 2001. Non-Spain WSI expenses increased $10.4 million primarily due to the acquisition of centers in Italy, Portugal, Argentina and Brazil. The decrease in expenses as a percentage of revenue for the 2001 fiscal year was primarily due to improved operating margin performance at UEM, higher margins at Les Roches and UDLA, strong

operating performance at UVM and management s efforts to control divisional overhead costs while expanding the university network.

Online expenses increased by $6.1 million to $35.2 million, or 79% of Online revenue for the 2001 fiscal year, compared to $29.1 million, or 79% of Online revenue for the 2000 fiscal year. Expenses as a percentage of revenue for the 2001 fiscal year remained constant compared to the 2000 fiscal year.

Other- English Language Instruction-Spain expenses decreased by $2.3 million to $17.8 million, or 92% of English Language Instruction-Spain revenue for the 2001 fiscal year, compared to $20.1 million, or 80% of English Language Instruction-Spain revenue in the 2000 fiscal year. The decrease in operating expenses was primarily attributable to lower margin sales related to the maturation of the market in Spain.

Other Expenses. Core operating segment general and administrative expenses increased by $1.7 million in the 2001 fiscal year compared to the 2000 fiscal year. During the 2000 fiscal year, the Company continued to provide certain general and administrative services to Prometric and Aspect after the sale of these companies for a short transition period. The increase in core operating segment general and administrative expenses was due to the decrease in the reimbursement of these administrative costs in 2001 and the additional costs of overseeing the international expansion of the Company. Core operating segment general and administrative expenses as a percentage of revenues decreased to 7% in the 2001 fiscal year from 14% in the 2000 fiscal year due to cost controls and the strong revenue expansion in the 2001 fiscal year.

Sylvan Ventures' management costs increased to $9.2 million for the 2001 fiscal year compared to $5.5 million for the 2000 fiscal year. This increase was primarily due to a full year of management operations in the 2001 fiscal year versus only a half year in 2000.

Sylvan Ventures equity in net losses of affiliates increased by $31.2 million to $52.4 million for the 2001 fiscal year, compared to $21.2 million for the 2000 fiscal year. This increase was the result of a full year of operations from a greater number of portfolio companies in the 2001 fiscal year as compared to the 2000 fiscal year. These losses relate to Sylvan Ventures share of operating losses generated by the early stage enterprises in the investment portfolio and the amortization of the difference between the initial carrying amount of equity method investments and the underlying equity in net assets of these investments at the time of purchase.

Sylvan Ventures fiscal year 2001 investment income of $22.1 million consisted of the $24.7 million gain on the sale of its Classwell investment, partially offset by impairment charges related to portfolio investments. For fiscal year 2000 the investment loss of $11.4 million consisted of realized losses pertaining to OnlineLearning.net, Inc. of $6.9 million, Zapme! Corporation of $3.0 million and Kawama, Inc. of $1.5 million.

The loss on investment in 2001 of 14.2 million was prompted by Caliber Learning Network, Inc. s (Caliber) filing for Chapter 11 bankruptcy protection on June 15, 2001. The Sylvan Ventures investment in Caliber of $2.9 million was reduced to $0 upon recording its allocable share of losses related to Caliber prior to the bankruptcy proceedings, which is included in Sylvan Ventures equity in net loss of affiliates. Additionally, the Company recorded a loss on investment of $14.2 million in the 2001 fiscal year. This charge consists of bad debt expense for notes

receivable and advances to Caliber of $7.5 million, as well as the accrual of a $6.7 million estimated liability relating to the Company s guarantee of certain non-cancelable Caliber lease obligations and other Caliber related liabilities incurred by the Company.

Other non-operating items decreased by $16.4 million for the 2001 fiscal year compared to the 2000 fiscal year. This net decrease was primarily attributable to a decrease in interest income of $10.9 million, an increase in interest expense of $2.3 million and an increase in minority interest allocations of $5.9 million, partially offset by a $2.1 million decrease in foreign currency exchange loss. The increased minority interest allocations were generated from strong operating performance of the universities in which the Campus Based segment maintains a controlling interest. The decrease in the exchange losses was primarily due to a loss of $3.1 million incurred in the 2000 fiscal year on the settlement of a forward exchange contract acquired to protect against fluctuations in local currency prior to the UVM acquisition.

Income Taxes. The Company s effective income tax rate was 44% and 68% for the 2001 and 2000 fiscal years, respectively. The decrease in rate in the 2001 fiscal year is due to the recognition of foreign earnings, currently taxable in the U.S. This additional taxable income in the U.S., a relatively high-tax-jurisdiction, has decreased the net tax benefit on the overall losses of the Company. This reported effective income tax rate differs from the U.S. federal statutory tax rate due to the impact of state income taxes, minority interests and foreign income taxed at lower rates.

Liquidity and Capital Resources

Condensed Statement of Cash Flows

Year Ended December 31, 2002

	Core Operating Segments	Sylvan Ventures	Consolidated
Operating activities			
Net loss	$ (64,239)	$ (31,704)	$ (95,943)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Cumulative pre-tax effect of change in accounting principle	86,334		86,334
Depreciation and amortization	28,876	2,161	31,037
Loss on investments	19,827	2,308	22,135
Loss on assets sold	20,244		20,244
Other non-cash items	2,388	575	2,963
Changes in working capital	12,446	1,909	14,355
Net cash provided by (used in) operating activities	105,876	(24,751)	81,125
Investing activities			
Purchases of property and equipment	(68,804)	(951)	(69,755)
Change in investments in affiliates and other investments	1,163	(5,280)	(4,117)
Cash paid for acquired businesses, net of cash received	(39,480)	(16,727)	(56,207)
Other investing activities, net	22,211	10,360	32,571
Net cash used in investing activities	(84,910)	(12,598)	(97,508)
Financing activities			
Net cash received from (distributed to) minority members of Sylvan Ventures	5,000	(1,575)	3,425
Intercompany funding	(43,329)	43,329	
Other financing activities, net	20,487	(2,115)	