COCA COLA BOTTLING CO CONSOLIDATED /DE/
Form 10-Q
August 16, 2006
Table of Contents

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 July 2, 2006

Commission File Number 0-9286

COCA-COLA BOTTLING CO. CONSOLIDATED

(Exact name of registrant as specified in its charter)

Delaware	**56-0950585**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

4100 Coca-Cola Plaza, Charlotte, North Carolina 28211

(Address of principal executive offices) (Zip Code)

(704) 557-4400

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject

to such filing requirements for the past 90 days. Yes x No ¨

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

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

Class	**Outstanding at July 31, 2006**
Common Stock, $1.00 Par Value	6,643,177
Class B Common Stock, $1.00 Par Value	2,460,152

Table of Contents

COCA-COLA BOTTLING CO. CONSOLIDATED

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JULY 2, 2006

INDEX

		Page
	PART I FINANCIAL INFORMATION	
Item 1.	Financial Statements (Unaudited)	
	Consolidated Statements of Operations	3
	Consolidated Balance Sheets	4
	Consolidated Statements of Changes in Stockholders Equity	6
	Consolidated Statements of Cash Flows	7
	Notes to Consolidated Financial Statements	8
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	30
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	51
Item 4.	Controls and Procedures	51
	PART II OTHER INFORMATION	
Item 1.	Legal Proceedings	52
Item 1A.	Risk Factors	52
Item 4.	Submission of Matters to a Vote of Security Holders	53
Item 6.	Exhibits	54

Table of Contents

PART I - FINANCIAL INFORMATION

Item l. Financial Statements.

Coca-Cola Bottling Co. Consolidated

CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

In Thousands (Except Per Share Data)

	Second Quarter		First Half	
	2006	**2005**	**2006**	**2005**
Net sales	$ 386,624	$ 361,224	$ 719,803	$ 670,409
Cost of sales	218,935	194,859	406,088	364,510
Gross margin	167,689	166,365	313,715	305,899
Selling, delivery and administrative expenses	138,310	132,025	270,038	257,924
Amortization of intangibles	142	157	290	566
Income from operations	29,237	34,183	43,387	47,409
Interest expense	12,843	12,893	25,063	24,391
Minority interest	1,149	1,441	1,705	1,961
Income before income taxes	15,245	19,849	16,619	21,057
Income taxes	6,358	8,330	6,917	8,819
Net income	$ 8,887	$ 11,519	$ 9,702	$ 12,238
Basic net income per share	$ .98	$ 1.27	$ 1.07	$ 1.35
Diluted net income per share	$ .97	$ 1.27	$ 1.06	$ 1.35
Weighted average number of common shares outstanding	9,103	9,083	9,103	9,083
Weighted average number of common shares outstanding assuming dilution	9,123	9,083	9,118	9,083
Cash dividends per share				
Common Stock	$ .25	$ .25	$ .50	$ .50
Class B Common Stock	$ .25	$ .25	$ .50	$ .50

See Accompanying Notes to Consolidated Financial Statements

3

Table of Contents

Coca-Cola Bottling Co. Consolidated

CONSOLIDATED BALANCE SHEETS

In Thousands (Except Share Data)

	Unaudited July 2, 2006	Jan. 1, 2006	Unaudited July 3, 2005
ASSETS			
Current Assets:			
Cash and cash equivalents	$ 30,971	$ 39,608	$ 10,155
Accounts receivable, trade, less allowance for doubtful accounts of $1,490, $1,318 and $1,262, respectively	106,740	94,576	100,640
Accounts receivable from The Coca-Cola Company	10,709	2,719	5,326
Accounts receivable, other	10,485	8,388	6,890
Inventories	63,932	58,233	55,324
Prepaid expenses and other current assets	15,848	8,862	12,806
Total current assets	238,685	212,386	191,141
Property, plant and equipment, net	385,813	389,199	398,368
Leased property under capital leases, net	71,511	73,244	75,051
Other assets	38,892	39,235	40,239
Franchise rights	520,672	520,672	520,672
Goodwill	102,049	102,049	102,049
Other identifiable intangible assets, net	4,986	5,054	5,369
Total	$ 1,362,608	$ 1,341,839	$ 1,332,889

See Accompanying Notes to Consolidated Financial Statements

4

Table of Contents

Coca-Cola Bottling Co. Consolidated

CONSOLIDATED BALANCE SHEETS

In Thousands (Except Share Data)

	Unaudited July 2, 2006	Jan. 1, 2006	Unaudited July 3, 2005
LIABILITIES AND STOCKHOLDERS EQUITY			
Current Liabilities:			
Current portion of debt		$ 6,539	$ 2,939
Current portion of obligations under capital leases	$ 1,594	1,709	1,794
Accounts payable, trade	40,890	35,333	35,068
Accounts payable to The Coca-Cola Company	34,695	15,516	29,285
Other accrued liabilities	51,973	60,079	61,010
Accrued compensation	13,073	18,969	14,346
Accrued interest payable	9,747	9,670	6,787
Total current liabilities	151,972	147,815	151,229
Deferred income taxes	163,650	167,131	168,433
Pension and postretirement benefit obligations	65,227	54,844	42,031
Other liabilities	89,458	85,188	78,935
Obligations under capital leases	76,728	77,493	78,336
Long-term debt	691,450	691,450	700,000
Total liabilities	1,238,485	1,223,921	1,218,964
Commitments and Contingencies (Note 14)			
Minority interest	44,489	42,784	40,648
Stockholders Equity:			
Common Stock, $1.00 par value:			
Authorized 30,000,000 shares; Issued 9,705,451, 9,705,451 and 9,704,951 shares, respectively	9,705	9,705	9,704
Class B Common Stock, $1.00 par value:			
Authorized 10,000,000 shares; Issued 3,088,366, 3,068,366 and 3,068,866 shares, respectively	3,088	3,068	3,069
Capital in excess of par value	100,681	99,376	99,376
Retained earnings	59,505	54,355	48,185
Accumulated other comprehensive loss	(32,091)	(30,116)	(25,803)
	140,888	136,388	134,531
Less: Treasury stock, at cost			
Common 3,062,374 shares	60,845	60,845	60,845
Class B Common 628,114 shares	409	409	409
Total stockholders equity	79,634	75,134	73,277
Total	$ 1,362,608	$ 1,341,839	$ 1,332,889

See Accompanying Notes to Consolidated Financial Statements

Table of Contents

Coca-Cola Bottling Co. Consolidated

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)

In Thousands

	Common Stock	Class B Common Stock	Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance on January 2, 2005	$ 9,704	$ 3,049	$ 98,255	$ 40,488	$ (25,803)	$ (61,254)	$ 64,439
Comprehensive income:							
Net income				12,238			12,238
Total comprehensive income							12,238
Cash dividends paid							
Common ($.50 per share)				(3,321)			(3,321)
Class B Common ($.50 per share)				(1,220)			(1,220)
Issuance of 20,000 shares of Class B Common Stock		20	1,121				1,141
Balance on July 3, 2005	$ 9,704	$ 3,069	$ 99,376	$ 48,185	$ (25,803)	$ (61,254)	$ 73,277
Balance on January 1, 2006	$ 9,705	$ 3,068	$ 99,376	$ 54,355	$ (30,116)	$ (61,254)	$ 75,134
Comprehensive income:							
Net income				9,702			9,702
Net change in minimum pension liability adjustment, net of tax					(1,975)		(1,975)
Total comprehensive income							7,727
Cash dividends paid							
Common ($.50 per share)				(3,322)			(3,322)
Class B Common ($.50 per share)				(1,230)			(1,230)
Issuance of 20,000 shares of Class B Common Stock		20	840				860
Stock compensation expense			465				465
Balance on July 2, 2006	$ 9,705	$ 3,088	$ 100,681	$ 59,505	$ (32,091)	$ (61,254)	$ 79,634

See Accompanying Notes to Consolidated Financial Statements

Table of Contents

Coca-Cola Bottling Co. Consolidated

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

In Thousands

	First Half	
	2006	**2005**
Cash Flows from Operating Activities		
Net income	$ 9,702	$ 12,238
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	33,572	34,166
Amortization of intangibles	290	566
Deferred income taxes	1,040	4,664
Losses on sale of property, plant and equipment	543	36
Amortization of debt costs	1,328	616
Amortization of deferred gain related to terminated interest rate agreements	(843)	(839)
Stock compensation expense	465	490
Minority interest	1,705	1,961
Increase in current assets less current liabilities	(17,984)	(5,382)
Increase in other noncurrent assets	(902)	(1,377)
Increase (decrease) in other noncurrent liabilities	3,123	(8,451)
Total adjustments	22,337	26,450
Net cash provided by operating activities	32,039	38,688
Cash Flows from Investing Activities		
Additions to property, plant and equipment	(29,833)	(14,881)
Proceeds from the sale of property, plant and equipment	837	2,970
Other	(222)	
Net cash used in investing activities	(29,218)	(11,911)
Cash Flows from Financing Activities		
Payment of current portion of long-term debt	(39)	
Payment of lines of credit, net	(6,500)	(5,100)
Cash dividends paid	(4,552)	(4,541)
Principal payments on capital lease obligations	(880)	(897)
Premium on exchange of long-term debt		(15,554)
Other	513	585
Net cash used in financing activities	(11,458)	(25,507)
Net increase (decrease) in cash	(8,637)	1,270
Cash at beginning of period	39,608	8,885
Cash at end of period	$ 30,971	$ 10,155
Significant non-cash investing and financing activities:		
Issuance of Class B Common Stock in connection with stock award	$ 860	$ 1,141

Exchange of long-term debt	164,757

See Accompanying Notes to Consolidated Financial Statements

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

1. Significant Accounting Policies

The consolidated financial statements include the accounts of Coca-Cola Bottling Co. Consolidated and its majority owned subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated.

The consolidated financial statements reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results for the interim periods presented. All such adjustments are of a normal, recurring nature.

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The accounting policies followed in the presentation of interim financial results are consistent with those followed on an annual basis. These policies are presented in Note 1 to the consolidated financial statements included in the Company s Annual Report on

Form 10-K for the year ended January 1, 2006 filed with the United States Securities and Exchange Commission (SEC).

Certain prior year amounts reported in the Company s consolidated statements of operations have been conformed to current year classifications. In prior periods, the Company reported depreciation expense separately in the consolidated statements of operations. The Company began reporting depreciation expense in cost of sales and selling, delivery and administrative (S,D&A) expenses in the first quarter of 2006 (Q1 2006). The Company s results of operations for the second quarter of 2005 (Q2 2005) and the first half of 2005 (YTD 2005) have been conformed to the second quarter of 2006 (Q2 2006) and the first half of 2006 (YTD 2006) presentation. Depreciation expense in cost of sales and S,D&A expenses in Q2 2006 was $2.3 million and $14.6 million, respectively. Depreciation expense in cost of sales and S,D&A expenses in YTD 2006 was $4.6 million and $29.0 million, respectively. Depreciation expense in cost of sales and S,D&A expenses in Q2 2005 was $2.2 million and $14.8 million, respectively. Depreciation expense in cost of sales and S,D&A expenses in YTD 2005 was $4.5 million and $29.7 million, respectively.

2. Seasonality of Business

Operating results for Q2 2006 and YTD 2006 are not indicative of results that may be expected for the fiscal year ending December 31, 2006 because of business seasonality. Business seasonality results primarily from higher sales of the Company s products in the second and third quarters versus the first and fourth quarters of the fiscal year. Fixed costs, such as depreciation and interest expense, are not significantly impacted by business seasonality.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

3. Piedmont Coca-Cola Bottling Partnership

On July 2, 1993, the Company and The Coca-Cola Company formed Piedmont Coca-Cola Bottling Partnership (Piedmont) to distribute and market nonalcoholic beverages primarily in portions of North Carolina and South Carolina. The Company provides a portion of the finished products to Piedmont at cost and receives a fee for managing the business of Piedmont pursuant to a management agreement. These intercompany transactions are eliminated in the consolidated financial statements.

Minority interest as of July 2, 2006, January 1, 2006 and July 3, 2005 represents the portion of Piedmont owned by The Coca-Cola Company, which was 22.7% for all periods presented.

4. Inventories

Inventories were summarized as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005
Finished products	$ 38,216	$ 34,181	$ 31,314
Manufacturing materials	9,073	9,222	10,074
Plastic shells, pallets and other inventories	16,643	14,830	13,936
Total inventories	$ 63,932	$ 58,233	$ 55,324

5. Property, Plant and Equipment

The principal categories and estimated useful lives of property, plant and equipment were as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005	Estimated Useful Lives
Land	$ 12,605	$ 12,605	$ 12,767	
Buildings	110,854	110,208	111,644	10-50 years
Machinery and equipment	99,519	96,495	92,837	5-20 years
Transportation equipment	174,903	167,762	164,909	4-13 years
Furniture and fixtures	39,291	44,364	41,849	4-10 years
Cold drink dispensing equipment	340,836	339,330	347,576	6-13 years
Leasehold and land improvements	57,726	56,788	55,584	5-20 years
Software for internal use	33,876	32,258	29,841	3-10 years
Construction in progress	8,660	6,627	7,229	
Total property, plant and equipment, at cost	878,270	866,437	864,236	
Less: Accumulated depreciation and amortization	492,457	477,238	465,868	
Property, plant and equipment, net	$ 385,813	$ 389,199	$ 398,368	

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

6. Leased Property Under Capital Leases

Leased property under capital leases was summarized as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005	Estimated Useful Lives
Leased property under capital leases	$ 84,035	$ 84,035	$ 84,035	3-29 years
Less: Accumulated amortization	12,524	10,791	8,984	
Leased property under capital leases, net	$ 71,511	$ 73,244	$ 75,051	

As of July 2, 2006, real estate represented $71.4 million of net leased property under capital leases, of which $64.8 million were with related parties as described in Note 19 to the consolidated financial statements.

7. Franchise Rights and Goodwill

There was no change in franchise rights and goodwill in the periods presented.

8. Other Identifiable Intangible Assets

Other identifiable intangible assets were summarized as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005	Estimated Useful Lives
Other identifiable intangible assets	$ 8,703	$ 9,877	$ 9,877	1-18 years
Less: Accumulated amortization	3,717	4,823	4,508	
Other identifiable intangible assets, net	$ 4,986	$ 5,054	$ 5,369	

Other identifiable intangible assets primarily represent customer relationships.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

9. Other Accrued Liabilities

Other accrued liabilities were summarized as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005
Accrued marketing costs	$ 7,263	$ 5,578	$ 4,735
Accrued insurance costs	11,886	10,463	11,608
Accrued taxes (other than income taxes)	3,357	729	3,861
Employee benefit plan accruals	7,999	8,945	10,481
Checks and transfers yet to be presented for payment from zero balance cash account	9,117	20,530	13,248
All other accrued liabilities	12,351	13,834	17,077
Total other accrued liabilities	$ 51,973	$ 60,079	$ 61,010

10. Debt

Debt was summarized as follows:

In Thousands	Maturity	Interest Rate	Interest Paid	July 2, 2006	Jan. 1, 2006	July 3, 2005
Lines of Credit	2006		Varies		$ 6,500	$ 2,900
Debentures	2007	6.85%	Semi-annually	$ 100,000	100,000	100,000
Debentures	2009	7.20%	Semi-annually	57,440	57,440	57,440
Debentures	2009	6.375%	Semi-annually	119,253	119,253	127,803
Senior Notes	2012	5.00%	Semi-annually	150,000	150,000	150,000
Senior Notes	2015	5.30%	Semi-annually	100,000	100,000	100,000
Senior Notes	2016	5.00%	Semi-annually	164,757	164,757	164,757
Other notes payable	2006		Quarterly		39	39
				691,450	697,989	702,939
Less: Current portion of debt					6,539	2,939
Long-term debt				$ 691,450	$ 691,450	$ 700,000

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

10. Debt

On April 7, 2005, the Company entered into a five-year $100 million revolving credit facility ($100 million facility) replacing a $125 million revolving credit facility scheduled to expire in December 2005. On July 2, 2006, there were no amounts outstanding under this $100 million facility. The $100 million facility matures in April 2010 and includes an option to extend the term for an additional year at the discretion of the participating banks and bears interest at a floating base rate or a floating rate of LIBOR plus an interest rate spread of .375%. In addition, there is a facility fee of .125% required for this $100 million facility. Both the interest rate spread and the facility fee are determined from a commonly-used pricing grid based on the Company s long-term senior unsecured debt rating. The Company s $100 million facility contains two financial covenants related to ratio requirements for interest coverage and long-term debt to cash flow, each as defined in the credit agreement. These covenants do not currently, and the Company does not anticipate they will, restrict its liquidity or capital resources.

The Company borrows periodically under its available lines of credit. These lines of credit, in the aggregate amount of $60 million at July 2, 2006, are made available at the discretion of two participating banks at rates negotiated at the time of borrowing and may be withdrawn at any time by such banks. On July 2, 2006, there were no amounts outstanding under the lines of credit.

After taking into account all of its interest rate hedging activities, the Company had weighted average interest rates of 6.7%, 6.2% and 5.8% for its debt and capital lease obligations as of July 2, 2006, January 1, 2006 and July 3, 2005, respectively. Excluding the impact of the $1.3 million financing transaction costs related to the exchange of $164.8 million of the Company s debentures during Q2 2005, the Company s overall weighted average interest rate on its debt and capital lease obligations was 6.6% for YTD 2006 compared to 5.9% for YTD 2005. Including the impact of the $1.3 million financing transaction costs, the Company s overall weighted average interest rate for YTD 2005 was 6.2%. As of July 2, 2006, approximately 42% of the Company s debt and capital lease obligations of $769.8 million was subject to changes in short-term interest rates. The Company considers all floating rate debt and fixed rate debt with a maturity of less than one year to be subject to changes in short-term interest rates.

The Company s public debt is not subject to financial covenants but does limit the incurrence of certain liens and encumbrances as well as the incurrence of indebtedness by the Company s subsidiaries in excess of certain amounts.

All of the outstanding long-term debt has been issued by the Company with none being issued by any of the Company s subsidiaries. There are no guarantees of the Company s debt.

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

11. Derivative Financial Instruments

The Company periodically uses interest rate hedging products to mitigate risk from interest rate fluctuations. The Company has historically altered its fixed/floating rate mix based upon anticipated cash flows from operations relative to the Company s debt level and the potential impact of changes in interest rates on the Company s overall financial condition. Sensitivity analyses are performed to review the impact on the Company s financial position and coverage of various interest rate movements. The Company does not use derivative financial instruments for trading purposes nor does it use leveraged financial instruments. All of the Company s outstanding interest rate swap agreements are LIBOR-based.

Derivative financial instruments were summarized as follows:

	July 2, 2006		January 1, 2006		July 3, 2005	
In Thousands	**Notional Amount**	**Remaining Term**	**Notional Amount**	**Remaining Term**	**Notional Amount**	**Remaining Term**
Interest rate swap agreement - floating	$ 25,000	1.42 years	$ 25,000	1.92 years	$ 25,000	2.42 years
Interest rate swap agreement - floating	25,000	1.42 years	25,000	1.92 years	25,000	2.42 years
Interest rate swap agreement - floating	50,000	2.92 years	50,000	3.42 years	50,000	3.92 years
Interest rate swap agreement - floating	50,000	1.42 years	50,000	1.92 years	50,000	2.42 years
Interest rate swap agreement - floating	50,000	3.08 years	50,000	3.58 years	50,000	4.08 years
Interest rate swap agreement - floating	50,000	6.42 years	50,000	6.92 years	50,000	7.42 years

The Company had six interest rate swap agreements as of July 2, 2006 with varying terms that effectively converted $250 million of the Company s fixed rate debt to floating rate debt. All of the interest rate swap agreements have been accounted for as fair value hedges.

The counterparties to these contractual arrangements are major financial institutions with which the Company also has other financial relationships. The Company uses several different financial institutions for interest rate derivative contracts to minimize the concentration of credit risk. While the Company is exposed to credit loss in the event of nonperformance by these counterparties, the Company does not anticipate nonperformance by these parties. The Company has master agreements with the counterparties to its derivative financial agreements that provide for net settlement of the derivative transactions.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

12. Fair Values of Financial Instruments

The following methods and assumptions were used by the Company in estimating the fair values of its financial instruments:

Cash and Cash Equivalents, Accounts Receivable and Accounts Payable

The fair values of cash and cash equivalents, accounts receivable and accounts payable approximate carrying values due to the short maturity of these financial instruments.

Public Debt Securities

The fair values of the Company s public debt securities are based on estimated market prices.

Non-Public Variable Rate Debt

The carrying amounts of the Company s variable rate borrowings approximate their fair values.

Non-Public Fixed Rate Long-Term Debt

The fair values of the Company s other notes payable are estimated using discounted cash flow analyses based on the Company s current borrowing rates for similar types of borrowing arrangements.

Derivative Financial Instruments

The fair values for the Company s interest rate swap agreements are based on current settlement values.

Letters of Credit

The fair values of the Company s letters of credit are based on the notional amounts of the instruments. These letters of credit primarily relate to the Company s property and casualty insurance programs.

The carrying amounts and fair values of the Company s debt, derivative financial instruments and letters of credit were as follows:

	July 2, 2006		January 1, 2006		July 3, 2005	
In Thousands	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**
Public debt securities	$ 691,450	$ 664,867	$ 691,450	$ 696,171	$ 700,000	$ 720,137
Non-public variable rate debt			6,500	6,500	2,900	2,900
Non-public fixed rate long-term debt			39	39	39	39
Interest rate swap agreements	11,693	11,693	8,118	8,118	2,855	2,855
Letters of credit		19,786		17,374		18,408

The fair values of the interest rate swap agreements at July 2, 2006, January 1, 2006 and July 3, 2005 represent the estimated amounts the Company would have paid upon termination of these agreements, which were the then current settlement values.

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

13. Other Liabilities

Other liabilities were summarized as follows:

In Thousands	July 2, 2006	Jan. 1, 2006	July 3, 2005
Accruals for executive benefit plans	$ 67,049	$ 61,674	$ 58,887
All other liabilities	22,409	23,514	20,048
Total other liabilities	$ 89,458	$ 85,188	$ 78,935

14. Commitments and Contingencies

The Company is a member of South Atlantic Canners, Inc. (SAC), a manufacturing cooperative from which it is obligated to purchase 17.5 million cases of finished product on an annual basis through May 2014. The Company is also a member of Southeastern Container (Southeastern), a plastic bottle manufacturing cooperative, from which it is obligated to purchase at least 80% of its requirements of plastic bottles for certain designated territories. See Note 19 to the consolidated financial statements for additional information concerning SAC and Southeastern.

The Company guarantees a portion of SAC s and Southeastern s debt and lease obligations. The amounts guaranteed were $44.7 million, $41.4 million and $44.4 million as of July 2, 2006, January 1, 2006 and July 3, 2005, respectively. The Company has not recorded any liability associated with these guarantees. The Company holds no assets as collateral against these guarantees and no contractual recourse exists that would enable the Company to recover amounts guaranteed. The guarantees relate to the debt and lease obligations of SAC and Southeastern, which resulted primarily from the purchase of production equipment and facilities. These guarantees expire at various times through 2021. The members of both cooperatives consist solely of Coca-Cola bottlers. The Company does not anticipate either of these cooperatives will fail to fulfill their commitments under these agreements. The Company further believes each of these cooperatives has sufficient assets, including production equipment, facilities and working capital, and the ability to adjust the selling prices of their products to adequately mitigate the risk of material loss.

The Company has identified SAC and Southeastern as variable interest entities and has determined it is not the primary beneficiary of either of the cooperatives. The Company s variable interest in these cooperatives includes an equity ownership in each of the entities and the guarantee of certain indebtedness. As of July 2, 2006, SAC had total assets of approximately $41 million and total debt of approximately $17 million. SAC had total revenue for YTD 2006 of approximately $91 million. As of July 2, 2006, Southeastern had total assets of approximately $379 million and total debt of approximately $285 million. Southeastern had total revenue for YTD 2006 of approximately $287 million. In the event either of these cooperatives fails to fulfill its commitments under the related debt and lease obligations, the Company would be responsible for payments to the lenders up to the level of the guarantees. If these cooperatives had borrowed up to

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

14. Commitments and Contingencies

their borrowing capacity, the Company s maximum exposure under these guarantees on July 2, 2006 would have been $57.4 million and the Company s maximum total exposure including its equity investment would have been $36.5 million for SAC and $29.7 million for Southeastern. The Company has been purchasing plastic bottles and finished products from these cooperatives for more than ten years.

Effective March 1, 2006, Southeastern requires its members to pay a capital deposit of $3 per thousand bottles purchased. The Company has paid $1.3 million in conjunction with this capital deposit.

The Company has standby letters of credit, primarily related to its property and casualty insurance programs. On July 2, 2006, these letters of credit totaled $19.8 million.

The Company participates in long-term marketing contractual arrangements with certain prestige properties, athletic venues and other locations. The future payments related to these contractual arrangements as of July 2, 2006 amounted to $29.5 million and expire at various dates through 2014.

On February 14, 2006, forty-eight Coca-Cola bottler plaintiffs filed suit in the United States District Court for the Western District of Missouri against The Coca-Cola Company and Coca-Cola Enterprises Inc. (CCE). On February 24, 2006, the plaintiffs filed an amended complaint adding twelve bottlers as plaintiffs. In the lawsuit, *Ozarks Coca-Cola/Dr Pepper Bottling Company, et al. vs. The Coca-Cola Company and Coca-Cola Enterprises Inc.,* the bottler plaintiffs purport to bring claims for breach of contract and breach of duty and other related claims arising out of CCE s plan to offer warehouse delivery of POWERade to Wal-Mart Stores, Inc. (Wal-Mart) within CCE s territory. The bottler plaintiffs seek preliminary and permanent injunctive relief prohibiting the warehouse delivery of POWERade and unspecified compensatory and punitive damages. On March 3, 2006, the Company filed a motion seeking permission to intervene in the lawsuit for the limited purpose of opposing the preliminary and permanent injunctive relief sought by the bottler plaintiffs. The Company seeks permission to intervene because it also plans to offer warehouse delivery of POWERade to Wal-Mart within the Company s territory and therefore opposes the relief requested by the bottler plaintiffs. The plaintiffs have opposed the Company s request to intervene. The Coca-Cola Company and CCE both support the Company s request. On March 17, 2006, the Missouri District Court granted The Coca-Cola Company s and CCE s request for an order transferring the case, for the convenience of the parties, to the United States District Court for the Northern District of Georgia. None of the plaintiffs seek to recover damages from the Company. In April, warehouse delivery of POWERade commenced in the Company s exclusive territories. On April 21, 2006, the plaintiffs requested the Court defer any hearing or further briefing on their motion for preliminary injunctive relief. The parties to the lawsuit are currently engaged in the discovery process. The Court has not ruled on the Company s motion to intervene.

The Company is involved in other claims and legal proceedings which have arisen in the ordinary course of its business. Although it is difficult to predict the ultimate outcome of these claims and legal

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

14. Commitments and Contingencies

proceedings, management believes the ultimate disposition of these matters will not have a material adverse effect on the financial condition, cash flows or results of operations of the Company. No material amount of loss in excess of recorded amounts is believed to be reasonably possible as a result of these other claims and legal proceedings.

The Company s tax filings are subject to audit by tax authorities in jurisdictions where it conducts business. These audits may result in assessments of additional taxes subsequently resolved with the authorities or potentially through the courts. Management believes the Company has adequately provided for any ultimate amounts likely to result from these audits; however, final assessments, if any, could be different than the amounts recorded in the consolidated financial statements.

15. Income Taxes

The Company s effective income tax rate for YTD 2006 and YTD 2005 was 41.6% and 41.9%, respectively. The following table provides a reconciliation of income tax expense at the statutory federal rate to actual income tax expense.

	First Half	
In Thousands	**2006**	**2005**
Statutory expense	$ 5,816	$ 7,370
State income taxes, net of federal benefit	761	881
Impact of state tax audit and updated assessment of state income tax liability		287
Meals and entertainment	321	350
Other, net	19	(69)
Income tax expense	$ 6,917	$ 8,819

The Company s income tax assets and liabilities are subject to adjustment in future periods based on the Company s ongoing evaluations of such assets and liabilities and new information that becomes available to the Company.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

16. Accumulated Other Comprehensive Loss

The reconciliation of the components of accumulated other comprehensive loss was as follows:

In Thousands	Minimum Pension Liability Adjustment	Total
Balance as of January 2, 2005 and July 3, 2005	$ (25,803)	$ (25,803)
Balance as of January 1, 2006	$ (30,116)	$ (30,116)
Additional minimum pension liability adjustment, net of tax	(1,975)	(1,975)
Balance as of July 2, 2006	$ (32,091)	$ (32,091)

A summary of the components of accumulated other comprehensive loss was as follows:

In Thousands	Before-Tax Amount	Income Tax Effect	After-Tax Amount
First Half of 2006			
Net change in minimum pension liability adjustment	$ (3,256)	$ 1,281	$ (1,975)
Other comprehensive loss	$ (3,256)	$ 1,281	$ (1,975)
First Half of 2005			
Other comprehensive loss	$	$	$

On February 22, 2006, the Board of Directors of the Company approved an amendment to the principal Company-sponsored pension plan to cease further benefit accruals under the plan effective June 30, 2006. An actuarial valuation of the principal Company-sponsored pension plan was performed by an independent actuary with a measurement date of February 28, 2006 and an adjustment to other comprehensive loss resulted from this valuation.

17. Capital Transactions

On May 12, 1999, the stockholders of the Company approved a restricted stock award for J. Frank Harrison, III, the Company s Chairman of the Board of Directors and Chief Executive Officer, consisting of 200,000 shares of the Company s Class B Common Stock. The fair value of the restricted stock award, when approved, was approximately $11.7 million based on the market price of the Common Stock on the effective date of the award. The award provides the shares of restricted

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

17. Capital Transactions

stock vest at the rate of 20,000 shares per year over a ten-year period. The vesting of each annual installment is contingent upon the Company achieving at least 80% of the overall goal achievement factor in the Company s Annual Bonus Plan. The restricted stock award does not entitle Mr. Harrison, III to participate in dividend or voting rights until each installment has vested and the shares are issued.

On February 23, 2005, the Compensation Committee of the Board of Directors determined 20,000 shares of restricted Class B Common Stock vested and should be issued pursuant to the performance-based award discussed above to Mr. Harrison, III in connection with his services as Chairman of the Board of Directors and Chief Executive Officer of the Company for the fiscal year ended January 2, 2005. On February 22, 2006, the Compensation Committee determined an additional 20,000 shares of restricted Class B Common Stock vested to Mr. Harrison, III in connection with his services for the fiscal year ended January 1, 2006.

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment, on January 2, 2006. The Company applied the modified prospective transition method and prior periods were not restated. The Company s only share based compensation is the restricted stock award to Mr. Harrison, III as described above. Each annual 20,000 share tranche has an independent performance requirement as it is not established until the Company s Annual Bonus Plan targets are approved each year by the Company s Board of Directors. As a result, each 20,000 share tranche is considered to have its own service inception date, grant-date fair value and requisite service period.

The Company s Annual Bonus Plan targets, which establish the performance requirement for the restricted stock award in 2006, were approved by the Board of Directors in Q1 2006 and the Company recorded the 20,000 share award at the grant-date price of $46.45 per share. Total stock compensation expense will be approximately $929,000 over the one-year service period, of which $465,000 was recognized in YTD 2006. In addition, the Company reimburses Mr. Harrison, III for income taxes to be paid on the shares if the performance requirement is met and the shares are issued. The Company accrues the estimated cost of the income tax reimbursement over the one-year service period.

Prior to the adoption of this statement, the Company accrued compensation cost over the course of the one-year service period with the final cost based upon the end of the period stock price. Total compensation expense, including income tax reimbursements to Mr. Harrison, III, for the restricted stock award, net of tax effect, was $475,000 in YTD 2006 and would have been $542,000, net of tax effect, in YTD 2005 under the new standard. Actual expense recorded in YTD 2005, net of tax effect, was $499,000. Pro forma net income would have been $12.2 million in YTD 2005 which was the net income reported for YTD 2005. Pro forma diluted earnings per share for YTD 2005 was $1.34 compared to actual diluted earnings per share of $1.35.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

17. Capital Transactions

The increase in the number of shares of Class B Common Stock outstanding in YTD 2006 and YTD 2005 was due to the issuance of 20,000 shares of Class B Common Stock related to the restricted stock award in the first quarter of each year.

The Company has two classes of common stock outstanding, Common Stock and Class B Common Stock. The Common Stock is traded on the Nasdaq Global Market^{sm} tier of The Nasdaq Stock Market, LLC® under the symbol COKE. There is no established public trading market for the Class B Common Stock. Shares of the Class B Common Stock are convertible on a share-for-share basis into shares of Common Stock at any time at the option of the holders of Class B Common Stock.

Pursuant to the Company s Certificate of Incorporation, no cash dividend or dividend of property or stock other than stock of the Company, as specifically described in the Certificate of Incorporation, may be declared and paid on the Class B Common Stock unless an equal or greater dividend is declared and paid on the Common Stock. During both YTD 2006 and YTD 2005, dividends of $.50 per share were declared and paid on both Common Stock and Class B Common Stock.

Each share of Common Stock is entitled to one vote per share at an Annual or Special Meeting of stockholders and each share of Class B Common Stock is entitled to 20 votes per share at such meetings. Except to the extent otherwise required by law, holders of the Common Stock and Class B Common Stock vote together as a single class on all matters brought before the Company s stockholders.

In the event of liquidation, there is no preference between the two classes of common stock.

18. Benefit Plans

Retirement benefits under the two Company-sponsored pension plans are based on the employee s length of service, average compensation over the five consecutive years which gives the highest average compensation and the average of the Social Security taxable wage base during the 35-year period before a participant reaches Social Security retirement age. Contributions to the plans are based on the projected unit credit actuarial funding method and are limited to the amounts currently deductible for income tax purposes.

On February 22, 2006, the Board of Directors of the Company approved an amendment to the principal Company-sponsored pension plan to cease further benefit accruals under the plan effective June 30, 2006. The plan amendment was accounted for as a plan curtailment under SFAS No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits (as amended). The curtailment resulted in a reduction of the Company s projected benefit obligation which was offset against the Company s unrecognized net loss.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

18. Benefit Plans

As a result of the curtailment, the impact on net income and the effect on pension expense prior to the effective date of June 30, 2006 was immaterial. Periodic pension expense will be reduced beginning in the third quarter of 2006 as the Company will no longer accrue current service cost.

The components of net periodic pension cost were as follows:

	Second Quarter		First Half	
In Thousands	**2006**	**2005**	**2006**	**2005**
Service cost	$ 3,304	$ 1,747	$ 5,348	$ 3,494
Interest cost	2,512	2,529	5,354	5,058
Expected return on plan assets	(3,048)	(2,672)	(6,009)	(5,344)
Amortization of prior service cost	6	6	12	12
Recognized net actuarial loss	961	1,335	2,520	2,670
Net periodic pension cost	$ 3,735	$ 2,945	$ 7,225	$ 5,890

The Company did not make cash contributions to its pension plans during YTD 2006.

The Company provides postretirement benefits for a portion of its current employees. The Company recognizes the cost of postretirement benefits, which consist principally of medical benefits, during employees periods of active service. The Company does not pre-fund these benefits and has the right to modify or terminate certain of these benefits in the future. In October 2005, the Company announced changes to certain provisions of its postretirement health care plan that reduced future benefit obligations to eligible participants. Due to the changes announced, the Company s postretirement benefit expense was reduced beginning in Q1 2006.

The components of net periodic postretirement benefit cost were as follows:

	Second Quarter		First Half	
In Thousands	**2006**	**2005**	**2006**	**2005**
Service cost	$ 83	$ 172	$ 166	$ 344
Interest cost	557	781	1,114	1,562
Amortization of unrecognized transitional assets	(6)	(6)	(12)	(12)
Recognized net actuarial loss	339	252	678	504
Amortization of prior service cost	(446)	(68)	(892)	(136)
Net periodic postretirement benefit cost	$ 527	$ 1,131	$ 1,054	$ 2,262

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

18. Benefit Plans

In conjunction with the change to the principal Company-sponsored pension plan discussed above, the Company s Board of Directors also approved an amendment to the 401(k) Savings Plan to increase the Company s matching contribution under the 401(k) Savings Plan effective January 1, 2007. The amendment to the 401(k) Savings Plan will provide for fully vested matching contributions equal to one hundred percent of a participant s elective deferrals to the 401(k) Savings Plan up to a maximum of 5% of a participant s eligible compensation.

19. Related Party Transactions

The Company s business consists primarily of the production, marketing and distribution of nonalcoholic beverages of The Coca-Cola Company, which is the sole owner of the secret formulas under which the primary components (either concentrate or syrup) of its soft drink products are manufactured. As of July 2, 2006, The Coca-Cola Company had a 27.3% interest in the Company s total outstanding Common Stock and Class B Common Stock on a combined basis.

The following table summarizes the significant transactions between the Company and The Coca-Cola Company:

	First Half	
In Millions	**2006**	**2005**
Payments by the Company for concentrate, syrup, sweetener and other purchases	$ 173.5	$ 161.2
Marketing funding support payments to the Company	12.0	10.4
Payments net of marketing funding support	$ 161.5	$ 150.8
Payments by the Company for customer marketing programs	$ 24.5	$ 24.5
Payments by the Company for cold drink equipment parts	3.3	2.0
Fountain delivery and equipment repair fees paid to the Company	4.5	3.9
Presence marketing funding support provided by The Coca-Cola Company on the Company s behalf	3.2	3.1
Sales of energy products to The Coca-Cola Company	19.2	12.0

The Company received proceeds in 2005 as a result of a settlement of a class action lawsuit known as *In re: High Fructose Corn Syrup Antitrust Litigation Master File No. 95-1477* in the United States District Court for the Central District of Illinois. The lawsuit related to purchases of high fructose corn syrup by several companies, including The Coca-Cola Company and its subsidiaries, The Coca-Cola Bottlers Association and various Coca-Cola bottlers, during the period from July 1, 1991 to June 30, 1995. The Company recognized $6.4 million of proceeds received in Q2 2005 and $.6 million of proceeds received in the fourth quarter of 2005 as a reduction of cost of sales.

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

19. Related Party Transactions

The Company has a production arrangement with CCE to buy and sell finished products at cost. Sales to CCE under this arrangement were $30.7 million and $21.5 million in YTD 2006 and YTD 2005, respectively. Purchases from CCE under this arrangement were $7.6 million and $9.2 million in YTD 2006 and YTD 2005, respectively. The Coca-Cola Company has significant equity interests in the Company and CCE. As of July 2, 2006, CCE held 10.5% of the Company s outstanding Common Stock but held no shares of the Company s Class B Common Stock, giving CCE a 7.6% interest in the Company s total outstanding Common Stock and Class B Common Stock on a combined basis.

Along with all other Coca-Cola bottlers in the United States, the Company is a member in Coca-Cola Bottlers Sales and Services Company, LLC (CCBSS), which was formed in 2003 for the purposes of facilitating various procurement functions and distributing certain specified beverage products of The Coca-Cola Company with the intention of enhancing the efficiency and competitiveness of the Coca-Cola bottling system in the United States. CCBSS negotiates the procurement for the majority of the Company s raw materials (excluding concentrate). CCE is also a member of CCBSS.

The Company provides a portion of the finished products for Piedmont at cost and receives a fee for managing the operations of Piedmont pursuant to a management agreement. The Company sold product at cost to Piedmont during YTD 2006 and YTD 2005 totaling $37.8 million and $33.7 million, respectively. The Company received $10.8 million and $10.3 million for management services pursuant to its management agreement with Piedmont for YTD 2006 and YTD 2005, respectively. The Company provides financing for Piedmont at the Company s average cost of funds plus 0.50%. As of July 2, 2006, the Company had loaned $100.2 million to Piedmont. The loan was amended on August 25, 2005 to extend the maturity date from December 31, 2005 to December 31, 2010 on terms comparable to the previous loan. The Company also subleases various fleet and vending equipment to Piedmont at cost. These sublease rentals were $4.1 million and $4.3 million in YTD 2006 and YTD 2005, respectively. All significant intercompany accounts and transactions between the Company and Piedmont have been eliminated.

The Company is a shareholder in two cooperatives from which it purchases substantially all its requirements for plastic bottles. Net purchases from these cooperatives were $34.6 million and $35.2 million in YTD 2006 and YTD 2005, respectively. In connection with its participation in one of these cooperatives, the Company has guaranteed a portion of the cooperative s debt. Such guarantee was $23.8 million as of July 2, 2006.

The Company is a member of SAC, a manufacturing cooperative. SAC sells finished products to the Company and Piedmont at cost. Purchases from SAC by the Company and Piedmont for finished products were $69.9 million and $59.8 million in YTD 2006 and YTD 2005, respectively. The Company also manages the operations of SAC pursuant to a management agreement. Management fees earned from SAC were $.8 million in both YTD 2006 and YTD 2005. The Company has also guaranteed a portion of debt for SAC. Such guarantee was $20.9 million as of July 2, 2006.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

19. Related Party Transactions

The Company leases from Harrison Limited Partnership One (HLP), the Snyder Production Center and an adjacent sales facility, which are located in Charlotte, North Carolina. HLP is directly and indirectly owned by trusts of which J. Frank Harrison, III, Chairman of the Board of Directors and Chief Executive Officer of the Company, and Deborah S. Harrison, a director of the Company, are trustees and beneficiaries. The principal balance outstanding under this capital lease as of July 2, 2006 was $39.4 million. Rental payments related to this lease were $1.9 million and $1.6 million in YTD 2006 and YTD 2005, respectively.

The Company leases from Beacon Investment Corporation (Beacon), the Company s headquarters office facility. Beacon s sole shareholder is J. Frank Harrison, III. The principal balance outstanding under this capital lease as of July 2, 2006 was $31.0 million. Rental payments related to this lease were $1.9 million and $1.6 million in YTD 2006 and YTD 2005, respectively.

In March 2005, the Company entered into a two-year consulting agreement with Robert D. Pettus, Jr. Mr. Pettus served as an officer and employee of the Company in various capacities from 1984 until his retirement in 2005 and is currently the Vice Chairman of the Board of Directors of the Company. Mr. Pettus receives $350,000 per year plus additional benefits during the term of this consulting agreement.

In June 2005, the Company entered into a two-year consulting agreement with David V. Singer. Mr. Singer served the Company as Executive Vice President and Chief Financial Officer until his resignation on May 11, 2005. Under the consulting agreement, the Company agreed to waive the 50% reduction in Mr. Singer s accrued benefits under the Company s Officer Retention Plan due to the termination of his employment before age 55 and Mr. Singer agreed to certain non-compete restrictions for a five-year period following his resignation.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

20. Net Sales by Product Category

Net sales by product category were as follows:

In Thousands	Second Quarter 2006	Second Quarter 2005	First Half 2006	First Half 2005
Product Category				
Bottle/can sales:				
Carbonated soft drinks (including energy drinks)	$ 273,185	$ 261,412	$ 512,399	$ 493,104
Noncarbonated beverages	51,721	45,544	90,639	78,810
Total bottle/can sales	324,906	306,956	603,038	571,914
Other sales:				
Sales to other bottlers	41,719	34,791	79,083	61,946
Post mix	19,999	19,477	37,682	36,549
Total other sales	61,718	54,268	116,765	98,495
Total net sales	$ 386,624	$ 361,224	$ 719,803	$ 670,409

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

21. Earnings Per Share/SEC Comment Letter

The following table sets forth the computation of basic net income per share and diluted net income per share:

	Second Quarter		First Half	
In Thousands (Except Per Share Data)	**2006**	**2005**	**2006**	**2005**
Numerator:				
Numerator for basic net income per share and diluted net income per share	$ 8,887	$ 11,519	$ 9,702	$ 12,238
Denominator:				
Denominator for basic net income per share weighted average common shares	9,103	9,083	9,103	9,083
Effect of restricted stock award	20		15	
Denominator for diluted net income per share weighted average common shares	9,123	9,083	9,118	9,083
Basic net income per share	$ .98	$ 1.27	$ 1.07	$ 1.35
Diluted net income per share	$ .97	$ 1.27	$ 1.06	$ 1.35

The Company recently received a comment letter from the staff of the Division of Corporation Finance of the SEC regarding its annual report on Form 10-K for the fiscal year ended January 1, 2006. The Company currently has an unresolved comment relating to its calculation and presentation of basic net income per share for its Common Stock and Class B Common Stock with respect to Emerging Issues Task Force Issue 03-6, Participating Securities and the Two-Class Method under FASB Statement No. 128. The Company is in the process of responding to this comment and assessing the impact, if any, of the resolution of the comment on the Company s consolidated financial statements for the fiscal quarter ended July 2, 2006 as well as any prior periods.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

22. Risks and Uncertainties

Approximately 90% of the Company s bottle/can volume to retail customers is from sales of products of The Coca-Cola Company, which is the sole supplier of the concentrates or syrups required to manufacture these products. Approximately 10% of the Company s bottle/can volume to retail customers is from sales of products of other beverage companies. The Company has bottling contracts which have various requirements. Failure to meet the requirements of these bottling contracts could result in the loss of distribution rights for the respective products.

The Company s products are sold and distributed directly by its employees to retail stores and other outlets. During YTD 2006, 68% of the Company s bottle/can volume to retail customers was product sold for future consumption. The remaining 32% of the Company s bottle/can volume to retail customers was product sold for immediate consumption. The Company s largest customers, Wal-Mart and Food Lion, LLC, accounted for approximately 15% and 12%, respectively, of the Company s total bottle/can volume to retail customers during YTD 2006. Wal-Mart accounted for approximately 11% of the Company s total net sales during YTD 2006.

The Company obtains the majority of its aluminum cans from one domestic supplier. The Company currently obtains all of its plastic bottles from two domestic cooperatives.

Certain liabilities of the Company are subject to risk of changes in both long-term and short-term interest rates. These liabilities include floating rate debt, leases with payments determined on floating interest rates, postretirement benefit obligations and the Company s pension liabilities.

Approximately 7% of the Company s labor force is currently covered by collective bargaining agreements. One collective bargaining contract covering less than .5% of the Company s employees will expire in the third quarter of 2006.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

23. Supplemental Disclosures of Cash Flow Information

Changes in current assets and current liabilities affecting cash were as follows:

	First Half	
In Thousands	**2006**	**2005**
Accounts receivable, trade, net	$ (12,164)	$ (18,604)
Accounts receivable from The Coca-Cola Company	(7,990)	1,723
Accounts receivable, other	(2,097)	(253)
Inventories	(5,699)	(6,438)
Prepaid expenses and other current assets	(7,038)	(3,293)
Accounts payable, trade	5,557	4,079
Accounts payable to The Coca-Cola Company	19,179	11,062
Other accrued liabilities	(2,229)	14,426
Accrued compensation	(5,036)	(2,189)
Accrued interest payable	(467)	(5,895)
Increase in current assets less current liabilities	$ (17,984)	$ (5,382)

24. New Accounting Pronouncements

Recently Adopted Pronouncements

In November 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4. This Statement clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage) and was effective for fiscal years beginning after June 15, 2005. The adoption of this Statement in Q1 2006 did not have a material impact on the Company s consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), Share-Based Payment. This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation and was effective as of the beginning of Q1 2006. The Statement requires public companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the grant-date fair value of the award. The adoption of this Statement did not have a material impact on the Company s consolidated financial statements. See Note 17 to the consolidated financial statements for additional information.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement requires retrospective application to prior period financial statements of a voluntary change in accounting principle unless it is impracticable and is effective for fiscal years beginning after December 15, 2005.

Table of Contents

Coca-Cola Bottling Co. Consolidated

Notes to Consolidated Financial Statements (Unaudited)

24. New Accounting Pronouncements

Previously, most voluntary changes in accounting principle were recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle.

In September 2005, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 04-13, Accounting for Purchases and Sales of Inventory with the Same Counterparty (EITF 04-13). EITF 04-13 addresses the circumstances under which two or more inventory purchase and sales transactions with the same counterparty should be viewed as a single exchange and the circumstances under which nonmonetary exchanges of inventory within the same line of business should be recognized at fair value. EITF 04-13 was effective for new arrangements and modifications or renewals of existing arrangements for the first interim reporting period beginning after March 15, 2006. The adoption of this EITF in Q2 2006 did not have a material impact on the Company s consolidated financial statements.

Recently Issued Pronouncements

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments an amendment of SFAS No. 133 and 140. This Statement simplifies accounting for certain hybrid financial instruments, eliminates the interim guidance in Statement 133 Implementation Issue No. D1, Application of Statement 133 to Beneficial Interest in Securitized Financial Assets, and eliminates a restriction of the passive derivative instruments that a qualifying special-purpose entity may hold. The Statement is effective for fiscal years beginning after September 15, 2006. The adoption of this Statement is not anticipated to have a material impact on the Company s consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes. This Interpretation clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The Interpretation is effective for fiscal years beginning after December 15, 2006. The Company is in the process of determining the impact of this Interpretation on the Company s consolidated financial statements.

Table of Contents

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

The following Management s Discussion and Analysis of Financial Condition and Results of Operations (M,D&A) should be read in conjunction with the Company s consolidated financial statements and the accompanying notes to consolidated financial statements. M,D&A includes the following sections:

United States Securities and Exchange Commission (SEC) Comment Letter.

Our Business and the Nonalcoholic Beverage Industry a general description of the Company s business and the nonalcoholic beverage industry.

Areas of Emphasis a summary of the Company s key priorities for 2006 and the next several years.

Overview of Operations and Financial Condition a summary of key information concerning the financial results for the second quarter of 2006 (Q2 2006) and the first half of 2006 (YTD 2006) and changes from the second quarter of 2005 (Q2 2005) and the first half of 2005 (YTD 2005).

Discussion of Critical Accounting Policies and New Accounting Pronouncements a discussion of accounting policies important to the portrayal of the Company s financial condition and results of operations and that require critical judgments and estimates and the anticipated impact of new accounting pronouncements.

Results of Operations an analysis of the Company s results of operations for Q2 2006 and YTD 2006 compared to Q2 2005 and YTD 2005.

Financial Condition an analysis of the Company s financial condition as of the end of Q2 2006 compared to year-end 2005 and the end of Q2 2005.

Liquidity and Capital Resources an analysis of capital resources, cash sources and uses, investing activities, financing activities, off-balance sheet arrangements, aggregate contractual obligations and interest rate hedging.

Cautionary Information Regarding Forward-Looking Statements.

The consolidated statements of operations and consolidated statements of cash flows for the six months ended July 2, 2006 and July 3, 2005 and the consolidated balance sheets at July 2, 2006, January 1, 2006 and July 3, 2005 include the consolidated operations of the Company and its majority-owned subsidiaries including Piedmont Coca-Cola Bottling Partnership (Piedmont). Minority interest consists of The Coca-Cola Company s interest in Piedmont, which was 22.7% for all periods presented.

SEC Comment Letter

The Company recently received a comment letter from the staff of the Division of Corporation Finance of the SEC regarding its annual report on Form 10-K for the fiscal year ended January 1, 2006. The Company currently has an unresolved comment relating to its calculation and presentation of basic net income per share for its Common Stock and Class B Common Stock with respect to Emerging Issues Task Force Issue 03-6, Participating Securities and the Two-Class Method under FASB Statement No. 128 (EITF 03-6). The Company is in the process of responding to this comment.

EITF 03-6 requires the allocation of undistributed earnings to each class of common stock based on the participation rights of each class. The Company has historically paid dividends to each class of common stock at the same rate and, as a result, has allocated both distributed and undistributed earnings evenly to each class of common stock in its calculation of basic net income per share. If the Company was required to change its application of EITF 03-6 and the manner in which it calculates basic net income per share, it would be required to allocate to (a) Class B Common Stock only those earnings actually distributed to the holders of the Class B Common Stock and (b) Common Stock both those earnings actually distributed to the holders of Common Stock as well as all other undistributed earnings. If the Company is required to change its application of EITF 03-6 and allocate earnings to its classes of common stock in such an uneven manner, the estimated impact on Q2 2006 and previous periods would have been as set forth below under the heading Uneven Allocation. Any change in the application of EITF 03-6 as it relates to the calculation of basic net income per share would not result in any change in net income or diluted net income per share.

Upon the resolution of the SEC comment letter, the Company will assess the impact, if any, of a change in the calculation and presentation of basic net income per share on the internal controls over financial reporting.

In Thousands (Except Per Share Data)	Q2 2006 Even Allocation	Q2 2006 Uneven Allocation	Q2 2005 Even Allocation	Q2 2005 Uneven Allocation
Numerator:				
Net income	$ 8,887	$ 8,887	$ 11,519	$ 11,519
Less - dividends on:				
Common Stock	1,662	1,662	1,660	1,660
Class B Common Stock	615	615	610	610
Undistributed earnings	$ 6,610	$ 6,610	$ 9,249	$ 9,249
Common Stock Numerator:				
Undistributed earnings	$ 4,824	$ 6,610	$ 6,764	$ 9,249
Dividends on Common Stock	1,662	1,662	1,660	1,660
Basic - Common Stock numerator	$ 6,486	$ 8,272	$ 8,424	$ 10,909
Class B Common Stock Numerator:				
Undistributed earnings	$ 1,786	$	$ 2,485	$
Dividends on Class B Common Stock	615	615	610	610
Basic - Class B Common Stock numerator	$ 2,401	$ 615	$ 3,095	$ 610
Denominator:				
Basic - Common Stock denominator	6,643	6,643	6,643	6,643
Basic - Class B Common Stock denominator	2,460	2,460	2,440	2,440
Diluted - denominator	9,123	9,123	9,083	9,083
Net income per share:				
Basic - Common Stock	$ 0.98	$ 1.25	$ 1.27	$ 1.64
Basic - Class B Common Stock	$ 0.98	$ 0.25	$ 1.27	$ 0.25
Diluted	$ 0.97	$ 0.97	$ 1.27	$ 1.27

In Thousands (Except Per Share Data)	YTD 2006 Even Allocation	YTD 2006 Uneven Allocation	YTD 2005 Even Allocation	YTD 2005 Uneven Allocation
Numerator:				
Net income	$ 9,702	$ 9,702	$ 12,238	$ 12,238
Less - dividends on:				
Common Stock	3,322	3,322	3,321	3,321
Class B Common Stock	1,230	1,230	1,220	1,220
Undistributed earnings	$ 5,150	$ 5,150	$ 7,697	$ 7,697
Common Stock Numerator:				
Undistributed earnings	$ 3,758	$ 5,150	$ 5,629	$ 7,697
Dividends on Common Stock	3,322	3,322	3,321	3,321
Basic - Common Stock numerator	$ 7,080	$ 8,472	$ 8,950	$ 11,018
Class B Common Stock Numerator:				

Undistributed earnings	$ 1,392	$	$ 2,068	$
Dividends on Class B Common Stock	1,230	1,230	1,220	1,220
Basic - Class B Common Stock numerator	$ 2,622	$ 1,230	$ 3,288	$ 1,220
Denominator:				
Basic - Common Stock denominator	6,643	6,643	6,643	6,643
Basic - Class B Common Stock denominator	2,460	2,460	2,440	2,440
Diluted -denominator	9,118	9,118	9,083	9,083
Net income per share:				
Basic - Common Stock	$ 1.07	$ 1.28	$ 1.35	$ 1.66
Basic - Class B Common Stock	$ 1.07	$ 0.50	$ 1.35	$ 0.50
Diluted	$ 1.06	$ 1.06	$ 1.35	$ 1.35

In Thousands (Except Per Share Data)	Q1 2006 Even Allocation	Q1 2006 Uneven Allocation	Q1 2005 Even Allocation	Q1 2005 Uneven Allocation
Numerator:				
Net income	$ 815	$ 815	$ 719	$ 719
Less - dividends on:				
Common Stock	1,660	1,660	1,661	1,661
Class B Common Stock	615	615	610	610
Undistributed earnings	$ (1,460)	$ (1,460)	$ (1,552)	$ (1,552)
Common Stock Numerator:				
Undistributed earnings	$ (1,066)	$ (1,460)	$ (1,135)	$ (1,552)
Dividends on Common Stock	1,660	1,660	1,661	1,661
Basic - Common Stock numerator	$ 594	$ 200	$ 526	$ 109
Class B Common Stock Numerator:				
Undistributed earnings	$ (394)	$	$ (417)	$
Dividends on Class B Common Stock	615	615	610	610
Basic - Class B Common Stock numerator	$ 221	$ 615	$ 193	$ 610
Denominator:				
Basic - Common Stock denominator	6,643	6,643	6,643	6,643
Basic - Class B Common Stock denominator	2,460	2,460	2,440	2,440
Diluted -denominator	9,112	9,112	9,083	9,083
Net income per share:				
Basic - Common Stock	$ 0.09	$ 0.03	$ 0.08	$ 0.02
Basic - Class B Common Stock	$ 0.09	$ 0.25	$ 0.08	$ 0.25
Diluted	$ 0.09	$ 0.09	$ 0.08	$ 0.08

In Thousands (Except Per Share Data)	Fiscal 2005 Even Allocation	Fiscal 2005 Uneven Allocation	Fiscal 2004 Even Allocation	Fiscal 2004 Uneven Allocation	Fiscal 2003 Even Allocation	Fiscal 2003 Uneven Allocation
Numerator:						
Net income	$ 22,951	$ 22,951	$ 21,848	$ 21,848	$ 30,703	$ 30,703
Less - dividends on:						
Common Stock	6,643	6,643	6,642	6,642	6,642	6,642
Class B Common Stock	2,441	2,441	2,421	2,421	2,401	2,401
Undistributed earnings	$ 13,867	$ 13,867	$ 12,785	$ 12,785	$ 21,660	$ 21,660
Common Stock Numerator:						
Undistributed earnings	$ 10,141	$ 13,867	$ 9,370	$ 12,785	$ 15,911	$ 21,660
Dividends on Common Stock	6,643	6,643	6,642	6,642	6,642	6,642
Basic - Common Stock numerator	$ 16,784	$ 20,510	$ 16,012	$ 19,427	$ 22,553	$ 28,302
Class B Common Stock Numerator:						
Undistributed earnings	$ 3,726	$	$ 3,415	$	$ 5,749	$
Dividends on Class B Common Stock	2,441	2,441	2,421	2,421	2,401	2,401

Basic - Class B Common Stock numerator	$	6,167	$	2,441	$	5,836	$	2,421	$	8,150	$	2,401
Denominator:												
Basic - Common Stock denominator		6,643		6,643		6,643		6,643		6,643		6,643
Basic - Class B Common Stock denominator		2,440		2,440		2,420		2,420		2,400		2,400
Diluted - denominator		9,083		9,083		9,063		9,063		9,043		9,043
Net income per share:												
Basic - Common Stock	$	2.53	$	3.09	$	2.41	$	2.92	$	3.40	$	4.26
Basic - Class B Common Stock	$	2.53	$	1.00	$	2.41	$	1.00	$	3.40	$	1.00
Diluted	$	2.53	$	2.53	$	2.41	$	2.41	$	3.40	$	3.40

The even allocation of undistributed earnings is utilized in the Company s current calculation of basic net income per share and corresponds with the historical dividend participation rates for each class of common stock, i.e., on a one-for-one basis. The Company has historically presented one calculation of basic net income per share, rather than presenting a separate calculation for each class of common stock, because basic net income per share is the same for each class of common stock under the even allocation methodology. Diluted earnings per share would not be impacted as the if-converted method, which the Company has used to calculate diluted net income per share historically, is unaffected by the two-class method.

Our Business and the Nonalcoholic Beverage Industry

Coca-Cola Bottling Co. Consolidated (the Company) produces, markets and distributes nonalcoholic beverages, primarily products of The Coca-Cola Company, which include some of the most recognized and popular beverage brands in the world. The Company is the second largest bottler of products of The Coca-Cola Company in the United States, operating in eleven states primarily in the Southeast. The Company also distributes several other beverage brands. The Company s product offerings include carbonated soft drinks, bottled water, teas, juices, isotonics and energy products. The Company had net sales of approximately $1.4 billion in 2005.

The nonalcoholic beverage industry is highly competitive. The Company s competitors in the industry include bottlers and distributors of nationally advertised and marketed products, regionally advertised and marketed products and private label products. In each region in which the Company operates, between 75% and 90% of carbonated soft drink sales in bottles, cans and other containers are accounted for by the Company and its principal competitors, which in each region includes the local bottler of Pepsi-Cola and, in some regions, the local bottler of Royal Crown and/or 7-Up products. During the past several years, the demand for sugar carbonated beverages has declined. The decline in sugar carbonated beverages has generally been offset by volume growth in other nonalcoholic beverages. The carbonated soft drink category (including energy drinks) represents 85% of the Company s YTD 2006 bottle/can net sales.

The principal methods of competition in the nonalcoholic beverage industry are point-of-sale merchandising, new product introductions, new vending and dispensing equipment, packaging changes, pricing, price promotions, product quality, retail space management, customer service, frequency of distribution and advertising. The Company believes it is competitive in its territories with respect to each of these methods of competition.

Operating results for Q2 2006 and YTD 2006 are not indicative of results that may be expected for the fiscal year ending December 31, 2006 because of business seasonality. Business seasonality results primarily from higher unit sales of the Company s products in the second and third quarters versus the first and fourth quarters of the fiscal year. Fixed costs, such as depreciation and interest expense, are not significantly impacted by business seasonality.

Table of Contents

Net sales by product category were as follows:

In Thousands	Second Quarter 2006	Second Quarter 2005	First Half 2006	First Half 2005
Product Category				
Bottle/can sales:				
Carbonated soft drinks (including energy drinks)	$ 273,185	$ 261,412	$ 512,399	$ 493,104
Noncarbonated beverages	51,721	45,544	90,639	78,810
Total bottle/can sales	324,906	306,956	603,038	571,914
Other sales:				
Sales to other bottlers	41,719	34,791	79,083	61,946
Post mix	19,999	19,477	37,682	36,549
Total other sales	61,718	54,268	116,765	98,495
Total net sales	$ 386,624	$ 361,224	$ 719,803	$ 670,409

Areas of Emphasis

Key priorities for the Company during 2006 and over the next several years include revenue management, product innovation, distribution cost management and productivity.

Revenue Management

Revenue management includes striking the appropriate balance between generating growth in volume, gross margin and market share. It requires a strategy which reflects consideration for pricing of brands and packages within channels, as well as highly effective working relationships with customers and disciplined, fact-based decision-making. Revenue management has been and continues to be a key performance driver which has significant impact on the Company s results of operations.

Product Innovation

Volume growth of carbonated soft drinks, other than energy drinks, has slowed over the past several years. Innovation of both new brands and packages has been and will continue to be critical to the Company s overall revenue. During YTD 2006, the Company introduced Tab Energy and Vault Zero. In 2005, the Company introduced Vault, Coca-Cola Zero and Dasani flavors. The Company has also developed specialty packaging for customers in certain channels over the past several years.

Distribution Cost Management

Distribution cost represents the cost of transporting finished goods from Company locations to customer outlets. Over the past several years, the Company has focused on converting its distribution system from a conventional routing system to a predictive system. This conversion to a predictive system has allowed the Company to more efficiently handle an increasing number of brands and packages.

Table of Contents

Distribution cost management will continue to be a key area of emphasis for the Company for the next several years. During the first quarter of 2006 (Q1 2006), the Company began the rollout of a change to its primary route delivery method. The implementation of this delivery method should generate significant vehicle productivity gains and labor productivity improvements in future years. The Company anticipates the implementation of this delivery method will continue over the next two to three years.

Productivity

To achieve improvements in operating performance over the long-term, the Company s gross margin must grow faster than the increase in selling, delivery and administrative (S,D&A) expenses. A key driver in the Company s S,D&A expense management relates to ongoing improvements in labor and asset productivity. The Company continues to focus on its supply chain and distribution functions for opportunities to improve productivity.

Overview of Operations and Financial Condition

The following overview provides a summary of key information concerning the Company s financial results for Q2 2006 and YTD 2006 compared to Q2 2005 and YTD 2005.

	Second Quarter			%
In Thousands (Except Per Share Data)	**2006**	**2005**	**Change**	**Change**
Net sales	$ 386,624	$ 361,224	$ 25,400	7.0%
Gross margin [1]	167,689	166,365	1,324	0.8%
S,D&A expenses [2]	138,310	132,025	6,285	4.8%
Income from operations [1] [2]	29,237	34,183	(4,946)	(14.5)%
Interest expense [3]	12,843	12,893	(50)	(0.4)%
Income before income taxes [1] [2] [3]	15,245	19,849	(4,604)	(23.2)%
Net income [1] [2] [3]	8,887	11,519	(2,632)	(22.8)%
Diluted net income per share [1] [2] [3]	$ .97	$ 1.27	$ (.30)	(23.6)%

	First Half			%
In Thousands (Except Per Share Data)	**2006**	**2005**	**Change**	**Change**
Net sales	$ 719,803	$ 670,409	$ 49,394	7.4%
Gross margin [1]	313,715	305,899	7,816	2.6%
S,D&A expenses [2]	270,038	257,924	12,114	4.7%
Income from operations [1] [2]	43,387	47,409	(4,022)	(8.5)%
Interest expense [3]	25,063	24,391	672	2.8%
Income before income taxes [1] [2] [3]	16,619	21,057	(4,438)	(21.1)%
Net income [1] [2] [3]	9,702	12,238	(2,536)	(20.7)%
Diluted net income per share [1] [2] [3]	$ 1.06	$ 1.35	$ (.29)	(21.5)%

(1) Results for Q2 2005 and YTD 2005 included a favorable adjustment of $6.4 million (pre-tax) related to proceeds received from the settlement of high fructose corn syrup litigation, which was reflected as a reduction in cost of sales.

(2) Results for Q2 2005 and YTD 2005 included a favorable adjustment of $1.1 million (pre-tax) related to an adjustment of amounts accrued for certain executive benefit plans upon the resignation of an executive.

(3) Interest expense for Q2 2005 and YTD 2005 included financing transaction costs of $1.3 million (pre-tax) related to the exchange of $164.8 million of the Company s long-term debt.

33

Table of Contents

The Company s net sales grew 7.0% and 7.4% in Q2 2006 and YTD 2006 from the same periods in 2005, respectively. The net sales increase in Q2 2006 compared to Q2 2005 was primarily due to an approximate 7.1% increase in bottle/can volume and an approximate 20%, or $6.9 million, increase in sales to other Coca-Cola bottlers, partially offset by a 1.3% decrease in average revenue per case. The decrease in average revenue per case resulted from price reductions made in response to competitive pressures, primarily in the supermarket channel. The price reductions in Q2 2006 represented a short-term departure from the Company s long-term pricing strategy of executing price increases necessary to maintain the Company s margins. The increase in net sales in YTD 2006 compared to YTD 2005 reflected an increase in bottle/can volume of 3.1%, an increase in sales to other Coca-Cola bottlers of $17.1 million, or approximately 28%, and an increase in average revenue per case of 2.1%. Energy products contributed 15% and 17%, respectively, of the increase in net sales in Q2 2006 and YTD 2006 compared to Q2 2005 and YTD 2005. The Q2 2006 and YTD 2006 increases in sales to other Coca-Cola bottlers were primarily related to sales of Full Throttle.

The Company has seen declines in the demand for sugar carbonated beverages over the past several years and expects this trend will continue. The Company anticipates overall bottle/can revenue will be primarily dependent upon continued growth in diet products, isotonics, bottled water and energy products; the introduction of new beverage products and the appropriate pricing of brands and packaging within sales channels.

Gross margin increased .8% in Q2 2006 compared to Q2 2005 and 2.6% in YTD 2006 compared to YTD 2005. Growth in energy products was the primary reason for the increase in gross margin in Q2 2006 compared to Q2 2005 and contributed 38% of the improvement in gross margin in YTD 2006 compared to YTD 2005.

The Company s gross margin percentage declined to 43.4% in Q2 2006 from 46.1% in Q2 2005 and declined to 43.6% in YTD 2006 from 45.6% in YTD 2005. The declines in gross margin percentage in 2006 were due to the receipt of $6.4 million from the settlement of a class action litigation in Q2 2005 (which was accounted for as a reduction of cost of goods sold), higher raw material costs in 2006 and an increase in sales to other Coca-Cola bottlers, which have lower margins than the Company s bottle/can sales to retail customers. The proceeds from the settlement of the litigation and sales to other Coca-Cola bottlers accounted for 2% of the 2.7% decrease in the gross margin percentage for Q2 2006 and 1.5% of the 2% decrease in the gross margin percentage for YTD 2006.

S,D&A expenses increased 4.8% and 4.7% in Q2 2006 and YTD 2006 from Q2 2005 and YTD 2005, respectively. The increase in S,D&A expenses in Q2 2006 compared to Q2 2005 was primarily attributable to increases in employee related expenses, property and casualty insurance costs and fuel costs. The increase in S,D&A expenses in YTD 2006 compared to YTD 2005 was primarily attributable to increases in employee related expenses, property and casualty insurance costs and fuel costs, offset by a decrease in depreciation expense.

Interest expense decreased by .4% in Q2 2006 from Q2 2005 and increased by 2.8% in YTD 2006 from YTD 2005. The changes primarily reflected higher interest rates on the Company s floating rate debt

offset by the $1.3 million financing transaction costs in Q2 2005 related to the exchange of $164.8 million of the Company s long-term debentures. Excluding the impact of the $1.3 million financing transaction costs, the Company s overall weighted average interest rate increased to 6.6% during YTD 2006 from 5.9% during YTD 2005.

Net debt and capital lease obligations were summarized as follows:

In Thousands	July 2, 2006	January 1, 2006	July 3, 2005
Debt	$ 691,450	$ 697,989	$ 702,939
Capital lease obligations	78,322	79,202	80,130
Total debt and capital lease obligations	769,772	777,191	783,069
Less: Cash and cash equivalents	30,971	39,608	10,155
Total net debt and capital lease obligations [1]	$ 738,801	$ 737,583	$ 772,914

(1) The non-GAAP measure Total net debt and capital lease obligations is used to provide investors with additional information to more clearly evaluate the Company s capital structure and financial leverage.

Discussion of Critical Accounting Policies and New Accounting Pronouncements

Critical Accounting Policies

In the ordinary course of business, the Company has made a number of estimates and assumptions relating to the reporting of results of operations and financial position in the preparation of its consolidated financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ significantly from those estimates under different assumptions and conditions. The Company included in its Annual Report on Form 10-K for the year ended January 1, 2006 a discussion of the Company s most critical accounting policies, which are those most important to the portrayal of the Company s financial condition and results of operations and require management s most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

The Company has not made changes in any critical accounting policies during YTD 2006. Any changes in critical accounting policies and estimates are discussed with the Audit Committee of the Board of Directors of the Company during the quarter in which a change is made.

New Accounting Pronouncements

Recently Adopted Pronouncements

In November 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4. This Statement clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage) and was effective for fiscal years beginning after June 15, 2005. The adoption of this Statement in Q1 2006 did not have a material impact on the Company s consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), Share-Based Payment. This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation and was effective as of the beginning of Q1 2006. The Statement requires public companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the grant-date fair value of the award. The adoption of this Statement did not have a material impact on the Company s consolidated financial statements.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement requires retrospective application to prior period financial statements of a voluntary change in accounting principle unless it is impracticable and is effective for fiscal years beginning after December 15, 2005. Previously, most voluntary changes in accounting principle were recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle.

In September 2005, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 04-13, Accounting for Purchases and Sales of Inventory with the Same Counterparty (EITF 04-13). EITF 04-13 addresses the circumstances under which two or more inventory purchase and sales transactions with the same counterparty should be viewed as a single exchange and the circumstances under which nonmonetary exchanges of inventory within the same line of business should be recognized at fair value. EITF 04-13 was effective for new arrangements and modifications or renewals of existing arrangements for the first interim reporting period beginning after March 15, 2006. The adoption of this EITF in Q2 2006 did not have a material impact on the Company s consolidated financial statements.

Recently Issued Pronouncements

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments an amendment of SFAS No. 133 and 140. This Statement simplifies accounting for certain hybrid financial instruments, eliminates the interim guidance in Statement 133 Implementation Issue No. D1, Application of Statement 133 to Beneficial Interest in Securitized Financial Assets, and eliminates a restriction of the passive derivative instruments that a qualifying special-purpose entity may hold. The Statement is effective for fiscal years beginning after September 15, 2006. The adoption of this Statement is not anticipated to have a material impact on the Company s consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes. This Interpretation clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The Interpretation is effective for fiscal years beginning after December 15, 2006. The Company is in the process of determining the impact of this Interpretation on the Company s consolidated financial statements.

Proposed Pronouncement

In March 2006, FASB issued a proposed SFAS, Employers Accounting for Defined Pension and Other Postretirement Plans. In July 2006, the FASB affirmed its decision to make this proposed SFAS effective for fiscal years ending after December 15, 2006. This proposed SFAS would require the following for defined pension and other postretirement plans:

(1) Recognition in the statement of financial position of the overfunded or underfunded status of the plans.

(2) Recognition as a component of other comprehensive income, net of tax, the actuarial gains and losses and the prior service costs and credits that arise during the period but are not recognized as components of net periodic benefit costs.

(3) Recognition as an adjustment to retained earnings, net of tax, any remaining transition asset or transition obligation.

(4) Measurement of defined benefit plan assets and obligations as of the date of the employer s statement of financial position.

(5) Disclosure of additional information in the notes to the consolidated financial statements about certain effects on periodic benefit costs in the upcoming fiscal year that arise from delayed recognition of the actuarial gains and losses and the prior service costs and credits.

The Company is in the process of determining the impact of the adoption of this proposed SFAS.

Results of Operations

Q2 2006 Compared to Q2 2005 and YTD 2006 Compared to YTD 2005

Net Income and Earnings Per Share

The Company reported net income of $8.9 million or $.97 per diluted share for Q2 2006 compared with net income of $11.5 million or $1.27 per diluted share for Q2 2005. Net income for YTD 2006 was $9.7 million or $1.06 per diluted share compared to $12.2 million or $1.35 per diluted share for YTD 2005.

Results in Q2 2005 and YTD 2005 include infrequent items (pre-tax) as follows:

- A favorable adjustment to cost of sales of $6.4 million related to proceeds received from the settlement of litigation regarding purchases of high fructose corn syrup, which was reflected as a reduction in cost of sales.

- A favorable adjustment of $1.1 million related to an adjustment of amounts accrued for certain executive benefit plans due to the resignation of an executive, which was reflected as a reduction to S,D&A expenses.

- Financing transaction costs of $1.3 million related to the exchange of $164.8 million of the Company s long-term debt, which was reflected as an increase to interest expense.

Table of Contents

Net Sales

Net sales in Q2 2006 and YTD 2006 increased 7.0% and 7.4% from the same periods in 2005, respectively. The increase in net sales in Q2 2006 compared to Q2 2005 reflected an increase in bottle/can volume of 7.1% and an increase in sales to other Coca-Cola bottlers of $6.9 million, or approximately 20%, partially offset by a decrease in average revenue per case of 1.3%. The increase in net sales in YTD 2006 compared to YTD 2005 reflected an increase in bottle/can volume of 3.1%, an increase in sales to other Coca-Cola bottlers of $17.1 million, or approximately 28%, and an increase in average revenue per case of 2.1%. Growth in energy products contributed 15% and 17%, respectively, of the increase in net sales in Q2 2006 and YTD 2006 compared to Q2 2005 and YTD 2005.

In YTD 2006, the Company s bottle/can volume to retail customers accounted for 84% of the Company s total net sales. Bottle/can net pricing is based on the invoice price charged to customers reduced by promotional allowances. Bottle/can net pricing per case is impacted by the price charged per package, the volume generated in each package and the channels in which those packages are sold. To the extent the Company is able to increase volume in higher margin packages sold through higher margin channels, bottle/can net pricing per case can increase without an actual increase in wholesale pricing. The decrease in the Company s bottle/can net price per case in Q2 2006 compared to Q2 2005 was primarily due to a decrease in wholesale pricing in the supermarket channel in response to competitive pressures. The reduction in pricing represented a short-term departure from the Company s long-term pricing strategy of executing price increases necessary to maintain the Company s margins. In YTD 2006, the increase in the Company s bottle/can net price per case was primarily achieved with price increases, but also reflects additional mix benefit associated with energy products, isotonics and new products, including Vault, Coca-Cola Zero and Dasani flavors. Energy products comprised 0.7% of the overall bottle/can volume in Q2 2006 and YTD 2006 compared to 0.5% in Q2 2005 and YTD 2005, respectively.

The percentage increase in bottle/can volume by product category in Q2 2006 and YTD 2006 compared to Q2 2005 and YTD 2005 was as follows:

	Bottle/Can Volume	
	% Increase	
Product Category	**Second Quarter**	**First Half**
Carbonated soft drinks (including energy products)	6.1%	1.5%
Noncarbonated beverages	14.4%	15.7%
Total bottle/can volume	7.1%	3.1%

The Company s net sales to other Coca-Cola bottlers and post-mix net sales increased to $79.1 million and $37.7 million in YTD 2006 compared to $61.9 million and $36.6 million in YTD 2005, respectively. The significant increase in sales to other Coca-Cola bottlers resulted primarily from sales of Full Throttle. The Company produces this product for the majority of the Coca-Cola bottlers in the eastern half of the United States.

Noncarbonated beverages comprised 13.7% and 13.0% of the overall bottle/can volume in Q2 2006 and YTD 2006 compared to 12.8% and 11.6% in Q2 2005 and YTD 2005, respectively.

Table of Contents

The Company s products are sold and distributed through various channels. The channels include selling directly to retail stores and other outlets such as food markets, institutional accounts and vending machine outlets. During YTD 2006, 68% of the Company s bottle/can volume to retail customers was from products sold for future consumption. The remaining bottle/can volume to retail customers of 32% was from products sold for immediate consumption. The Company s largest customer, Wal-Mart Stores, Inc., accounted for approximately 15% of the Company s total bottle/can volume to retail customers during YTD 2006. The Company s second largest customer, Food Lion, LLC, accounted for approximately 12% of the Company s total bottle/can volume to retail customers during YTD 2006. All of the Company s sales are to customers in the United States.

Cost of Sales

Cost of sales includes the following: raw material costs, manufacturing labor, manufacturing overhead including depreciation expense, manufacturing warehousing costs and shipping and handling costs related to the movement of finished goods from manufacturing locations to sales distribution centers.

Cost of sales per case for bottle/can volume increased 4.4% in Q2 2006 and 5.8% for YTD 2006 compared to the same periods of 2005. The increase in cost of sales per case in Q2 2006 compared to Q2 2005 was due to an approximate 2.3% increase in concentrate, sweetener and packaging costs, and increases due to higher sales of energy products, which have a higher per unit cost, and the impact of proceeds of $6.4 million received from the high fructose corn syrup litigation settlement in Q2 2005. The increase in cost of sales per case in YTD 2006 compared to YTD 2005 was due to an approximate 5.8% increase in concentrate, sweetener and packaging costs and increases due to higher sales of energy products, which have a higher per unit cost, and the impact of proceeds received from the high fructose corn syrup litigation settlement in Q2 2005. There were also higher energy costs, increased labor rates and increases in other manufacturing costs in both Q2 2006 compared to Q2 2005 and YTD 2006 compared to YTD 2005. The increases in cost of sales per case for bottle/can volume in Q2 2006 and YTD 2006 compared to the same periods in 2005 were partially offset by higher utilization due to increased unit sales and increased sales to other bottlers and increased marketing funding support.

Beginning in 2007, it is anticipated the majority of the Company s aluminum requirements will not have any ceiling price protection. Based upon current market prices for aluminum, the Company anticipates the cost of aluminum can bodies may increase in excess of 10% in 2007. High fructose corn syrup costs are also expected to increase significantly in 2007 as a result of increasing demand for corn products around the world and as a result of alternate uses for corn, such as ethanol. Based upon current market prices for corn, the Company anticipates the cost of high fructose corn syrup may increase in excess of 15% in 2007. If during YTD 2006, the cost of aluminum can bodies was 10% higher, the cost of high fructose corn syrup was 15% higher and the Company s bottle/can pricing was unchanged, gross margin would have decreased by approximately $7 million.

The Company relies extensively on advertising and sales promotion in the marketing of its products. The Coca-Cola Company and other beverage companies that supply concentrates, syrups and finished

Table of Contents

products to the Company make substantial marketing and advertising expenditures to promote sales in the local territories served by the Company. The Company also benefits from national advertising programs conducted by The Coca-Cola Company and other beverage companies. Certain of the marketing expenditures by The Coca-Cola Company and other beverage companies are made pursuant to annual arrangements. Although The Coca-Cola Company has advised the Company it intends to provide marketing funding support, it is not obligated to do so under the Company s Bottle Contracts. Significant decreases in marketing funding support from The Coca-Cola Company or other beverage companies could adversely impact operating results of the Company in the future.

Total marketing funding support from The Coca-Cola Company and other beverage companies, which includes direct payments to the Company and payments to customers for marketing programs, was $17.2 million for YTD 2006 compared to $15.1 million for YTD 2005, and was recorded as a reduction in cost of sales.

Gross Margin

Gross margin increased $1.3 million or .8% in Q2 2006 compared to Q2 2005 and $7.8 million or 2.6% in YTD 2006 compared to YTD 2005.

Gross margin as a percentage of net sales decreased to 43.4% in Q2 2006 from 46.1% in Q2 2005 and 43.6% in YTD 2006 from 45.6% in YTD 2005. The decrease in gross margin percentage was primarily due to proceeds received related to the litigation settlement in Q2 2005 and an increase in sales to other Coca-Cola bottlers, which have lower margins than the Company s bottle/can sales to retail customers. Gross margin as a percentage of sales without the impact of the litigation settlement and sales to other Coca-Cola bottlers decreased to 48.2% in Q2 2006 from 48.9% in Q2 2005 and decreased to 48.6% in YTD 2006 from 49.1% in YTD 2005.

The Company s gross margins may not be comparable to other companies, since some entities include all costs related to their distribution network in cost of sales. The Company includes a portion of these costs in S,D&A expenses.

S,D&A Expenses

S,D&A expenses include the following: sales management labor costs, distribution costs from sales distribution centers to customer locations, sales distribution center warehouse costs, depreciation expense related to sales centers, delivery vehicles and cold drink equipment, point-of-sale expenses, advertising expenses, vending equipment repair costs and administrative support labor and operating costs such as treasury, legal, information services, accounting, internal audit and executive management costs.

S,D&A expenses increased by 4.8% in Q2 2006 compared to Q2 2005 and 4.7% in YTD 2006 compared to YTD 2005. The increase in S,D&A expenses for Q2 2006 was due to wage increases for the Company s employees and additional employee personnel of 5.9%, higher employee benefit costs of 5.4%, increased property and casualty costs of 20.9% and higher fuel costs of 24.3% related to the movement of finished goods from sales distribution centers to customer locations, offset by a decrease in depreciation of 1.5%. The increase in S,D&A expenses for YTD 2006 was due to wage increases for the Company employees and additional employee personnel of 5.7%, higher employee

benefit costs of 3.6%, increased property and casualty costs of 18.7% and higher fuel costs of 23.5%, offset by a decrease in depreciation expense of 2.4%. The decrease in depreciation expense from 2006 to 2005 was primarily due to lower levels of capital spending over the past several years. S,D&A expenses in Q2 2006 and YTD 2006 compared to the same periods in 2005 were also effected by a favorable adjustment of $1.1 million related to an adjustment of amounts accrued for certain benefit plans upon the resignation of an executive in Q2 2005.

Shipping and handling costs related to the movement of finished goods from manufacturing locations to sales distribution centers are included in cost of sales, as noted above. Distribution costs related to the movement of finished goods from sales distribution centers to customer locations are included in S,D&A expenses and totaled $97.7 million and $89.6 million in YTD 2006 and YTD 2005, respectively. For certain lower volume customers, the Company charges a delivery fee to offset a portion of the increased fuel costs. The Company initiated this delivery fee charge in the third quarter of 2005. The delivery fee is recorded in net sales and was $1.3 million in YTD 2006.

In February 2006, the Company announced an amendment to its principal Company-sponsored pension plan to cease further benefit accruals under the plan effective June 30, 2006. The Company anticipates the annual expense for its pension plans will decrease by approximately $3.7 million in 2006 from 2005 with such decrease to be recognized in the third and fourth quarters of 2006. The Company also announced in February 2006 plans to enhance its 401(k) Savings Plan for eligible employees beginning in the first quarter of 2007.

In October 2005, the Company announced changes to its postretirement health care plan. As a result of these changes, the Company s annual expense for postretirement health care will decrease approximately $2.4 million in 2006 as compared to 2005. Such expense decreased $1.2 million in YTD 2006 compared to YTD 2005.

Amortization of Intangibles

Amortization of intangibles for YTD 2006 declined by $.3 million compared to YTD 2005. The decline in amortization expense was due to the impact of certain customer relationships recorded in other identifiable intangible assets which are now fully amortized.

Interest Expense

Interest expense decreased by .4% in Q2 2006 from Q2 2005 and increased by 2.8% in YTD 2006 from YTD 2005. The changes primarily reflect higher interest rates on the Company s floating rate debt and the $1.3 million financing transaction costs in Q2 2005 related to the exchange of $164.8 million of the Company s debentures. Excluding the impact of the $1.3 million financing transaction costs, the Company s overall weighted average interest rate increased to 6.6% during YTD 2006 from 5.9% during YTD 2005. See the Liquidity and Capital Resources, Interest Rate Hedging section of M,D&A for additional information.

Minority Interest

The Company recognized minority interest of $1.7 million in YTD 2006 compared to $2.0 million in YTD 2005 related to the portion of Piedmont owned by The Coca-Cola Company.

Income Taxes

The Company s effective income tax rate for YTD 2006 was 41.6% compared to 41.9% for YTD 2005. The effective income tax rate reflects expected full year 2006 earnings. The Company s income tax rate for the remainder of 2006 is dependent upon results of operations and may change if the results for 2006 are different from current expectations.

The Company s income tax assets and liabilities are subject to adjustment in future periods based on the Company s ongoing evaluations of such assets and liabilities and new information that becomes available to the Company.

Financial Condition

Total assets increased to $1.36 billion at July 2, 2006 from $1.34 billion at January 1, 2006 primarily due to increases in accounts receivable, trade, inventories and prepaid expenses and other current assets. Total assets increased to $1.36 billion at July 2, 2006 from $1.33 billion at July 3, 2005 primarily due to increases in cash and cash equivalents and inventories.

Net working capital, defined as current assets less current liabilities, increased by $22.1 million at July 2, 2006 from January 1, 2006 and increased by $46.8 million at July 2, 2006 from July 3, 2005.

Significant changes in net working capital from January 1, 2006 were as follows:

A decrease in cash and cash equivalents of $8.6 million primarily due to increased capital expenditures and payment of accrued employee incentives.

An increase in accounts receivable, trade, of $12.2 million due to increased sales revenue.

An increase in accounts receivable from The Coca-Cola Company of $8.0 million primarily due to the timing of payments.

An increase in inventories of $5.7 million primarily due to cost increases and changes in the Company s product mix.

An increase in prepaid expenses and other current assets of $7.0 million primarily due to the timing of payments.

An increase in accounts payable to The Coca-Cola Company of $19.2 million due to the timing of payments and higher bottle/can revenue.

A decrease in other accrued liabilities of $8.1 million primarily due to the timing of payments and a $5.0 million payment related to a state income tax audit.

A decrease in accrued compensation of $5.9 million due to the payment of accrued employee incentives in March 2006.

Significant changes in net working capital from July 3, 2005 were as follows:

An increase in cash and cash equivalents of $20.8 million primarily due to cash flows from operating activities.

An increase in inventories of $8.6 million primarily due to cost increases and changes in the Company s product mix.

A decrease in current portion of debt of $2.9 million due to the payment from cash flows from operating activities of amounts due on the lines of credit.

An increase in accounts payable, trade of $5.8 million primarily due to increased bottle/can sales.

An increase in accounts payable to The Coca-Cola Company of $5.4 million primarily due to the timing of payments.

A decrease in other accrued liabilities of $9.0 million primarily due to the timing of payments and a decrease in state income taxes payable. Debt and capital lease obligations were $769.8 million as of July 2, 2006 compared to $777.2 million as of January 1, 2006 and $783.1 million as of July 3, 2005. Debt and capital lease obligations as of July 2, 2006 included $78.3 million of capital lease obligations related primarily to Company facilities.

Liquidity and Capital Resources

Capital Resources

Sources of capital for the Company include cash flows from operating activities, bank borrowings and the issuance of debt and equity securities. Management believes the Company, through these sources, has sufficient financial resources available to maintain its current operations and provide for its current capital expenditure and working capital requirements, scheduled debt payments, interest and income tax payments and dividends for stockholders. The amount and frequency of future dividends will be determined by the Company s Board of Directors in light of the earnings and financial condition of the Company at such time, and no assurance can be given that dividends will be declared in the future.

The Company primarily uses cash flows from operations and available credit facilities to meet its cash requirements. As of July 2, 2006, the Company had $100 million available under its revolving credit facility to meet its cash requirements. The Company borrows periodically under its available lines of credit. These lines of credit, in the aggregate amount of $60 million at July 2, 2006, are made available at the discretion of two participating banks at rates negotiated at the time of borrowing and may be withdrawn at any time by such banks.

The Company has obtained the majority of its long-term financing from public markets. As of July 2, 2006, $691.5 million of the Company s total outstanding balance of debt and capital lease obligations of $769.8 million was financed through publicly offered debt. The Company had capital lease obligations of $78.3 million as of July 2, 2006. The Company s interest rate derivative contracts are with several different financial institutions to minimize the concentration of credit risk. The Company has master agreements with the counterparties to its derivative financial agreements that provide for net settlement of derivative transactions.

Cash Sources and Uses

The primary sources of cash for the Company have been cash provided by operating activities. The primary uses of cash have been for capital expenditures, the payment of debt and capital lease obligations, income tax payments and dividends.

Table of Contents

A summary of activity for YTD 2006 and YTD 2005 follows:

In Millions	First Half 2006	First Half 2005
Cash Sources		
Cash provided by operating activities (excluding income tax payments)	$ 40.3	$ 44.7
Other	1.4	3.6
Total cash sources	$ 41.7	$ 48.3
Cash Uses		
Capital expenditures	$ 29.8	$ 14.9
Payments of lines of credit, debt and capital lease obligations	7.4	6.0
Dividends	4.6	4.5
Income tax payments	8.3	6.0
Premium on exchange of debt		15.6
Other	.2	
Total cash uses	$ 50.3	$ 47.0
Increase (decrease) in cash	$ (8.6)	$ 1.3

Based on current projections which include a number of assumptions such as the Company s pre-tax earnings, the Company anticipates its cash requirements for income taxes will increase to a range of $14 million to $18 million in 2006 from $11.2 million in 2005. The estimated cash requirements for 2006 include $5 million related to the settlement of a state tax audit, which was paid in Q1 2006.

Investing Activities

Additions to property, plant and equipment during YTD 2006 were $29.8 million compared to $14.9 million during YTD 2005. The increase in capital expenditures in YTD 2006 was due to the purchase of new route delivery vehicles and costs associated with the Company s ongoing implementation of its ERP computer systems. Capital expenditures during YTD 2006 were funded with cash flows from operations and cash and cash equivalents. Leasing is used for certain capital additions when considered cost effective relative to other sources of capital.

At the end of Q2 2006, the Company had commitments of $8.1 million for the purchase of route delivery vehicles related to the initial rollout of an improved delivery system. The Company anticipates additions to property, plant and equipment in 2006 will be in the range of $60 million to $65 million and plans to fund such additions through cash flows from operations and its available lines of credit.

Financing Activities

In December 2005, the Company repurchased $8.6 million of its outstanding 6.375% debentures due May 2009. The Company used cash on hand to retire these debentures.

In Q2 2005, the Company issued $164.8 million of new 5.00% senior notes due 2016 in exchange for $122.2 million of its outstanding 6.375% debentures due 2009 and $42.6 million of its outstanding 7.20% debentures due 2009. The exchange of debt will reduce the Company s interest costs prospectively and lengthens maturities on portions of the Company s debt, reducing refinancing requirements in the near-term by extending the maturity dates on a portion of its total debt.

The Company has a five-year $100 million revolving credit facility. On July 2, 2006, there were no amounts outstanding under the facility. The facility matures in April 2010 and includes an option to extend the term for an additional year at the discretion of the participating banks. The facility bears interest at a floating base rate or a floating rate of LIBOR plus an interest rate spread of .375%. In addition, there is a facility fee of .125% required for this facility. Both the interest rate spread and the facility fee are determined from a commonly-used pricing grid based on the Company s long-term senior unsecured debt rating. The facility contains two financial covenants related to ratio requirements for interest coverage and long-term debt to cash flow, each as defined in the credit agreement. These covenants do not currently, and the Company does not anticipate they will, restrict its liquidity or capital resources.

The Company borrows periodically under its available lines of credit. These lines of credit, in the aggregate amount of $60 million at July 2, 2006, are made available at the discretion of two participating banks at rates negotiated at the time of borrowing and may be withdrawn at any time by such banks. The Company can utilize its revolving credit facility in the event the lines of credit are not available. On July 2, 2006, there were no amounts outstanding under the lines of credit. On January 1, 2006 and July 3, 2005, $6.5 million and $2.9 million, respectively, were outstanding under the lines of credit.

All of the outstanding debt has been issued by the Company with none having been issued by any of the Company s subsidiaries. There are no guarantees of the Company s debt.

At July 2, 2006, the Company s credit ratings were as follows:

	Long-Term Debt
Standard & Poor s	BBB
Moody s	Baa2

The Company s credit ratings are reviewed periodically by the respective rating agencies. Changes in the Company s operating results or financial position could result in changes in the Company s credit ratings. Lower credit ratings could result in higher borrowing costs for the Company. There were no changes in these credit ratings from the prior year. It is the Company s intent to continue to reduce its financial leverage over time.

The Company s public debt is not subject to financial covenants but does limit the incurrence of certain liens and encumbrances as well as indebtedness by the Company s subsidiaries in excess of certain amounts.

The Company issued 20,000 shares of Class B Common Stock to J. Frank Harrison, III, Chairman of the Board of Directors and Chief Executive Officer, with respect to 2005 performance, effective January 2,

2006, under a restricted stock award plan that provides for annual awards of such shares subject to the Company achieving at least 80% of the overall goal achievement factor in the Company s Annual Bonus Plan.

The Company adopted SFAS No. 123 (revised 2004), Share-Based Payment on January 2, 2006. The Company applied the modified prospective transition method and prior periods were not restated. The Company s only share based compensation is the restricted stock award to Mr. Harrison, III. The award provides the shares of restricted stock vest at the rate of 20,000 shares per year over a ten-year period. The vesting of each annual installment is contingent upon the Company achieving at least 80% of the overall goal achievement factor in the Company s Annual Bonus Plan. Each annual 20,000 share tranche has an independent performance requirement as it is not established until the Company s Annual Bonus Plan targets are approved for each year. As a result, each 20,000 share tranche is considered to have its own service inception date, grant-date fair value and requisite service period.

The Company s Annual Bonus Plan targets, which establish the performance requirement for the restricted stock award in 2006, were approved by the Board of Directors in Q1 2006 and the Company recorded the 20,000 share award at the grant-date price of $46.45 per share. Total stock compensation expense will be approximately $929,000 over the one-year service period of which $465,000 was recognized in YTD 2006. In addition, the Company reimburses Mr. Harrison, III for income taxes to be paid on the shares if the performance requirement is met and the shares are issued. The Company accrues the estimated cost of the income tax reimbursement over the one-year service period.

Prior to the adoption of this statement, the Company accrued compensation cost over the course of the one-year service period with the final cost based upon the end of the period stock price. Total compensation expense, including income tax reimbursements to Mr. Harrison, III, for the restricted stock award, net of tax effect, was $475,000 in YTD 2006 and would have been $542,000, net of tax effect, in YTD 2005 under the new standard. Actual expense recorded in YTD 2005, net of tax effect, was $499,000. Pro forma net income would have been $12.2 million in YTD 2005, which was the net income reported for YTD 2005. Pro forma diluted earnings per share for YTD 2005 was $1.34 compared to actual diluted earnings per share of $1.35.

Off-Balance Sheet Arrangements

The Company has identified two manufacturing cooperatives in which it is a member as variable interest entities. The Company has guaranteed $44.7 million of debt and related lease obligations for these cooperatives. As of July 2, 2006, the Company s variable interest in these cooperatives includes an equity ownership in each of the entities and the guarantees. As of July 2, 2006, the Company s maximum exposure, if the cooperatives borrowed up to their borrowing capacity, would have been $66.2 million including the Company s equity interest. The Company has determined it is not the primary beneficiary of either of the cooperatives. See Note 14 of the consolidated financial statements for additional information about these cooperatives.

Table of Contents

Aggregate Contractual Obligations

The following table summarizes the Company s contractual obligations and commercial commitments as of July 2, 2006:

	Payments Due by Period				
In Thousands	Total	July 2006-June 2007	July 2007-June 2009	July 2009-June 2011	After June 2011
Contractual obligations:					
Total debt, net of interest	$ 691,450		$ 100,000	$ 176,693	$ 414,757
Capital lease obligations, net of interest	78,322	$ 1,594	3,408	3,936	69,384
Estimated interest on long-term debt and capital lease obligations [1]	382,331	47,327	82,397	56,664	195,943
Interest rate swap agreements [1]	12,165	4,759	5,718	988	700
Purchase obligations [2]	631,790	79,805	159,610	159,610	232,765
Other long-term liabilities [3]	84,019	5,096	10,212	9,406	59,305
Operating leases	18,702	2,732	4,311	2,557	9,102
Long-term contractual arrangements [4]	29,538	7,285	11,789	7,768	2,696
Purchase orders [5]	38,935	38,935			
Total contractual obligations	$ 1,967,252	$ 187,533	$ 377,445	$ 417,622	$ 984,652

(1) Includes interest payments based on contractual terms and current interest rates for variable rate debt.
(2) Represents an estimate of the Company s obligation to purchase 17.5 million cases of finished product on an annual basis through May 2014 from South Atlantic Canners, a manufacturing cooperative.
(3) Includes obligations under executive benefit plans, non-compete liabilities and other long-term liabilities.
(4) Includes contractual arrangements with certain prestige properties, athletics venues and other locations, and other long-term marketing commitments.
(5) Purchase orders include commitments in which a written purchase order has been issued to a vendor, but the goods have not been received or the services have not been performed. Amount includes approximately $8.1 million related to route delivery trucks.

The Company is a member of Southeastern Container, a plastic bottle manufacturing cooperative, from which the Company is obligated to purchase at least 80% of its requirements of plastic bottles for certain designated territories. This obligation is not included in the Company s table of contractual obligations and commercial commitments since there are no minimum purchase requirements.

The Company has $19.8 million of standby letters of credit, primarily related to its property and casualty insurance programs, as of July 2, 2006. See Note 14 of the consolidated financial statements for additional information related to commercial commitments, guarantees and legal and tax matters.

The Company anticipates contributions to the Company-sponsored pension plans will be less than $1 million in 2006. Postretirement benefit payments are expected to be approximately $2.4 million in 2006. See Note 18 to the consolidated financial statements for additional information related to pension and postretirement obligations.

Interest Rate Hedging

The Company periodically uses interest rate hedging products to mitigate risk from interest rate fluctuations. The Company has historically altered its fixed/floating rate mix based upon anticipated cash flows from operations relative to the Company s debt level and the potential impact of changes in interest rates on the Company s overall financial condition. Sensitivity analyses are performed to review the impact on the Company s financial position and coverage of various interest rate movements. The Company does not use derivative financial instruments for trading purposes nor does it use leveraged financial instruments.

The Company currently has six interest rate swap agreements. These interest rate swap agreements effectively convert $250 million of the Company s debt from a fixed rate to a floating rate and are accounted for as fair value hedges.

During both YTD 2006 and YTD 2005, interest expense was reduced due to the amortization of deferred gains on previously terminated interest rate swap agreements and forward interest rate agreements by $.8 million in each period.

The weighted average interest rate of the Company s debt and capital lease obligations after taking into account all of the interest rate hedging activities was 6.7% as of July 2, 2006 compared to 6.2% as of January 1, 2006 and 5.8% as of July 3, 2005. Approximately 42% of the Company s debt and capital lease obligations of $769.8 million as of July 2, 2006 was maintained on a floating rate basis and was subject to changes in short-term interest rates.

Assuming no changes in the Company s capital structure, if market interest rates average 1% more over the next twelve months than the interest rates as of July 2, 2006, interest expense for the next twelve months would increase by approximately $3.3 million. This amount is determined by calculating the effect of a hypothetical interest rate increase of 1% on outstanding floating rate debt and capital lease obligations as of July 2, 2006, including the effects of the Company s derivative financial instruments. This calculated, hypothetical increase in interest expense for the following twelve months may be different from the actual increase in interest expense from a 1% increase in interest rates due to varying interest rate reset dates on the Company s floating rate debt and derivative financial instruments.

Table of Contents

Cautionary Information Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q, as well as information included in future filings by the Company with the Securities and Exchange Commission and information contained in written material, press releases and oral statements issued by or on behalf of the Company, contains, or may contain, forward-looking management comments and other statements that reflect management s current outlook for future periods. These statements include, among others, statements relating to:

- anticipated return on pension plan investments;
- potential marketing funding support from The Coca-Cola Company and other beverage companies;
- the Company s belief that disposition of certain claims and legal proceedings will not have a material adverse effect on its financial condition, cash flows or results of operations and that no material amount of loss in excess of recorded amounts is reasonably possible;
- management s belief that the Company has adequately provided for any ultimate amounts that are likely to result from tax audits;
- management s belief that the Company has sufficient financial resources to maintain current operations and provide for its current capital expenditure and working capital requirements, scheduled debt payments, interest and income tax payments and dividends for stockholders;
- the Company s intention to reduce its financial leverage over time;
- the Company s belief that the cooperatives whose debt and lease obligations the Company guarantees have sufficient assets and the ability to adjust selling prices of their products to adequately mitigate the risk of material loss and that the cooperatives will perform their obligations under their debt and lease agreements;
- the Company s key priorities for 2006 and the next several years;
- the Company s belief that its liquidity or capital resources will not be restricted by certain financial covenants in the Company s credit agreements;
- the Company s hypothetical calculation of the impact of a 1% increase in interest rates on outstanding floating rate debt and capital lease obligations for the next twelve months as of July 2, 2006;
- the Company s belief that contributions to the Company-sponsored pension plans will be less than $1 million in 2006;
- the Company s belief that postretirement benefit payments are expected to be approximately $2.4 million in 2006;

anticipated cash payments for income taxes will be in the range of approximately $14 million to $18 million in 2006;

anticipated additions to property, plant and equipment in 2006 will be in the range of $60 million to $65 million;

the Company s belief that demand for sugar carbonated soft drinks will continue to decline;

the Company s belief that its pension expense will decrease by approximately $3.7 million in 2006;

the Company s belief that its postretirement health care expense will decrease by approximately $2.4 million in 2006;

the Company s beliefs and estimates regarding the impact of the adoption of certain new accounting pronouncements;

Table of Contents

- the Company s belief that the implementation of its new delivery method will continue over the next two to three years and should generate significant vehicle productivity gains and labor productivity improvements in future years;

- the Company s expectation that its overall bottle/can revenue will be primarily dependent upon continued growth in diet products, isotonics, bottled water and energy drinks, the introduction of new products and the pricing of brands and packages within sales channels;

- the Company s long-term strategy of executing price increases necessary to maintain its margins;

- the Company s belief that the cost of aluminum can bodies may increase in excess of 10% in 2007;

- the Company s belief that the cost of high fructose corn syrup may increase in excess of 15% in 2007; and

- the Company s hypothetical calculation of the impact on YTD 2006 if aluminum can bodies were 10% higher and if the cost of high fructose corn syrup was 15% higher.

These statements and expectations are based on currently available competitive, financial and economic data along with the Company s operating plans, and are subject to future events and uncertainties that could cause anticipated events not to occur or actual results to differ materially from historical or anticipated results. Factors that could impact those differences or adversely affect future periods include, but are not limited to, the factors set forth in the Company s Annual Report on Form 10-K for the year ended January 1, 2006 under Part I, Item 1A, Risk Factors.

Caution should be taken not to place undue reliance on the Company s forward-looking statements, which reflect the expectations of management of the Company only as of the time such statements are made. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Table of Contents

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Raw Material and Commodity Price Risk

Beginning in 2007, it is anticipated the majority of the Company s aluminum requirements will not have any ceiling price protection. Based upon current market prices for aluminum, the Company anticipates the cost of aluminum can bodies may increase in excess of 10% in 2007. High fructose corn syrup costs are also expected to increase significantly in 2007 as a result of increasing demand for corn products around the world and as a result of alternate uses for corn, such as ethanol. Based upon current market prices for corn, the Company anticipates the cost of high fructose corn syrup may increase in excess of 15% in 2007. If during YTD 2006, the cost of aluminum can bodies was 10% higher, the cost of high fructose corn syrup was 15% higher and the Company s bottle/can pricing was unchanged, gross margin would have decreased by approximately $7 million.

Item 4. Controls and Procedures.

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company s management, including the Company s Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company s disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the Exchange Act)), pursuant to Rule 13a-15 of the Exchange Act. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded the Company s disclosure controls and procedures are effective for the purpose of providing reasonable assurance the information required to be disclosed in the reports the Company files or submits under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms and (ii) is accumulated and communicated to the Company s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

There has been no change in the Company s internal control over financial reporting during the quarter ended July 2, 2006 that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

Table of Contents

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

On February 14, 2006, forty-eight Coca-Cola bottler plaintiffs filed suit in the United States District Court for the Western District of Missouri against The Coca-Cola Company and Coca-Cola Enterprises Inc. (CCE). On February 24, 2006, the plaintiffs filed an amended complaint adding twelve bottlers as plaintiffs. In the lawsuit, *Ozarks Coca-Cola/Dr Pepper Bottling Company, et al. vs. The Coca-Cola Company and Coca-Cola Enterprises Inc.,* the bottler plaintiffs purport to bring claims for breach of contract and breach of duty and other related claims arising out of CCE s plan to offer warehouse delivery of POWERade to Wal-Mart Stores, Inc. (Wal-Mart) within CCE s territory. The bottler plaintiffs seek preliminary and permanent injunctive relief prohibiting the warehouse delivery of POWERade and unspecified compensatory and punitive damages. On March 3, 2006, the Company filed a motion seeking permission to intervene in the lawsuit for the limited purpose of opposing the preliminary and permanent injunctive relief sought by the bottler plaintiffs. The Company seeks permission to intervene because it also plans to offer warehouse delivery of POWERade to Wal-Mart within the Company s territory and therefore opposes the relief requested by the bottler plaintiffs. The plaintiffs have opposed the Company s request to intervene. The Coca-Cola Company and CCE both support the Company s request. On March 17, 2006, the Missouri District Court granted The Coca-Cola Company s and CCE s request for an order transferring the case, for the convenience of the parties, to the United States District Court for the Northern District of Georgia. None of the plaintiffs seek to recover damages from the Company. In April, warehouse delivery of POWERade commenced in the Company s exclusive territories. On April 21, 2006, the plaintiffs requested the Court defer any hearing or further briefing on their motion for preliminary injunctive relief. The parties to the lawsuit are currently engaged in the discovery process. The Court has not ruled on the Company s motion to intervene.

The Company is involved in other claims and legal proceedings which have arisen in the ordinary course of its business. Although it is difficult to predict the ultimate outcome of these other claims and legal proceedings, management believes the ultimate disposition of these claims will not have a material adverse effect on the financial condition, cash flows or results of operations of the Company. No material amount of loss in excess of recorded amounts is believed to be reasonably possible as a result of these other claims and legal proceedings.

Item 1A. Risk Factors.

There have been no material changes to the factors disclosed in Part I, Item 1A, Risk Factors in the Company s Annual Report on Form 10-K for the year ended January 1, 2006.

Table of Contents

Item 4. Submission of Matters to a Vote of Security Holders.

(a) The Annual Meeting of the Company s stockholders was held on April 28, 2006.

(b) All director nominees were elected.

(c) The meeting was held to consider and vote upon electing eleven directors, each for a term of one year or until their successors have been elected and qualified. The votes with respect to each director were as follows:

Director Name	For	Withheld
J. Frank Harrison, III	7,157,758	1,360,960
H. W. McKay Belk	8,273,451	245,267
Sharon A. Decker	8,317,396	201,322
William B. Elmore	7,157,505	1,361,213
James E. Harris	8,317,877	200,841
Deborah S. Harrison	8,289,813	228,905
Robert D. Pettus, Jr.	8,290,223	228,495
Ned R. McWherter	8,425,933	92,785
John W. Murrey, III	8,427,114	91,604
Carl Ware	7,335,664	1,183,054
Dennis A. Wicker	8,317,514	201,204

Table of Contents

Item 6. Exhibits.

(a) Exhibits.

Exhibit Number	Description
4.1	The registrant, by signing this report, agrees to furnish the Securities and Exchange Commission, upon its request, a copy of any instrument which defines the rights of holders of long-term debt of the registrant and its consolidated subsidiaries which authorizes a total amount of securities not in excess of 10 percent of the total assets of the registrant and its subsidiaries on a consolidated basis.
12	Ratio of earnings to fixed charges (filed herewith).
31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

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Table of Contents

SIGNATURE

Pursuant to the requirements 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.

- Other assets and liabilities – The carrying value of all other assets and liabilities approximated fair value at the time of acquisition.

4. Restructuring and Related Charges

In October 2013, the Company implemented a restructuring to better align the Company's resources with student enrollments at the time. This restructuring included the closing of 20 physical locations and reductions in the number of campus-based and corporate employees. A liability for lease obligations, some of which continue through 2022, was recorded and is measured at fair value using a discounted cash flow approach encompassing significant unobservable inputs (Level 3). The estimation of future cash flows includes non-cancelable contractual lease costs over the remaining terms of the leases discounted at the Company's marginal borrowing rate of 4.5%, partially offset by estimated future sublease rental income discounted at credit-adjusted rates. The Company's estimates, which involve significant judgment, also consider the amount and timing of sublease rental income based on subleases that have been executed and subleases expected to be executed based on current commercial real estate market data and conditions, and other qualitative factors specific to the facilities. The estimates are subject to adjustment as market conditions change or as new information becomes available, including the execution of additional sublease agreements.

Table of Contents

The following details the changes in the Company's restructuring liability for lease and related costs during the six months ended June 30, 2015 and 2016 (in thousands):

	June 30, 2015	June 30, 2016
Balance at beginning of period(1)	$ 27,283	$ 20,055
Adjustments(2)	435	(1,558)
Payments	(3,451)	(3,212)
Balance at end of period(1)	$ 24,267	$ 15,285

(1) The current portion of restructuring liabilities was $4.8 million and $5.3 million as of December 31, 2015 and June 30, 2016, respectively, which are included in accounts payable and accrued expenses. The long-term portion is included in other long-term liabilities.

(2) Adjustments include accretion of interest on lease costs, partially offset by changes in the timing and expected income from sublease agreements.

5. Fair Value Measurement

Assets and liabilities measured at fair value on a recurring basis consist of the following as of June 30, 2016 (in thousands):

		Fair Value Measurements at Reporting Date Using		
	June 30, 2016	Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 100	$ 100	$ —	$ —
Liabilities:				
Deferred payments	$ 12,590	$ —	$ —	$ 12,590

Assets and liabilities measured at fair value on a recurring basis consist of the following as of December 31, 2015 (in thousands):

		Fair Value Measurements at Reporting Date Using		
	December 31, 2015	Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 100	$ 100	$ —	$ —
Liabilities:				
Deferred payments	$ 3,278	$ —	$ —	$ 3,278

The Company measures the above items on a recurring basis at fair value as follows:

· Money market funds – Classified in Level 1 is excess cash the Company holds in both taxable and tax-exempt money market funds and are included in cash and cash equivalents in the accompanying unaudited condensed consolidated balance sheets. The Company records any net unrealized gains and losses for changes in fair value as a component of Accumulated other comprehensive income in stockholders' equity. The Company's cash and cash equivalents held at December 31, 2015 and June 30, 2016, approximate fair value and are not disclosed in the above tables because of the short-term nature of the financial instruments.

· Deferred payments – The Company acquired certain assets and entered into deferred payment arrangements with the sellers in transactions in 2011 and January 2016, which are classified within Level 3 as there is no liquid market for similarly priced instruments. The deferred payments are valued using a discounted cash flow model that encompasses significant unobservable inputs to estimate the operating results of the acquired assets. The assumptions used to

prepare the discounted cash flows include estimates for interest rates, enrollment growth, retention rates, obtaining regulatory approvals for expansion into new markets, and pricing strategies. These assumptions are subject to change as the underlying data sources evolve and the programs mature. The short-term portion of deferred payments was $1.4 million as of June 30, 2016 and is included in accounts payable and accrued expense.

The Company's lease loss liability incorporates an assessment of current sublease market conditions and uses Level 3 inputs, but is not deemed a fair value liability as the future lease payments are required to be discounted using the Company's incremental borrowing rate at the date of lease abandonment without subsequent adjustment. See Note 4 for further discussion of the Company's lease loss liability.

The Company did not change its valuation techniques associated with recurring fair value measurements from prior periods, and no assets or liabilities were transferred between levels of the fair value hierarchy during the six months ended June 30, 2015 or 2016.

Changes in the fair value of the Company's Level 3 liabilities during the six months ended June 30, 2016 are as follows (in thousands):

	Deferred Payments
Balance at December 31, 2015	$ 3,278
Amounts earned	(468)
Contingent consideration in connection with NYCDA acquisition	8,500
Adjustments to fair value	1,280
Balance at June 30, 2016	$ 12,590

6. Long Term Debt

On July 2, 2015, the Company entered into an amended credit facility (the "Amended Credit Facility") which provides for a revolving line of credit (the "Revolver") up to $150 million and provides the Company with an option, under certain conditions, to increase the commitments under the Revolver or establish one or more incremental term loans in an amount up to $50 million in the aggregate in the future. The maturity date of the Amended Credit Facility is July 2, 2020. The Amended Credit Facility replaced the Company's prior credit agreement (the "Prior Credit Agreement"), dated November 8, 2012, which had provided for both a term loan and revolving line of credit and an original maturity date of December 31, 2016. All amounts outstanding under the Prior Credit Agreement were repaid upon execution of the Amended Credit Facility. The Company paid approximately $0.9 million in debt financing costs associated with the Amended Credit Facility.

Borrowings under the Revolver will bear interest at a per annum rate equal to, at the Company’s election, LIBOR or a base rate, plus a margin ranging from 1.75% to 2.25% depending on the Company’s leverage ratio. The Company also is subject to a quarterly unused commitment fee ranging from 0.25% to 0.35% per annum, depending on the Company’s leverage ratio, times the daily unused amount under the Revolver.

All other remaining terms of the Prior Credit Agreement remain in full force and effect. The Amended Credit Facility is guaranteed by the University and is secured by substantially all of the personal property and assets of the Company and its subsidiaries. The Amended Credit Facility contains customary affirmative and negative covenants, representations, warranties, events of default and remedies upon default, including acceleration and rights to foreclose on the collateral securing the Amended Credit Facility. In addition, as with the Prior Credit Agreement, the Amended Credit Facility requires that the Company satisfy certain financial maintenance covenants, including:

· A leverage ratio of not greater than 2 to 1. Leverage ratio is defined as the ratio of total debt to trailing four-quarter EBITDA (earnings before interest, taxes, depreciation, amortization and non-cash charges such as stock-based compensation).

· A coverage ratio of not less than 1.75 to 1. Coverage ratio is defined as the ratio of trailing four-quarter EBITDA and rent expense to trailing four-quarter interest and rent expense.

· A Department of Education Financial Responsibility Composite Score of not less than 1.5.

The Company was in compliance with all the terms of the Amended Credit Facility as of June 30, 2016.

During both the three and six months ended June 30, 2016, the Company paid cash interest of $0.1 million, compared to $1.1 million during both the three and six months ended June 30, 2015. The Company had no balance outstanding under the Revolver as of June 30, 2016.

7. Stock Options, Restricted Stock and Restricted Stock Units

On May 5, 2015, the Company's shareholders approved the Strayer Education, Inc. 2015 Equity Compensation Plan (the "2015 Plan"), which provides for the granting of restricted stock, restricted stock units, stock options intended to qualify as incentive stock options, options that do not qualify as incentive stock options, and other forms of equity compensation and performance-based awards to employees, officers and directors of the Company, or to a consultant or advisor to the Company, at the discretion of the Board of Directors. Vesting provisions are at the discretion of the Board of Directors. Options may be granted at option prices based at or above the fair market value of the shares at the date of grant. The maximum term of the awards granted under the 2015 Plan is ten years. The number of shares of common stock reserved for issuance under the 2015 Plan is 500,000 authorized but unissued shares, plus the number of shares available for grant under the Company's previously existing equity compensation plans at the time of stockholder approval of the 2015 Plan, and plus the number of shares which may in the future become available under any previously existing equity compensation plan due to forfeitures of outstanding awards.

In February 2016, the Company's Board of Directors approved grants of 176,802 shares of restricted stock and restricted stock units to certain employees. These shares, which vest over a two to four year period, were granted pursuant to the 2015 Plan. The Company's stock price closed at $50.67 on the date of these restricted stock grants.

In May 2016, the Company's Board of Directors approved grants of 11,365 shares of restricted stock. These shares, which vest annually over a three-year period, were awarded to non-employee members of the Company's Board of Directors, as part of the Company's annual director compensation program and the 2015 Plan. The Company's stock price closed at $49.27 on the date of these restricted stock grants.

Dividends paid on unvested restricted stock are reimbursed to the Company if the recipient forfeits his or her shares as a result of termination of employment prior to vesting in the award, unless waived by the Board of Directors.

Restricted Stock and Restricted Stock Units

The table below sets forth the restricted stock and restricted stock units activity for the six months ended June 30, 2016:

	Number of shares or units	Weighted-average Grant price
Balance, December 31, 2015	634,327	$ 104.66
Grants	188,167	50.59
Vested shares	(23,539)	50.43
Forfeitures	(433)	115.55
Balance, June 30, 2016	798,522	$ 94.36

Table of Contents

Stock Options

The table below sets forth the stock option activity and other stock option information as of and for the six months ended June 30, 2016:

	Number of shares	Weighted-average exercise price	Weighted-average remaining contractual life (years)	Aggregate intrinsic value(1) (in thousands)
Balance, December 31, 2015	100,000	$ 51.95	5.1	$ 817
Grants	—	—		
Exercises	—	—		
Forfeitures/Expirations	—	—		
Balance, June 30, 2016	100,000	$ 51.95	4.6	$ —
Exercisable, June 30, 2016	100,000	$ 51.95	4.6	$ —

(1) The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the respective trading day and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holder had all options been exercised on the respective trading day. The amount of intrinsic value will change based on the fair market value of the Company's common stock.

Valuation and Expense Information under Stock Compensation Topic ASC 718

At June 30, 2016, total stock-based compensation cost which has not yet been recognized was $27.1 million for unvested restricted stock, restricted stock units, and stock option awards. This cost is expected to be recognized over the next 31 months on a weighted-average basis. Awards of approximately 606,000 shares of restricted stock and restricted stock units are subject to performance conditions. The accrual for stock-based compensation for performance awards is based on the Company's estimates that such performance criteria are probable of being achieved over the respective vesting periods. Such a determination involves significant judgment surrounding the Company's ability to maintain regulatory compliance. If the performance targets are not reached during the respective vesting period, or it is determined it is more likely than not that the performance criteria will not be achieved, related compensation expense is adjusted.

The following table sets forth the amount of stock-based compensation expense recorded in each of the expense line items for the three and six months ended June 30, 2015 and 2016 (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2016	2015	2016
Instruction and educational support	$ 546	$ (438)	$ 914	$ 155
Marketing	—	—	—	—
Admissions advisory	—	—	—	—
General and administration	1,926	2,474	4,009	4,771
Stock-based compensation expense included in operating expense	2,472	2,036	4,923	4,926
Tax benefit	986	802	1,942	1,900
Stock-based compensation expense, net of tax	$ 1,486	$ 1,234	$ 2,981	$ 3,026

During the six months ended June 30, 2015 and 2016, the Company recognized a tax shortfall related to share-based payment arrangements of approximately $25,000 and $50,000, respectively. No stock options were exercised during the six months ended June 30, 2015 or 2016.

Table of Contents

8. Other Long-Term Liabilities

Other long-term liabilities consist of the following (in thousands):

	December 31, 2015	June 30, 2016
Deferred payments related to acquisitions	$ 6,078	$ 14,415
Deferred revenue, net of current portion	14,429	13,827
Loss on facilities not in use	15,229	9,999
Deferred rent and other facility costs	8,993	8,936
Lease incentives	3,125	2,896
Deferred gain on sale of campus building	133	—
	$ 47,987	$ 50,073

Deferred Payments Related to Acquisitions

In the first quarter of 2016, the Company acquired NYCDA and entered into deferred payment arrangements with the sellers in connection with this transaction. The deferred payment arrangements of up to $11.5 million are valued at approximately $8.5 million as of June 30, 2016. In April 2016, NYCDA achieved a performance target and the Company subsequently paid $6.0 million of deferred payments to the sellers. See Note 3 for further information on the NYCDA deferred payments.

In 2011, the Company acquired certain assets and entered into deferred payment arrangements with the sellers in connection with that acquisition. The deferred payment arrangements are valued at approximately $3.3 million and $3.1 million as of December 31, 2015 and June 30, 2016, respectively. In addition, one of the sellers contributed $2.8 million to the Company representing the seller's continuing interest in the assets acquired.

Deferred Revenue

The Company provides for certain scholarship and awards programs, such as the Graduation Fund (see Note 2 for additional information), that are earned by students when they successfully complete course requirements. The Company also has licensed certain of its non-credit bearing course content to a third party. Included in long-term deferred revenue is the amount of revenue under these arrangements that the Company expects will be realized after one year.

Loss on Facilities Not in Use and Deferred Rent and Other Facility Costs

The Company records a liability for lease costs of campuses and non-campus facilities that are not currently in use (see Note 3). For facilities still in use, the Company records rent expense on a straight-line basis over the initial term of a lease. The difference between the rent payment and the straight-line rent expense is recorded as a liability.

Lease Incentives

In conjunction with the opening of new campuses or renovating existing ones, the Company, in some instances, was reimbursed by the lessors for improvements made to the leased properties. In accordance with ASC 840-20, the underlying assets were capitalized as leasehold improvements and a liability was established for the reimbursements. The leasehold improvements and the liability are amortized on a straight-line basis over the corresponding lease terms, which generally range from five to 10 years.

Deferred Gain on Sale of Campus Building

In June 2007, the Company sold one of its campus buildings for $5.8 million. The Company is leasing back most of the campus building over a 10-year period. In conjunction with this sale and lease back transaction, the Company realized a gain of $2.8 million before tax, which is deferred and recognized over the 10-year lease term.

9. Income Taxes

The Company had $0.1 million of unrecognized tax benefits at June 30, 2016, all of which resulted from tax positions taken prior to the year ended December 31, 2015. The Company recognized approximately $0.3 million of benefits in the six months ended June 30, 2016. The Company also recorded approximately $0.1 million of expense in the six months ended June 30, 2016, related to interest and penalties.

It is reasonably possible that approximately $0.1 million of unrecognized tax benefits will be reduced in the next twelve months due to expiration of the applicable statutes of limitations, which would favorably affect the Company's effective tax rate if recognized. If amounts accrued are less than amounts ultimately assessed by taxing authorities, the Company would record additional income tax expense. The Company does not anticipate significant changes to other unrecognized tax benefits.

The Company paid $13.6 million and $18.2 million in income taxes during the six months ended June 30, 2015 and 2016, respectively.

10. Litigation

From time to time, the Company is involved in litigation and other legal proceedings arising out of the ordinary course of its business. There are no pending material legal proceedings to which the Company or its property are subject.

11. Regulation

The Company, the University, and NYCDA are subject to significant state and regulatory oversight, as well as federal oversight in the case of the Company and the University.

Gainful Employment

The Department of Education (the "Department") previously attempted to define "an eligible program of training to prepare students for gainful employment in a recognized occupation." After a federal court invalidated the Department's regulation, the Department established a negotiated rulemaking committee to consider the issue of gainful employment. The negotiations did not result in consensus. On March 25, 2014, the Department issued a Notice of Proposed Rulemaking for public comment, and on October 31, 2014, the Department published the final regulation which became effective on July 1, 2015.

The new requirements, which are applicable to the University but not NYCDA, include two debt-to-earnings measures, consisting of an annual earnings rate and a discretionary income rate. The annual earnings rate is calculated by comparing (1) the annual loan payment required on the median student loan debt incurred by students receiving

Title IV funds who completed a particular program and (2) the higher of the mean or median of those graduates' annual earnings two to four years after graduation. The discretionary income rate is calculated by comparing (1) the annual loan payment required on the median student loan debt incurred by students receiving Title IV funds who completed a particular program and (2) the higher of the mean or median annual earnings of those graduates two to four years after graduation, less 1.5 times the government issued Poverty Guideline. Under the new gainful employment regulation, a program would pass if:

- the annual loan payment required on the median student loan debt is less than or equal to 8% of the higher of the mean or median annual earnings of graduates in the relevant period; or

- the annual loan payment required on the median student loan debt is less than or equal to 20% of the discretionary income of graduates in the relevant period.

In addition, a program that does not pass either of the debt-to-earnings metrics, and that has an annual earnings rate between 8% and 12%, or a discretionary income rate between 20% and 30%, would be considered to be in a warning zone. A program would fail if the program's graduates have an annual earnings rate of 12% or greater and a discretionary income rate of 30% or greater. A program would become Title IV-ineligible for three years if it fails both metrics for two out of three consecutive years, or fails to pass at least one metric for four consecutive award years. If an institution is notified by the Secretary of Education that a program could become ineligible, based on its final rates, for the next award year:

- The institution must provide a warning with respect to the program to students and prospective students indicating, among other things, that students may not be able to use Title IV funds to attend or continue in the program; and

- The institution must not enroll, register or enter into a financial commitment with a prospective student until a specified time after providing the warning to the prospective student.

The new regulation also requires institutions to report student and program level data to the Department, and comply with additional disclosure requirements beginning in January 2017.

19

In addition, the gainful employment regulation required institutions to certify by December 31, 2015, among other things, that each eligible gainful employment program is programmatically accredited if required by a federal governmental entity or a state governmental entity in the state in which it is located or is otherwise required to obtain state approval, and that each eligible program satisfies the applicable educational prerequisites for professional licensure or certification requirements in each state in which it is located or is otherwise required to obtain state approval, so that a student who completes the program and seeks employment in that state qualifies to take any licensure or certification exam that is needed for the student to practice or find employment in an occupation that the program prepares students to enter. The Company timely made the required certification.

The requirements associated with the gainful employment regulations may substantially increase the Company's administrative burdens and could affect student enrollment, persistence and retention. Further, although the regulations provide opportunities for an institution to correct any potential deficiencies in a program prior to the loss of Title IV eligibility, the continuing eligibility of the University's academic programs will be affected by factors beyond management's control such as changes in the University's graduates' income levels, changes in student borrowing levels, increases in interest rates, changes in the percentage of former students who are current in the repayment of their student loans, and various other factors. Even if the Company were able to correct any deficiency in the gainful employment metrics in a timely manner, the disclosure requirements associated with a program's failure to meet at least one metric may adversely affect student enrollments in that program and may adversely affect the reputation of the University.

Borrower Defenses to Repayment

The Department's current regulations permit a Federal Direct Loan borrower to obtain a loan discharge if the institution's acts or omissions give rise to a cause of action against the institution under state law. The regulations do not address the applicable process. In January 2016, the Department of Education convened a negotiated rulemaking committee to discuss the processes and standards for the discharge of Federal Direct Loans, commonly known as defenses to repayment, and other issues. The committee failed to reach consensus. In June 2016, the Department issued a Notice of Proposed Rulemaking to establish a new federal standard and processes for determining whether a borrower has a defense to repayment and a right to recover amounts previously paid to the Department on Federal Direct Loans based on an act or omission of a school. While Federal Direct Loans disbursed prior to July 1, 2017 would remain subject to the current rule, the proposed regulations would provide three categories of borrower defenses that could be asserted by students with Federal Direct Loans disbursed on or after July 1, 2017, including:

- the institution has had a judgment issued against it in an action brought by a student or a government official or entity, related to the loan or educational services, in a contested proceeding;
- the institution failed to perform its obligations under the terms of a contract with the student; or

- the institution made a "substantial misrepresentation" about the nature of its programs, financial charges or employability of its graduates that the borrower reasonably relied upon on when he or she decided to attend or continue attending the institution.

In addition, the proposed regulation would permit the Department to grant relief to an individual or group of individuals, including individuals who have not applied to the Department seeking relief. In most cases, the proposed regulation would entitle the Department to seek reimbursement from the institution for any loans discharged under the new procedure.

The proposed regulation would also specify triggering events that would automatically lead to a determination that an institution is not able to meet its financial or administrative obligations, to include:

- certain lawsuits and other legal actions, including, among others:

  - the institution incurring a debt or liability arising from an audit, investigation, or similar action initiated by a state, federal, or other oversight entity, including settlements, that is based on claims related to the making of federal loans or the provision of educational services, for an amount that exceeds the lesser of $750,000 or 10% of the institution's current assets;

  - the commencement of a suit initiated by a state, federal, or other oversight entity based on claims of any kind, where the potential monetary sanctions or damages arising from the suit are in an amount that exceeds 10% of the institution's current assets;

- a judicial or administrative proceeding, that is not part of a state or federal action, that the institution discloses in a report filed with the SEC;

- payment to the Department of substantial monetary liabilities from claims asserted under borrower defense procedures;

- action by the institution's accreditor that could result in the loss of accreditation;

- failure of the 90/10 regulation in any given year; and/or

- default by the school on its debt obligations.

In addition, other triggering events could lead to a determination that the institution is not able to meet its financial obligations, if the Secretary of the Department determines that the event is reasonably likely to have a material effect on the institution, as determined in the discretion of the Secretary. If any of the automatic or discretionary triggering events materialize, the institution would be required to post a letter of credit, for each triggering event, in an amount of at least 10% of the school's annual Title IV disbursements, and to provide warnings to prospective and current students that the institution has been required to provide enhanced financial protection to the Department.

In addition, the proposed regulation would establish a new metric to measure student loan repayment rates as a ratio of present balance to original principal balance, and proprietary institutions which fall below an established threshold would be required to provide prospective and current students with disclosures regarding the repayment rate.

The Company cannot predict the impact, if any, that these proposed regulations would have if adopted.

The effective date of the proposed regulations, if adopted, cannot be determined at this time, but the proposed regulations could be effective as early as July 1, 2017.

State authorization for distance education and foreign locations

Under the Higher Education Act and the Department's implementing regulations, in order to be eligible to participate in Title IV programs, an institution must be legally authorized to offer a program of postsecondary education in the state in which the institution is physically located. The Department previously attempted to regulate the state authorization that an institution offering distance education programs must have in order to offer Title IV aid to

students enrolled in such programs. After a federal court vacated the Department's regulation on procedural grounds, the Department established a negotiated rulemaking committee to consider state authorization for distance education and foreign locations, among other topics. The negotiations resulted in consensus as to foreign locations, but not as to distance education. In June 2016, the Department issued a Notice of Proposed Rulemaking for public comment.

The proposed regulations, among other things, would require an institution offering distance education or correspondence courses to be authorized by each state in which the institution enrolls students, if such authorization is required by the state, in order to award Title IV aid to such students. An institution could obtain such authorization directly from the state or through a state authorization reciprocity agreement. A state authorization reciprocity agreement would be defined as an agreement between two or more states that authorizes an institution located and legally authorized in a state covered by the agreement to provide postsecondary education through distance education or correspondence courses to students in other states covered by the agreement and does not prohibit a participating state from enforcing its own consumer protection laws. The proposed regulations would also require an institution to document the state process for resolving complaints from students enrolled in programs offered through distance education or correspondence courses for each state in which such students reside.

The proposed regulations would require an institution to provide public and individualized disclosures to enrolled and prospective students regarding its programs offered solely through distance education or correspondence courses. The public disclosures would include state authorization for the program or course, the process for submitting complaints to relevant states, any adverse actions by a state or accrediting agency related to the distance education program or correspondence course within the past five years, refund policies, and applicable licensure or certification requirements for a career a student prepares to enter and the program's sufficiency to meet those requirements. An institution must disclose directly to all prospective students when a distance education or correspondence course does not meet the licensure or certification requirements for a state. An institution must

21

disclose to each enrolled and prospective student when an adverse action is taken against an institution's postsecondary distance education or correspondence program and any determination that a program ceases to meet licensure or certification requirements.

The Company cannot predict the impact, if any, that these proposed regulations would have if adopted. The effective date of the proposed regulations, if adopted, cannot be determined at this time, but the proposed regulations could be effective as early as July 1, 2017.

The Clery Act

Strayer University must comply with the campus safety and security reporting requirements as well as other requirements in the Jeanne Clery Disclosure of Campus Security Policy and Campus Crime Statistics Act (the "Clery Act"), including recent changes made to the Clery Act by the Violence Against Women Reauthorization Act of 2013, which was signed into law on March 7, 2013. On April 1, 2014, a negotiated rulemaking committee reached consensus on proposed regulations, and on October 20, 2014, the Department promulgated regulations implementing the recent amendments to the Clery Act, effective July 1, 2015. In addition, the Department has interpreted Title IX to categorize sexual violence as a form of prohibited sex discrimination and to require institutions to follow certain disciplinary procedures with respect to such offenses. Failure to comply with the Clery Act or Title IX requirements or regulations thereunder could result in action by the Department to require correction action, fine the Company or limit or suspend its participation in Title IV programs, could lead to litigation, and could harm the Company's reputation. The Company is in compliance with these requirements.

Compliance Reviews

Strayer University is subject to announced and unannounced compliance reviews and audits by various external agencies, including the Department, its Office of Inspector General, state licensing agencies, and accrediting agencies. The Department conducted four campus-based program reviews of Strayer University campuses in three states and the District of Columbia during 2014. The reviews covered federal financial aid years 2012-2013 and 2013-2014, and two of the reviews also covered compliance with the Clery Act, the Drug-Free Schools and Communities Act, and regulations related thereto. Strayer University received Final Program Review Determination letters for each of the four program reviews, closing out each with no further action required.

Program Participation Agreement

As a participant in Title IV programs, the University must enter into a Program Participation Agreement with the Department. Under the agreement, the institution agrees to follow the Department's rules and regulations governing Title IV programs. On October 1, 2014, Strayer University received an executed provisional Program Participation Agreement from the Department allowing it to participate in Title IV programs until June 30, 2017. The Program Participation Agreement was issued on a provisional basis because of the Department's program reviews open at the time of issuance. Under the provisional agreement, the only material additional condition that the University must comply with is obtaining Department approval for substantial changes, including the addition of any new location, level of academic offering, non-degree program, or degree program.

NYCDA

NYCDA is licensed to operate in New York, Texas, Georgia, Utah, North Carolina, Washington, Colorado, and Washington, D.C., but is not accredited, does not participate in state or federal student financial aid programs, and is not subject to the regulatory requirements applicable to accredited schools and schools that participate in such financial aid programs such as those described above. Programs such as those offered by NYCDA are regulated by each individual state, and the Company is in the process of seeking authorizations in additional states to offer NYCDA programs.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Notice Regarding Forward-Looking Statements

Certain of the statements included in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" as well as elsewhere in this report on Form 10-Q are forward-looking statements made pursuant to the Private Securities Litigation Reform Act of 1995 ("Reform Act"). Such statements may be identified by the use of words such as "expect,"

"estimate," "assume," "believe," "anticipate," "will," "forecast," "plan," "project," or similar words, and include, without limit statements relating to future enrollment, revenues, revenues per student, earnings growth, operating expenses and capital expenditures. These statements are based on the Company's current expectations and are subject to a number of assumptions, risks and uncertainties. In accordance with the Safe Harbor provisions of the Reform Act, the Company has identified important factors that could cause the actual results to differ materially from those expressed in or implied by such statements. The assumptions, risks and uncertainties include the pace of growth of student enrollment, our continued compliance with Title IV of the Higher Education Act, and the regulations thereunder, as well as regional accreditation standards and state regulatory requirements, rulemaking by the Department of Education and increased focus by the U. S. Congress on for-profit education institutions, competitive factors, risks associated with the opening of new campuses, risks associated with the offering of new educational programs and adapting to other changes, risks associated with the acquisition of existing educational institutions, risks relating to the timing of regulatory approvals, our ability to implement our growth strategy, risks associated with the ability of our students to finance their education in a timely manner, and general economic and market conditions. Further information about these and other relevant risks and uncertainties may be found in the Company's Annual Report on Form 10-K and its other filings with the Securities and Exchange Commission. The Company undertakes no obligation to update or revise forward-looking statements, except as may be required by law.

Additional Information

We maintain a website at http://www.strayereducation.com. The information on our website is not incorporated by reference in this Quarterly Report on Form 10-Q, and our web address is included as an inactive textual reference only. We make available, free of charge through our website, our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission.

Background and Overview

We are an education services holding company that owns Strayer University (the "University") and, as of January 13, 2016, the New York Code and Design Academy ("NYCDA"). The University is an institution of higher education which offers undergraduate and graduate degree programs at physical campuses, predominantly located in the eastern United States, and online.

The University derives approximately 95% of its revenue from tuition for educational programs, whether delivered in person at a physical campus or delivered online. The academic year of the University is divided into four quarters, which approximately coincide with the four quarters of the calendar year. Students make payment arrangements for the tuition for each course at the time of enrollment. Tuition revenue is recognized in the quarter of instruction. If a student withdraws from a course prior to completion, the University refunds a portion of the tuition depending on when the withdrawal occurs. Tuition revenue is shown net of any refunds, withdrawals, corporate discounts, employee

tuition discounts and scholarships. The University also derives revenue from other sources such as textbook-related income, certificate revenue, certain academic fees, licensing revenue, and other income, which are all recognized when earned. NYCDA provides non-degree courses in web and application software development and revenue is recognized ratably as services are provided.

Tuition receivable and deferred revenue for our students are recorded upon the start of the academic term or program. Because the University's academic quarters coincide with the calendar quarters, at the end of the fiscal quarter (and academic term), tuition receivable generally represents amounts due from students for educational services already provided and deferred revenue generally represents advance payments for academic services to be provided in the future. Based upon past experience and judgment, the University establishes an allowance for doubtful accounts with respect to accounts receivable. Any uncollected account more than one year past due is charged against the allowance. Accounts less than one year past due are reserved according to the length of time the balance has been outstanding. In establishing reserve amounts, we also consider the status of students as to whether or not they are currently enrolled for the next term, as well as the likelihood of recovering balances that have previously been written off, based on historical experience. Bad debt expense as a percentage of revenues for the second quarter of 2016 and 2015 was 3.8% and 3.2%, respectively.

Below is a description of the nature of the consolidated costs included in our operating expense categories:

- Instruction and educational support expenses generally contain items of expense directly attributable to educational activities of the University. This expense category includes salaries and benefits of faculty and academic administrators,

as well as administrative personnel who support and serve student interests. Instruction and educational support expenses also include costs of educational supplies and facilities, including rent for campus facilities, certain costs of establishing and maintaining computer laboratories and all other physical plant and occupancy costs, with the exception of costs attributable to the corporate offices. Bad debt expense incurred on delinquent student account balances is also included in instruction and educational support expenses.

· Marketing expenses include the costs of advertising and production of marketing materials and related personnel costs.

· Admissions advisory expenses include salaries, benefits and related costs of personnel engaged in admissions.

· General and administration expenses include salaries and benefits of management and employees engaged in accounting, human resources, legal, regulatory compliance, and other corporate functions, along with the occupancy and other related costs attributable to such functions.

Investment income consists primarily of earnings and realized gains or losses on investments. Interest expense consists of interest incurred on our outstanding borrowings, fees on the unused portion of our revolving credit facility, and amortization of deferred financing costs.

We acquired NYCDA on January 13, 2016. NYCDA provides non-degree courses in web and application software development, primarily at its campus in New York City. The acquisition did not impact our 2015 results and NYCDA's results of operations are included in our results from the acquisition date.

Critical Accounting Policies and Estimates

"Management's Discussion and Analysis of Financial Condition and Results of Operations" discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and the related disclosures of contingent assets and liabilities. On an ongoing basis, management evaluates its estimates and judgments related to its allowance for doubtful accounts; income tax provisions; the useful lives of property and equipment; redemption rates for scholarship programs; fair value of future contractual operating lease obligations for facilities that have been closed; valuation of deferred tax assets, goodwill, and intangible assets; forfeiture rates and achievability of performance targets for stock-based compensation plans; and accrued expenses. Management bases its estimates and judgments on historical experience and various other factors and assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments regarding the carrying values of assets and liabilities that are not readily apparent from other sources. Management regularly reviews its estimates and judgments for reasonableness and may modify them in the future. Actual results may differ from these estimates under different assumptions or conditions.

Management believes that the following critical accounting policies are its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue recognition — Like many traditional institutions, Strayer University offers its educational programs on a quarter system having four academic terms, which coincide with our quarterly financial reporting periods. Approximately 95% of our revenues during the three months ended June 30, 2016 consisted of tuition revenue. Tuition revenue is recognized ratably in the quarter of instruction as the University provides academic services in a given term, whether delivered in person at a physical campus or online. Tuition revenue is shown net of any refunds, withdrawals, corporate discounts, scholarships and employee tuition discounts. The University also derives revenue from other sources such as textbook-related income, certificate revenue, certain academic fees, licensing revenue, and other income, which are all recognized when earned. At the start of each academic term or program, a liability (deferred revenue) is recorded for academic services to be provided and a tuition receivable is recorded for the portion of the tuition not paid in advance. Any cash received prior to the start of an academic term is recorded as deferred revenue. NYCDA provides non-degree courses in web and application software development and tuition revenue is recognized ratably over the duration of each course.

Students finance their education in a variety of ways, and historically about three quarters of our students participated in one or more financial aid programs provided through Title IV of the Higher Education Act. In addition, many of our working adult students finance their own education or receive full or partial tuition reimbursement from their employers. Those students who are veterans or active duty military personnel have access to various additional government-funded educational benefit programs.

A typical University class is offered in weekly increments over a ten-week period and is followed by an exam. Students who withdraw from a course may be eligible for a refund of tuition charges based on the timing of the withdrawal. We use the student's last date of attendance for this purpose. Student attendance is based on physical presence in class for on-ground classes. For online classes, attendance consists of logging into one's course shell and performing an academically related activity (e.g., engaging in a discussion post or taking a quiz).

If a student withdraws from a course prior to completion, a portion of the tuition is refundable depending on when the withdrawal occurs. Our refund policy typically permits students who complete less than half of a course to receive a partial refund of tuition for that course. Refunds reduce the tuition revenue that would have otherwise been recognized for that student. Since the University's academic terms coincide with our financial reporting periods, nearly all refunds are processed and recorded in the same quarter as the corresponding revenue. The amount of tuition revenue refundable to students may vary based on the student's state of residence.

For undergraduate students who withdraw from all their courses during the quarter of instruction, we reassess collectibility of tuition and fees for revenue recognition purposes. In addition, we cease revenue recognition when a student fully withdraws from all of his or her courses in the academic term. Tuition charges billed in accordance with our billing schedule may be greater than the pro rata revenue amount, but the additional amounts are not recognized as revenue unless they are collected in cash.

For students who receive funding under Title IV, funds are subject to return provisions as defined by the Department of Education. If Title IV funds are returned to the Department of Education, the student is responsible for paying the amount of prorated tuition charged to him or her. Loss of financial aid eligibility during an academic term is rare and would normally coincide with the student's withdrawal from the institution. As discussed above, we cease revenue recognition upon a student's withdrawal from all of his or her classes in an academic term.

New University students registering in credit-bearing courses in any undergraduate program for the summer 2013 term (fiscal third quarter) and subsequent terms qualify for the Graduation Fund, whereby qualifying students earn tuition credits that are redeemable in the final year of a student's course of study if he or she successfully remains in the program. Students must meet all of the University's admission requirements and not be eligible for any previously offered scholarship program. Our employees and their dependents are not eligible for the program. To maintain eligibility, students must be enrolled in a bachelor's degree program. Students who have more than one consecutive term of non-attendance lose any Graduation Fund credits earned to date, but may earn and accumulate new credits if the student is reinstated or readmitted by the University in the future. In their final academic year, qualifying students will receive one free course for every three courses that were successfully completed. Revenue and the value of the benefit earned by students participating in the Graduation Fund is recognized based on a systematic and rational allocation of the cost of honoring the benefit earned to each of the underlying revenue transactions that result in progress by the student toward earning the benefit. The estimated value of awards under the Graduation Fund that will be recognized in the future is based on historical experience of students' persistence in completing their course of study and earning a degree. Estimated redemption rates of eligible students vary based on their term of enrollment. As of

June 30, 2016, we had deferred $25.3 million for estimated redemptions earned under the Graduation Fund, as compared to $15.6 million at June 30, 2015. Each quarter we assess our methodologies and assumptions underlying our estimates for persistence and estimated redemptions based on actual experience. To date, any adjustments to our estimates have not been material. However, if actual persistence or redemption rates change, adjustments to the reserve may be necessary and could be material.

Tuition receivable — We record estimates for our allowance for doubtful accounts for tuition receivable from students primarily based on our historical collection rates by age of receivable, net of recoveries, and consideration of other relevant factors. Our experience is that payment of outstanding balances is significantly influenced by whether the student returns to the institution as we require students to make payment arrangements for their outstanding balances prior to enrollment. Therefore, we monitor outstanding tuition receivable balances through subsequent terms, increasing the reserve on such balances over time as the likelihood of returning to the institution diminishes and our historical experience indicates collection is less likely. We periodically assess our methodologies for estimating bad debts in consideration of actual experience. If the financial condition of our students were to deteriorate, resulting in evidence of impairment of their ability to make required payments for tuition payable to us, additional allowances or write-offs may be required. For the second quarter of 2016, our bad debt expense was 3.8% of revenue, compared to 3.2% for the same period in 2015. A change in our allowance for doubtful accounts of 1% of gross tuition receivable as of June 30, 2016 would have changed our income from operations by approximately $0.3 million.

Accrued lease and related costs — We estimate potential sublease income and vacancy periods for space that is not in use, adjusting our estimates when circumstances change. If our estimates change or if we enter into subleases at rates that are

substantially different than our current estimates, we will adjust our liability for lease and related costs. During the six months ended June 30, 2016 and 2015, we reduced our liability for leases by approximately $1.7 million and $0.1 million, respectively.

Other estimates — We record estimates for certain of our accrued expenses and income tax liabilities. We estimate the useful lives of our property and equipment. We periodically assess goodwill and intangible assets for impairment. We periodically review our assumed forfeiture rates and ability to achieve performance targets for stock-based awards and adjust them as necessary. Should actual results differ from our estimates, revisions to our accrued expenses, carrying amount of goodwill and intangible assets, stock-based compensation expense, and income tax liabilities may be required.

Results of Operations

In the second quarter of 2016, we generated $108.5 million in revenue, a 1% decrease compared to 2015, principally due to a 2% decline in revenue per student and partially offset by slightly higher enrollment growth. Income from operations was $12.9 million for the second quarter of 2016, and includes approximately $0.1 million in adjustments to reduce our liability for losses on facilities no longer in use. Income from operations for the second quarter of 2015 was $20.9 million, which includes $0.1 million in adjustments to our liability for losses on facilities no longer in use. Net income in the second quarter of 2016 was $7.8 million, including approximately $0.1 million in after-tax benefits from adjustments to the Company's liability for facilities no longer in use, compared to $11.9 million for the same period in 2015, which reflected approximately $0.1 million in after-tax charges from adjustments to the Company's liability for facilities no longer in use. Diluted earnings per share was $0.72 compared to $1.11 for the same period in 2015. Diluted earnings per share for the second quarter of 2016 includes $0.01 per share in after-tax earnings related to the reduction of the Company's liability for losses on facilities no longer in use. For the second quarter of 2015, the after-tax adjustments related to the Company's liability for facilities no longer in use had no impact on diluted earnings per share. The impact of NYCDA's financial results since the acquisition date was not material relative to our consolidated results of operations for the six months ended June 30, 2016.

Key enrollment trends by quarter for the University were as follows:

Enrollment

% Change vs Prior Year

Since 2013, we have introduced a number of initiatives in response to the variability in our enrollment. Recognizing that affordability is an important factor in a prospective student's decision to seek a college degree, we reduced Strayer

University undergraduate tuition for new students by 20% beginning in our 2014 winter academic term. We also introduced the Graduation Fund in mid-2013, whereby qualifying students can receive one free course for every three courses successfully completed. The free courses are redeemable in the student's final academic year. In 2015, we launched Strayer@Work, which works with Fortune

26

Table of Contents

1000 companies to structure customized degree and certificate programs for their employees, often with significant discounts to our published tuition rates. In January 2016, we acquired the New York Code and Design Academy, which charges variable tuition by program based on the number of hours of instruction. These initiatives could result in increased volatility in our revenue per student. However, we believe these initiatives, and others, will continue to support our competitive position in adult education and, over the long term, will lead to growth.

Three Months Ended June 30, 2016 Compared to Three Months Ended June 30, 2015

Enrollment. Total enrollments at Strayer University for the spring term 2016 increased to 41,029 students, from 40,875 for the spring term 2015. New student enrollments decreased by 7%, and continuing student enrollments increased by 2%.

Revenues. Revenues decreased 1% to $108.5 million in the second quarter of 2016 from $109.8 million in the second quarter of 2015, principally due to a decline in revenue per student of 2%, partially offset by slightly higher enrollment growth. The decline in revenue per student is largely attributable to a new pricing structure which was implemented for the first quarter of 2014 which reduced tuition for new undergraduate students by approximately 20%, and made them eligible for our Graduation Fund. Revenues for undergraduate students were generally unchanged in 2016, driven by an increase in enrollment of 3% and a decline of 3% in revenue per student. We expect this decline in revenue per student to continue at the undergraduate level, though more gradually, as we enroll more new undergraduate students. For graduate students, revenues decreased 3% in 2016, driven by an increase in revenue per student of 3%, offset by a decline in enrollment of 5%. The increase in graduate revenue per student was due primarily to increased tuition and higher classes per student compared to 2015.

Instruction and educational support expenses. Instruction and educational support expenses increased $2.6 million, or 4%, to $61.8 million in the second quarter of 2016 from $59.2 million in the second quarter of 2015. The increase primarily resulted from instructional costs for NYCDA, which was acquired in the first quarter of 2016, higher costs associated with new academic content, and higher bad debt expense as compared to the prior year. Instruction and educational support expenses as a percentage of revenues increased to 56.9% in the second quarter of 2016 from 54.0% in the second quarter of 2015.

Marketing expenses. Marketing expenses increased $3.0 million, or 21%, to $17.7 million in the second quarter of 2016 from $14.7 million in the second quarter of 2015, principally due to investments in branding initiatives at NYCDA and Strayer University. Marketing expenses as a percentage of revenues increased to 16.4% in 2016 from 13.4% in 2015. We expect to continue to invest in our marketing efforts such that marketing expenses may increase in absolute terms and as a percentage of revenue in 2016 as compared to 2015.

Admissions advisory expenses. Admissions advisory expenses remained unchanged at $4.1 million in the second quarter of 2016 and 2015. Admissions advisory expenses as a percentage of revenues increased to 3.8% in the second quarter of 2016 from 3.7% in the second quarter of 2015.

General and administration expenses. General and administration expenses increased $1.1 million, or 10%, to $11.9 million in the second quarter of 2016 from $10.8 million in 2015, as we incurred higher regulatory and related costs associated with expanding NYCDA's operations into new markets. General and administration expenses as a percentage of revenues increased to 11.0% in the second quarter of 2016 from 9.9% in the second quarter of 2015.

Income from operations. Income from operations decreased $8.0 million, or 38%, to $12.9 million in the second quarter of 2016 from $20.9 million in the second quarter of 2015.

Interest expense. Interest expense decreased to $0.2 million in the second quarter of 2016 from $1.3 million in the second quarter of 2015 following the repayment in July 2015 of all our outstanding debt in connection with our amended credit facility. We have $150.0 million available under our revolving credit facility and no balance outstanding as of June 30, 2016.

Provision for income taxes. Income tax expense decreased $2.8 million, or 36%, to $5.1 million in the second quarter of 2016 from $7.9 million in the second quarter of 2015, primarily due to the decrease in income before income taxes attributable to the factors discussed above. Our effective tax rate was 39.4% for the second quarter of 2016 compared to 39.9% for the same period in 2015.

Net income. Net income decreased $4.1 million to $7.8 million in the second quarter of 2016 from $11.9 million in the second quarter of 2015 due to the factors discussed above.

Six Months Ended June 30, 2016 Compared to Six Months Ended June 30, 2015

Enrollment. Average enrollments at Strayer University increased less than 1% to 40,951 students for the six months ended June 30, 2016 compared to 40,802 students for the same period in 2015.

Revenues. Revenues decreased 1% to $219.7 million in the six months ended June 30, 2016 from $221.6 million in the six months ended June 30, 2015, principally due to a decline in revenue per student of 1%, partially offset by slightly higher enrollment growth. The decline in revenue per student is largely attributable to a new pricing structure which was implemented for the first quarter of 2014 which reduced tuition for new undergraduate students by approximately 20%, and made them eligible for our Graduation Fund. Revenues for undergraduate students were generally unchanged in 2016, driven by an increase in enrollment of 3% and a decline of 3% in revenue per student. We expect this decline in revenue per student to continue at the undergraduate level, though more gradually, as we enroll more new undergraduate students. For graduate students, revenues decreased 4% in 2016, driven by an increase in revenue per student of 2%, offset by a decline in enrollment of 6%. The increase in graduate revenue per student was due primarily to increased tuition and higher classes per student compared to 2015.

Instruction and educational support expenses. Instruction and educational support expenses increased $1.0 million, or 1%, to $119.9 million in the six months ended June 30, 2016 from $118.9 million in the six months ended June 30, 2015. We recorded adjustments in each of the six months ended June 30, 2016 and 2015, resulting from changes in the timing and expected income from settlements and sublease agreements, and may record additional adjustments in the future. These adjustments were partially offset by the instruction and educational costs of NYCDA following the acquisition, as well as costs associated with new academic content. Instruction and educational support expenses as a percentage of revenues increased to 54.6% in the six months ended June 30, 2016 from 53.7% in the six months ended June 30, 2015.

Marketing expenses. Marketing expenses increased $4.6 million, or 15%, to $36.0 million in the six months ended June 30, 2016 from $31.4 million in the six months ended June 30, 2015, principally due to investments in branding initiatives at NYCDA and Strayer University. Marketing expenses as a percentage of revenues increased to 16.4% in 2016 from 14.1% in 2015. We expect to continue to invest in our marketing efforts such that marketing expenses may increase in absolute terms and as a percentage of revenue in 2016 as compared to 2015.

Admissions advisory expenses. Admissions advisory expenses increased by $0.4 million, or 5%, to $8.5 million in the six months ended June 30, 2016 from $8.1 million in the six months June 30, 2015, primarily as a result of higher personnel costs. Admissions advisory expenses as a percentage of revenues increased to 3.9% in the six months ended June 30, 2016 from 3.6% in the six months ended June 30, 2015.

General and administration expenses. General and administration expenses decreased $0.2 million, or 1.1%, to $22.3 million in the six months ended June 30, 2016 from $22.5 million in the six months ended June 30, 2015. During the six months ended June 30, 2016 we recorded an adjustment to reduce our lease loss liability resulting from the sublease of a portion of our corporate office space, partially offset by higher regulatory and related costs associated with expanding NYCDA’s operations into new markets. General and administration expenses as a percentage of revenues decreased to 10.1% in the six months ended June 30, 2016 from 10.2% in the six months ended June 30, 2015.

Income from operations. Income from operations decreased $7.8 million, or 19%, to $33.0 million in the six months ended June 30, 2016 from $40.8 million in the six months ended June 30, 2015.

Interest expense. Interest expense decreased to $0.3 million in the six months ended June 30, 2016 from $2.5 million in the six months ended June 30, 2015 following the repayment in July 2015 of all our outstanding debt in connection with our amended credit facility. We have $150.0 million available under our revolving credit facility and no balance outstanding as of June 30, 2016.

Provision for income taxes. Income tax expense decreased $2.5 million, or 16%, to $12.7 million in the six months ended June 30, 2016 from $15.2 million in the six months ended June 30, 2015, primarily due to the decrease in income before income taxes attributable to the factors discussed above. Our effective tax rate was 38.5% in the six months ended June 30, 2016, compared to 39.5% for the six months ended June 30, 2015.

Net income. Net income decreased $3.1 million to $20.2 million in the six months ended June 30, 2016 from $23.3 million in the six months ended June 30, 2015 due to the factors discussed above.

Table of Contents

Liquidity and Capital Resources

At June 30, 2016, we had cash and cash equivalents of $117.4 million compared to $106.9 million at December 31, 2015 and $195.6 million at June 30, 2015, prior to the repayment of the entire balance on our term loan of approximately $115.6 million. At June 30, 2016, most of our cash was invested in bank overnight deposits.

In January 2016, we completed the acquisition of New York Code and Design Academy, which provides non-degree courses in web and application software development, primarily at its campus in New York City. We have paid $8.4 million to date and may pay up to an additional $12.0 million to the sellers consisting of (a) up to $11.5 million payable based on NYCDA’s results of operations over a five-year period and (b) $0.5 million payable based on NYCDA’s receipt of a state regulatory permit. In addition, we paid $4.6 million to the founders in connection with their continued employment, which is reimbursable to us if either of the founders voluntarily terminates his employment within three years of the acquisition date.

In July 2015, we repaid all balances outstanding under a prior credit facility, and entered into an amended credit agreement which provides for a $150 million revolving credit facility and an option to establish incremental term loans under certain conditions. The amended credit agreement has a maturity date of July 2, 2020. We had no borrowings outstanding under the revolving credit facility as of June 30, 2016.

Borrowings under the revolving credit facility bear interest at LIBOR or a base rate, plus a margin ranging from 1.75% to 2.25%, depending on our leverage ratio. An unused commitment fee ranging from 0.25% to 0.35%, depending on our leverage ratio, accrues on unused amounts under the revolving credit facility. During the six months ended June 30, 2016 and 2015, we paid cash interest of $0.1 million and $2.2 million, respectively.

The amended credit agreement is guaranteed by our subsidiaries and is secured by substantially all of the personal property and assets of the Company and the guarantors. The amended credit agreement contains customary covenants, representations, warranties, events of default and remedies upon default. In addition, we must satisfy certain financial maintenance covenants, including a total leverage ratio, a coverage ratio and a U.S. Department of Education financial responsibility composite score. We were in compliance with all applicable covenants related to the amended credit agreement as of June 30, 2016.

Our net cash from operating activities for the six months ended June 30, 2016 decreased to $22.4 million, as compared to $43.8 million for the same period in 2015. The decrease in net cash from operating activities was largely due to changes in working capital, the timing of income tax payments, and payment of retention agreements in connection with the NYCDA acquisition. Capital expenditures were $3.9 million for the three months ended June 30, 2016, compared to $7.1 million for the same period in 2015.

For the six months ended June 30, 2016, we did not repurchase any shares of common stock and, at June 30, 2016, had $70 million in repurchase authorization to use through December 31, 2016. We did not pay a regular quarterly dividend in either 2016 or 2015.

For the second quarter of 2016, bad debt expense as a percentage of revenue was 3.8% compared to 3.2% for 2015.

We have available $150 million under our revolving credit facility. We believe that existing cash and cash equivalents, cash generated from operating activities, and if necessary, cash borrowed under the credit facility, will be sufficient to meet our requirements for at least the next 12 months. Currently, we maintain our cash in mostly FDIC-insured bank accounts. Excess cash is invested in money market funds, which is included in cash and cash equivalents at June 30, 2016 and 2015. We earned interest income of $0.2 million in the six months ended June 30, 2016 and 2015.

The table below sets forth our contractual commitments associated with operating leases, excluding subleases as of June 30, 2016 (in thousands):

	Payments Due By Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Operating leases	$ 160,418	$ 36,751	$ 60,481	$ 40,103	$ 23,083

29

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to the impact of interest rate changes and may be subject to changes in the market values of our future investments. We invest our excess cash in bank overnight deposits, money market funds and marketable securities. We have not used derivative financial instruments in our investment portfolio. Earnings from investments in bank overnight deposits, money market mutual funds, and marketable securities may be adversely affected in the future should interest rates decline, although such a decline may reduce the interest rate payable on any borrowings under our revolving credit facility. Our future investment income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if forced to sell securities that have declined in market value due to changes in interest rates. As of June 30, 2016, a 1% increase or decrease in interest rates would not have a material impact on our future earnings, fair values, or cash flows related to investments in cash equivalents or interest earning marketable securities.

Changing interest rates could also have a negative impact on the amount of interest expense we incur. On July 2, 2015, we used approximately $116 million of our existing cash and cash equivalents to prepay our term loan and terminate an interest rate swap as part of an amendment to our credit and term loan agreement. The amended credit agreement provides for a $150 million revolving credit facility and an option to establish incremental term loans under certain conditions. The amended credit agreement has a maturity date of July 2, 2020. We had no borrowings outstanding under the revolving credit facility after prepayment of the term loan facility, and as of June 30, 2016. Borrowings under the revolving credit facility bear interest at LIBOR or a base rate, plus a margin ranging from 1.75% to 2.25%, depending on our leverage ratio. An unused commitment fee ranging from 0.25% to 0.35%, depending on our leverage ratio, accrues on unused amounts under the revolving credit facility. An increase in LIBOR would affect interest expense on any outstanding balance of the revolving credit facility. For every 100 basis points increase in LIBOR, we would incur an incremental $1.5 million in interest expense per year assuming the entire $150 million revolving credit facility was utilized.

ITEM 4: CONTROLS AND PROCEDURES

a) Disclosure Controls and Procedures. The Company's management, with the participation of its Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of June 30, 2016. Based upon such review, the Chief Executive Officer and Chief Financial Officer have concluded that the Company had in place, as of June 30, 2016, effective disclosure controls and procedures designed to ensure that information required to be disclosed by the Company (including consolidated subsidiaries) in the reports it files or submits under the Securities Exchange Act of 1934, as amended, and the rules thereunder, is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in reports it files or submits under the Securities Exchange Act is accumulated and communicated to the Company's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

b) Internal Control Over Financial Reporting. There have not been any changes in the Company's internal control over financial reporting during the quarter ended June 30, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we are involved in litigation and other legal proceedings arising out of the ordinary course of our business. There are no pending material legal proceedings to which we or our property are subject.

Item 1A. Risk Factors

You should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015, and in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2016, which could materially affect our business, adversely affect the market price of our common stock and could cause you to suffer a partial or complete loss of your investment. There have been no material changes to the risk factors previously described in Part I, Item 1A included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, and in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2016. Those risks are incorporated herein by this reference. The risks described in our Annual Report on Form 10-K and in our Quarterly Report are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business. See "Cautionary Notice Regarding Forward-Looking Statements."

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the three months ended June 30, 2016, we did not repurchase any shares of common stock under our repurchase program. The remaining authorization for our common stock repurchases was $70.0 million at June 30, 2016, and is available for use through December 31, 2016.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

Not applicable

Item 6. Exhibits

The exhibits required to be filed as part of this Quarterly Report on Form 10-Q are listed in the Exhibit Index attached hereto and are incorporated herein by reference.

Table of Contents

SIGNATURES

Pursuant to the requirements 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.

STRAYER EDUCATION, INC.

By: /s/ Daniel W. Jackson
Daniel W. Jackson
Executive Vice President
and Chief Financial Officer
Date: July 28, 2016

32

Table of Contents

Exhibit Index

Exhibit	Description
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.	INS XBRL Instance Document
101.	SCH XBRL Schema Document
101.	CAL XBRL Calculation Linkbase Document
101.	DEF XBRL Definition Linkbase Document
101.	LAB XBRL Label Linkbase Document
101.	PRE XBRL Presentation Linkbase Document