

NELNET INC  
Form 10-Q  
August 06, 2015

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

or

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

For the transition period from to .

COMMISSION FILE NUMBER 001-31924

NELNET, INC.

(Exact name of registrant as specified in its charter)

NEBRASKA

(State or other jurisdiction of incorporation or  
organization)

84-0748903

(I.R.S. Employer Identification No.)

121 SOUTH 13TH STREET

SUITE 100

LINCOLN, NEBRASKA

(Address of principal executive offices)

(402) 458-2370

(Registrant's telephone number, including area code)

68508

(Zip 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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

Edgar Filing: NELNET INC - Form 10-Q

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

Large accelerated filer ☒ [X]

Accelerated filer ☐ [ ]

Non-accelerated filer ☐ [ ]

Smaller reporting company ☐ [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ [ ] No ☒ [X]

As of July 31, 2015, there were 33,368,589 and 11,486,932 shares of Class A Common Stock and Class B Common Stock, par value \$0.01 per share, outstanding, respectively (excluding 11,317,364 shares of Class A Common Stock held by wholly owned subsidiaries).

---

NELNET, INC.  
FORM 10-Q  
INDEX  
June 30, 2015

PART I. FINANCIAL INFORMATION

|         |  |           |
|---------|--|-----------|
| Item 1. | <u>Financial Statements</u>  | <u>2</u>  |
| Item 2. | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>24</u> |
| Item 3. | <u>Quantitative and Qualitative Disclosures About Market Risk</u>                            | <u>46</u> |
| Item 4. | <u>Controls and Procedures</u>   | <u>50</u> |

PART II. OTHER INFORMATION

|          |  |           |
|----------|--|-----------|
| Item 1.  | <u>Legal Proceedings</u>   | <u>50</u> |
| Item 1A. | <u>Risk Factors</u>  | <u>50</u> |
| Item 2.  | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | <u>51</u> |
| Item 6.  | <u>Exhibits</u>  | <u>52</u> |

|                   |           |
|-------------------|-----------|
| <u>Signatures</u> | <u>53</u> |
|-------------------|-----------|

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

NELNET, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
(Dollars in thousands, except share data)  
(unaudited)

|  | As of<br>June 30, 2015 | As of<br>December 31,<br>2014 |
|--|------------------------|-------------------------------|
| Assets:  |                        |                               |
| Student loans receivable (net of allowance for loan losses of \$50,024 and \$48,900, respectively)                                     | \$28,095,775           | 28,005,195                    |
| Cash and cash equivalents:   |                        |                               |
| Cash and cash equivalents - not held at a related party  | 32,222                 | 37,781                        |
| Cash and cash equivalents - held at a related party  | 150,058                | 92,700                        |
| Total cash and cash equivalents  | 182,280                | 130,481                       |
| Investments and notes receivable   | 245,748                | 235,709                       |
| Restricted cash and investments  | 857,853                | 850,440                       |
| Restricted cash - due to customers   | 117,820                | 118,488                       |
| Accrued interest receivable  | 364,211                | 351,588                       |
| Accounts receivable (net of allowance for doubtful accounts of \$1,957 and \$1,656, respectively)                                      | 60,893                 | 50,552                        |
| Goodwill   | 126,200                | 126,200                       |
| Intangible assets, net   | 37,784                 | 42,582                        |
| Property and equipment, net  | 48,047                 | 45,894                        |
| Other assets   | 79,996                 | 76,622                        |
| Fair value of derivative instruments   | 30,216                 | 64,392                        |
| Total assets   | \$30,246,823           | 30,098,143                    |
| Liabilities:   |                        |                               |
| Bonds and notes payable  | \$28,070,423           | 28,027,350                    |
| Accrued interest payable   | 28,859                 | 25,904                        |
| Other liabilities  | 157,096                | 167,881                       |
| Due to customers   | 117,820                | 118,488                       |
| Fair value of derivative instruments   | 67,133                 | 32,842                        |
| Total liabilities  | 28,441,331             | 28,372,465                    |
| Commitments and contingencies  |                        |                               |
| Equity:  |                        |                               |
| Nelnet, Inc. shareholders' equity:   |                        |                               |
| Preferred stock, \$0.01 par value. Authorized 50,000,000 shares; no shares issued or outstanding                                       | —                      | —                             |
| Common stock:  |                        |                               |
| Class A, \$0.01 par value. Authorized 600,000,000 shares; issued and outstanding 33,724,471 shares and 34,756,384 shares, respectively | 337                    | 348                           |
| Class B, convertible, \$0.01 par value. Authorized 60,000,000 shares; issued and outstanding 11,486,932 shares                         | 115                    | 115                           |
| Additional paid-in capital   | —                      | 17,290                        |

Edgar Filing: NELNET INC - Form 10-Q

|  |              |            |
|--|--------------|------------|
| Retained earnings                        | 1,801,457    | 1,702,560  |
| Accumulated other comprehensive earnings | 3,283        | 5,135      |
| Total Nelnet, Inc. shareholders' equity  | 1,805,192    | 1,725,448  |
| Noncontrolling interest                  | 300          | 230        |
| Total equity                             | 1,805,492    | 1,725,678  |
| Total liabilities and equity             | \$30,246,823 | 30,098,143 |

Supplemental information - assets and liabilities of consolidated variable interest entities:

|  |               |               |
|--|---------------|---------------|
| Student loans receivable                                     | \$28,234,240  | 28,181,244    |
| Restricted cash and investments                              | 844,854       | 846,199       |
| Other assets   | 364,858       | 351,934       |
| Bonds and notes payable                                      | (28,287,682 ) | (28,391,530 ) |
| Other liabilities  | (329,055 )    | (280,233 )    |
| Fair value of derivative instruments, net                    | (53,593 )     | (20,455 )     |
| Net assets of consolidated variable interest entities        | \$773,622     | 687,159       |
| See accompanying notes to consolidated financial statements. |               |               |

NELNET, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands, except share data)  
(unaudited)

|  | Three months<br>ended June 30, |            | Six months<br>ended June 30, |            |
|--|--------------------------------|------------|------------------------------|------------|
|  | 2015                           | 2014       | 2015                         | 2014       |
| Interest income:   |                                |            |                              |            |
| Loan interest  | \$ 175,835                     | 175,466    | 347,779                      | 332,362    |
| Investment interest  | 1,887                          | 1,482      | 4,092                        | 3,461      |
| Total interest income  | 177,722                        | 176,948    | 351,871                      | 335,823    |
| Interest expense:  |                                |            |                              |            |
| Interest on bonds and notes payable  | 72,626                         | 69,235     | 144,180                      | 129,239    |
| Net interest income  | 105,096                        | 107,713    | 207,691                      | 206,584    |
| Less provision for loan losses   | 2,150                          | 1,500      | 4,150                        | 4,000      |
| Net interest income after provision for loan losses                                      | 102,946                        | 106,213    | 203,541                      | 202,584    |
| Other income:  |                                |            |                              |            |
| Loan and guaranty servicing revenue  | 63,833                         | 66,460     | 121,644                      | 131,217    |
| Tuition payment processing, school information, and campus commerce revenue              | 27,686                         | 21,834     | 62,366                       | 47,069     |
| Enrollment services revenue  | 17,161                         | 20,145     | 35,024                       | 42,156     |
| Other income   | 7,504                          | 15,315     | 14,422                       | 33,446     |
| Gain on sale of loans and debt repurchases   | 1,515                          | 18         | 4,390                        | 57         |
| Derivative market value and foreign currency adjustments and derivative settlements, net | 6,502                          | 1,570      | 3,424                        | (2,695)    |
| Total other income   | 124,201                        | 125,342    | 241,270                      | 251,250    |
| Operating expenses:  |                                |            |                              |            |
| Salaries and benefits  | 58,787                         | 53,888     | 119,837                      | 106,372    |
| Cost to provide enrollment services  | 11,162                         | 13,311     | 22,864                       | 27,786     |
| Loan servicing fees  | 7,420                          | 7,317      | 15,036                       | 12,720     |
| Depreciation and amortization  | 6,501                          | 5,214      | 12,163                       | 9,997      |
| Other  | 31,958                         | 33,060     | 61,156                       | 63,284     |
| Total operating expenses   | 115,828                        | 112,790    | 231,056                      | 220,159    |
| Income before income taxes   | 111,319                        | 118,765    | 213,755                      | 233,675    |
| Income tax expense   | 40,356                         | 43,078     | 77,986                       | 83,689     |
| Net income   | 70,963                         | 75,687     | 135,769                      | 149,986    |
| Net income attributable to noncontrolling interest                                       | 54                             | 693        | 95                           | 1,206      |
| Net income attributable to Nelnet, Inc.  | \$ 70,909                      | 74,994     | 135,674                      | 148,780    |
| Earnings per common share:   |                                |            |                              |            |
| Net income attributable to Nelnet, Inc. shareholders - basic and diluted                 | \$ 1.54                        | 1.61       | 2.94                         | 3.20       |
| Weighted average common shares outstanding - basic and diluted                           | 45,946,415                     | 46,529,377 | 46,127,207                   | 46,528,651 |

See accompanying notes to consolidated financial statements.

## NELNET, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

(unaudited)

|  | Three months<br>ended June 30, |          | Six months<br>ended June 30, |          |
|--|--------------------------------|----------|------------------------------|----------|
|  | 2015                           | 2014     | 2015                         | 2014     |
| Net income   | \$70,963                       | 75,687   | 135,769                      | 149,986  |
| Other comprehensive (loss) income:   |                                |          |                              |          |
| Available-for-sale securities:   |                                |          |                              |          |
| Unrealized holding (losses) gains arising during period, net                       | (436                           | ) 5,826  | (649                         | ) 9,501  |
| Less reclassification adjustment for gains recognized in net income, net of losses | (2,093                         | ) (1,238 | ) (2,297                     | ) (8,311 |
| Income tax effect  | 940                            | (1,698   | ) 1,094                      | (440     |
| Total other comprehensive (loss) income  | (1,589                         | ) 2,890  | (1,852                       | ) 750    |
| Comprehensive income   | 69,374                         | 78,577   | 133,917                      | 150,736  |
| Comprehensive income attributable to noncontrolling interest                       | 54                             | 693      | 95                           | 1,206    |
| Comprehensive income attributable to Nelnet, Inc.                                  | \$69,320                       | 77,884   | 133,822                      | 149,530  |

See accompanying notes to consolidated financial statements.

NELNET, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands, except share data)

(unaudited)

|  | Nelnet, Inc. Shareholders |            | Class A    |         | Class B | Preferred stock | Class A common stock | Class B common stock | Additional paid-in capital | Retained earnings | Accumulated other comprehensive earnings | Noncontrolling interest | Total equity |
|--|---------------------------|------------|------------|---------|---------|-----------------|----------------------|----------------------|----------------------------|-------------------|--|-------------------------|--------------|
|  | Common stock shares       | Class A    | Class B    | Class A | Class B | Class A         | Class B              | Class A              | Class B                    | Class A           | Class B                                  | Class A                 | Class B      |
| Balance as of March 31, 2014                 | —                         | 35,019,924 | 11,491,932 | \$—     | 350     | 115             | 27,138               | 1,482,637            | 2,679                      | 755               | 1,513,674                                |                         |              |
| Net income                                   | —                         | —          | —          | —       | —       | —               | —                    | 74,994               | —                          | 693               | 75,687                                   |                         |              |
| Other comprehensive income                   | —                         | —          | —          | —       | —       | —               | —                    | —                    | 2,890                      | —                 | 2,890                                    |                         |              |
| Distribution to noncontrolling interest      | —                         | —          | —          | —       | —       | —               | —                    | —                    | —                          | (1,062 )          | (1,062 )                                 |                         |              |
| Cash dividend on Class A and Class B         | —                         | —          | —          | —       | —       | —               | —                    | (4,643 )             | —                          | —                 | (4,643 )                                 |                         |              |
| common stock - \$0.10 per share              |                           |            |            |         |         |                 |                      |                      |                            |                   |  |                         |              |
| Issuance of common stock, net of forfeitures | —                         | 49,802     | —          | —       | 1       | —               | 882                  | —                    | —                          | —                 | 883                                      |                         |              |
| Compensation expense for stock based awards  | —                         | —          | —          | —       | —       | —               | 1,135                | —                    | —                          | —                 | 1,135                                    |                         |              |
| Repurchase of common stock                   | —                         | (209,940 ) | —          | —       | (2 )    | —               | (8,434 )             | —                    | —                          | —                 | (8,436 )                                 |                         |              |
| Balance as of June 30, 2014                  | —                         | 34,859,786 | 11,491,932 | \$—     | 349     | 115             | 20,721               | 1,552,988            | 5,569                      | 386               | 1,580,128                                |                         |              |
| Balance as of March 31, 2015                 | —                         | 34,713,065 | 11,486,932 | \$—     | 347     | 115             | 13,177               | 1,762,711            | 4,872                      | 271               | 1,781,493                                |                         |              |
| Issuance of noncontrolling interest          | —                         | —          | —          | —       | —       | —               | —                    | —                    | —                          | 19                | 19                                       |                         |              |
| Net income                                   | —                         | —          | —          | —       | —       | —               | —                    | 70,909               | —                          | 54                | 70,963                                   |                         |              |
| Other comprehensive loss                     | —                         | —          | —          | —       | —       | —               | —                    | —                    | (1,589 )                   | —                 | (1,589 )                                 |                         |              |
| Distribution to noncontrolling interest      | —                         | —          | —          | —       | —       | —               | —                    | —                    | —                          | (44 )             | (44 )                                    |                         |              |
| Cash dividend on Class A and                 | —                         | —          | —          | —       | —       | —               | —                    | (4,559 )             | —                          | —                 | (4,559 )                                 |                         |              |



Edgar Filing: NELNET INC - Form 10-Q

|   |             |            |        |       |        |           |           |          |          |           |
|---|-------------|------------|--------|-------|--------|-----------|-----------|----------|----------|-----------|
| Class B<br>common stock -<br>\$0.10 per share                                     |             |            |        |       |        |           |           |          |          |           |
| Issuance of<br>common stock,<br>net of<br>forfeitures                             | —9,616      | —          | —      | —     | —      | 945       | —         | —        | —        | 945       |
| Compensation<br>expense for<br>stock based<br>awards                              | —           | —          | —      | —     | —      | 1,353     | —         | —        | —        | 1,353     |
| Repurchase of<br>common stock   | —(998,210 ) | —          | —      | (10 ) | —      | (15,475 ) | (27,604 ) | —        | —        | (43,089 ) |
| Balance as of<br>June 30, 2015  | —33,724,471 | 11,486,932 | \$—337 | 115   | —      | 1,801,457 | 3,283     | 300      |          | 1,805,492 |
| Balance as of<br>December 31,<br>2013   | —34,881,338 | 11,495,377 | \$—349 | 115   | 24,887 | 1,413,492 | 4,819     | 328      |          | 1,443,990 |
| Issuance of<br>noncontrolling<br>interest   | —           | —          | —      | —     | —      | —         | —         | 201      |          | 201       |
| Net income  | —           | —          | —      | —     | —      | 148,780   | —         | 1,206    |          | 149,986   |
| Other<br>comprehensive<br>income  | —           | —          | —      | —     | —      | —         | 750       | —        |          | 750       |
| Distribution to<br>noncontrolling<br>interest                                     | —           | —          | —      | —     | —      | —         | —         | (1,349 ) | (1,349 ) |           |
| Cash dividends<br>on Class A and<br>Class B<br>common stock -<br>\$0.20 per share | —           | —          | —      | —     | —      | (9,284 )  | —         | —        |          | (9,284 )  |
| Issuance of<br>common stock,<br>net of<br>forfeitures                             | —205,507    | —          | —      | 2     | —      | 3,126     | —         | —        |          | 3,128     |
| Compensation<br>expense for<br>stock based<br>awards                              | —           | —          | —      | —     | —      | 2,010     | —         | —        |          | 2,010     |
| Repurchase of<br>common stock   | —(230,504 ) | —          | —      | (2 )  | —      | (9,302 )  | —         | —        |          | (9,304 )  |
| Conversion of<br>common stock   | —3,445      | (3,445 )   | —      | —     | —      | —         | —         | —        |          | —         |
| Balance as of<br>June 30, 2014  | —34,859,786 | 11,491,932 | \$—349 | 115   | 20,721 | 1,552,988 | 5,569     | 386      |          | 1,580,128 |
| Balance as of<br>December 31,<br>2014   | —34,756,384 | 11,486,932 | \$—348 | 115   | 17,290 | 1,702,560 | 5,135     | 230      |          | 1,725,678 |
|   | —           | —          | —      | —     | —      | —         | —         | 19       |          | 19        |

Edgar Filing: NELNET INC - Form 10-Q

|   |   |              |            |     |       |          |           |           |          |           |
|---|---|--------------|------------|-----|-------|----------|-----------|-----------|----------|-----------|
| Issuance of noncontrolling interest                                   |   |              |            |     |       |          |           |           |          |           |
| Net income  | — | —            | —          | —   | —     | 135,674  | —         | 95        | 135,769  |           |
| Other comprehensive loss  | — | —            | —          | —   | —     | —        | (1,852 )  | —         | (1,852 ) |           |
| Distribution to noncontrolling interest                               | — | —            | —          | —   | —     | —        | —         | (44 )     | (44 )    |           |
| Cash dividends on Class A and Class B common stock - \$0.20 per share | — | —            | —          | —   | —     | (9,173 ) | —         | —         | (9,173 ) |           |
| Issuance of common stock, net of forfeitures                          | — | 142,095      | —          | —   | 1     | —        | 3,411     | —         | —        | 3,412     |
| Compensation expense for stock based awards                           | — | —            | —          | —   | —     | 2,711    | —         | —         | —        | 2,711     |
| Repurchase of common stock  | — | (1,174,008 ) | —          | —   | (12 ) | —        | (23,412 ) | (27,604 ) | —        | (51,028 ) |
| Balance as of June 30, 2015   | — | 33,724,471   | 11,486,932 | \$— | 337   | 115      | —         | 1,801,457 | 3,283    | 300       |
|   |   |              |            |     |       |          |           |           |          | 1,805,492 |

See accompanying notes to consolidated financial statements.

NELNET, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Dollars in thousands)  
(unaudited)

|  | Six months<br>ended June 30, |             |
|--|------------------------------|-------------|
|  | 2015                         | 2014        |
| Net income attributable to Nelnet, Inc.  | \$ 135,674                   | 148,780     |
| Net income attributable to noncontrolling interest   | 95                           | 1,206       |
| Net income   | 135,769                      | 149,986     |
| Adjustments to reconcile net income to net cash provided by operating activities, net of acquisitions:           |                              |             |
| Depreciation and amortization, including debt discounts and student loan premiums and deferred origination costs | 60,191                       | 49,206      |
| Student loan discount accretion  | (21,506)                     | (21,087)    |
| Provision for loan losses  | 4,150                        | 4,000       |
| Derivative market value adjustment   | 19,457                       | (7,950)     |
| Foreign currency transaction adjustment  | (33,538)                     | (1,798)     |
| Proceeds from termination of derivative instruments  | 51,947                       | —           |
| Payment to enter into interest rate caps   | (585)                        | —           |
| Gain on sale of loans  | (351)                        | —           |
| Gain from debt repurchases   | (4,039)                      | (57)        |
| Gain from sales of available-for-sale securities, net  | (2,297)                      | (8,311)     |
| Payments for purchases of trading securities, net  | (11,697)                     | —           |
| Deferred income tax expense  | 3,119                        | 5,653       |
| Other  | 6,376                        | 4,967       |
| Increase in accrued interest receivable  | (743)                        | (3,567)     |
| Increase in accounts receivable  | (10,341)                     | (695)       |
| (Increase) decrease in other assets  | (1,967)                      | 1,383       |
| Increase in accrued interest payable   | 2,566                        | 1,432       |
| Decrease in other liabilities  | (4,526)                      | (16,690)    |
| Net cash provided by operating activities  | 191,985                      | 156,472     |
| Cash flows from investing activities, net of acquisitions:   |                              |             |
| Purchases of student loans and student loan residual interests   | (1,637,650)                  | (2,843,236) |
| Net proceeds from student loan repayments, claims, capitalized interest, participations, and other               | 1,953,437                    | 1,712,350   |
| Proceeds from sale of student loans  | 3,996                        | 6           |
| Purchases of available-for-sale securities   | (5,550)                      | (135,890)   |
| Proceeds from sales of available-for-sale securities   | 47,951                       | 195,938     |
| Purchases of investments and issuance of notes receivable  | (53,770)                     | (27,011)    |
| Proceeds from investments and notes receivable   | 8,824                        | 3,821       |
| Purchases of property and equipment, net   | (9,519)                      | (9,022)     |
| Decrease (increase) in restricted cash and investments, net  | 16,532                       | (27,247)    |
| Business and asset acquisitions, net of cash acquired  | —                            | (45,583)    |
| Net cash provided by (used in) investing activities  | 324,251                      | (1,175,874) |
| Cash flows from financing activities:  |                              |             |
| Payments on bonds and notes payable  | (2,629,565)                  | (1,821,723) |
| Proceeds from issuance of bonds and notes payable  | 2,233,630                    | 2,901,639   |
| Payments of debt issuance costs  | (8,707)                      | (12,241)    |

Edgar Filing: NELNET INC - Form 10-Q

|   |           |             |   |
|---|-----------|-------------|---|
| Dividends paid  | (9,173    | ) (9,284    | ) |
| Repurchases of common stock   | (51,028   | ) (9,304    | ) |
| Proceeds from issuance of common stock  | 431       | 295         |   |
| Issuance of noncontrolling interest   | 19        | 201         |   |
| Distribution to noncontrolling interest   | (44       | ) (1,349    | ) |
| Net cash (used in) provided by financing activities   | (464,437  | ) 1,048,234 |   |
| Net increase in cash and cash equivalents   | 51,799    | 28,832      |   |
| Cash and cash equivalents, beginning of period  | 130,481   | 63,267      |   |
| Cash and cash equivalents, end of period  | \$182,280 | 92,099      |   |
| Cash disbursements made for:  |           |             |   |
| Interest  | \$108,436 | 97,668      |   |
| Income taxes, net of refunds  | \$67,211  | 83,706      |   |
| Noncash activity:   |           |             |   |
| Investing activity - student loans and other assets acquired                                  | \$517,845 | \$2,571,997 |   |
| Financing activity - borrowings and other liabilities assumed in acquisition of student loans | \$451,845 | \$2,444,874 |   |

See accompanying notes to consolidated financial statements.

## NELNET, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share amounts, unless otherwise noted)

(unaudited)

## 1. Basis of Financial Reporting

The accompanying unaudited consolidated financial statements of Nelnet, Inc. and subsidiaries (the "Company") as of June 30, 2015 and for the three and six months ended June 30, 2015 and 2014 have been prepared on the same basis as the audited consolidated financial statements for the year ended December 31, 2014 and, in the opinion of the Company's management, the unaudited consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of results of operations for the interim periods presented. The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Operating results for the three and six months ended June 30, 2015 are not necessarily indicative of the results for the year ending December 31, 2015. The unaudited consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2014 (the "2014 Annual Report").

## Reclassifications

Certain amounts previously reported within the Company's consolidated balance sheet and statements of income have been reclassified to conform to the current period presentation. These reclassifications include:

• Reclassifying certain investments and notes receivable, which were previously included in "other assets" to "investments and notes receivable."

• Reclassifying third-party loan servicing fees, which were previously included in "other" operating expenses to "loan servicing fees."

The reclassifications had no effect on consolidated net income or consolidated assets and liabilities.

## 2. Student Loans Receivable and Allowance for Loan Losses

Student loans receivable consisted of the following:

|  | As of<br>June 30, 2015 | As of<br>December 31, 2014 |
|--|------------------------|----------------------------|
| Federally insured loans  |                        |                            |
| Stafford and other   | \$6,574,079            | 6,030,825                  |
| Consolidation  | 21,564,569             | 22,165,605                 |
| Total  | 28,138,648             | 28,196,430                 |
| Private education loans  | 175,202                | 27,478                     |
|  | 28,313,850             | 28,223,908                 |
| Loan discount, net of unamortized loan premiums and deferred origination costs (a) | (168,051)              | ) (169,813 )               |
| Allowance for loan losses – federally insured loans                                | (36,762)               | ) (39,170 )                |
| Allowance for loan losses – private education loans                                | (13,262)               | ) (9,730 )                 |
|  | \$28,095,775           | 28,005,195                 |

As of June 30, 2015 and December 31, 2014, "loan discount, net of unamortized loan premiums and deferred (a) origination costs" included \$33.1 million and \$28.8 million, respectively, of non-accretable discount associated with purchased loans of \$9.5 billion and \$8.5 billion, respectively.

## Private Education Loans

On February 5, 2015, the Company entered into an agreement with CommonBond, Inc. ("CommonBond"), a student lending company that provides private education loans to graduate students, under which the Company committed to purchase private education loans for a period of 18 months, with the total purchase obligation limited to \$150.0 million. As of June 30, 2015, the Company had purchased \$64.2 million in private loans from CommonBond pursuant to this agreement.

## Acquisition of Student Loan Residual Interest

On May 26, 2015, the Company acquired the ownership interest in a federally insured student loan securitization trust (the "Trust"), giving the Company rights to the residual interest in \$504.2 million of securitized federally insured loans. The Trust includes loans funded to term with \$448.9 million (par value) of bonds and notes payable.

The Company has consolidated this Trust on its consolidated balance sheet because management has determined the Company is the primary beneficiary of the Trust. Upon acquisition of the Trust, the Company recorded all assets and liabilities of the Trust at fair value, resulting in the recognition of a student loan fair value discount of \$20.7 million and a bonds and notes payable fair value premium of \$2.2 million. The discount and premium will be accreted and amortized, respectively, using the effective interest method over the lives of the underlying assets and liabilities. All other assets and liabilities acquired and liabilities assumed (restricted cash, accrued interest receivable /payable, and other assets/liabilities) were recorded at cost, which approximates fair value.

## Activity in the Allowance for Loan Losses

The provision for loan losses represents the periodic expense of maintaining an allowance sufficient to absorb losses, net of recoveries, inherent in the portfolio of student loans. Activity in the allowance for loan losses is shown below.

|  | Three months ended<br>June 30, |         | Six months ended June<br>30, |         |
|--|--------------------------------|---------|------------------------------|---------|
|  | 2015                           | 2014    | 2015                         | 2014    |
| Balance at beginning of period   | \$51,161                       | 54,628  | 48,900                       | 55,122  |
| Provision for loan losses:   |                                |         |                              |         |
| Federally insured loans  | 2,000                          | 2,000   | 4,000                        | 5,000   |
| Private education loans  | 150                            | (500)   | 150                          | (1,000) |
| Total provision for loan losses  | 2,150                          | 1,500   | 4,150                        | 4,000   |
| Charge-offs:   |                                |         |                              |         |
| Federally insured loans  | (3,259)                        | (4,138) | (6,408)                      | (7,769) |
| Private education loans  | (446)                          | (598)   | (1,122)                      | (1,019) |
| Total charge-offs  | (3,705)                        | (4,736) | (7,530)                      | (8,788) |
| Recoveries - private education loans   | 238                            | 339     | 492                          | 710     |
| Purchase (sale) of federally insured and private education loans, net              | —                              | 150     | (230)                        | 250     |
| Transfer from repurchase obligation related to private education loans repurchased | 180                            | 586     | 4,242                        | 1,173   |
| Balance at end of period   | \$50,024                       | 52,467  | 50,024                       | 52,467  |
| Allocation of the allowance for loan losses:                                       |                                |         |                              |         |
| Federally insured loans  | \$36,762                       | 40,921  | 36,762                       | 40,921  |
| Private education loans  | 13,262                         | 11,546  | 13,262                       | 11,546  |
| Total allowance for loan losses  | \$50,024                       | 52,467  | 50,024                       | 52,467  |

## Repurchase Obligation

The Company has sold various portfolios of private education loans to third-parties. Per the terms of the servicing agreements, the Company's servicing operations are obligated to repurchase loans subject to the sale agreements in the event such loans become 60 or 90 days delinquent. As of June 30, 2015 and December 31, 2014, the balance of loans subject to these repurchase obligations was \$57.0 million and \$155.3 million, respectively. The Company repurchased \$94.1 million of private education loans during the first quarter of 2015. The Company's estimate related to its obligation to repurchase these loans is included in "other liabilities"



in the Company's consolidated balance sheets and was \$3.7 million and \$11.8 million as of June 30, 2015 and December 31, 2014, respectively.

#### Student Loan Status and Delinquencies

Delinquencies have the potential to adversely impact the Company's earnings through increased servicing and collection costs and account charge-offs. The table below shows the Company's loan delinquency amounts.

|                                      | As of June 30, 2015 |       |   | As of December 31, 2014 |       |   | As of June 30, 2014 |       |   |
|--------------------------------------|---------------------|-------|---|-------------------------|-------|---|---------------------|-------|---|
| Federally insured loans:             |                     |       |   |                         |       |   |                     |       |   |
| Loans in-school/grace/deferment      | \$2,634,088         |       |   | \$2,805,228             |       |   | \$3,095,741         |       |   |
| Loans in forbearance                 | 3,118,774           |       |   | 3,288,412               |       |   | 3,593,891           |       |   |
| Loans in repayment status:           |                     |       |   |                         |       |   |                     |       |   |
| Loans current                        | 19,055,994          | 85.2  | % | 18,460,279              | 83.5  | % | 19,164,660          | 84.0  | % |
| Loans delinquent 31-60 days          | 950,055             | 4.2   |   | 1,043,119               | 4.8   |   | 1,026,046           | 4.5   |   |
| Loans delinquent 61-90 days          | 612,657             | 2.7   |   | 588,777                 | 2.7   |   | 674,918             | 3.0   |   |
| Loans delinquent 91-120 days         | 355,636             | 1.6   |   | 404,905                 | 1.8   |   | 376,068             | 1.5   |   |
| Loans delinquent 121-270 days        | 1,051,843           | 4.7   |   | 1,204,405               | 5.4   |   | 1,133,527           | 5.0   |   |
| Loans delinquent 271 days or greater | 359,601             | 1.6   |   | 401,305                 | 1.8   |   | 447,264             | 2.0   |   |
| Total loans in repayment             | 22,385,786          | 100.0 | % | 22,102,790              | 100.0 | % | 22,822,483          | 100.0 | % |
| Total federally insured loans        | \$28,138,648        |       |   | \$28,196,430            |       |   | \$29,512,115        |       |   |
| Private education loans:             |                     |       |   |                         |       |   |                     |       |   |
| Loans in-school/grace/deferment      | \$5,268             |       |   | \$905                   |       |   | \$2,123             |       |   |
| Loans in forbearance                 | 142                 |       |   | —                       |       |   | —                   |       |   |
| Loans in repayment status:           |                     |       |   |                         |       |   |                     |       |   |
| Loans current                        | 161,355             | 95.0  | % | 18,390                  | 69.2  | % | 57,048              | 87.1  | % |
| Loans delinquent 31-60 days          | 1,407               | 0.8   |   | 1,078                   | 4.1   |   | 1,008               | 1.5   |   |
| Loans delinquent 61-90 days          | 1,647               | 1.0   |   | 1,035                   | 3.9   |   | 1,867               | 2.8   |   |
| Loans delinquent 91 days or greater  | 5,383               | 3.2   |   | 6,070                   | 22.8  |   | 5,624               | 8.6   |   |
| Total loans in repayment             | 169,792             | 100.0 | % | 26,573                  | 100.0 | % | 65,547              | 100.0 | % |
| Total non-federally insured loans    | \$175,202           |       |   | \$27,478                |       |   | \$67,670            |       |   |

## 3. Bonds and Notes Payable

The following tables summarize the Company's outstanding debt obligations by type of instrument:

|   | As of June 30, 2015     |                     |                     |
|---|-------------------------|---------------------|---------------------|
|   | Carrying amount         | Interest rate range | Final maturity      |
| Variable-rate bonds and notes issued in asset-backed securitizations: |                         |                     |                     |
| Bonds and notes based on indices                                      | \$25,754,105            | 0.10% - 6.90%       | 8/26/19 - 8/26/52   |
| Bonds and notes based on auction                                      | 1,171,515               | 1.06% - 2.09%       | 3/22/32 - 11/26/46  |
| Total variable-rate bonds and notes                                   | 26,925,620              |                     |                     |
| FFELP warehouse facilities  | 1,190,705               | 0.19% - 0.30%       | 6/11/17 - 4/29/18   |
| Private education loan warehouse facility                             | 89,265                  | 0.31%               | 12/26/16            |
| Unsecured line of credit  | 100,000                 | 1.69%               | 6/30/19             |
| Unsecured debt - Junior Subordinated Hybrid Securities                | 57,582                  | 3.66%               | 9/15/61             |
| Other borrowings  | 79,336                  | 1.69% - 5.10%       | 11/11/15 - 10/31/16 |
|   | 28,442,508              |                     |                     |
| Discount on bonds and notes payable                                   | (372,085 )              |                     |                     |
| Total   | \$28,070,423            |                     |                     |
|   | As of December 31, 2014 |                     |                     |
|   | Carrying amount         | Interest rate range | Final maturity      |
| Variable-rate bonds and notes issued in asset-backed securitizations: |                         |                     |                     |
| Bonds and notes based on indices                                      | \$25,713,431            | 0.19% - 6.90%       | 5/25/18 - 8/26/52   |
| Bonds and notes based on auction                                      | 1,311,669               | 0.47% - 2.17%       | 3/22/32 - 11/26/46  |
| Total variable-rate bonds and notes                                   | 27,025,100              |                     |                     |
| FFELP warehouse facilities  | 1,241,665               | 0.16% - 0.26%       | 1/17/16 - 6/11/17   |
| Unsecured line of credit  | —                       | —                   | 6/30/19             |
| Unsecured debt - Junior Subordinated Hybrid Securities                | 71,688                  | 3.63%               | 9/15/61             |
| Other borrowings  | 81,969                  | 1.67% - 5.10%       | 11/11/15 - 12/31/18 |
|   | 28,420,422              |                     |                     |
| Discount on bonds and notes payable                                   | (393,072 )              |                     |                     |
| Total   | \$28,027,350            |                     |                     |

## FFELP Warehouse Facilities

The Company funds a portion of its FFELP loan acquisitions using its FFELP warehouse facilities. Student loan warehousing allows the Company to buy and manage student loans prior to transferring them into more permanent financing arrangements.

As of June 30, 2015, the Company had three FFELP warehouse facilities as summarized below.

|                                    | NHELP-III (a)  | NFSLW-I (b)   | NHELP-II          | Total     |
|------------------------------------|----------------|---------------|-------------------|-----------|
| Maximum financing amount           | \$750,000      | 750,000       | 500,000           | 2,000,000 |
| Amount outstanding                 | 282,005        | 571,084       | 337,616           | 1,190,705 |
| Amount available                   | \$467,995      | 178,916       | 162,384           | 809,295   |
| Expiration of liquidity provisions | April 29, 2016 | July 30, 2015 | December 17, 2015 |           |
| Final maturity date                | April 29, 2018 | June 11, 2017 | December 17, 2017 |           |
| Maximum advance rates              | 92.2 - 95.0%   | 92.0 - 98.0%  | 91.0 - 97.0%      |           |
| Minimum advance rates              | 92.2 - 95.0%   | 84.0 - 90.0%  | 91.0 - 97.0%      |           |
| Advanced as equity support         | \$7,751        | 27,211        | 18,808            | 53,770    |

(a) On April 30, 2015, the Company amended the agreement for this warehouse facility to change the expiration date for the liquidity provisions to April 29, 2016, and to change the final maturity date to April 29, 2018.

On May 14, 2015, the Company amended the agreement for this warehouse facility to extend the expiration of the liquidity provisions to July 30, 2015. On July 10, 2015, the Company amended the agreement for this warehouse (b) facility to temporarily increase the maximum financing amount to \$875.0 million, extend the expiration of the liquidity provisions to July 8, 2016, and extend the maturity date to July 9, 2018. The maximum financing amount is scheduled to decrease by \$125.0 million on March 31, 2016.

## Asset-backed Securitizations

The following table summarizes the asset-backed securitization transactions completed during the six months ended June 30, 2015.

|                                 | 2015-1    | 2015-2    |           | 2015-3  | Total     |           |           |             |
|---------------------------------|-----------|-----------|-----------|---------|-----------|-----------|-----------|-------------|
|                                 |           | Class A-1 | Class A-2 | 2015-2  | Class A-1 | Class A-2 | Class A-3 | 2015-3      |
|                                 |           | notes     | notes     | total   | notes     | notes     | notes     | total       |
| Date securities issued          | 2/27/15   | 3/26/15   | 3/26/15   | 3/26/15 | 5/21/15   | 5/21/15   | 5/21/15   | 5/21/15     |
| Total original principal amount | \$566,346 | 122,500   | 584,500   | 722,000 | 82,500    | 270,000   | 41,400    | 401,400     |
|                                 |           |           |           |         |           |           |           | \$1,689,746 |
| Class A senior notes:           |           |           |           |         |           |           |           |             |
| Total original principal amount | \$553,232 | 122,500   | 584,500   | 707,000 | 82,500    | 270,000   | 41,400    | 393,900     |
|                                 |           |           |           |         |           |           |           | 1,654,132   |
| Bond discount                   | —         | —         | —         | —       | —         | (380 )    | (1,095 )  | (1,475 )    |
|                                 |           |           |           |         |           |           |           | (1,475 )    |

Edgar Filing: NELNET INC - Form 10-Q

|  |           |         |         |         |         |         |         |         |           |
|--|-----------|---------|---------|---------|---------|---------|---------|---------|-----------|
| Issue price                                  | \$553,232 | 122,500 | 584,500 | 707,000 | 82,500  | 269,620 | 40,305  | 392,425 | 1,652,657 |
| Cost of funds<br>(1-month<br>LIBOR<br>plus:) | 0.59      | % 0.27  | % 0.60  | %       | 0.30    | % 0.60  | % 0.90  | %       |           |
| Final<br>maturity date                       | 4/25/41   | 3/25/20 | 9/25/42 |         | 1/27/25 | 2/26/46 | 6/25/49 |         |           |

Class B  
subordinated  
notes:

|  |          |   |  |          |   |  |         |          |
|--|----------|---|--|----------|---|--|---------|----------|
| Total original<br>principal<br>amount        | \$13,114 |   |  | 15,000   |   |  | 7,500   | 35,614   |
| Bond<br>discount                             | (1,157 ) |   |  | (1,793 ) |   |  | (968 )  | (3,918 ) |
| Issue price                                  | \$11,957 |   |  | 13,207   |   |  | 6,532   | 31,696   |
| Cost of funds<br>(1-month<br>LIBOR<br>plus:) | 1.50     | % |  | 1.50     | % |  | 1.50    | %        |
| Final<br>maturity date                       | 6/25/46  |   |  | 5/25/49  |   |  | 6/27/50 |          |

## Private Education Loan Warehouse Facility

On June 26, 2015, the Company entered into a \$275.0 million private education loan warehouse facility. As of June 30, 2015, there was \$89.3 million outstanding on the facility and \$185.7 million was available for future use. The facility has a static advance rate that requires initial equity for loan funding, but does not require increased equity based on market movements. The maximum advance rate on the entire facility is 88 percent and minimum advance rates, depending on loan characteristics and program type, range from 64 percent to 99 percent. As of June 30, 2015, \$12.8 million was advanced on the facility as equity support. The facility is supported by liquidity provisions, which have a defined expiration date of June 24, 2016. In the event the Company is unable to renew the liquidity provisions by such date, the facility would become a term facility at a stepped-up cost, with no additional student loans being eligible for financing, and the Company would be required to refinance the existing loans in the facility by the facility's final maturity date of December 26, 2016.

## Unsecured Line of Credit

The Company has a \$350.0 million line of credit that has a maturity date of June 30, 2019. As of June 30, 2015, the unsecured line of credit had an outstanding balance of \$100.0 million and \$250.0 million was available for future use.

## Debt Repurchases

The following table summarizes the Company's repurchases of its own debt. Gains recorded by the Company from the repurchase of debt are included in "gain on sale of loans and debt repurchases" on the Company's consolidated statements of income.

|                                    | Par value                           | Purchase price | Gain  | Par value     | Purchase price | Gain |
|------------------------------------|-------------------------------------|----------------|-------|---------------|----------------|------|
|                                    | Three months ended<br>June 30, 2015 |                |       | June 30, 2014 |                |      |
| Unsecured debt - Hybrid Securities | \$2,255                             | 1,781          | 474   | —             | —              | —    |
| Asset-backed securities            | 22,146                              | 21,105         | 1,041 | 200           | 182            | 18   |
|                                    | \$24,401                            | 22,886         | 1,515 | 200           | 182            | 18   |
|                                    | Six months ended<br>June 30, 2015   |                |       | June 30, 2014 |                |      |
| Unsecured debt - Hybrid Securities | \$14,106                            | 11,108         | 2,998 | —             | —              | —    |
| Asset-backed securities            | 22,146                              | 21,105         | 1,041 | 1,550         | 1,493          | 57   |
|                                    | \$36,252                            | 32,213         | 4,039 | 1,550         | 1,493          | 57   |

#### 4. Derivative Financial Instruments

The Company uses derivative financial instruments primarily to manage interest rate risk and foreign currency exchange risk. Derivative instruments used as part of the Company's risk management strategy are further described in note 5 of the notes to consolidated financial statements included in the 2014 Annual Report. A tabular presentation of such derivatives outstanding as of June 30, 2015 and December 31, 2014 is presented below.

##### Basis Swaps

The following table summarizes the Company's basis swaps outstanding as of June 30, 2015 and December 31, 2014 in which the Company receives three-month LIBOR set discretely in advance and pays one-month LIBOR plus or minus a spread as defined in the agreements (the "1:3 Basis Swaps").

|          | As of June 30,<br>2015 | As of December 31,<br>2014 |
|----------|------------------------|----------------------------|
| Maturity | Notional amount        | Notional amount            |
| 2016     | \$4,000,000            | \$—                        |
| 2021     | —                      | 250,000                    |
| 2022     | 800,000                | 1,900,000                  |
| 2023     | 1,250,000              | 3,650,000                  |
| 2024     | —                      | 250,000                    |
| 2026     | 300,000                | 800,000                    |
| 2028     | —                      | 100,000                    |
| 2036     | —                      | 700,000                    |
| 2039     | —                      | 150,000                    |
|          | \$6,350,000            | \$7,800,000                |

The weighted average rate paid by the Company on the 1:3 Basis Swaps as of June 30, 2015 and December 31, 2014 was one-month LIBOR plus 8.5 basis points and 3.5 basis points, respectively.

##### Interest Rate Swaps – Floor Income Hedges

The following table summarizes the outstanding derivative instruments used by the Company to economically hedge loans earning fixed rate floor income.

|          | As of June 30, 2015 |   | As of December 31, 2014 |   |
|----------|---------------------|---|-------------------------|---|
| Maturity | Notional amount     | Weighted average<br>fixed rate paid by the<br>Company (a) | Notional amount         | Weighted average<br>fixed rate paid by the<br>Company (a) |
| 2015     | \$500,000           | 0.71  | % \$1,100,000           | 0.89  |
| 2016     | 750,000             | 0.85  | 750,000                 | 0.85  |
| 2017     | 1,850,000           | 0.83  | 1,250,000               | 0.86  |
| 2018     | 100,000             | 1.02  | —                       | —   |
| 2025     | 100,000             | 2.32  | —                       | —   |
|          | \$3,300,000         | 0.87  | % \$3,100,000           | 0.87  |

(a) For all interest rate derivatives, the Company receives discrete three-month LIBOR.

On August 20, 2014, the Company paid \$9.1 million for an interest rate swap option to economically hedge loans earning fixed rate floor income. The interest rate swap option gives the Company the right, but not the obligation, to enter into a \$250 million notional interest rate swap in which the Company would pay a fixed amount of 3.30% and receive discrete one-month LIBOR. If the interest rate swap option is exercised, the swap would become effective in

2019 and mature in 2024.

## Interest Rate Swaps – Unsecured Debt Hedges

The Company had the following derivatives outstanding as of June 30, 2015 and December 31, 2014 that are used to effectively convert the variable interest rate on a portion of the Junior Subordinated Hybrid Securities to a fixed rate of 7.66%.

| Maturity | Notional amount | Weighted average<br>fixed rate paid by<br>the Company (a) |
|----------|-----------------|---|
| 2036     | \$ 25,000       | 4.28 %  |

(a) For all interest rate derivatives, the Company receives discrete three-month LIBOR.

## Interest Rate Caps

In June 2015, in conjunction with the entry into the \$275.0 million private education loan warehouse facility, the Company paid \$2.9 million for two interest rate cap contracts with a total notional amount of \$275.0 million. The first interest rate cap has a notional amount of \$125.0 million and a one-month LIBOR strike rate of 2.50%, and the second interest rate cap has a notional amount of \$150.0 million and a one-month LIBOR strike rate of 4.99%. In the event that the one-month LIBOR rate rises above the applicable strike rate, the Company would receive monthly payments related to the spread difference. Both interest rate cap contracts have a maturity date of July 15, 2020.

## Foreign Currency Exchange Risk

In 2006, the Company issued €352.7 million of student loan asset-backed Euro Notes (the "Euro Notes") with an interest rate based on a spread to the EURIBOR index. As a result of the Euro Notes, the Company is exposed to market risk related to fluctuations in foreign currency exchange rates between the U.S. dollar and Euro. The principal and accrued interest on these notes are re-measured at each reporting period and recorded in the Company's consolidated balance sheet in U.S. dollars based on the foreign currency exchange rate on that date.

The Company entered into a cross-currency interest rate swap in connection with the issuance of the Euro Notes. Under the terms of the cross-currency interest rate swap, the Company receives from the counterparty a spread to the EURIBOR index based on a notional amount of €352.7 million and pays a spread to the LIBOR index based on a notional amount of \$450.0 million. In addition, under the terms of this agreement, all principal payments on the Euro Notes will effectively be paid at the exchange rate in effect between the U.S. dollar and Euro as of the issuance of the notes.

The following table shows the income statement impact as a result of the re-measurement of the Euro Notes and the change in the fair value of the related derivative instrument.

|  | Three months ended June 30, |         | Six months ended June 30, |          |
|--|-----------------------------|---------|---------------------------|----------|
|  | 2015                        | 2014    | 2015                      | 2014     |
| Re-measurement of Euro Notes   | \$(14,671                   | ) 2,751 | 33,538                    | 1,798    |
| Change in fair value of cross-currency interest rate swap                | 13,933                      | (2,999  | ) (35,873                 | ) (3,037 |
| Total impact to consolidated statements of income - income (expense) (a) | \$(738                      | ) (248  | ) (2,335                  | ) (1,239 |

(a) The financial statement impact of the above items is included in "Derivative market value and foreign currency adjustments and derivative settlements, net" in the Company's consolidated statements of income.

The re-measurement of the Euro-denominated bonds generally correlates with the change in fair value of the corresponding cross-currency interest rate swap. However, the Company will experience unrealized gains or losses related to the cross-currency interest rate swap if the two underlying indices (and related forward curve) do not move



in parallel.

14

---

## Consolidated Financial Statement Impact Related to Derivatives

The following table summarizes the fair value of the Company's derivatives as reflected in the consolidated balance sheets:

|  | Fair value of asset derivatives |                               | Fair value of liability derivatives |                               |
|--|---------------------------------|-------------------------------|-------------------------------------|-------------------------------|
|  | As of<br>June 30,<br>2015       | As of<br>December 31,<br>2014 | As of<br>June 30,<br>2015           | As of<br>December 31,<br>2014 |
| 1:3 basis swaps                                | \$ 14,071                       | 53,549                        | 71                                  | —                             |
| Interest rate swaps - floor income hedges      | 7,262                           | 5,165                         | 4,470                               | 5,034                         |
| Interest rate swap option - floor income hedge | 6,148                           | 5,678                         | —                                   | —                             |
| Interest rate swaps - hybrid debt hedges       | —                               | —                             | 6,264                               | 7,353                         |
| Interest rate caps                             | 2,735                           | —                             | —                                   | —                             |
| Cross-currency interest rate swap              | —                               | —                             | 56,328                              | 20,455                        |
| Total  | \$ 30,216                       | 64,392                        | 67,133                              | 32,842                        |

During the six months ended June 30, 2015, the Company terminated a total notional amount of \$5.5 billion of 1:3 Basis Swaps for gross proceeds of \$51.9 million. There were no derivative terminations during the first six months of 2014.

## Offsetting of Derivative Assets/Liabilities

The Company records derivative instruments in the consolidated balance sheets on a gross basis as either an asset or liability measured at its fair value. Certain of the Company's derivative instruments are subject to right of offset provisions with counterparties. The following tables include the gross amounts related to the Company's derivative portfolio recognized in the consolidated balance sheets, reconciled to the net amount when excluding derivatives subject to enforceable master netting arrangements and cash collateral received/pledged:

| Derivative assets               | Gross amounts of<br>recognized assets<br>presented in the<br>consolidated balance<br>sheets | Gross amounts not offset in the consolidated<br>balance sheets      |                                       |  | Net asset (liability) |
|---------------------------------|---|---|---------------------------------------|--|-----------------------|
|                                 |   | Derivatives subject to<br>enforceable master<br>netting arrangement | Cash collateral pledged<br>(received) |  |                       |
| Balance as of June 30, 2015     | \$ 30,216   | (6,801  | ) 2,046                               |  | 25,461                |
| Balance as of December 31, 2014 | 64,392  | (12,387   | ) —                                   |  | 52,005                |

  

| Derivative liabilities | Gross amounts of<br>recognized liabilities<br>presented in the<br>consolidated balance | Gross amounts not offset in the consolidated<br>balance sheets      |                                       |  | Net asset (liability) |
|------------------------|--|---|---------------------------------------|--|-----------------------|
|                        |  | Derivatives subject to<br>enforceable master<br>netting arrangement | Cash collateral<br>pledged (received) |  |                       |

Edgar Filing: NELNET INC - Form 10-Q

|                                 |           |          |        |           |   |  |
|---------------------------------|-----------|----------|--------|-----------|---|--|
|                                 | sheets    |          |        |           |   |  |
| Balance as of June 30, 2015     | \$(67,133 | ) 6,801  | (9,091 | ) (69,423 | ) |  |
| Balance as of December 31, 2014 | (32,842   | ) 12,387 | (1,454 | ) (21,909 | ) |  |

15

---

The following table summarizes the effect of derivative instruments in the consolidated statements of income.

|   | Three months ended June 30, |          | Six months ended June 30, |           |
|---|-----------------------------|----------|---------------------------|-----------|
|   | 2015                        | 2014     | 2015                      | 2014      |
| Settlements:  |                             |          |                           |           |
| 1:3 basis swaps   | \$123                       | 858      | 389                       | 1,739     |
| Interest rate swaps - floor income hedges   | (5,019)                     | ) (6,974 | ) (10,034                 | ) (13,924 |
| Interest rate swaps - hybrid debt hedges  | (253)                       | ) (256   | ) (505                    | ) (508    |
| Cross-currency interest rate swap   | (293)                       | ) 158    | (507                      | ) 250     |
| Total settlements - (expense) income  | (5,442                      | ) (6,214 | ) (10,657                 | ) (12,443 |
| Change in fair value:   |                             |          |                           |           |
| 1:3 basis swaps   | 1,428                       | 11,910   | 12,398                    | 13,020    |
| Interest rate swaps - floor income hedges   | 7,534                       | (2,813   | ) 2,662                   | 545       |
| Interest rate swap option - floor income hedge  | 1,381                       | —        | 470                       | —         |
| Interest rate swaps - hybrid debt hedges  | 2,540                       | (1,065   | ) 1,087                   | (2,578    |
| Interest rate caps  | (201                        | ) —      | (201                      | ) —       |
| Cross-currency interest rate swap   | 13,933                      | (2,999   | ) (35,873                 | ) (3,037  |
| Total change in fair value - income (expense)   | 26,615                      | 5,033    | (19,457                   | ) 7,950   |
| Re-measurement of Euro Notes (foreign currency transaction adjustment) - (expense) income                   | (14,671                     | ) 2,751  | 33,538                    | 1,798     |
| Derivative market value and foreign currency adjustments and derivative settlements, net - income (expense) | \$6,502                     | 1,570    | 3,424                     | (2,695    |

## 5. Investments and Notes Receivable

A summary of the Company's investments and notes receivable follows:

|  | As of June 30, 2015 |                        |                             |            | As of December 31, 2014 |                        |                         |            |
|--|---------------------|------------------------|-----------------------------|------------|-------------------------|------------------------|-------------------------|------------|
|  | Amortized cost      | Gross unrealized gains | Gross unrealized losses (a) | Fair value | Amortized cost          | Gross unrealized gains | Gross unrealized losses | Fair value |
| Investments (at fair value):   |                     |                        |                             |            |                         |                        |                         |            |
| Available-for-sale investments:                                      |                     |                        |                             |            |                         |                        |                         |            |
| Student loan asset-backed and other debt securities (b)              | \$92,192            | 4,137                  | (608                        | ) 95,721   | 131,589                 | 6,204                  | (236                    | ) 137,557  |
| Equity securities  | 846                 | 1,734                  | (58                         | ) 2,522    | 1,553                   | 2,216                  | (33                     | ) 3,736    |
| Total available-for-sale investments                                 | \$93,038            | 5,871                  | (666                        | ) 98,243   | 133,142                 | 8,420                  | (269                    | ) 141,293  |
| Trading investments:   |                     |                        |                             |            |                         |                        |                         |            |
| Student loan asset-backed securities                                 |                     |                        |                             | 6,443      |                         |                        |                         | 7,830      |
| Equity securities  |                     |                        |                             | 13,084     |                         |                        |                         | —          |
| Total trading investments  |                     |                        |                             | 19,527     |                         |                        |                         | 7,830      |
| Total available-for-sale and trading investments                     |                     |                        |                             | 117,770    |                         |                        |                         | 149,123    |
| Other Investments and Notes Receivable (not measured at fair value): |                     |                        |                             |            |                         |                        |                         |            |
| Investments accounted for under the cost and equity methods          |                     |                        |                             | 82,281     |                         |                        |                         | 36,991     |
| Notes receivable   |                     |                        |                             | 31,321     |                         |                        |                         | 30,643     |

Edgar Filing: NELNET INC - Form 10-Q

|   |           |         |
|---|-----------|---------|
| Other                                     | 14,376    | 18,952  |
| Total investments and notes<br>receivable | \$245,748 | 235,709 |

- (a) As of June 30, 2015, the Company considered the decline in market value of its available-for-sale investments to be temporary in nature and did not consider any of its investments other-than-temporarily impaired.
- (b) As of June 30, 2015, the stated maturities of the majority of the Company's student loan asset-backed and other debt securities classified as available-for-sale were greater than 10 years.

## 6. Intangible Assets and Goodwill

Intangible assets consist of the following:

|   | Weighted<br>average<br>remaining<br>useful life as of<br>June 30, 2015<br>(months) | As of June 30,<br>2015 | As of<br>December 31,<br>2014 |
|---|--|------------------------|-------------------------------|
| Amortizable intangible assets:  |  |                        |                               |
| Customer relationships (net of accumulated amortization of \$20,278 and \$17,361, respectively) | 213  | \$ 24,413              | 27,330                        |
| Trade names (net of accumulated amortization of \$534 and \$272, respectively)                  | 227  | 5,888                  | 6,150                         |
| Computer software (net of accumulated amortization of \$3,048 and \$1,896, respectively)        | 37   | 5,817                  | 6,969                         |
| Content (net of accumulated amortization of \$450 and \$0, respectively)                        | 18   | 1,350                  | 1,800                         |
| Covenants not to compete (net of accumulated amortization of \$38 and \$21, respectively)       | 107  | 316                    | 333                           |
| Total - amortizable intangible assets   | 180  | \$ 37,784              | 42,582                        |

The Company recorded amortization expense on its intangible assets of \$2.4 million and \$1.4 million during the three months ended June 30, 2015 and 2014, respectively, and \$4.8 million and \$2.4 million during the six months ended June 30, 2015 and 2014, respectively. The Company will continue to amortize intangible assets over their remaining useful lives. As of June 30, 2015, the Company estimates it will record amortization expense as follows:

|                             |          |
|-----------------------------|----------|
| 2015 (July 1 - December 31) | \$4,797  |
| 2016                        | 6,249    |
| 2017                        | 3,752    |
| 2018                        | 3,533    |
| 2019                        | 2,861    |
| 2020 and thereafter         | 16,592   |
|                             | \$37,784 |

There were no changes in the carrying amount of goodwill during the six months ended June 30, 2015. The carrying amount of goodwill by reportable operating segment as of June 30, 2015 and December 31, 2014 is shown in the table below.

|   | Student Loan<br>and Guaranty<br>Servicing | Tuition<br>Payment<br>Processing<br>and Campus<br>Commerce | Asset<br>Generation<br>and<br>Management | Corporate and<br>Other<br>Activities | Total   |
|---|---|--|--|--------------------------------------|---------|
| Balance as of December 31, 2014 and June 30, 2015 | \$8,596                                   | 67,168   | 41,883                                   | 8,553                                | 126,200 |

## 7. Earnings per Common Share

Presented below is a summary of the components used to calculate basic and diluted earnings per share. The Company applies the two-class method in computing both basic and diluted earnings per share, which requires the calculation of separate earnings per share amounts for common stock and unvested share based awards. Unvested share-based awards that contain nonforfeitable rights to dividends are considered securities which participate in undistributed earnings with common stock.

|  | Three months ended June 30,<br>2015 |   |            | 2014                   |   |            |
|--|-------------------------------------|---|------------|------------------------|---|------------|
|  | Common<br>shareholders              | Unvested<br>restricted<br>stock<br>shareholders | Total      | Common<br>shareholders | Unvested<br>restricted<br>stock<br>shareholders | Total      |
| Numerator:   |                                     |   |            |                        |   |            |
| Net income attributable to<br>Nelnet, Inc.                           | \$ 70,146                           | 763   | 70,909     | 74,263                 | 731   | 74,994     |
| Denominator:   |                                     |   |            |                        |   |            |
| Weighted-average common<br>shares outstanding - basic and<br>diluted | 45,451,888                          | 494,527   | 45,946,415 | 46,075,869             | 453,508   | 46,529,377 |
| Earnings per share - basic and<br>diluted                            | \$ 1.54                             | 1.54  | 1.54       | 1.61                   | 1.61  | 1.61       |
|  |                                     |   |            |                        |   |            |
|  | Six months ended June 30,<br>2015   |   |            | 2014                   |   |            |
|  | Common<br>shareholders              | Unvested<br>restricted<br>stock<br>shareholders | Total      | Common<br>shareholders | Unvested<br>restricted<br>stock<br>shareholders | Total      |
| Numerator:   |                                     |   |            |                        |   |            |
| Net income attributable to<br>Nelnet, Inc.                           | \$ 134,227                          | 1,447   | 135,674    | 147,388                | 1,392   | 148,780    |
| Denominator:   |                                     |   |            |                        |   |            |
| Weighted-average common<br>shares outstanding - basic and<br>diluted | 45,635,155                          | 492,052   | 46,127,207 | 46,093,314             | 435,337   | 46,528,651 |
| Earnings per share - basic and<br>diluted                            | \$ 2.94                             | 2.94  | 2.94       | 3.20                   | 3.20  | 3.20       |

Unvested restricted stock awards are the Company's only potential common shares and, accordingly, there were no awards that were antidilutive and not included in average shares outstanding for the diluted earnings per share calculation.

## 8. Segment Reporting

See note 14 of the notes to consolidated financial statements included in the 2014 Annual Report for a description of the Company's operating segments. The following tables include the results of each of the Company's operating segments reconciled to the consolidated financial statements.

Effective January 1, 2015, internal reporting to executive management (the "chief operating decision maker") changed to reflect operational changes made within the organization. The operational and internal reporting changes included moving the majority of information technology infrastructure personnel and related functions to Corporate and Other Activities. The associated costs are allocated to the other operating segments based on those segments' actual use of information technology related products and services. Information technology infrastructure personnel and related functions were historically included within the Student Loan and Guaranty Servicing operating segment, and associated costs were allocated to the other operating segments based on those segments' actual use of the related products and services. Prior period segment operating results have been reclassified to reflect these changes; however, the reclassifications had no effect on any operating segment's net income.

## Three months ended June 30, 2015

|   | Student<br>Loan and<br>Guaranty<br>Servicing | Tuition<br>Payment<br>Processing<br>and<br>Campus<br>Commerce | Asset<br>Generation<br>and<br>Management | Corporate<br>and Other<br>Activities | Eliminations | Total    |
|---|--|---|--|--------------------------------------|--------------|----------|
| Total interest income   | \$ 13  | 1   | 176,279                                  | 1,814                                | (385 )       | 177,722  |
| Interest expense  | —  | —   | 71,441                                   | 1,570                                | (385 )       | 72,626   |
| Net interest income   | 13   | 1   | 104,838                                  | 244                                  | —            | 105,096  |
| Less provision for loan losses  | —  | —   | 2,150                                    | —                                    | —            | 2,150    |
| Net interest income after provision for loan losses                         | 13   | 1   | 102,688                                  | 244                                  | —            | 102,946  |
| Other income:   |  |   |  |                                      |              |          |
| Loan and guaranty servicing revenue   | 63,833                                       | —   | —  | —                                    | —            | 63,833   |
| Intersegment servicing revenue  | 12,223                                       | —   | —  | —                                    | (12,223 )    | —        |
| Tuition payment processing, school information, and campus commerce revenue | —  | 27,686  | —  | —                                    | —            | 27,686   |
| Enrollment services revenue   | —  | —   | —  | 17,161                               | —            | 17,161   |
| Other income  | —  | —   | 3,950                                    | 3,554                                | —            | 7,504    |
| Gain on sale of loans and debt repurchases                                  | —  | —   | 1,041                                    | 474                                  | —            | 1,515    |
| Derivative market value and foreign currency adjustments, net               | —  | —   | 9,404                                    | 2,540                                | —            | 11,944   |
| Derivative settlements, net   | —  | —   | (5,189 )                                 | (253 )                               | —            | (5,442 ) |
| Total other income  | 76,056                                       | 27,686  | 9,206                                    | 23,476                               | (12,223 )    | 124,201  |
| Operating expenses:   |  |   |  |                                      |              |          |
| Salaries and benefits   | 31,585                                       | 13,583  | 524                                      | 13,095                               | —            | 58,787   |
| Cost to provide enrollment services   | —  | —   | —  | 11,162                               | —            | 11,162   |
| Loan servicing fees   | —  | —   | 7,420                                    | —                                    | —            | 7,420    |
| Depreciation and amortization   | 527  | 2,195   | —  | 3,779                                | —            | 6,501    |
| Other   | 15,376                                       | 4,112   | 1,270                                    | 11,200                               | —            | 31,958   |
| Intersegment expenses, net  | 11,566                                       | 2,785   | 12,398                                   | (14,526 )                            | (12,223 )    | —        |



Edgar Filing: NELNET INC - Form 10-Q

|   |          |          |           |        |           |           |
|---|----------|----------|-----------|--------|-----------|-----------|
| Total operating expenses  | 59,054   | 22,675   | 21,612    | 24,710 | (12,223 ) | 115,828   |
| Income (loss) before income taxes and corporate overhead allocation | 17,015   | 5,012    | 90,282    | (990 ) | —         | 111,319   |
| Corporate overhead allocation                                       | (2,294 ) | (918 )   | (1,147 )  | 4,359  | —         | —         |
| Income before income taxes  | 14,721   | 4,094    | 89,135    | 3,369  | —         | 111,319   |
| Income tax (expense) benefit  | (5,594 ) | (1,556 ) | (33,871 ) | 665    | —         | (40,356 ) |
| Net income  | 9,127    | 2,538    | 55,264    | 4,034  | —         | 70,963    |
| Net income attributable to noncontrolling interest                  | —        | —        | —         | 54     | —         | 54        |
| Net income attributable to Nelnet, Inc.                             | \$9,127  | 2,538    | 55,264    | 3,980  | —         | 70,909    |

Edgar Filing: NELNET INC - Form 10-Q

|   | Three months ended June 30, 2014             |   |  |                                      |              |           |
|---|--|---|--|--------------------------------------|--------------|-----------|
|   | Student<br>Loan and<br>Guaranty<br>Servicing | Tuition<br>Payment<br>Processing<br>and<br>Campus<br>Commerce | Asset<br>Generation<br>and<br>Management | Corporate<br>and Other<br>Activities | Eliminations | Total     |
| Total interest income   | \$9  | 3   | 175,562                                  | 2,036                                | (662 )       | 176,948   |
| Interest expense  | —  | —   | 67,936                                   | 1,961                                | (662 )       | 69,235    |
| Net interest income   | 9  | 3   | 107,626                                  | 75                                   | —            | 107,713   |
| Less provision for loan losses  | —  | —   | 1,500                                    | —                                    | —            | 1,500     |
| Net interest income after provision for loan losses                         | 9  | 3   | 106,126                                  | 75                                   | —            | 106,213   |
| Other income:   |  |   |  |                                      |              |           |
| Loan and guaranty servicing revenue   | 66,460                                       | —   | —  | —                                    | —            | 66,460    |
| Intersegment servicing revenue  | 13,800                                       | —   | —  | —                                    | (13,800 )    | —         |
| Tuition payment processing, school information, and campus commerce revenue | —  | 21,834  | —  | —                                    | —            | 21,834    |
| Enrollment services revenue   | —  | —   | —  | 20,145                               | —            | 20,145    |
| Other income  | —  | —   | 4,496                                    | 10,819                               | —            | 15,315    |
| Gain on sale of loans and debt repurchases                                  | —  | —   | 18                                       | —                                    | —            | 18        |
| Derivative market value and foreign currency adjustments, net               | —  | —   | 8,848                                    | (1,064 )                             | —            | 7,784     |
| Derivative settlements, net   | —  | —   | (5,958 )                                 | (256 )                               | —            | (6,214 )  |
| Total other income  | 80,260                                       | 21,834  | 7,404                                    | 29,644                               | (13,800 )    | 125,342   |
| Operating expenses:   |  |   |  |                                      |              |           |
| Salaries and benefits   | 30,082                                       | 11,112  | 570                                      | 12,124                               | —            | 53,888    |
| Cost to provide enrollment services   | —  | —   | —  | 13,311                               | —            | 13,311    |
| Loan servicing fees   | —  | —   | 7,317                                    | —                                    | —            | 7,317     |
| Depreciation and amortization   | 438  | 1,845   | —  | 2,931                                | —            | 5,214     |
| Other   | 16,975                                       | 2,956   | 1,528                                    | 11,601                               | —            | 33,060    |
| Intersegment expenses, net  | 9,356  | 1,404   | 13,968                                   | (10,928 )                            | (13,800 )    | —         |
| Total operating expenses  | 56,851                                       | 17,317  | 23,383                                   | 29,039                               | (13,800 )    | 112,790   |
| Income before income taxes and corporate overhead allocation                | 23,418                                       | 4,520   | 90,147                                   | 680                                  | —            | 118,765   |
| Corporate overhead allocation   | (2,060 )                                     | (687 )  | (1,249 )                                 | 3,996                                | —            | —         |
| Income before income taxes  | 21,358                                       | 3,833   | 88,898                                   | 4,676                                | —            | 118,765   |
| Income tax (expense) benefit  | (8,116 )                                     | (1,456 )  | (33,781 )                                | 275                                  | —            | (43,078 ) |
| Net income  | 13,242                                       | 2,377   | 55,117                                   | 4,951                                | —            | 75,687    |
| Net income attributable to noncontrolling interest                          | —  | —   | —  | 693                                  | —            | 693       |
| Net income attributable to Nelnet, Inc.                                     | \$ 13,242                                    | 2,377   | 55,117                                   | 4,258                                | —            | 74,994    |



|   | Six months ended June 30, 2015               |   |  |                                      |              |           |  |
|---|--|---|--|--------------------------------------|--------------|-----------|--|
|   | Student<br>Loan and<br>Guaranty<br>Servicing | Tuition<br>Payment<br>Processing<br>and<br>Campus<br>Commerce | Asset<br>Generation<br>and<br>Management | Corporate<br>and Other<br>Activities | Eliminations | Total     |  |
| Total interest income   | \$20   | 3   | 348,702                                  | 3,967                                | (821 )       | 351,871   |  |
| Interest expense  | —  | —   | 141,981                                  | 3,020                                | (821 )       | 144,180   |  |
| Net interest income   | 20   | 3   | 206,721                                  | 947                                  | —            | 207,691   |  |
| Less provision for loan losses  | —  | —   | 4,150                                    | —                                    | —            | 4,150     |  |
| Net interest income after provision for loan losses                         | 20   | 3   | 202,571                                  | 947                                  | —            | 203,541   |  |
| Other income:   |  |   |  |                                      |              |           |  |
| Loan and guaranty servicing revenue   | 121,644                                      | —   | —  | —                                    | —            | 121,644   |  |
| Intersegment servicing revenue  | 25,094                                       | —   | —  | —                                    | (25,094 )    | —         |  |
| Tuition payment processing, school information, and campus commerce revenue | —  | 62,366  | —  | —                                    | —            | 62,366    |  |
| Enrollment services revenue   | —  | —   | —  | 35,024                               | —            | 35,024    |  |
| Other income  | —  | —   | 8,526                                    | 5,896                                | —            | 14,422    |  |
| Gain on sale of loans and debt repurchases                                  | —  | —   | 1,392                                    | 2,998                                | —            | 4,390     |  |
| Derivative market value and foreign currency adjustments, net               | —  | —   | 12,994                                   | 1,087                                | —            | 14,081    |  |
| Derivative settlements, net   | —  | —   | (10,152 )                                | (505 )                               | —            | (10,657 ) |  |
| Total other income  | 146,738                                      | 62,366  | 12,760                                   | 44,500                               | (25,094 )    | 241,270   |  |
| Operating expenses:   |  |   |  |                                      |              |           |  |
| Salaries and benefits   | 65,288                                       | 26,904  | 1,065                                    | 26,580                               | —            | 119,837   |  |
| Cost to provide enrollment services   | —  | —   | —  | 22,864                               | —            | 22,864    |  |
| Loan servicing fees   | —  | —   | 15,036                                   | —                                    | —            | 15,036    |  |
| Depreciation and amortization   | 973  | 4,390   | —  | 6,800                                | —            | 12,163    |  |
| Other   | 29,976                                       | 7,914   | 2,407                                    | 20,859                               | —            | 61,156    |  |
| Intersegment expenses, net  | 21,266                                       | 5,399   | 25,438                                   | (27,009 )                            | (25,094 )    | —         |  |
| Total operating expenses  | 117,503                                      | 44,607  | 43,946                                   | 50,094                               | (25,094 )    | 231,056   |  |
| Income (loss) before income taxes and corporate overhead allocation         | 29,255                                       | 17,762  | 171,385                                  | (4,647 )                             | —            | 213,755   |  |
| Corporate overhead allocation   | (4,447 )                                     | (1,780 )  | (2,225 )                                 | 8,452                                | —            | —         |  |
| Income before income taxes  | 24,808                                       | 15,982  | 169,160                                  | 3,805                                | —            | 213,755   |  |
| Income tax (expense) benefit  | (9,428 )                                     | (6,074 )  | (64,280 )                                | 1,796                                | —            | (77,986 ) |  |
| Net income  | 15,380                                       | 9,908   | 104,880                                  | 5,601                                | —            | 135,769   |  |
| Net income attributable to noncontrolling interest                          | —  | —   | —  | 95                                   | —            | 95        |  |
| Net income attributable to Nelnet, Inc.                                     | \$ 15,380                                    | 9,908   | 104,880                                  | 5,506                                | —            | 135,674   |  |

|   | Six months ended June 30, 2014               |   |  |                                      |              |           |
|---|--|---|--|--------------------------------------|--------------|-----------|
|   | Student<br>Loan and<br>Guaranty<br>Servicing | Tuition<br>Payment<br>Processing<br>and<br>Campus<br>Commerce | Asset<br>Generation<br>and<br>Management | Corporate<br>and Other<br>Activities | Eliminations | Total     |
| Total interest income   | \$20   | 3   | 332,565                                  | 4,694                                | (1,459 )     | 335,823   |
| Interest expense  | —  | —   | 127,412                                  | 3,286                                | (1,459 )     | 129,239   |
| Net interest income   | 20   | 3   | 205,153                                  | 1,408                                | —            | 206,584   |
| Less provision for loan losses  | —  | —   | 4,000                                    | —                                    | —            | 4,000     |
| Net interest income after provision for loan losses                         | 20   | 3   | 201,153                                  | 1,408                                | —            | 202,584   |
| Other income:   |  |   |  |                                      |              |           |
| Loan and guaranty servicing revenue   | 131,217                                      | —   | —  | —                                    | —            | 131,217   |
| Intersegment servicing revenue  | 28,021                                       | —   | —  | —                                    | (28,021 )    | —         |
| Tuition payment processing, school information, and campus commerce revenue | —  | 47,069  | —  | —                                    | —            | 47,069    |
| Enrollment services revenue   | —  | —   | —  | 42,156                               | —            | 42,156    |
| Other income  | —  | —   | 8,660                                    | 24,786                               | —            | 33,446    |
| Gain on sale of loans and debt repurchases                                  | —  | —   | 57                                       | —                                    | —            | 57        |
| Derivative market value and foreign currency adjustments, net               | —  | —   | 12,325                                   | (2,577 )                             | —            | 9,748     |
| Derivative settlements, net   | —  | —   | (11,935 )                                | (508 )                               | —            | (12,443 ) |
| Total other income  | 159,238                                      | 47,069  | 9,107                                    | 63,857                               | (28,021 )    | 251,250   |
| Operating expenses:   |  |   |  |                                      |              |           |
| Salaries and benefits   | 59,481                                       | 21,139  | 1,179                                    | 24,573                               | —            | 106,372   |
| Cost to provide enrollment services   | —  | —   | —  | 27,786                               | —            | 27,786    |
| Loan servicing fees   | —  | —   | 12,720                                   | —                                    | —            | 12,720    |
| Depreciation and amortization   | 857  | 3,273   | —  | 5,867                                | —            | 9,997     |
| Other   | 32,625                                       | 5,603   | 3,271                                    | 21,785                               | —            | 63,284    |
| Intersegment expenses, net  | 18,519                                       | 2,824   | 28,339                                   | (21,661 )                            | (28,021 )    | —         |
| Total operating expenses  | 111,482                                      | 32,839  | 45,509                                   | 58,350                               | (28,021 )    | 220,159   |
| Income before income taxes and corporate overhead allocation                | 47,776                                       | 14,233  | 164,751                                  | 6,915                                | —            | 233,675   |
| Corporate overhead allocation   | (3,920 )                                     | (1,307 )  | (2,578 )                                 | 7,805                                | —            | —         |
| Income before income taxes  | 43,856                                       | 12,926  | 162,173                                  | 14,720                               | —            | 233,675   |
| Income tax (expense) benefit  | (16,665 )                                    | (4,911 )  | (61,625 )                                | (488 )                               | —            | (83,689 ) |
| Net income  | 27,191                                       | 8,015   | 100,548                                  | 14,232                               | —            | 149,986   |
| Net income attributable to noncontrolling interest                          | —  | —   | —  | 1,206                                | —            | 1,206     |
| Net income attributable to Nelnet, Inc.                                     | \$27,191                                     | 8,015   | 100,548                                  | 13,026                               | —            | 148,780   |

## 9. Major Customer

The Company earns loan servicing revenue from a servicing contract with the U.S. Department of Education that currently expires on June 16, 2019. Revenue earned by the Company's Student Loan and Guaranty Servicing

operating segment related to this contract was \$33.6 million and \$31.0 million for the three months ended June 30, 2015 and 2014, respectively, and \$66.0 million and \$60.9 million for the six months ended June 30, 2015 and 2014, respectively.

#### 10. Related Parties

The Company has entered into certain contractual arrangements with related parties as described in note 20 of the notes to consolidated financial statements included in the 2014 Annual Report. The following provides an update for related party transactions that occurred during the first six months of 2015.

On March 17, 2015, the Company made a \$40.5 million equity investment in Agile Sports Technologies, Inc. (doing business as "Hudl"). David Graff, who has served on the Company's Board of Directors since May 2014, is CEO, co-founder, and a director of Hudl. Prior to the 2015 investment, the Company and Michael Dunlap, the Company's Executive Chairman and a principal shareholder, made separate equity investments in Hudl. Subsequent to the Company's March 2015 investment, the Company and Mr. Dunlap hold combined direct and indirect equity ownership interests in Hudl of 18.7% and 2.8%, respectively. The Company's and Mr. Dunlap's direct and indirect equity ownership interests in Hudl consist of preferred stock with certain liquidation preferences that are considered substantive. Accordingly, for accounting purposes, the Company's and Mr. Dunlap's equity ownership interests are not considered in-substance common stock and the Company is accounting for its equity investment in Hudl under the cost

method. The Company's investment in Hudl is included in "investments and notes receivable" in the Company's consolidated balance sheet.

On January 1, 2014, the Company subparticipated the Company's participation interest in a loan receivable from an unrelated third party to Union Bank and Trust Company ("Union Bank"). On May 22, 2015, the Company paid Union Bank \$3.1 million to pay off the outstanding loan balance and terminated the subparticipation agreement.

## 11. Fair Value

The following tables present the Company's financial assets and liabilities that are measured at fair value on a recurring basis. There were no transfers into or out of level 1, level 2, or level 3 for the six months ended June 30, 2015.

|  | As of June 30, 2015 |         |         | As of December 31, 2014 |         |         |
|--|---------------------|---------|---------|-------------------------|---------|---------|
|  | Level 1             | Level 2 | Total   | Level 1                 | Level 2 | Total   |
| <b>Assets:</b>                                       |                     |         |         |                         |         |         |
| <b>Investments (available-for-sale and trading):</b> |                     |         |         |                         |         |         |
| Student loan asset-backed securities                 | \$—                 | 101,821 | 101,821 | —                       | 145,000 | 145,000 |
| Equity securities                                    | 15,606              | —       | 15,606  | 3,736                   | —       | 3,736   |
| Debt securities                                      | 343                 | —       | 343     | 387                     | —       | 387     |
| Total investments (available-for-sale and trading)   | 15,949              | 101,821 | 117,770 | 4,123                   | 145,000 | 149,123 |
| Fair value of derivative instruments                 | —                   | 30,216  | 30,216  | —                       | 64,392  | 64,392  |
| Total assets   | \$15,949            | 132,037 | 147,986 | 4,123                   | 209,392 | 213,515 |
| <b>Liabilities:</b>                                  |                     |         |         |                         |         |         |
| Fair value of derivative instruments                 | \$—                 | 67,133  | 67,133  | —                       | 32,842  | 32,842  |
| Total liabilities                                    | \$—                 | 67,133  | 67,133  | —                       | 32,842  | 32,842  |

The following table summarizes the fair values of all of the Company's financial instruments on the consolidated balance sheets:

|  | As of June 30, 2015 |                |         |            |            |
|--|---------------------|----------------|---------|------------|------------|
|  | Fair value          | Carrying value | Level 1 | Level 2    | Level 3    |
| Financial assets:                            |                     |                |         |            |            |
| Student loans receivable                     | \$28,824,415        | 28,095,775     | —       | —          | 28,824,415 |
| Cash and cash equivalents                    | 182,280             | 182,280        | 182,280 | —          | —          |
| Investments (available-for-sale and trading) | 117,770             | 117,770        | 15,949  | 101,821    | —          |
| Notes receivable                             | 28,644              | 31,321         | —       | 28,644     | —          |
| Restricted cash                              | 848,479             | 848,479        | 848,479 | —          | —          |
| Restricted cash – due to customers           | 117,820             | 117,820        | 117,820 | —          | —          |
| Restricted investments                       | 9,374               | 9,374          | 9,374   | —          | —          |
| Accrued interest receivable                  | 364,211             | 364,211        | —       | 364,211    | —          |
| Derivative instruments                       | 30,216              | 30,216         | —       | 30,216     | —          |
| Financial liabilities:                       |                     |                |         |            |            |
| Bonds and notes payable                      | 27,661,342          | 28,070,423     | —       | 27,661,342 | —          |
| Accrued interest payable                     | 28,859              | 28,859         | —       | 28,859     | —          |
| Due to customers                             | 117,820             | 117,820        | 117,820 | —          | —          |
| Derivative instruments                       | 67,133              | 67,133         | —       | 67,133     | —          |





|  | As of December 31, 2014 |                | Level 1 | Level 2    | Level 3    |
|--|-------------------------|----------------|---------|------------|------------|
|  | Fair value              | Carrying value |         |            |            |
| Financial assets:                            |                         |                |         |            |            |
| Student loans receivable                     | \$28,954,226            | 28,005,195     | —       | —          | 28,954,226 |
| Cash and cash equivalents                    | 130,481                 | 130,481        | 130,481 | —          | —          |
| Investments (available-for-sale and trading) | 149,123                 | 149,123        | 4,123   | 145,000    | —          |
| Notes receivable                             | 28,832                  | 30,643         | —       | 28,832     | —          |
| Restricted cash                              | 800,164                 | 800,164        | 800,164 | —          | —          |
| Restricted cash – due to customers           | 118,488                 | 118,488        | 118,488 | —          | —          |
| Restricted investments                       | 50,276                  | 50,276         | 50,276  | —          | —          |
| Accrued interest receivable                  | 351,588                 | 351,588        | —       | 351,588    | —          |
| Derivative instruments                       | 64,392                  | 64,392         | —       | 64,392     | —          |
| Financial liabilities:                       |                         |                |         |            |            |
| Bonds and notes payable                      | 27,809,997              | 28,027,350     | —       | 27,809,997 | —          |
| Accrued interest payable                     | 25,904                  | 25,904         | —       | 25,904     | —          |
| Due to customers                             | 118,488                 | 118,488        | 118,488 | —          | —          |
| Derivative instruments                       | 32,842                  | 32,842         | —       | 32,842     | —          |

The methodologies for estimating the fair value of financial assets and liabilities are described in note 21 of the notes to consolidated financial statements included in the 2014 Annual Report.

## 12. Legal Proceedings

### Grant Keating v. Peterson's Nelnet, LLC et al

On August 6, 2012, an Amended Complaint was served on Peterson's Nelnet, LLC, a subsidiary of Nelnet, Inc. ("Nelnet"), CUnet, LLC, a subsidiary of Nelnet, and on Nelnet (collectively, the "Keating Defendants"), in connection with a lawsuit by Grant Keating in the U.S. Federal District Court for the Northern District of Ohio (the "District Court"). The lawsuit was originally instituted on August 24, 2011, and alleged that the Keating Defendants sent an advertising text message to the named plaintiff in June 2011 using an automatic telephone dialing system, and without the plaintiff's express consent. The complaint also alleged that this text message violated the Telephone Consumer Protection Act, purportedly entitling the plaintiff to \$500, trebled for a willful violation. The complaint further alleged that the Keating Defendants sent putative class members similar text messages using an automatic telephone dialing system, without such purported class members' consent, and sought to establish a class action. On May 12, 2014, the District Court granted the Keating Defendants' motion for summary judgment, and ordered that the case be dismissed. On September 8, 2014, the named plaintiff filed an appeal brief with the Circuit Court of Appeals. On July 21, 2015, the Circuit Court of Appeals affirmed the District Court's judgment in favor of the Keating Defendants, resulting in the dismissal of the case.

## 13. Subsequent Events

On August 3, 2015, the Company acquired the residual interests in two securitized student loan trusts. The two trusts collectively own approximately \$1.5 billion of FFELP student loans and related assets and have issued a corresponding amount of related student loan asset-backed debt secured by those FFELP student loans and related assets. The purchase was funded from the Company's operating cash and unsecured line of credit. The acquired FFELP student loans, related assets, and related asset-backed debt will be included in the Company's consolidated financial statements.

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

(Management's Discussion and Analysis of Financial Condition and Results of Operations is for the three and six months ended June 30, 2015 and 2014. All dollars are in thousands, except per share amounts, unless otherwise noted.)

The following discussion and analysis provides information that the Company's management believes is relevant to an assessment and understanding of the consolidated results of operations and financial condition of the Company. The discussion should be read in conjunction with the Company's consolidated financial statements included in the 2014 Annual Report.

## Forward-looking and cautionary statements

This report contains forward-looking statements and information that are based on management's current expectations as of the date of this document. Statements that are not historical facts, including statements about the Company's plans and expectations for future financial condition, results of operations or economic performance, or that address management's plans and objectives for future operations, and statements that assume or are dependent upon future events, are forward-looking statements. The words "may," "should," "could," "would," "predict," "potential," "continue," "expect," "anticipate," "future," "intend," "plan," "believe," "estimate," "assume," "forecast," "will," and similar expressions, as well as statements in future tense, are intended to identify forward-looking statements.

The forward-looking statements are based on assumptions and analyses made by management in light of management's experience and its perception of historical trends, current conditions, expected future developments, and other factors that management believes are appropriate under the circumstances. These statements are subject to known and unknown risks, uncertainties, assumptions, and other factors that may cause the actual results and performance to be materially different from any future results or performance expressed or implied by such forward-looking statements. These factors include, among others, the risks and uncertainties set forth in the "Risk Factors" section of the 2014 Annual Report and elsewhere in this report, and include such risks and uncertainties as:

student loan portfolio risks such as interest rate basis and repricing risk resulting from the fact that the interest rate characteristics of the student loan assets do not match the interest rate characteristics of the funding for those assets, the risk of loss of floor income on certain student loans originated under the Federal Family Education Loan Program (the "FFEL Program" or "FFELP"), risks related to the use of derivatives to manage exposure to interest rate fluctuations, uncertainties regarding the expected benefits from recently purchased securitized and unsecuritized FFELP and private education loans and initiatives to purchase additional FFELP and private education loans, and risks from changes in levels of student loan prepayment or default rates;

financing and liquidity risks, including risks of changes in the general interest rate environment and in the securitization and other financing markets for student loans, which may increase the costs or limit the availability of financings necessary to purchase, refinance, or continue to hold student loans;

risks from changes in the educational credit and services markets resulting from changes in applicable laws, regulations, and government programs and budgets, such as the expected decline over time in FFELP loan interest income and fee-based revenues due to the discontinuation of new FFELP loan originations in 2010 and potential government initiatives or legislative proposals to consolidate existing FFELP loans to the Federal Direct Loan Program or otherwise allow FFELP loans to be refinanced with Federal Direct Loan Program loans, risks related to reduced government payments to guaranty agencies to rehabilitate defaulted FFELP loans and services in support of those activities, including potential adverse effects on the Company's guaranty servicing contracts, risks related to the Company's ability to maintain or increase volumes under the Company's loan servicing contract with the U.S. Department of Education (the "Department"), which accounted for approximately 10 percent of the Company's revenue in 2014 and for which the loan allocation metrics were modified effective September 1, 2014, and risks related to the Company's ability to comply with agreements with third-party customers for the servicing of FFELP, Federal Direct Loan Program, and private education loans;

risks related to a breach of or failure in the Company's operational or information systems or infrastructure, or those of third-party vendors;

uncertainties inherent in forecasting future cash flows from student loan assets and related asset-backed securitizations; and

risks and uncertainties associated with litigation matters and with maintaining compliance with the extensive regulatory requirements applicable to the Company's businesses, and uncertainties inherent in the estimates and assumptions about future events that management is required to make in the preparation of the Company's consolidated financial statements.

All forward-looking statements contained in this report are qualified by these cautionary statements and are made only as of the date of this document. Although the Company may from time to time voluntarily update or revise its prior forward-looking statements to reflect actual results or changes in the Company's expectations, the Company disclaims any commitment to do so except as required by securities laws.

## OVERVIEW

The Company provides educational products and services in loan servicing, payment processing, education planning, and asset management. These products and services help students and families plan, prepare, and pay for their education and make the administrative and financial processes more efficient for schools and financial organizations. In addition, the Company earns interest income on a portfolio of federally insured student loans.

A reconciliation of the Company's GAAP net income to net income, excluding derivative market value and foreign currency adjustments, is provided below.

|  | Three months ended June 30, |          | Six months ended June 30, |          |
|--|-----------------------------|----------|---------------------------|----------|
|  | 2015                        | 2014     | 2015                      | 2014     |
| GAAP net income attributable to Nelnet, Inc.                                       | \$70,909                    | 74,994   | 135,674                   | 148,780  |
| Derivative market value and foreign currency adjustments, net of tax               | (7,405                      | ) (4,826 | ) (8,730                  | ) (6,044 |
| Net income, excluding derivative market value and foreign currency adjustments (a) | \$63,504                    | 70,168   | 126,944                   | 142,736  |
| Earnings per share:  |                             |          |                           |          |
| GAAP net income attributable to Nelnet, Inc.                                       | \$1.54                      | 1.61     | 2.94                      | 3.20     |
| Derivative market value and foreign currency adjustments, net of tax               | (0.16                       | ) (0.10  | ) (0.19                   | ) (0.13  |
| Net income, excluding derivative market value and foreign currency adjustments (a) | \$1.38                      | 1.51     | 2.75                      | 3.07     |

The Company provides non-GAAP information that reflects specific items management believes to be important in the evaluation of its financial position and performance. "Derivative market value and foreign currency adjustments" include (i) the unrealized gains and losses that are caused by changes in fair values of derivatives which do not qualify for "hedge treatment" under GAAP; and (ii) the foreign currency transaction gains or losses caused by the re-measurement of the Company's Euro-denominated bonds to U.S. dollars. The Company believes these point-in-time estimates of asset and liability values related to these financial instruments that are subject to interest and currency rate fluctuations affect the period-to-period comparability of the results of operations. Accordingly, the Company provides operating results excluding these items for comparability purposes.

The Company earns net interest income on its FFELP student loan portfolio in its Asset Generation and Management ("AGM") operating segment. This segment is expected to generate a stable net interest margin and significant amounts of cash as the FFELP portfolio amortizes. As of June 30, 2015, the Company had a \$28.1 billion student loan portfolio that will amortize over the next approximately 25 years. The Company actively seeks to acquire additional FFELP loan portfolios to leverage its servicing scale and expertise to generate incremental earnings and cash flow.

In addition, the Company earns fee-based revenue through the following reportable operating segments:

- Student Loan and Guaranty Servicing ("LGS") - referred to as Nelnet Diversified Solutions ("NDS")
- Tuition Payment Processing and Campus Commerce ("TPP&CC") - referred to as Nelnet Business Solutions ("NBS")

Other business activities and operating segments that are not reportable are combined and included in Corporate and Other Activities. Corporate and Other Activities also includes income earned on certain investments and interest expense incurred on unsecured debt transactions.



The information below provides the operating results for each reportable operating segment and Corporate and Other Activities ("Corporate") for the three and six months ended June 30, 2015 and 2014 (dollars in millions).

(a) Revenue includes intersegment revenue earned by LGS as a result of servicing loans for AGM.

(b) Total revenue includes "net interest income after provision for loan losses" and "total other income" from the Company's segment statements of income, excluding the impact from changes in fair values of derivatives and foreign currency transaction adjustments. Net income excludes changes in fair values of derivatives and foreign currency transaction adjustments, net of tax.

(c) Computed as income before income taxes divided by total revenue.

#### Student Loan and Guaranty Servicing

As of June 30, 2015, the Company was servicing \$169.9 billion in FFELP, private, and government owned student loans, as compared with \$150.0 billion of loans as of June 30, 2014.

Revenue decreased in the three and six months ended June 30, 2015 compared to the same periods in 2014 due primarily to a decrease in rehabilitation collection revenue. Federal budget provisions that became effective July 1, 2014 have reduced payments by the Department to guaranty agencies for assisting student loan borrowers with the rehabilitation of defaulted loans under FFELP, and as a result, rehabilitation revenue has been negatively affected. Rehabilitation collection revenue recognized by the Company was \$11.5 million and \$17.3 million for the three months ended June 30, 2015 and 2014, respectively, and \$18.9 million and \$30.7 million for the six months ended June 30, 2015 and 2014, respectively.

Revenue from the Department servicing contract increased to \$33.6 million for the three months ended June 30, 2015 compared to \$31.0 million for the same period in 2014, and increased to \$66.0 million for the six months ended June 30, 2015, compared to \$60.9 million for the same period in 2014. As of June 30, 2015, the Company was servicing \$141.5 billion of loans for 5.8 million borrowers under this contract.

A significant amount of the Company's guaranty servicing revenue comes from a single guaranty servicing client. The current term of the contract with this client expires on October 31, 2015. During the second quarter of 2015, the client notified the Company of their intent to not renew this contract. FFELP guaranty servicing and FFELP guaranty collection revenue recognized by the Company from this client for the year ended December 31, 2014 and six months ended June 30, 2015 was \$48.5 million and \$21.3 million, respectively. The Company incurs collection costs that are directly related to guaranty collection revenue earned on this contract.

Before tax operating margin was 19.4% and 26.6% for the three months ended June 30, 2015 and 2014, respectively, and 16.9% and 27.5% for the six months ended June 30, 2015 and 2014, respectively. Operating margin decreased as a result of the implementation of federal budget reductions for guaranty agencies revenue. In addition, as the volume of loans serviced under the Department servicing contract continues to grow and loans serviced under the legacy commercial programs continue to run off, the Company expects operating margins to tighten accordingly. The Company also anticipates that margins will tighten as a result of the loss of the FFELP guaranty servicing and FFELP guaranty collection client discussed above.

### Tuition Payment Processing and Campus Commerce

Revenue increased in the three and six months ended June 30, 2015 compared to the same periods in 2014 due to the acquisition of RenWeb on June 3, 2014 and due to increases in the number of managed tuition payment plans, campus commerce customer transaction and payments volume, and new school customers.

Excluding the amortization of intangibles, before tax operating margin was 22.6% and 24.1% for the three months ended June 30, 2015 and 2014, respectively, and 32.6% and 32.7% for the six months ended June 30, 2015 and 2014, respectively. The decrease in margin is due to new products and services as a result of recent acquisitions.

### Asset Generation and Management

The Company acquired \$2.1 billion of student loans during the first six months of 2015, of which \$1.2 billion were purchased in the second quarter. The average loan portfolio balance was \$28.3 billion and \$28.2 billion for the three months ended June 30, 2015 and 2014, respectively, and \$28.3 billion and \$27.0 billion for the six months ended June 30, 2015 and 2014, respectively.

Core student loan spread was 1.41% for the three months ended June 30, 2015, compared to 1.41% and 1.46% for the three months ended March 31, 2015 and June 30, 2014, respectively. The year over year decrease was the result of recent acquisitions of consolidation loans, which have lower margins but longer terms.

Due to historically low interest rates, the Company continues to earn significant fixed rate floor income. During the three months ended June 30, 2015 and 2014 and six months ended June 30, 2015 and 2014, the Company earned \$45.1 million, \$43.6 million, \$91.3 million, and \$81.5 million, respectively, of fixed rate floor income (net of \$5.0 million, \$7.0 million, \$10.0 million, and \$13.9 million of derivative settlements, respectively, used to hedge such loans).

On August 3, 2015, the Company acquired the residual interests in two securitized student loan trusts. The two trusts collectively own approximately \$1.5 billion of FFELP student loans and related assets and have issued a corresponding amount of related student loan asset-backed debt secured by those FFELP student loans and related assets. The purchase was funded from the Company's operating cash and unsecured line of credit. The acquired FFELP student loans, related assets, and related asset-backed debt will be included in the Company's consolidated financial statements.

### Corporate and Other Activities

The Company recognized \$1.9 million and \$2.1 million in net gains from investment activity during the three months ended June 30, 2015 and 2014, respectively, and \$2.4 million and \$9.3 million during the six months ended June 30, 2015 and 2014, respectively. The majority of gains recognized in 2014 were from sales of student loan asset-backed security investments.

- Whitetail Rock Capital Management, LLC ("WRCM"), the Company's SEC-registered investment advisory subsidiary, recognized investment advisory revenue of \$0.8 million and \$7.0 million for the three months ended June 30, 2015 and 2014, respectively, and \$1.5 million and \$12.3 million for the six months ended June 30, 2015 and 2014, respectively. Due to improvements in the capital markets, the opportunities to earn performance fees on the sale of student loan asset-backed securities are becoming increasingly limited.
-



During the three months ended June 30, 2015 and 2014, the Company recognized gains of \$1.5 million and \$18,000, respectively, on repurchases of its own debt. Gains from debt repurchases in the six months ended June 30, 2015 and 2014 were \$4.0 million and \$57,000, respectively.

#### Liquidity and Capital Resources

As of June 30, 2015, the Company had cash and cash equivalents of \$182.3 million. In addition, the Company had a portfolio of available-for-sale and trading investments, consisting primarily of student loan asset-backed securities, with a fair value of \$117.8 million as of June 30, 2015.

For the six months ended June 30, 2015, the Company generated \$192.0 million in net cash provided by operating activities, including \$51.9 million from the termination of certain derivative financial instruments.

Forecasted future cash flows from the Company's FFELP student loan portfolio financed in asset-backed securitization transactions are estimated to be approximately \$2.32 billion as of June 30, 2015.

As of June 30, 2015, \$100.0 million was outstanding on the Company's unsecured line of credit and \$250.0 million was available for future use. The unsecured line of credit has a maturity date of June 30, 2019.

During the six months ended June 30, 2015, the Company repurchased a total of 1,174,008 shares of Class A common stock for \$51.0 million (\$43.46 per share), including 998,210 shares for \$43.1 million (\$43.17 per share) during the second quarter.

During the six months ended June 30, 2015, the Company paid cash dividends of \$9.2 million (\$0.20 per share), including \$4.6 million (\$0.10 per share) during the second quarter.

The Company intends to use its liquidity position to capitalize on market opportunities, including FFELP and private education loan acquisitions; strategic acquisitions and investments; and capital management initiatives, including stock repurchases, debt repurchases, and dividend distributions. Dependent upon the timing and size of the opportunities, the Company may continue to accumulate additional cash and investments.

#### CONSOLIDATED RESULTS OF OPERATIONS

Analysis of the Company's operating results for the three and six months ended June 30, 2015 compared to the same periods in 2014 is summarized below.

The Company's operating results are primarily driven by the performance of its existing portfolio and the revenues generated by its fee-based businesses and the costs to provide their products and services. The performance of the Company's portfolio is driven by net interest income (which includes financing costs) and losses related to credit quality of the assets, along with the cost to administer and service the assets and related debt.

The Company operates in distinct operating segments as described previously. For a reconciliation of the segment operating results to the consolidated results of operations, see note 8 of the notes to consolidated financial statements included under Part I, Item 1 of this report. Since the Company monitors and assesses its operations and results based on these segments, the discussion following the consolidated results of operations is presented on a segment basis.

Edgar Filing: NELNET INC - Form 10-Q

|   | Three months<br>ended June 30,<br>2015 |          | Six months<br>ended June 30,<br>2015 |           | Additional information  |
|---|--|----------|--------------------------------------|-----------|---|
|   |  | 2014     |                                      | 2014      |   |
| Loan interest   | \$175,835                              | 175,466  | 347,779                              | 332,362   | Increase was due to an increase in the average student loan portfolio balance and gross fixed rate floor income, partially offset by an increase in consolidation rebate fees.  |
| Investment interest   | 1,887                                  | 1,482    | 4,092                                | 3,461     | Includes income from unrestricted interest-earning deposits and investments and funds in asset-backed securitizations.  |
| Total interest income   | 177,722                                | 176,948  | 351,871                              | 335,823   |   |
| Interest expense  | 72,626                                 | 69,235   | 144,180                              | 129,239   | Increase due to an increase in average debt outstanding and an increase in the Company's cost of funds.   |
| Net interest income   | 105,096                                | 107,713  | 207,691                              | 206,584   | See table below for additional analysis.  |
| Less provision for loan losses                                | 2,150                                  | 1,500    | 4,150                                | 4,000     | Represents the periodic expense of maintaining an allowance appropriate to absorb losses inherent in the portfolio of student loans. See AGM operating segment - results of operations.   |
| Net interest income after provision for loan losses           | 102,946                                | 106,213  | 203,541                              | 202,584   |   |
| Other income:   |  |          |                                      |           |   |
| LGS revenue   | 63,833                                 | 66,460   | 121,644                              | 131,217   | See LGS operating segment - results of operations.  |
| TPP&CC revenue  | 27,686                                 | 21,834   | 62,366                               | 47,069    | See TPP&CC operating segment - results of operations.   |
| NES revenue   | 17,161                                 | 20,145   | 35,024                               | 42,156    | See table below for additional analysis.  |
| Other income  | 7,504                                  | 15,315   | 14,422                               | 33,446    | See table below for the components of "other income."   |
| Gain on sale of loans and debt repurchases                    | 1,515                                  | 18       | 4,390                                | 57        | Gains are primarily from the Company repurchasing its own debt.   |
| Derivative settlements, net                                   | (5,442 )                               | (6,214 ) | (10,657 )                            | (12,443 ) | The Company maintains an overall risk management strategy that incorporates the use of derivative instruments to reduce the economic effect of interest rate volatility. Derivative settlements for each applicable period should be evaluated with the Company's net interest income. See table below for additional analysis. |
| Derivative market value and foreign currency adjustments, net | 11,944                                 | 7,784    | 14,081                               | 9,748     | Includes (i) the unrealized gains and losses that are caused by changes in fair values of derivatives which do not qualify for "hedge treatment" under GAAP; and (ii) the foreign currency transaction gains or losses caused by the re-measurement of the Company's Euro-denominated bonds to U.S. dollars.                    |

Edgar Filing: NELNET INC - Form 10-Q

|   |           |          |           |          |   |
|---|-----------|----------|-----------|----------|---|
| Total other income  | 124,201   | 125,342  | 241,270   | 251,250  |   |
| Operating expenses:   |           |          |           |          |   |
| Salaries and benefits   | 58,787    | 53,888   | 119,837   | 106,372  | Increase was due to additional personnel to support increased LGS servicing volume and TPP&CC revenue.  |
| Cost to provide enrollment services   | 11,162    | 13,311   | 22,864    | 27,786   | See table below for additional analysis.  |
| Loan servicing fees   | 7,420     | 7,317    | 15,036    | 12,720   | Increase was due to an increase in third party loan servicing fees incurred by AGM as volume at third parties has grown with recent loan purchases.   |
| Depreciation and amortization   | 6,501     | 5,214    | 12,163    | 9,997    | Increase was due to additional expense from the amortization of intangible assets. Intangible amortization expense was \$2.4 million and \$1.4 million for the three months ended June 30, 2015 and 2014, respectively, and \$4.8 million and \$2.4 million for the six months ended June 30, 2015 and 2014, respectively.  |
| Other   | 31,958    | 33,060   | 61,156    | 63,284   | Decrease was due to a decrease in collection costs directly related to the decrease in FFELP guaranty collection revenue, partially offset by an increase in other costs to support increased LGS servicing volume and TPP&CC revenue.  |
| Total operating expenses  | 115,828   | 112,790  | 231,056   | 220,159  |   |
| Income before income taxes  | 111,319   | 118,765  | 213,755   | 233,675  |   |
| Income tax expense  | 40,356    | 43,078   | 77,986    | 83,689   | The effective tax rate was 36.3% and 36.5% in the three months ended June 30, 2015 and 2014, respectively, and 36.5% and 36.0% in the six months ended June 30, 2015 and 2014, respectively.  |
| Net income  | 70,963    | 75,687   | 135,769   | 149,986  |   |
| Net income attributable to noncontrolling interest  | 54        | 693      | 95        | 1,206    |   |
| Net income attributable to Nelnet, Inc.   | \$70,909  | 74,994   | 135,674   | 148,780  |   |
| Additional information:   |           |          |           |          |   |
| Net income attributable to Nelnet, Inc.   | \$70,909  | 74,994   | 135,674   | 148,780  | The Company provides non-GAAP information that reflects specific items management believes to be important in the evaluation of its operating results. The Company believes the point-in-time estimates of asset and liability values related to its derivatives and Euro-denominated bonds that are subject to interest and currency rate fluctuations affect the period-to-period comparability of the results of operations. These items are excluded here for comparability purposes. |
| Derivative market value and foreign currency adjustments  | (11,944 ) | (7,784 ) | (14,081 ) | (9,748 ) |   |
| Tax effect  | 4,539     | 2,958    | 5,351     | 3,704    |   |
| Net income attributable to Nelnet, Inc., excluding derivative market value and foreign currency adjustments | \$63,504  | 70,168   | 126,944   | 142,736  |   |



The following table summarizes the components of "net interest income" and "derivative settlements, net."

|  | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          | Additional information  |
|--|--------------------------------|----------|------------------------------|----------|---|
|  | 2015                           | 2014     | 2015                         | 2014     |   |
| Variable student loan interest margin, net of settlements on derivatives | \$54,521                       | 58,627   | 105,155                      | 113,023  | Represents the yield the Company receives on its student loan portfolio less the cost of funding these loans. Variable student loan spread is also impacted by the amortization/accretion of loan premiums and discounts, the 1.05% per year consolidation loan rebate fee paid to the Department, and yield adjustments from borrower benefit programs. See AGM operating segment - results of operations. |
| Fixed rate floor income, net of settlements on derivatives               | 45,069                         | 43,607   | 91,313                       | 81,451   | The Company has a portfolio of student loans that are earning interest at a fixed borrower rate which exceeds the statutorily defined variable lender rates, generating fixed rate floor income. See Item 3, "Quantitative and Qualitative Disclosures About Market Risk - Interest Rate Risk" for additional information.  |
| Investment interest  | 1,887                          | 1,482    | 4,092                        | 3,461    |   |
| Non-portfolio related derivative settlements                             | (253 )                         | (256 )   | (506 )                       | (508 )   |   |
| Corporate debt interest expense  | (1,570 )                       | (1,961 ) | (3,020 )                     | (3,286 ) | Includes interest expense on the Junior Subordinated Hybrid Securities and unsecured and secured lines of credit.   |
| Net interest income (net of settlements on derivatives)                  | \$99,654                       | 101,499  | 197,034                      | 194,141  |   |

The following table summarizes the components of "Enrollment services revenue" and "cost to provide enrollment services."

|                                     | Inquiry management (marketing) (a) | Inquiry management (software) | Inquiry generation (b) | Digital marketing | Content solutions | Total  |
|-------------------------------------|------------------------------------|-------------------------------|------------------------|-------------------|-------------------|--------|
|                                     | Three months ended June 30, 2015   |                               |                        |                   |                   |        |
| Enrollment services revenue         | \$11,751                           | 929                           | —                      | 1,068             | 3,413             | 17,161 |
| Cost to provide enrollment services | 10,395                             | —                             | —                      | 67                | 700               | 11,162 |
| Gross profit                        | \$1,356                            | 929                           | —                      | 1,001             | 2,713             | 5,999  |
| Gross profit %                      | 11.5%                              |                               |                        |                   |                   |        |
|                                     | Three months ended June 30, 2014   |                               |                        |                   |                   |        |
| Enrollment services revenue         | \$12,507                           | 945                           | 2,513                  | 908               | 3,272             | 20,145 |
| Cost to provide enrollment services | 10,976                             | —                             | 1,645                  | 47                | 643               | 13,311 |
| Gross profit                        | \$1,531                            | 945                           | 868                    | 861               | 2,629             | 6,834  |

Edgar Filing: NELNET INC - Form 10-Q

Gross profit % 12.2%

|                                     | Six months ended June 30, 2015 |       |   |       |       |        |
|-------------------------------------|--------------------------------|-------|---|-------|-------|--------|
| Enrollment services revenue         | \$23,960                       | 2,047 | — | 2,304 | 6,713 | 35,024 |
| Cost to provide enrollment services | 21,194                         | —     | — | 188   | 1,482 | 22,864 |
| Gross profit                        | \$2,766                        | 2,047 | — | 2,116 | 5,231 | 12,160 |
| Gross profit %                      | 11.5%                          |       |   |       |       |        |

|                                     | Six months ended June 30, 2014 |       |       |       |       |        |
|-------------------------------------|--------------------------------|-------|-------|-------|-------|--------|
| Enrollment services revenue         | \$26,044                       | 2,014 | 5,359 | 1,976 | 6,763 | 42,156 |
| Cost to provide enrollment services | 22,929                         | —     | 3,431 | 135   | 1,291 | 27,786 |
| Gross profit                        | \$3,115                        | 2,014 | 1,928 | 1,841 | 5,472 | 14,370 |
| Gross profit %                      | 12.0%                          |       |       |       |       |        |

Inquiry management (marketing) revenue decreased \$0.8 million (6.0%) and \$2.1 million (8.0%) for the three and (a) six months ended June 30, 2015, respectively, compared to the same periods in 2014 as a result of a decrease in spending on marketing efforts by school clients.

(b) Effective August 29, 2014, the Company stopped providing inquiry generation services.

The following table summarizes the components of "other income."

|  | Three months ended June 30, |        | Six months ended June 30, |        |
|--|-----------------------------|--------|---------------------------|--------|
|  | 2015                        | 2014   | 2015                      | 2014   |
| Borrower late fee income                                   | \$3,621                     | 3,557  | 7,752                     | 7,244  |
| Investment advisory fees (a)                               | 833                         | 7,035  | 1,490                     | 12,264 |
| Realized and unrealized gains/(losses) on investments, net | 1,852                       | 2,081  | 2,369                     | 9,291  |
| Other  | 1,198                       | 2,642  | 2,811                     | 4,647  |
| Other income   | \$7,504                     | 15,315 | 14,422                    | 33,446 |

WRCM earns annual fees of up to 25 basis points on the outstanding balance of investments and up to 50 percent of the gains from the sale of securities for which it provides advisory services. Due to improvements in the capital (a) markets, the opportunities to earn performance fees on the sale of student loan asset-backed securities are becoming increasingly limited. As of June 30, 2015, WRCM was managing an investment portfolio of \$913.3 million for third-party entities.

#### STUDENT LOAN AND GUARANTY SERVICING OPERATING SEGMENT – RESULTS OF OPERATIONS

##### Student Loan Servicing Volumes (dollars in millions)

|                                |           |           |           |           |           |           |           |           |           |
|--------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Company owned                  | \$22,650  | \$21,237  | \$21,397  | \$21,192  | \$21,110  | \$20,511  | \$19,742  | \$19,369  | \$18,934  |
| % of total                     | 29.8%     | 21.8%     | 15.5%     | 14.3%     | 14.1%     | 12.9%     | 12.2%     | 11.5%     | 11.1%     |
| Number of servicing borrowers: |           |           |           |           |           |           |           |           |           |
| Government servicing:          | 3,036,534 | 3,892,929 | 5,305,498 | 5,438,933 | 5,465,395 | 5,824,743 | 5,915,449 | 5,882,446 | 5,817,078 |
| FFELP servicing:               | 1,799,484 | 1,626,146 | 1,462,122 | 1,426,435 | 1,390,541 |           |           |           |           |