

FRANKLIN COVEY CO
Form 10-Q
April 11, 2013

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 March 2, 2013

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

For the transition period from _____ to _____

Commission file no. 1-11107

FRANKLIN COVEY CO.
(Exact name of registrant as specified in its charter)

Utah 87-0401551
(State of (I.R.S.
incorporation) employer
identification
number)

2200 West 84119-2099
Parkway (Zip Code)
Boulevard
Salt Lake City,
Utah
(Address of
principal
executive
offices)

Registrant's
telephone (801)

number, 817-1776
Including area
code

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

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

| | | | |
|-------------------------|-------------------------------------|---|---|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | (Do not check if a smaller reporting company) | Smaller reporting company <input checked="" type="checkbox"/> |

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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock as of the latest practicable date:

16,322,425 shares of Common Stock as of March 29, 2013

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

FRANKLIN COVEY CO.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

| | March 2, 2013 | August 31, 2012 |
|---|------------------|--------------------|
| | (unaudited) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$15,541 | \$11,011 |
| Accounts receivable, less allowance for doubtful accounts of \$644 and \$851 | 31,712 | 38,087 |
| Receivable from related party | 608 | 3,588 |
| Inventories | 3,816 | 4,161 |
| Deferred income tax assets | 3,522 | 3,634 |
| Prepaid expenses and other current assets | 4,674 | 3,714 |
| Total current assets | 59,873 | 64,195 |
| Property and equipment, net | 17,925 | 18,496 |
| Intangible assets, net | 57,962 | 59,205 |
| Goodwill | 9,172 | 9,172 |
| Long-term receivable from related party | 3,969 | 3,478 |
| Other long-term assets | 9,401 | 9,534 |
| | \$158,302 | \$164,080 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current portion of financing obligation | \$1,064 | \$992 |
| Current portion of bank note payable | 1,250 | 2,500 |
| Accounts payable | 6,399 | 7,758 |
| Income taxes payable | 704 | 869 |
| Accrued liabilities | 17,977 | 24,530 |
| Total current liabilities | 27,394 | 36,649 |
| Financing obligation, less current portion | 27,962 | 28,515 |
| Bank note payable, less current portion | - | 208 |
| Other liabilities | 1,601 | 1,152 |
| Deferred income tax liabilities | 6,859 | 7,001 |
| Total liabilities | 63,816 | 73,525 |
| Shareholders' equity: | | |
| Common stock, \$.05 par value; 40,000 shares authorized, 27,056 shares issued | 1,353 | 1,353 |

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| | | |
|--|------------|------------|
| Additional paid-in capital | 207,924 | 182,534 |
| Common stock warrants | 111 | 5,260 |
| Retained earnings | 30,599 | 26,110 |
| Accumulated other comprehensive income | 2,471 | 3,410 |
| Treasury stock at cost, 10,816 shares and 9,365 shares | (147,972) | (128,112) |
| Total shareholders' equity | 94,486 | 90,555 |
| | \$ 158,302 | \$ 164,080 |

See notes to condensed consolidated financial statements.

FRANKLIN COVEY CO.

CONDENSED CONSOLIDATED INCOME STATEMENTS AND STATEMENTS OF COMPREHENSIVE
INCOME

(in thousands, except per share amounts)

| | Quarter Ended | | Two Quarters Ended | |
|--|---------------------------------|--|---------------------------------|--|
| | March 2, 2013 (unaudited) | February 25, 2012 (unaudited) | March 2, 2013 (unaudited) | February 25, 2012 (unaudited) |
| Net sales: | | | | |
| Training and consulting services | \$37,744 | \$35,606 | \$78,807 | \$71,988 |
| Products | 1,624 | 2,303 | 3,567 | 4,766 |
| Leasing | 1,062 | 718 | 2,117 | 1,413 |
| | 40,430 | 38,627 | 84,491 | 78,167 |
| Cost of sales: | | | | |
| Training and consulting services | 11,939 | 11,973 | 25,528 | 23,832 |
| Products | 746 | 1,247 | 1,171 | 1,982 |
| Leasing | 461 | 426 | 949 | 830 |
| | 13,146 | 13,646 | 27,648 | 26,644 |
| Gross profit | 27,284 | 24,981 | 56,843 | 51,523 |
| Selling, general, and administrative | 22,691 | 20,714 | 45,634 | 42,087 |
| Depreciation | 722 | 860 | 1,423 | 1,694 |
| Amortization | 619 | 626 | 1,241 | 1,256 |
| Income from operations | 3,252 | 2,781 | 8,545 | 6,486 |
| Interest income | 150 | 4 | 288 | 7 |
| Interest expense | (598) | (626) | (1,188) | (1,260) |
| Discount on related party receivable | (135) | - | (283) | - |
| Income before income taxes | 2,669 | 2,159 | 7,362 | 5,233 |
| Provision for income taxes | (1,077) | (997) | (2,873) | (2,409) |
| Net income | \$1,592 | \$1,162 | \$4,489 | \$2,824 |
| Net income per share: | | | | |
| Basic | \$0.09 | \$0.07 | \$0.24 | \$0.16 |
| Diluted | 0.08 | 0.06 | 0.23 | 0.16 |
| Weighted average number of common shares: | | | | |
| Basic | 18,550 | 17,764 | 18,356 | 17,748 |
| Diluted | 19,709 | 18,287 | 19,493 | 18,142 |
| COMPREHENSIVE INCOME | | | | |
| Net income | \$1,592 | \$1,162 | \$4,489 | \$2,824 |
| Foreign currency translation adjustments, net of tax | (681) | (131) | (939) | (307) |

| | | | | |
|----------------------|-------|---------|---------|---------|
| Comprehensive income | \$911 | \$1,031 | \$3,550 | \$2,517 |
|----------------------|-------|---------|---------|---------|

See notes to condensed consolidated financial statements.

FRANKLIN COVEY CO.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | Two Quarters Ended | |
|---|--------------------|----------|
| | March 2, | February |
| | 2013 | 2012 |
| | (unaudited) | |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$4,489 | \$2,824 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 2,668 | 2,982 |
| Share-based compensation cost | 1,445 | 2,245 |
| Amortization of capitalized curriculum costs | 958 | 902 |
| Deferred income taxes | (138) | 1,056 |
| Loss on disposals of property and equipment | - | 18 |
| Changes in assets and liabilities: | | |
| Decrease in accounts receivable, net | 5,976 | 4,847 |
| Decrease in inventories | 204 | 390 |
| Decrease in receivable from related party | 2,489 | 315 |
| Increase in prepaid expenses and other assets | (986) | (681) |
| Decrease in accounts payable and accrued liabilities | (7,323) | (5,831) |
| Increase (decrease) in income taxes payable | (97) | 119 |
| Increase (decrease) in other long-term liabilities | 494 | (8) |
| Net cash provided by operating activities | 10,179 | 9,178 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchases of property and equipment | (1,432) | (1,013) |
| Curriculum development costs | (1,061) | (1,667) |
| Net cash used for investing activities | (2,493) | (2,680) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from line of credit borrowings | - | 8,523 |
| Payments on line of credit borrowings | - | (8,523) |
| Principal payments on notes payable financing | (1,458) | (1,042) |
| Principal payments on financing obligation | (506) | (443) |
| Purchases of common stock for treasury | (1,217) | (21) |
| Proceeds from sales of common stock held in treasury | 201 | 205 |
| Proceeds from exercise of common stock warrants | 86 | - |
| Net cash used for financing activities | (2,894) | (1,301) |
| Effect of foreign currency exchange rates on cash and cash equivalents | (262) | 1 |
| Net increase in cash and cash equivalents | 4,530 | 5,198 |

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| | | |
|--|----------|---------|
| Cash and cash equivalents at the beginning of the period | 11,011 | 3,016 |
| Cash and cash equivalents at the end of the period | \$15,541 | \$8,214 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for income taxes | \$1,832 | \$1,081 |
| Cash paid for interest | 1,183 | 1,255 |
| Non-cash investing and financing activities: | | |
| Purchases of property and equipment financed by accounts payable | \$46 | \$307 |

See notes to condensed consolidated financial statements.

FRANKLIN COVEY CO.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
(in thousands and unaudited)

| | Common Stock Shares | Common Stock Amount | Additional Paid-In Capital | Common Stock Warrants | Retained Earnings | Accumulated Other Comprehensive Income | Treasury Stock Shares | Treasury Stock Amount |
|--|---------------------------|---------------------------|----------------------------------|-----------------------------|----------------------|---|-----------------------------|-----------------------------|
| Balance at August 31, 2012 | 27,056 | \$1,353 | \$ 182,534 | \$5,260 | \$26,110 | \$ 3,410 | (9,365) | \$(128,112) |
| Issuance of common stock from treasury | | | (2,896) | | | | 225 | 3,097 |
| Purchase of treasury shares | | | | | | | (106) | (1,217) |
| Common stock warrant activity | | | (18,026) | (5,149) | | | 1,692 | 23,261 |
| Share-based compensation | | | 1,445 | | | | | |
| Unvested share award | | | (421) | | | | 31 | 421 |
| Cumulative translation adjustments | | | | | | (939) | | |
| Management stock loan payments | | | 45,299 | | | | (3,296) | (45,433) |
| Other | | | (11) | | | | 3 | 11 |
| Net income | | | | | 4,489 | | | |
| Balance at March 2, 2013 | 27,056 | \$1,353 | \$ 207,924 | \$111 | \$30,599 | \$ 2,471 | (10,816) | \$(147,972) |

See notes to condensed consolidated financial statements.

FRANKLIN COVEY CO.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 – BASIS OF PRESENTATION

Franklin Covey Co. (hereafter referred to as us, we, our, or the Company) is a global content and intellectual property company focused on individual and organizational performance. Our mission is to “enable greatness in people and organizations everywhere,” and we believe that we are experts at solving seven pervasive, intractable problems, each of which requires a change in human behavior. We are organized to address these seven problems, which include the following: Leadership, Execution, Productivity, Trust, Loyalty, Sales Performance, and Education. As we deliver our solutions to these problems, we believe there are four important characteristics that distinguish us from our competitors.

1. World Class Content – Our content is principle centered and based on natural laws of human behavior and effectiveness. Our content is designed to build new skillsets, establish new mindsets, and provide enabling toolsets.
2. Breadth and Scalability of Delivery Options – We have a wide range of content delivery options, including: on-site training, training led through certified facilitators, on-line learning, blended learning, intellectual property licenses, and organization-wide transformational processes, including consulting and coaching.
3. Global Capability – We operate four regional sales offices and a government services office in the United States; wholly-owned subsidiaries in Australia, Japan, and the United Kingdom; and contract with licensee partners who deliver our curriculum and provide services in over 140 other countries and territories around the world.
4. Transformational Impact and Reach – We hold ourselves responsible for and measure ourselves by our clients’ achievement of transformational results.

Our offerings are described in further detail at www.franklincovey.com. We have some of the best-known offerings in the training industry, including a suite of individual-effectiveness and leadership-development training products based on the best-selling book, *The 7 Habits of Highly Effective People* and its execution process, *The 4 Disciplines of Execution*.

The accompanying unaudited condensed consolidated financial statements reflect, in the opinion of management, all adjustments (consisting of normal recurring accruals) necessary to present fairly the financial position and results of operations of the Company as of the dates and for the periods indicated. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to Securities and Exchange Commission (SEC) rules and regulations. The information included in this quarterly report on Form 10-Q should be read in conjunction with the consolidated financial statements and related notes included in our annual report on Form 10-K for the fiscal year ended August 31, 2012.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets

and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

The Company utilizes a modified 52/53-week fiscal year that ends on August 31 of each year. Corresponding quarterly periods generally consist of 13-week periods that end on December 1, 2012, March 2, 2013, and June 1, 2013 during fiscal 2013. Under the modified 52/53-week fiscal year, the two quarters ended March 2, 2013 had four more business days than the two quarters ended February 25, 2012. Unless otherwise noted, references to fiscal years apply to the 12 months ended on August 31 of the specified year.

The results of operations for the quarter ended March 2, 2013 are not necessarily indicative of results expected for the entire fiscal year ending August 31, 2013, or for any future periods.

At March 2, 2013, the carrying value of our financial instruments approximated their fair values.

NOTE 2 – INVENTORIES

Inventories are stated at the lower of cost or market, cost being determined using the first-in, first-out method, and were comprised of the following (in thousands):

| | March 2, 2013 | August 31, 2012 |
|----------------|------------------|-----------------------|
| Finished goods | \$ 3,725 | \$ 4,028 |
| Raw materials | 91 | 133 |
| | \$ 3,816 | \$ 4,161 |

NOTE 3 – SHAREHOLDERS' EQUITY

Management Common Stock Loan Program

During fiscal 2000, certain members of our management team purchased shares of our common stock under the Management Stock Loan Program. Subsequent to a modification to the loans in fiscal 2004, the loans have been accounted for as non-recourse stock compensation instruments. Following a modification in fiscal 2006, approximately 94 percent of the remaining shares outstanding under the loan program were placed into an escrow account. Under the terms of the fiscal 2006 modification, the Company had the right to purchase and redeem from loan participants the number of loan program shares necessary to satisfy the participant's obligation if the Company's share price reached the breakeven price.

During the quarter ended March 2, 2013, we determined that the breakeven price for management stock loans with shares held in escrow was achieved. Accordingly, we transferred 3.3 million shares of common stock held by management loan participants in escrow to our transfer agent as full payment on the loans. These shares were valued at the closing market price of our common stock on the date the breakeven price was achieved and were added to our treasury stock with a corresponding increase to additional paid-in capital.

Common Stock Warrants

Our common stock warrants with an exercise price of \$8.00 per share expired on March 8, 2013. Through March 2, 2013, we have issued 2.3 million shares of our common stock, including 1.7 million shares issued in fiscal 2013, and were paid \$0.1 million for net cash exercises. Knowledge Capital Investment Group, a related entity that originally

held a warrant to purchase 5,913,402 shares of our common stock, exercised its warrant at various dates on a net settlement basis according to terms of an exercise agreement, and received a total of 2,197,803 shares of our common stock.

NOTE 4 – SHARE-BASED COMPENSATION

We utilize various share-based compensation plans as integral components of our overall compensation and associate retention strategy. The compensation cost of our share-based compensation plans is included in selling, general, and administrative expenses in the accompanying condensed consolidated income statements and no share-based compensation was

capitalized during the quarter or two quarters ended March 2, 2013. The total cost of our share-based compensation plans was as follows for the periods presented (in thousands):

| | Quarter Ended | | Two Quarters Ended | |
|-------------------------------|---------------|----------|--------------------|----------|
| | March 2, | February | March 2, | February |
| | 2013 | 25, | 2013 | 25, |
| | | 2012 | | 2012 |
| Performance awards | \$ 354 | \$ 949 | \$ 701 | \$ 1,873 |
| Management stock loan shares | 497 | - | 497 | - |
| Unvested share awards | 96 | 85 | 184 | 165 |
| Compensation cost of the ESPP | 24 | 20 | 41 | 39 |
| Fully vested share awards | - | - | 22 | - |
| Stock options | - | - | - | 168 |
| | \$ 971 | \$ 1,054 | \$ 1,445 | \$ 2,245 |

The following is a description of recent developments in our share-based compensation plans.

Performance Awards

During the quarter ended March 2, 2013, the first tranche of the fiscal 2012 executive long-term incentive plan (LTIP) for Productivity Practice sales vested to the participants. The first tranche of this award required the achievement of \$20.5 million in Productivity Practice sales as measured on a trailing four quarters basis. Accordingly, a total of 10,610 shares of our common stock were issued to the participants for this achievement.

As of March 2, 2013, we determined that participants in the fiscal 2010 LTIP award were entitled to receive a total of 18,028 shares of our common stock for cumulative financial performance through the second vesting date. Based on projected fiscal 2013 operating results, we currently expect to award approximately 16,000 additional shares of our common stock on the final vesting date which occurs on August 31, 2013. The cumulative adjustment to share-based compensation expense for the actual and expected shares to vest under the 2010 LTIP award was immaterial to our consolidated financial statements for the quarter and two quarters ended March 2, 2013.

There were no performance awards granted or modified during the quarter ended March 2, 2013. Compensation expense recognized during the quarter and two quarters ended March 2, 2013 for performance awards includes expense related to awards granted in previously reported periods for which the performance targets are probable of being achieved.

Management Stock Loan Shares

During the quarter ended March 2, 2013, we determined that the breakeven price for management stock loans with shares held in escrow was achieved. Accordingly, we transferred 3.3 million shares of common stock held by management loan participants in escrow to our transfer agent as full payment on the loans. Since these loans were accounted for as share-based instruments, we recorded \$0.5 million of share-based compensation expense for the

value of the common stock retained by management stock loan participants that was in excess of the break-even value on the date the loans were repaid.

Unvested Share Awards

Our annual unvested share awards granted to non-employee members of our Board of Directors is administered under the terms of the Franklin Covey Co. Second Amended and Restated 1992 Stock Incentive Plan, and is designed to provide our non-employee directors, who are not eligible to participate in our employee stock purchase plan, an opportunity to obtain an interest in the Company through the acquisition of shares of our common stock. The annual unvested award is generally granted in January (following the annual shareholders' meeting) of each year. During January 2013, the fiscal 2012 award vested and was issued to the participating members of our

Board of Directors. For the fiscal 2013 award, each eligible director received a whole-share grant equal to \$50,000 with a one-year vesting period, which resulted in a total of 30,672 shares granted to members of the Board of Directors under this program. At March 2, 2013, there was \$0.3 million of unrecognized compensation expense associated with the fiscal 2013 Board of Director unvested share award.

Employee Stock Purchase Plan

We have an employee stock purchase plan that offers qualified employees the opportunity to purchase shares of our common stock at a price equal to 85 percent of the average fair market value of our common stock on the last trading day of the calendar month in each fiscal quarter. During the quarter and two quarters ended March 2, 2013, we issued 9,083 shares and 20,814 shares, respectively, to participants in the ESPP.

Stock Options

We have an incentive stock option plan whereby options to purchase shares of our common stock are issued to key employees at an exercise price not less than the fair market value of our common stock on the date of grant. During the quarter ended March 2, 2013 we did not grant any new stock options or modify any existing stock option awards. However, with the successful repayment of the management stock loan program, all previously granted stock options that were outstanding at August 31, 2012 are now vested and exercisable.

NOTE 5 – INCOME TAXES

In order to determine our quarterly provision for income taxes, we use an estimated annual effective tax rate, which is based on expected annual income and statutory tax rates in the various jurisdictions in which we operate. Certain discrete items are separately recognized in the quarter during which they occur and can be a source of variability in the effective tax rates from quarter to quarter.

Our effective tax rate for the quarter ended March 2, 2013 of approximately 40 percent resulted from income being taxed at statutory combined rates, increased by taxable interest on management stock loans, nondeductible share-based compensation relating to management stock loans repaid during the quarter, nondeductible executive compensation, and certain permanent items.

Due to the utilization of foreign tax credit carryforwards and other deferred income tax assets, we expect our cash paid for income taxes will remain significantly less than our income tax provision through fiscal 2015. During the two quarters ended March 2, 2013, we paid \$1.8 million of cash for income taxes compared with an income tax provision of \$2.9 million during the same period.

NOTE 6 – EARNINGS PER SHARE

Basic earnings per common share (EPS) is calculated by dividing net income or loss by the weighted-average number of common shares outstanding for the period. Diluted EPS is calculated by dividing net income or loss by the weighted-average number of common shares outstanding plus the assumed exercise of all dilutive securities using the treasury stock method or the “if converted” method, as appropriate. In conjunction with modifications to our management stock loan program in previous periods, we determined that the shares of management stock loan participants that were placed in the escrow account are participating securities because they continue to have equivalent common stock dividend rights. Accordingly, these management stock loan shares are included in our basic EPS calculation during periods of net income and are excluded from the basic EPS calculation in periods of net

loss. Our unvested share-based compensation awards are not entitled to participate in dividends until they vest and are excluded from our EPS calculation.

The following table presents the computation of our EPS for the periods indicated (in thousands, except per share amounts):

| | Quarter Ended | | Two Quarters Ended | |
|---|---------------|----------|--------------------|----------|
| | March 2, | February | March 2, | February |
| | 2013 | 25, | 2013 | 25, |
| | | 2012 | | 2012 |
| Numerator for basic and diluted earnings per share: | | | | |
| Income before income taxes | \$ 2,669 | \$ 2,159 | \$ 7,362 | \$ 5,233 |
| Provision for income taxes | (1,077) | (997) | (2,873) | (2,409) |
| Net income | \$ 1,592 | \$ 1,162 | \$ 4,489 | \$ 2,824 |
| Denominator for basic and diluted earnings per share: | | | | |
| Basic weighted average shares outstanding(1) | | | | |
| | 18,550 | 17,764 | 18,356 | 17,748 |
| Effect of dilutive securities: | | | | |
| Stock options and other share-based awards | | | | |
| | 117 | 27 | 74 | 29 |
| Common stock warrants | | | | |
| | 1,042 | 496 | 1,063 | 365 |
| Diluted weighted average shares outstanding | | | | |
| | 19,709 | 18,287 | 19,493 | 18,142 |
| EPS Calculations: | | | | |
| Net income per share: | | | | |
| Basic | \$ 0.09 | \$ 0.07 | \$ 0.24 | \$ 0.16 |

| | | | | |
|---------|------|------|------|------|
| Diluted | 0.08 | 0.06 | 0.23 | 0.16 |
|---------|------|------|------|------|

(1) Since we recognized net income for the quarter and two quarters ended March 2, 2013 and February 25, 2012, basic weighted average shares for those periods include 3.3 million shares of common stock held by management stock loan participants that were placed in escrow. Since the management stock loans were repaid near the end of the quarter ended March 2, 2013, common shares formerly held in escrow will not be outstanding in future periods.

At March 2, 2013 and February 25, 2012, we had approximately 0.2 million and 0.7 million stock options outstanding, which were not included in the computation of diluted EPS because the options' exercise prices were greater than the average market price of our common shares for the respective periods. Although these shares were not included in our calculation of diluted EPS, these stock options, and other dilutive securities, including performance share-based compensation instruments, may have a dilutive effect on our EPS calculation in future periods if the price of our common stock increases. At March 2, 2013, our common stock warrants were substantially exercised (Note 3). Accordingly, future dilution from these instruments will be insignificant.

NOTE 7 – SEGMENT INFORMATION

Our sales are primarily comprised of training and consulting sales and related products. Based on the consistent nature of our services and products and the types of customers for these services, we function as a single operating segment. However, to improve comparability with previous periods, operating information for our U.S./Canada, international, and corporate services operations is presented below. Our U.S./Canada operations are responsible for the sale and delivery of our training and consulting services in the United States and Canada. Our international sales group includes the financial results of our directly owned foreign offices and royalty revenues from licensees. Our corporate services information includes leasing income and certain corporate operating expenses.

The Company's chief operating decision maker is the CEO, and the primary measurement tool used in business unit performance analysis is Adjusted EBITDA, which may not be calculated as similarly titled amounts calculated by other companies. For segment reporting purposes, our consolidated Adjusted EBITDA can be calculated as our income or loss from operations excluding share-based compensation, depreciation expense, amortization expense, and certain other charges.

In the normal course of business, we may make structural and cost allocation revisions to our segment information to reflect new reporting responsibilities within the organization. There were no significant organizational or structural changes during the quarter and two quarters ended March 2, 2013. We account for our segment information on the same basis as the accompanying condensed consolidated financial statements.

ENTERPRISE INFORMATION

(in thousands)

| Quarter Ended | Sales to External Customers | Gross Profit | Adjusted EBITDA | Depreciation | Amortization |
|-------------------------------|-----------------------------------|-----------------|--------------------|--------------|--------------|
| March 2, 2013 | | | | | |
| U.S./Canada | \$ 29,262 | \$ 18,580 | \$ 2,158 | \$ 299 | \$ 616 |
| International | 10,106 | 8,103 | 4,437 | 84 | 3 |
| Total | 39,368 | 26,683 | 6,595 | 383 | 619 |
| Corporate and eliminations | 1,062 | 601 | (1,031) | 339 | - |
| Consolidated | \$ 40,430 | \$ 27,284 | \$ 5,564 | \$ 722 | \$ 619 |

Quarter Ended
February 25,
2012

| | | | | | |
|-------------------------------|-----------|-----------|----------|--------|--------|
| U.S./Canada | \$ 27,320 | \$ 16,664 | \$ 2,482 | \$ 450 | \$ 622 |
| International | 10,589 | 8,025 | 3,941 | 101 | 4 |
| Total | 37,909 | 24,689 | 6,423 | 551 | 626 |
| Corporate and eliminations | 718 | 292 | (1,102) | 309 | - |
| Consolidated | \$ 38,627 | \$ 24,981 | \$ 5,321 | \$ 860 | \$ 626 |

Two Quarters
Ended
March 2, 2013

| | | | | | |
|-------------------------------|-----------|-----------|-----------|----------|----------|
| U.S./Canada | \$ 59,605 | \$ 37,410 | \$ 4,484 | \$ 566 | \$ 1,235 |
| International | 22,769 | 18,265 | 10,354 | 165 | 6 |
| Total | 82,374 | 55,675 | 14,838 | 731 | 1,241 |
| Corporate and eliminations | 2,117 | 1,168 | (2,184) | 692 | - |
| Consolidated | \$ 84,491 | \$ 56,843 | \$ 12,654 | \$ 1,423 | \$ 1,241 |

Two Quarters
 Ended
 February 25,
 2012

| | | | | | |
|-------------------------------|-----------|-----------|-----------|----------|----------|
| U.S./Canada | \$ 54,767 | \$ 33,808 | \$ 4,916 | \$ 869 | \$ 1,248 |
| International | 21,987 | 17,131 | 9,061 | 191 | 8 |
| Total | 76,754 | 50,939 | 13,977 | 1,060 | 1,256 |
| Corporate and eliminations | 1,413 | 584 | (2,296) | 634 | - |
| Consolidated | \$ 78,167 | \$ 51,523 | \$ 11,681 | \$ 1,694 | \$ 1,256 |

A reconciliation of our consolidated Adjusted EBITDA to consolidated income from continuing operations before taxes is provided below (in thousands):

| | Quarter Ended | | Two Quarters Ended | |
|------------------|---------------|----------|--------------------|-----------|
| | March 2, | February | March 2, | February |
| | 2013 | 25, | 2013 | 25, |
| | | 2012 | | 2012 |
| Enterprise | | | | |
| Adjusted EBITDA | \$ 6,595 | \$ 6,423 | \$ 14,838 | \$ 13,977 |
| Corporate | | | | |
| expenses | (1,031) | (1,102) | (2,184) | (2,296) |
| Consolidated | | | | |
| Adjusted EBITDA | 5,564 | 5,321 | 12,654 | 11,681 |
| Share-based | | | | |
| compensation | (971) | (1,054) | (1,445) | (2,245) |
| Depreciation | (722) | (860) | (1,423) | (1,694) |
| Amortization | (619) | (626) | (1,241) | (1,256) |
| Consolidated | | | | |
| income from | | | | |
| operations | 3,252 | 2,781 | 8,545 | 6,486 |
| Interest income | 150 | 4 | 288 | 7 |
| Interest expense | (598) | (626) | (1,188) | (1,260) |
| Discount on | | | | |
| related party | | | | |
| receivable | (135) | - | (283) | - |
| Income before | | | | |
| taxes | \$ 2,669 | \$ 2,159 | \$ 7,362 | \$ 5,233 |

NOTE 8 – INVESTMENT IN FC ORGANIZATIONAL PRODUCTS

We own a 19.5 percent interest in FC Organizational Products (FCOP), an entity that purchased substantially all of our consumer solution business unit assets in fiscal 2008 for the purpose of expanding the sales of planners and related organizational products under a comprehensive licensing agreement. During fiscal 2012, we reconsidered whether FCOP was a variable interest entity as defined under ASC 810, and determined that FCOP was a variable interest entity. We further determined that we are not the primary beneficiary of FCOP because we do not have the ability to direct the activities that most significantly impact FCOP's economic performance, which primarily consist of the day-to-day sale of planning products and related accessories, and we do not have an obligation to absorb losses or the right to receive benefits from FCOP that could potentially be significant. Our voting rights and management board representation approximate our ownership interest and we are unable to exercise control through voting interests or through other means.

We are required to account for our investment in FCOP using the equity method of accounting and we have historically recorded our share of FCOP's profit and loss based upon specified allocations as defined in the associated operating agreement. However, we have not recorded our share of FCOP's losses in the accompanying condensed consolidated income statements because we have impaired and written off investment balances, as defined within the applicable accounting guidance, in previous periods in excess of our share of FCOP's losses through March 2, 2013.

Our primary exposure related to FCOP is from amounts owed to us by FCOP. We receive reimbursement from FCOP for certain operating costs, such as warehousing and distribution costs, which are billed to us by third party providers, and for working capital or other advances that we may make to FCOP. We are not contractually required to make advances to FCOP, but we believe that this additional financing will improve our ability to collect amounts owed to us, including amounts previously impaired and written off. The operations of FCOP are primarily financed by the sale of planning products and accessories in the normal course of business.

At March 2, 2013 and August 31, 2012, we had \$4.6 million and \$7.1 million receivable from FCOP, respectively, which have been classified in current assets and long-term assets in our condensed consolidated balance sheets based on expected payment dates. The long-term receivable has been discounted using a rate of 15 percent.

NOTE 9 – SUBSEQUENT EVENTS

Acquisition of NinetyFive 5 LLC

Subsequent to March 2, 2013, we entered into an asset purchase agreement with NinetyFive 5 LLC (NinetyFive 5) to acquire substantially all of the assets of NinetyFive 5. NinetyFive 5 provides sales success training services and will become a component of our Sale Performance Practice. The closing of the purchase occurred on March 11, 2013. The consideration for the assets purchased consists of \$4.2 million paid in cash, the assumption of certain liabilities, and potential earnout payments up to a maximum of \$8.5 million based on cumulative EBITDA as set forth in the purchase agreement.

Line of Credit Renewal

On March 25, 2013, we entered into the Third Modification Agreement (the Third Modification Agreement) to our previously existing amended and restated secured credit agreement (the Restated Credit Agreement) with our existing lender. The primary purposes of the Third Modification Agreement are to extend the maturity date of the Restated Credit Agreement from March 31, 2015 to March 31, 2016 and to increase the caps for permitted business acquisitions. The Third Modification Agreement continues to provide a revolving line of credit facility with a maximum borrowing amount of \$10.0 million with interest at LIBOR plus 2.50 percent per year. The revolving credit facility may be used for general business purposes.

The other terms, conditions, and financial covenants in the Third Modification Agreement are substantially the same as those defined in the Restated Credit Agreement as amended and modified. In the event of noncompliance with the financial covenants and other defined events of default, the lender is entitled to certain remedies, including acceleration of the repayment of amounts outstanding on the line of credit facility.

We believe that the Restated Credit Agreement will be a key component of our operations that will allow us to maintain adequate liquidity for at least the next twelve months.

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

Management's discussion and analysis contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based upon management's current expectations and are subject to various uncertainties and changes in circumstances. Important factors that could cause actual results to differ materially from those described in forward-looking statements are set forth below under the heading "Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995."

We suggest that the following discussion and analysis be read in conjunction with the Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended August 31, 2012.

RESULTS OF OPERATIONS

Overview

Our second fiscal quarter includes the months of December, January, and February. Primarily due to the holidays observed throughout the world during these months, we may conduct fewer training programs and engage in reduced consulting arrangements in our second quarter when compared to other quarters in our fiscal year.

The second quarter of fiscal 2013, which ended on March 2, 2013 was the strongest second fiscal quarter ever under our current business model, and continued the growth and favorable momentum that we experienced during fiscal 2012 and the first quarter of fiscal 2013 as sales increased in most of our major delivery channels compared with the prior year. Our consolidated sales increased by 5 percent to \$40.4 million in the second quarter of fiscal 2013 compared with \$38.6 million in the corresponding quarter of fiscal 2012. As a result of increased sales and increased gross profit, our income from operations for the quarter improved 17 percent to \$3.3 million compared with \$2.8 million in the prior year and our income before income taxes increased 24 percent to \$2.7 million compared with \$2.2 million in the second quarter of fiscal 2012. Improved operating results flowed through to net income, which increased 37 percent to \$1.6 million, or \$.08 per diluted share, compared with \$1.2 million, or \$.06 per diluted share, in the second quarter of the prior year.

The primary factors that influenced our operating results for the quarter ended March 2, 2013 were as follows:

- Sales – Our consolidated sales increased to \$40.4 million compared with \$38.6 million in the second quarter of fiscal 2012. Sales increased at all of our U.S./Canada direct offices, at many of our international licensees, from our national account practices, and from increased leasing revenues on our corporate campus. Partially offsetting growth in these areas were decreased sales from our Sales Performance Practice, primarily due to activity on maturing contracts; our Government Services office, primarily resulting from the effects of sequestration in the United States; and at our direct office in Japan, which was adversely impacted by foreign exchange rates.
- Gross Profit – Our gross profit increased 9 percent to \$27.3 million compared with \$25.0 million in the corresponding period of the prior year due to increased sales and improved gross margin. Our consolidated gross margin, which is gross profit as a percentage of sales, improved to 67.5 percent compared with 64.7 percent in the second quarter of fiscal 2012.

- Operating Expenses – Our operating expenses increased by \$1.8 million compared with the second quarter of the prior year, which was primarily due to a \$2.0 million increase in selling, general, and administrative expenses. Increased selling, general, and administrative expense was partially offset by decreased depreciation and amortization expenses.

Further details regarding these factors and their impact on our operating results and liquidity are provided throughout the following management’s discussion and analysis.

The following table sets forth consolidated sales data by category and by our primary delivery channels for the periods indicated (in thousands):

| | Quarter Ended | | | Two Quarters Ended | | |
|----------------------------------|------------------|-------------------------|-------------------|--------------------|-------------------------|-------------------|
| | March 2, 2013 | February 25, 2012 | Percent Change | March 2, 2013 | February 25, 2012 | Percent Change |
| Sales by Category: | | | | | | |
| Training and consulting services | \$ 37,744 | \$ 35,606 | 6 | \$ 78,807 | \$ 71,988 | 9 |
| Products | 1,624 | 2,303 | (29) | 3,567 | 4,766 | (25) |
| Leasing | 1,062 | 718 | 48 | 2,117 | 1,413 | 50 |
| | \$ 40,430 | \$ 38,627 | 5 | \$ 84,491 | \$ 78,167 | 8 |
| Sales by Channel: | | | | | | |
| U.S./Canada direct | \$ 20,952 | \$ 19,107 | 10 | \$ 42,711 | \$ 37,505 | 14 |
| International direct | 6,767 | 7,507 | (10) | 15,198 | 15,081 | 1 |
| International licensees | 3,588 | 3,291 | 9 | 7,918 | 7,212 | 10 |
| National account practices | 6,108 | 5,801 | 5 | 12,280 | 11,280 | 9 |
| Self-funded marketing | 1,395 | 1,812 | (23) | 2,888 | 4,739 | (39) |
| Other | 1,620 | 1,109 | 46 | 3,496 | 2,350 | 49 |
| | \$ 40,430 | \$ 38,627 | 5 | \$ 84,491 | \$ 78,167 | 8 |

Quarter Ended March 2, 2013 Compared with the Quarter Ended February 25, 2012

Sales

We offer a variety of training courses, consulting services, and training related products that are focused on solving organizational problems that require a change in human behavior. Our training and consulting solutions are provided both domestically and internationally through our sales force, facilitators, international licensees, and through the

internet on various web-based delivery platforms. The following sales analysis for the quarter ended March 2, 2013 is based on activity through our primary delivery channels as shown above:

U.S./Canada Direct – This channel includes our four regional sales offices that serve our clients in the United States and Canada and our government services group. During the quarter ended March 2, 2013, sales increased at our regional sales offices, which resulted in a \$2.6 million improvement over the prior year. Sales increases through our regional offices were generally broad based across our practices and were favorably impacted by increased facilitator sales during the quarter when compared with the prior year. Increased sales at our regional offices were partially offset by a \$0.8 million decrease in sales through our government services office as some programs were postponed or canceled due to changes in U.S. federal government spending required by sequestration. The impact of U.S. federal spending reductions may continue to have an adverse impact on our government services office during the remainder of fiscal 2013 and in future periods. However, we believe that our pipeline of awarded revenue through our regional sales offices continues to remain strong and our outlook for the remainder of fiscal 2013 is encouraging for continued overall growth over the prior year in this channel.

International Direct – Our directly owned international offices are located in Australia, Japan, and the United Kingdom. The decrease in sales through our international direct offices was primarily due to a \$0.8 million decrease in sales from our office in Japan, of which \$0.7

million was due to the translation of Japanese Yen to U.S. dollars. In functional currency, sales at our Japan office only declined by one percent compared to the second quarter of fiscal 2012. We currently anticipate that the translation of Japanese Yen to the U.S. dollar will continue to have an adverse impact on our reported sales from Japan during the remainder of fiscal 2013. Partially offsetting decreased sales from Japan were increased sales from our office in the United Kingdom.

International Licensees – In countries or foreign locations where we do not have a directly owned office, our training and consulting services are delivered through independent licensees, which may translate and adapt our curriculum to local preferences and customs, if necessary. During the quarter ended March 2, 2013, many of our foreign licensees had increased training sales compared with the prior year, which resulted in a 9 percent increase in licensee royalty revenues compared with fiscal 2012. We believe that our increased efforts to support our licensees through additional program training, international branding, and the introduction of new products has had a favorable impact on their sales growth and we expect future growth from our international licensee partners during fiscal 2013.

National Account Practices – Our national account practices are comprised of programs that are not typically offered in our regional sales offices and include Helping Clients Succeed from the Sales Performance Practice, The Leader In Me curriculum designed for students from our Education Practice, and Winning Customer Loyalty from our Customer Loyalty Practice. The increase in national account practice sales was due to increased sales from our Education Practice, which increased by \$1.2 million compared with the prior year. We continue to see increased demand for The Leader in Me program in many school districts in the United States as well as in some international locations. Increased Education Practice sales were partially offset by decreased Sales Performance Practice sales and essentially flat Customer Loyalty Practice sales.

Subsequent to March 2, 2013 we completed the acquisition of NinetyFive 5 LLC (NinetyFive 5), an entity that provides sales success training services that are highly complementary to our existing Sales Performance Practice offerings. We believe the acquisition of NinetyFive 5 will significantly strengthen our Sales Performance Practice offerings and lead to increased sales in future periods.

Self-Funded Marketing – This group includes our public programs, book and audio sales, and speeches. The decrease in self-funded marketing sales was primarily due to the timing of book and audio distribution royalties received in the second quarter of fiscal 2012 which did not repeat in the current year. We expect to continue to release new publications in future periods and believe that these new publications will continue to show strong performance in the marketplace.

Other – Our other sales are comprised primarily of leasing and shipping and handling revenues. The increase in other sales was primarily due to increased leasing revenues resulting from new lease contracts at our corporate headquarters. We continue to have vacant space available for lease at our corporate headquarters campus and we are actively seeking new tenants for this available property to increase sales in future periods.

Gross Profit

Gross profit consists of net sales less the cost of services provided or the cost of products sold. For the quarter ended March 2, 2013, our consolidated gross profit increased to \$27.3 million compared with \$25.0 million in the second quarter of fiscal 2012. The increase in gross profit was attributable to increased sales, as described above, and improved gross margin. Our gross margin for the quarter ended March 2, 2013 increased to 67.5 percent compared with 64.7 percent in the prior year. Our improved gross margin was primarily due to increased facilitator sales in the U.S./Canada direct offices during the quarter and increased international licensee royalty revenues. Facilitator sales and licensee royalty revenues have higher gross margins than the majority of our other services or revenue categories.

Operating Expenses

Selling, General and Administrative – Our selling, general, and administrative (SG&A) expenses increased \$2.0 million compared with the second quarter of fiscal 2012. The increase in SG&A expenses over the prior year was primarily due to 1) a \$0.8 million increase in advertising and promotional costs that were primarily related to strategic initiatives which we believe had a favorable impact on the current quarter's sales; 2) a \$0.5 million increase in travel expenses related primarily to marketing and promotional activities, and increased training sales delivery during the quarter; 3) a \$0.4 million increase in associate costs primarily related to the addition of new sales-related personnel and increased commissions on higher sales; and 4) a \$0.4 million increase in legal expenses resulting primarily from a fiscal 2012 reimbursement of previously expensed legal costs for litigation that was settled in the prior year. These increases were partially offset by decreased expenses in various other areas of our operations.

Depreciation – Depreciation expense decreased by \$0.1 million compared to the second quarter of fiscal 2012 primarily due to certain assets becoming fully depreciated. Based on acquisitions that occurred during the quarter and two quarters ended March 2, 2013 and expected capital asset activity during the remainder of fiscal 2013, we expect depreciation expense to total approximately \$2.8 million for fiscal 2013.

Interest Income

The increase in interest income was primarily attributable to the accretion of interest on previously discounted long-term receivables from FC Organizational Products (FCOP). Interest income is computed using the effective interest method using a rate of 15 percent, which was the discount rate at which these receivables were marked to estimated net present value (refer to the discussion below).

Discount on Related Party Receivable

We record receivables from FCOP for reimbursement of certain operating costs, such as warehousing and distribution costs, which are billed to us by third party providers, and for working capital and other advances that we make, even though we are not contractually required to make advances or absorb the losses of FCOP. Based on expected payment, some of these receivables are recorded as long-term receivables and are required to be recorded at net present value. We discounted the long-term portion of the FCOP receivable based on forecasted repayments at a discount rate of 15 percent, which was the estimated risk-adjusted borrowing rate of FCOP. The impact of this discount on long-term receivables added in the quarter ended March 2, 2013 was \$0.1 million.

Income Taxes

Our effective tax rate for the quarter ended March 2, 2013 was 40 percent compared with 46 percent for the second quarter of fiscal 2012. Our effective tax rate decreased primarily due to increased pre-tax income (which reduces the unfavorable impact on the effective rate of certain permanent items), reduced tax on income subject to both U.S. and foreign taxation, and reduced taxable income on outstanding management stock loans.

We anticipate that our cash paid for income taxes will remain less than our income tax provision during the foreseeable future as we utilize foreign tax credit carryforwards and other deferred income tax assets. For instance, during the quarter ended March 2, 2013, we paid \$0.5 million of cash for income taxes compared with an income tax provision of \$1.1 million. After utilization of our foreign tax credit carryforwards, which we currently expect to be fully utilized by fiscal 2016, we anticipate that our cash paid for income taxes will increase and approximate our income tax provision.

Two Quarters Ended March 2, 2013 Compared with the Two Quarters Ended February 25, 2012

Sales

Our consolidated sales for the first two quarters of fiscal 2013 increased \$6.3 million, or 8 percent, compared with the corresponding period of the prior year. The following sales analysis for the two quarters ended March 2, 2013 is based on activity through our primary delivery channels as defined in the discussion of the quarter ended March 2, 2013 compared with the quarter ended February 25, 2012, which precedes this section of the report.

U.S./Canada Direct – For the two quarters ended March 2, 2013, sales increased at our regional sales offices, which resulted in a \$5.6 million improvement in these offices over the prior year. Increased sales through our regional sales offices were generally broad based across our practices and were favorably impacted by increased facilitator sales during the first two quarters when compared with the prior year. Increased sales at our regional offices were partially offset by a \$0.4 million decrease in sales through our government services office as some programs were postponed or canceled during our second fiscal quarter due to changes in U.S. federal government spending required by sequestration. The impact of U.S. federal spending reductions may continue to have an adverse impact on our government services office during the remainder of fiscal 2013 and in future periods.

International Direct – The slight increase in sales through our international direct offices was primarily driven by increased sales from our offices in Australia and the United Kingdom. Increased sales in these offices were partially offset by decreased reported sales from our Japan office, caused primarily by the translation of Japanese Yen to the U.S. dollar that occurred primarily in our second fiscal quarter of 2013. During the two quarters ended March 2, 2013 sales at our Japan office denominated in Yen have increased by 8 percent compared with the first two quarters of fiscal 2012.

International Licensees – During the two quarters ended March 2, 2013, most of our foreign licensees had increased training sales compared with the prior year, which resulted in increased licensee royalty revenues compared with the prior year. We continue to be encouraged by the growth of our international licensee partners and expect royalty revenues to increase compared with the prior year throughout the remainder of fiscal 2013.

National Account Practices – The increase in national account practice sales was due to increased sales from our Education Practice, which increased by \$2.6 million compared with the prior year. Increased Education Practice sales were partially offset by decreased Sales Performance Practice sales and decreased Customer Loyalty Practice sales.

Self-Funded Marketing – The decrease in self-funded marketing sales was primarily due to book and audio distribution royalties received primarily in the first quarter of fiscal 2012 which did not repeat in the current fiscal year.

Other – The increase in other sales was primarily due to increased leasing revenues resulting from new lease contracts at our corporate headquarters. We continue to have vacant space available for lease at our corporate headquarters campus and we are actively seeking new tenants for this available property to increase sales in future periods.

Gross Profit

For the two quarters ended March 2, 2013, our consolidated gross profit increased to \$56.8 million compared with \$51.5 million in the first two quarters of fiscal 2012. The increase in gross profit was attributable to increased sales, as described above, and an improved gross margin in our second fiscal quarter. Our gross margin for the two quarters ended March 2, 2013 increased to 67.3

percent compared with 65.9 percent in the prior year. Our improved gross margin percentage was primarily due to increased facilitator sales in the U.S./Canada direct offices and increased international licensee royalty revenues in the first two quarters of fiscal 2013. Facilitator sales and licensee royalty revenues have higher gross margins than the majority of our other services or revenue categories.

Operating Expenses

Selling, General and Administrative – Our SG&A expenses increased \$3.5 million compared with the first two quarters of the prior year. As a percent of sales, SG&A expenses increased slightly to 54.0 percent of sales compared with 53.8 percent of sales in the first two quarters of the prior year. The increase in SG&A expenses was primarily due to 1) a \$2.7 million increase in associate costs primarily related to the addition of new sales-related personnel and increased commissions on higher sales; 2) a \$0.9 million increase in advertising and promotional costs that were primarily related to strategic initiatives that we believe had a favorable impact on the current fiscal year's sales; and 3) a \$0.9 million increase in travel expenses related primarily to marketing and promotional activities, and increased training sales delivery during the fiscal year. These increases were partially offset by a \$0.8 million decrease in non-cash share-based compensation, due primarily to the full amortization of awards granted in prior periods, and decreases in various other expense categories.

Depreciation – Depreciation expense for the two quarters ended March 2, 2013 decreased by \$0.2 million compared with the same period of fiscal 2012 primarily due to certain assets becoming fully depreciated.

Interest Income

The increase in interest income was primarily attributable to the accretion of interest on previously discounted long-term receivables from FCOP. Interest income is computed using the effective interest method using a rate of 15 percent, which was the discount rate at which these receivables were marked to estimated net present value as previously discussed.

Discount on Related Party Receivable

Based on expected payment, we discount long-term receivables from FCOP to their net present value. We discounted the long-term portion of the FCOP receivable at a discount rate of 15 percent, which was the estimated risk-adjusted borrowing rate of FCOP. The impact of this discount on long-term FCOP receivables added during the two quarters ended March 2, 2013 was \$0.3 million. For more information on discounting FCOP long-term receivables, refer to the comparison of the quarter ended March 2, 2013 with the quarter ended February 25, 2012, which precedes this section of the report.

Income Taxes

Our effective tax rate for the two quarters ended March 2, 2013 was 39 percent compared with 46 percent in the first two quarters of fiscal 2012. Our effective rate decreased primarily due to increased pre-tax income (which reduces the unfavorable impact on the effective rate of certain permanent items), reduced tax on income subject to both U.S. and foreign taxation, reduced taxable income on outstanding management stock loans, and the recognition of tax benefits following the completion of a routine Internal Revenue Service audit.

We anticipate that our cash paid for income taxes will remain less than our income tax provision during the foreseeable future as we utilize foreign tax credit carryforwards and other deferred income tax assets. For instance, during the two quarters ended March 2, 2013, we paid \$1.8 million of cash for income taxes compared with an income tax provision of \$2.9 million.

LIQUIDITY AND CAPITAL RESOURCES

At March 2, 2013 our liquidity position continued to remain strong as we had \$15.5 million of cash and cash equivalents, with no borrowings on our line of credit, compared with \$11.0 million at August 31, 2012. Our net working capital (current assets less current liabilities) increased to \$32.5 million at March 2, 2013 compared with \$27.5 million at August 31, 2012. Of our \$15.5 million in cash and cash equivalents at March 2, 2013, \$4.6 million was held at our foreign subsidiaries. We routinely repatriate cash from our foreign subsidiaries and consider foreign cash a key component of our overall liquidity position. Our primary sources of liquidity are cash flows from the sale of services in the normal course of business and proceeds from our available \$10.0 million revolving line of credit when needed. Our primary uses of liquidity include payments for operating activities, capital expenditures, working capital expansion, business acquisitions, and debt repayment.

Subsequent to March 2, 2013, we entered into the Third Modification Agreement (the Third Modification Agreement) to our previously existing amended and restated secured credit agreement (the Restated Credit Agreement) with our existing lender. The primary purposes of the Third Modification Agreement are to extend the maturity date of the Restated Credit Agreement from March 31, 2015 to March 31, 2016 and to increase the caps for permitted business acquisitions. The Third Modification Agreement continues to provide a revolving line of credit facility with a maximum borrowing amount of \$10.0 million with interest at LIBOR plus 2.50 percent.

We may use our line of credit facility for general corporate purposes as well as for other transactions, unless prohibited by the terms of the line of credit agreement. The Restated Credit Agreement and subsequent modifications also contain customary representations and guarantees as well as provisions for repayment and liens. In addition to customary non-financial terms and conditions, our line of credit requires us to be in compliance with specified financial covenants, including (i) a funded debt to EBITDAR ratio requirement of less than 3.00 to 1.00; (ii) a fixed charge coverage ratio requirement in excess of 1.5 to 1.0; and (iii) an \$8.0 million limitation on capital expenditures, excluding capitalized curriculum development. We believe that we were in compliance with the terms and covenants of the line of credit agreement for the quarter ended March 2, 2013.

In addition to our \$10.0 million revolving line of credit facility, we have \$1.3 million remaining on a term note payable, and we have a long-term lease on our corporate campus that is accounted for as a long-term financing obligation.

The following discussion is a description of the primary factors affecting our cash flows and their effects upon our liquidity and capital resources during the two quarters ended March 2, 2013.

Cash Flows From Operating Activities

Our primary source of cash from operating activities was the sale of goods and services to our customers in the normal course of business. The primary uses of cash for operating activities were payments for selling, general, and administrative expenses, payments for direct costs necessary to conduct training programs, payments to suppliers for materials used in products sold, and to fund working capital needs. Our cash provided by operating activities totaled \$10.2 million for the two quarters ended March 2, 2013 compared with \$9.2 million for the same period of the prior year. The increase in cash flows from operating activities was primarily attributable to increased net income, collections of accounts receivable, and increased cash received from FC Organizational Products. These increases were partially offset by increased payments to reduce seasonally high accrued liabilities (primarily accrued bonuses and commissions) and accounts payable. We believe that our continued efforts to improve working capital balances and increase income from operations will improve our cash flows from operating activities during future periods. However, the success of these efforts, and their eventual contribution to our cash flows, is dependent upon numerous factors, many of which are not within our control.

Cash Flows From Investing Activities and Capital Expenditures

Our cash used for investing activities during the two quarters ended March 2, 2013 totaled \$2.5 million. Our primary uses of cash for investing activities were the purchase of property and equipment in the normal course of business and additional spending on curriculum development. Our purchases of property and equipment, which totaled \$1.4 million, consisted primarily of computer hardware, leasehold improvements, and computer software. We spent \$1.1 million during the first half of fiscal 2013 that was eligible to be capitalized for the development of various new curriculums and offerings.

Subsequent to March 2, 2013 we completed the acquisition of NinetyFive 5, an entity that provides sales success training services. The consideration for the acquisition consists of an initial \$4.2 million, and additional potential earnout payments up to a maximum of \$8.5 million based on cumulative EBITDA as set forth in the purchase agreement. We also paid \$2.2 million to the former owners of CoveyLink Worldwide, LLC (CoveyLink) for the fourth of five contingent earnout payments. The acquisition of NinetyFive 5 and the payment of the contingent earnout to the former owners of CoveyLink will increase our use of cash for investing activities in future periods.

Cash Flows From Financing Activities

For the two quarters ended March 2, 2013 we used \$2.9 million of net cash for financing activities. Our uses of cash for financing activities consisted primarily of \$2.0 million used for principal payments on our term loan and long-term financing obligation, and \$1.2 million used to repurchase shares of common stock (including shares withheld for statutory taxes on share-based compensation awards) that occurred primarily during our first quarter of fiscal 2013. Partially offsetting these uses of cash was \$0.2 million of cash received from participants in our employee stock purchase plan.

During fiscal 2012 we announced the approval of a plan to repurchase up to \$10.0 million of our common stock. We intend to use cash in excess of \$10.0 million, provided we have no balance outstanding on our line of credit, for the purchases. Through March 2, 2013, we have purchased a total of 73,320 shares of our common stock for \$0.8 million. We anticipate that the purchases of our common stock under this approved plan will increase the use of cash for financing activities in future periods provided that we maintain adequate liquidity to allow for the purchases.

Sources of Liquidity

We expect to meet our projected capital expenditures, service our existing financing obligation and term loan payable, and meet other working capital requirements during fiscal 2013 through current cash balances and future cash flows from operating activities. Going forward, we will continue to incur costs necessary for the day-to-day operation and potential growth of the business and may use our available line of credit and other financing alternatives, if necessary, for these expenditures. Subsequent to March 2, 2013 we extended the maturity date on our line of credit to March 2016 and we expect to renew the line of credit on an annual basis in future periods to maintain the three-year availability of this credit facility. Additional potential sources of liquidity available to us include factoring receivables, issuance of additional equity, or issuance of debt from public or private sources. If necessary, we will evaluate all of these options and select one or more of them depending on overall capital needs and the associated cost of capital.

Considering the foregoing, we anticipate that our existing capital resources should be adequate to enable us to maintain our operations for at least the upcoming twelve months. However, our ability to maintain adequate capital for our operations in the future is dependent upon a number of factors, including sales trends, macroeconomic activity, our ability to contain costs, levels of capital expenditures, collection of accounts receivable, and other factors. Some of the factors that influence our operations are not within our control, such as general economic conditions and the

introduction of new curriculums and technology by our competitors. We will continue to monitor

our liquidity position and may pursue additional financing alternatives, as described above, to maintain sufficient resources for future growth and capital requirements. However, there can be no assurance such financing alternatives will be available to us on acceptable terms, or at all.

Contractual Obligations

The Company has not structured any special purpose entities, or participated in any commodity trading activities, which would expose us to potential undisclosed liabilities or create adverse consequences to our liquidity. Required contractual payments primarily consist of 1) lease payments resulting from the sale of our corporate campus (financing obligation); 2) payments to HP Enterprise Services for outsourcing services related to information systems, warehousing, and distribution services; 3) minimum rent payments for office and warehouse space; 4) the repayment of our note payable obligation; and 5) short-term purchase obligations for inventory items and other products and services used in the ordinary course of business. There have been no significant changes to our expected required contractual obligations from those disclosed at August 31, 2012.

FC Organizational Products is contractually obligated to pay us for rented warehouse and office space, a portion of the fixed costs for warehousing and distribution facilities, and is primarily liable for leasing costs at its retail stores. As of March 2, 2013 we remain secondarily liable for only \$0.1 million of retail store leasing costs. In the event that FCOP is unable to pay these items, our liquidity, cash flows, and operating results may be adversely affected.

USE OF ESTIMATES AND CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America. The significant accounting policies used to prepare our consolidated financial statements are outlined primarily in Note 1 of the consolidated financial statements presented in Part II, Item 8 of our annual report on Form 10-K for the fiscal year ended August 31, 2012. Some of those accounting policies require us to make estimates and assumptions that affect the amounts reported in our consolidated financial statements. We regularly evaluate our estimates and assumptions and base those estimates and assumptions on historical experience, factors that are believed to be reasonable under the circumstances, and requirements under accounting principles generally accepted in the United States of America. Actual results may differ from these estimates under different assumptions or conditions, including changes in economic conditions and other circumstances that are not within our control, but which may have an impact on these estimates and our actual financial results.

The following items require significant judgment and often involve complex estimates:

Revenue Recognition

We derive revenues primarily from the following sources:

- Training and Consulting Services – We provide training and consulting services to both organizations and individuals.
- Products – We sell books, audio media, training accessories, and other related products.

We recognize revenue when: 1) persuasive evidence of an agreement exists, 2) delivery of product has occurred or services have been rendered, 3) the price to the customer is fixed or determinable, and 4) collectability is reasonably assured. For training and service sales, these conditions are generally met upon presentation of the training seminar or delivery of the consulting services. For product sales, these conditions are generally met upon shipment of the

product to the customer.

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Some of our training and consulting contracts contain multiple element deliverables that include training along with other products and services. For transactions that contain more than one element, we recognize revenue in accordance with the guidance for multiple element arrangements using the relative selling price method.

Our international strategy includes the use of licensees in countries where we do not have a wholly-owned operation. Licensee companies are unrelated entities that have been granted a license to translate our content and curriculum, adapt the content and curriculum to the local culture, and sell our training seminars and products in a specific country or region. Licensees are required to pay us royalties based upon a percentage of their sales to clients. We recognize royalty income each period based upon the sales information reported to us from our licensees. International royalty revenue is reported as a component of training and consulting service sales in our consolidated income statements.

Revenue is recognized as the net amount to be received after deducting estimated amounts for discounts and product returns.

Share-Based Compensation

Our shareholders have approved a performance based long-term incentive plan (LTIP) that provides for grants of share-based performance awards to certain managerial personnel and executive management as directed by the Organization and Compensation Committee of the Board of Directors. The number of common shares that are vested and issued to LTIP participants is variable and is based entirely upon the achievement of specified financial performance objectives during a defined performance period. Due to the variable number of common shares that may be issued under the LTIP, we reevaluate our LTIP grants on a quarterly basis and adjust the number of shares expected to be awarded based upon actual and estimated financial results of the Company compared to the performance goals set for the award. Adjustments to the number of shares awarded, and to the corresponding compensation expense, are made on a cumulative basis at the adjustment date based upon the estimated probable number of common shares to be awarded.

The analysis of our LTIP awards contains uncertainties because we are required to make assumptions and judgments about the eventual number of shares that will vest in each LTIP grant. The assumptions and judgments that are essential to the analysis include forecasted sales and operating income levels during the LTIP service periods. The evaluation of LTIP performance awards and the corresponding use of estimated amounts may produce additional volatility in our consolidated financial statements as we record cumulative adjustments to the estimated number of common shares to be awarded under the LTIP grants as described above.

During prior fiscal years we have also granted share-based compensation awards that have a share price, or market based, vesting conditions. As a result, we used a Monte Carlo simulation to determine the fair value and expected term of these awards. The Monte Carlo pricing models required the input of subjective assumptions, including items such as the expected term of the options. If factors change, and we use different assumptions for estimating share-based compensation expense related to future awards, our share-based compensation expense may differ materially from that recorded in the current period.

Accounts Receivable Valuation

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. Our allowance for doubtful accounts calculations contain uncertainties because the calculations require us to make assumptions and judgments regarding the collectability of customer accounts, which may be influenced by a number of factors that are not within our control, such as the financial health of each customer. We regularly review the collectability assumptions of our allowance for doubtful accounts calculation and compare them against historical collections. Adjustments to the

assumptions may either increase or decrease our total allowance for doubtful accounts. For

example, a 10 percent increase to our allowance for doubtful accounts at March 2, 2013 would decrease our reported income from operations by approximately \$0.1 million.

Related Party Receivable

At March 2, 2013 we had receivables from FC Organizational Products, an entity in which we own 19.5 percent, for reimbursement of certain operating costs, such as warehousing and distribution costs, which are billed to us by third party providers, and for working capital and other advances that we made during fiscal 2012, even though we are not obligated to provide advances to, or fund the losses of FCOP. We make use of estimates to account for these receivables, including estimates of the collectability of amounts receivable from FCOP in future periods. In accordance with applicable accounting guidance, a portion of these receivables is classified as non-current, and we are required to discount the long-term portion of these receivables to its net present value using an estimated effective borrowing rate for FCOP.

We estimated the effective risk-adjusted borrowing rate to discount additions to the long-term portion of the FCOP receivable at 15 percent, which was recorded as a discount on a related party receivable in our condensed consolidated income statements. Our estimate of the effective borrowing rate required us to estimate a variety of factors, including the availability of debt financing for FCOP, projected borrowing rates for comparable debt, and the timing and our ability to realize projected cash flows from FCOP. These estimates were based on information known at the time of the preparation of these financial statements. A change in the assumptions and factors used, including estimated interest rates, may change the amount of discount taken. Due to the small amount added to the receivable in the quarter ended March 2, 2013, a one percent increase in the discount rate used for receivables discounted during the quarter ended March 2, 2013 would have had an immaterial impact on our income before income taxes.

Our assessments regarding the collectability of the FCOP receivable requires us to make assumptions and judgments regarding the financial health of FCOP and are dependent on projected financial information for FCOP in future periods. Such financial information contains inherent uncertainties, and is subject to factors that are not within our control. Failure to receive projected cash flows from FCOP in future periods may result in adverse consequences to our liquidity, financial position, and results of operations.

For further information regarding our investment in FCOP, refer to the notes to our financial statements for the fiscal year ended August 31, 2012.

Inventory Valuation

Our inventories are primarily comprised of training materials and related accessories. Inventories are reduced to their fair market value through the use of inventory valuation reserves, which are recorded during the normal course of business. Our inventory valuation calculations contain uncertainties because the calculations require us to make assumptions and judgments regarding a number of factors, including future inventory demand requirements and pricing strategies. During the evaluation process we consider historical sales patterns and current sales trends, but these may not be indicative of future inventory losses. While we have not made material changes to our inventory valuation methodology during the past three years, our inventory requirements may change based on projected customer demand, technological and product life cycle changes, longer or shorter than expected usage periods, and other factors that could affect the valuation of our inventories. If our estimates regarding consumer demand and other factors are inaccurate, we may be exposed to losses that may have an adverse impact upon our financial position and results of operations. For example, a 10 percent increase to our inventory valuation reserves at March 2, 2013 would decrease our reported income from operations by \$0.1 million.

Indefinite-Lived Intangible Assets and Goodwill

Intangible assets that are deemed to have an indefinite life and goodwill balances are not amortized, but rather are tested for impairment on an annual basis, or more often if events or circumstances

indicate that a potential impairment exists. The Covey trade name intangible asset was generated by the merger with the Covey Leadership Center and has been deemed to have an indefinite life. This intangible asset is quantitatively tested for impairment using the present value of estimated royalties on trade name related revenues, which consist primarily of training seminars and international licensee royalties. Our goodwill at March 2, 2013 was generated by the acquisition of CoveyLink Worldwide, LLC during fiscal 2009 and the subsequent payment of the first two of five possible contingent annual earnout payments as required in the acquisition agreement.

Our impairment evaluation calculations for goodwill and the Covey trade name contain uncertainties because they require us to make assumptions and apply judgment in order to qualitatively assess the fair value of these assets, and may require estimated future cash flows, an estimated appropriate royalty rate, and an estimated discount rate that reflects the inherent risk of future cash flows when these assets are evaluated on a quantitative basis. Our quantitative valuation methodology for the Covey trade name has remained unchanged during the past three years. However, if forecasts and assumptions used to support the carrying value of our indefinite-lived intangible asset change in future periods, significant impairment charges could result that would have an adverse effect upon our results of operations and financial condition. The valuation methodologies for both indefinite-lived intangible assets and goodwill are also dependent upon the share price of our common stock and our corresponding market capitalization, which may differ from estimated royalties used in our impairment testing. Based upon the fiscal 2012 evaluation (our most recent evaluation) of the Covey trade name and goodwill, our trade-name related revenues, licensee royalties, and overall sales levels would have to suffer significant reductions before we would be required to impair them. However, future declines in our share price may trigger additional impairment testing and may result in impairment charges.

Impairment of Long-Lived Assets

Long-lived tangible assets and definite-lived intangible assets are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. We use an estimate of undiscounted future net cash flows of the assets over their remaining useful lives in determining whether the carrying value of the assets is recoverable. If the carrying values of the assets exceed the anticipated future cash flows of the assets, we calculate an impairment loss. The impairment loss calculation compares the carrying value of the asset to the asset's estimated fair value, which may be based upon discounted cash flows over the estimated remaining useful life of the asset. If we recognize an impairment loss, the adjusted carrying amount of the asset becomes its new cost basis, which is then depreciated or amortized over the remaining useful life of the asset. Impairment of long-lived assets is assessed at the lowest levels for which there are identifiable cash flows that are independent from other groups of assets.

Our impairment evaluation calculations contain uncertainties because they require us to make assumptions and apply judgment in order to estimate future cash flows, forecast the useful lives of the assets, and select a discount rate that reflects the risk inherent in future cash flows. Although we have not made any material recent changes to our long-lived assets impairment assessment methodology, if forecasts and assumptions used to support the carrying value of our long-lived tangible and definite-lived intangible assets change in the future, significant impairment charges could result that would adversely affect our results of operations and financial condition.

Income Taxes

We regularly evaluate our United States federal and various state and foreign jurisdiction income tax exposures. We account for certain aspects of our income tax provision using the provisions of FASC 740-10-05, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. We may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained upon examination by the taxing authorities, based on the technical merits of the

position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon final settlement. The provisions of FASC 740-10-05 also provide guidance on de-recognition, classification, interest, and penalties on income taxes, accounting for income taxes in interim periods, and require increased disclosure of various income tax items. Taxes and penalties are components of our overall income tax provision.

We record previously unrecognized tax benefits in the financial statements when it becomes more likely than not (greater than a 50 percent likelihood) that the tax position will be sustained. To assess the probability of sustaining a tax position, we consider all available evidence. In many instances, sufficient positive evidence may not be available until the expiration of the statute of limitations for audits by taxing jurisdictions, at which time the entire benefit will be recognized as a discrete item in the applicable period.

Our unrecognized tax benefits result from uncertain tax positions about which we are required to make assumptions and apply judgment to estimate the exposures associated with our various tax filing positions. The calculation of our income tax provision or benefit, as applicable, requires estimates of future taxable income or losses. During the course of the fiscal year, these estimates are compared to actual financial results and adjustments may be made to our tax provision or benefit to reflect these revised estimates. Our effective income tax rate is also affected by changes in tax law and the results of tax audits by various jurisdictions. Although we believe that our judgments and estimates discussed herein are reasonable, actual results could differ, and we could be exposed to losses or gains that could be material.

We establish valuation allowances for deferred tax assets when we estimate it is more likely than not that the tax assets will not be realized. The determination of whether valuation allowances are needed on our deferred income tax assets contains uncertainties because we must project future income, including the use of tax-planning strategies, by individual tax jurisdictions. Changes in industry and economic conditions and the competitive environment may impact the accuracy of our projections. We regularly assess the likelihood that our deferred tax assets will be realized and determine if adjustments to our valuation allowance are necessary.

SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Certain written and oral statements made by the Company in this report are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act of 1934 as amended (the Exchange Act). Forward-looking statements include, without limitation, any statement that may predict, forecast, indicate, or imply future results, performance, or achievements, and may contain words such as “believe,” “anticipate,” “expect,” “estimate,” “project,” or words or phrases of similar meaning. In our reports and filings we may make forward looking statements regarding our expectations about future sales levels, future training and consulting sales activity, anticipated expenses, future gross margins, the effects of the acquisition of NinetyFive 5, the release of new services or products, the adequacy of existing capital resources, our ability to extend our line of credit facility, the amount of cash expected to be paid for income taxes, our ability to maintain adequate capital for our operations, projected cost reduction and strategic initiatives, expected levels of depreciation expense, expectations regarding tangible and intangible asset valuations, the seasonality of future sales, the seasonal fluctuations in cash used for and provided by operating activities, expected improvements in cash flows from operating activities, expected improvements in our working capital, future compliance with the terms and conditions of our line of credit, the ability to borrow on our line of credit, expected repayment of our term loan payable, expected collection of amounts receivable from FC Organizational Products LLC, estimated capital expenditures, and cash flow estimates used to determine the fair value of long-lived assets. These, and other forward-looking statements, are subject to certain risks and uncertainties that may cause actual results to differ materially from the

forward-looking statements. These risks and uncertainties are disclosed from time to time in reports filed by us with the SEC, including reports on Forms 8-K, 10-Q, and 10-K. Such risks and uncertainties include, but are not limited to, the matters discussed in Item 1A of our annual report on Form 10-K for the fiscal year ended August 31, 2012, entitled "Risk Factors." In addition, such risks and uncertainties may include unanticipated developments in any one or more of the following areas: unanticipated costs or capital expenditures; difficulties encountered by HP Enterprise Services in operating and maintaining our information systems and controls, including without limitation, the systems related to demand and supply planning, inventory control, and order fulfillment; delays or unanticipated outcomes relating to our strategic plans; dependence on existing products or services; the rate and consumer acceptance of new product introductions; competition; the number and nature of customers and their product orders, including changes in the timing or mix of product or training orders; pricing of our products and services and those of competitors; adverse publicity; and other factors which may adversely affect our business.

The risks included here are not exhaustive. Other sections of this report may include additional factors that could adversely affect our business and financial performance. Moreover, we operate in a very competitive and rapidly changing environment. New risk factors may emerge and it is not possible for our management to predict all such risk factors, nor can we assess the impact of all such risk factors on our business or the extent to which any single factor, or combination of factors, may cause actual results to differ materially from those contained in forward-looking statements. Given these risks and uncertainties, investors should not rely on forward-looking statements as a prediction of actual results.

The market price of our common stock has been and may remain volatile. In addition, the stock markets in general have experienced increased volatility. Factors such as quarter-to-quarter variations in revenues and earnings or losses and our failure to meet expectations could have a significant impact on the market price of our common stock. In addition, the price of our common stock can change for reasons unrelated to our performance. Due to our low market capitalization, the price of our common stock may also be affected by conditions such as a lack of analyst coverage and fewer potential investors.

Forward-looking statements are based on management's expectations as of the date made, and the Company does not undertake any responsibility to update any of these statements in the future except as required by law. Actual future performance and results will differ and may differ materially from that contained in or suggested by forward-looking statements as a result of the factors set forth in this Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in our filings with the SEC.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes from the information previously reported under Item 7A of our Annual Report on Form 10-K for the fiscal year ended August 31, 2012. During the quarter or two quarters ended March 2, 2013, we did not utilize any foreign currency or interest rate derivative instruments.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including the Chief Executive Officer and the Chief Financial Officer, as

appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no

matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

We evaluated the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act, as of the end of the period covered by this report. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) or 15d-15(f)) during the most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II. OTHER INFORMATION

Item 1A. RISK FACTORS

For further information regarding our Risk Factors, please refer to Item 1A in our Annual Report on Form 10-K for the fiscal year ended August 31, 2012.

Item 6. EXHIBITS

(A) Exhibits:

- 10.1 Asset Purchase Agreement made as of March 11, 2013 by and among NinetyFive 5 LLC and Franklin Covey Client Sales, Inc. and other parties thereto (filed as exhibit 2.1 to a current report on Form 8-K filed with the Commission on March 14, 2013 and incorporated by reference herein).
- 10.2 Third Modification Agreement by and between JPMorgan Chase Bank, N.A. and Franklin Covey Co., dated March 25, 2013 (filed as exhibit 10.1 to a current report on Form 8-K filed with the Commission on March 26, 2013 and incorporated by reference herein).
- 10.3 Consent and Agreement of Guarantor by and between JPMorgan Chase Bank, N.A. and Franklin Covey Co., dated March 25, 2013 (filed as exhibit 10.2 to a current report on Form 8-K filed with the Commission on March 26, 2013 and incorporated by reference herein).
- 31.1 Rule 13a-14(a) Certifications of the Chief Executive Officer.**
- 31.2 Rule 13a-14(a) Certifications of the Chief Financial Officer.**
- 32 Section 1350 Certifications.**

101.INS XBRL Instance Document.

101.SCHXBRL Taxonomy Extension Schema Document.

101.CALXBRL Taxonomy Extension Calculation Linkbase Document.

101.DEF XBRL Taxonomy Definition Linkbase Document.

101.LABXBRL Taxonomy Extension Label Linkbase Document.

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.

**Filed herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FRANKLIN
COVEY CO.

Date: April 11,
2013

By: /s/ Robert A.
Whitman
Robert A.
Whitman
Chief
Executive
Officer
(Duly
Authorized
Officer)

Date: April 11,
2013

By: /s/ Stephen
D. Young
Stephen D.
Young
Chief
Financial
Officer
(Principal
Financial
and
Accounting
Officer)