CAMBIUM LEARNING GROUP, INC.
Form 10-K
March 10, 2011

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

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

For the fiscal year ended December 31, 2010

or

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

For the transition period from __________ to __________

Commission file number 001-34575

Cambium Learning Group, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**27-0587428**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
17855 North Dallas Parkway, Suite 400, Dallas, Texas	**75287**
(Address of Principal Executive Offices)	(Zip Code)

Registrant s telephone number, including area code:

(214) 932-9500

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, par value $0.001 per share	**The NASDAQ Global Market**
(Title of class)	(Name of exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No þ

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 þ No o

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 o No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

Large accelerated filer o	Accelerated filer o	Non-accelerated filer þ	Smaller reporting company o

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

The aggregate market value of the registrant s common stock, par value $0.001 per share, held by non-affiliates of the registrant was $59,910,530 based on the closing sale price of the registrant s common stock on June 30, 2010, the last business day of the registrant s most recently completed second fiscal quarter, as reported on the NASDAQ Global Market. As of March 4, 2011, there were 43,868,676 shares of the registrant s common stock outstanding.

Documents Incorporated by Reference:

Part III incorporates certain information by reference from the registrant s definitive proxy statement for the 2011 Annual Meeting of Stockholders, which definitive proxy statement will be filed by the registrant with the Securities and Exchange Commission within 120 days after the end of the registrant s fiscal year ended December 31, 2010.

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PART I

Cautionary Note Regarding Forward-looking Statements.

This report contains forward-looking statements within the meaning of the federal securities laws that involve risks and uncertainties, and which are based on beliefs, expectations, estimates, projections, forecasts, plans, anticipations, targets, outlooks, initiatives, visions, objectives, strategies, opportunities, drivers and intents of our management. Such statements are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical facts included in this report, including, without limitation, statements regarding our future financial position, economic performance and results of operations, as well as our business strategy, objectives of management for future operations, and the information set forth under Management s Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements. Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Forward-looking statements can be identified by, among other things, the use of forward-looking language, such as believes, expects, estimates, projects, forecasts, plans, anticipates, targets, outlooks, visions, objectives, strategies, opportunities, drivers, intends, scheduled to, seeks, may, will, or of those terms, or other variations of those terms or comparable language, or by discussions of strategy, plans, targets, models or intentions. Forward-looking statements speak only as of the date they are made, and except for our ongoing obligations under the federal securities laws, we undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events, or otherwise, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements. Accordingly, you are cautioned that any such forward-looking statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict. Although we believe that the expectations reflected in such forward-looking statements are reasonable as of the date made, expectations may prove to have been materially different from the results expressed or implied by such forward-looking statements, as it is impossible for us to anticipate all factors that could affect our actual results. We discuss certain of these risks in greater detail under the heading Risk Factors in Item 1A of this report. Unless otherwise required by law, we also disclaim any obligation to update our view of any such risks or uncertainties or to announce publicly the results of any revisions to the forward-looking statements made in this report.

Item 1. Business.

Unless otherwise expressly indicated in this Item 1, the discussions set forth herein are as of December 31, 2010. The Company , we , us , or our when used in this report refers to Cambium Learning Group, Inc. and its predecessors and consolidated subsidiaries.

Overview

Our mission is to enable educators to unlock every child s potential through learning, no matter where their journey begins. We are one of the largest providers of proprietary intervention curricula, educational technologies and other research-based education solutions for students in the Pre-K through 12th grade education market in the United States. The intervention market, where we focus, provides supplemental education solutions to at-risk and special education students. We offer a distinctive blended intervention solution that combines different forms of current instruction techniques, including text books, education games, data management and e-learning. We believe that our approach builds a more effective learning environment that combines teacher-led instruction and technology and that this approach sets us apart from our competitors, as we believe it better engages at-risk students, leading to more favorable student results. Our solutions are designed to enable the most challenged learners to achieve their potential by utilizing a range of content that primarily focuses on reading and math.

We take a holistic approach to learning and our intervention solutions address both the behavioral and cognitive needs of the students we serve. We believe our focus on the Pre-K through 12th grade intervention market and our significantly greater scale and scope of operations compared to those other companies primarily focused on the intervention market gives us a competitive edge relative to our peers. Further, our products and services are highly results-oriented and enable school districts and parents across the country to improve student performance and better satisfy rigorous accountability standards.

School districts have become increasingly accountable for student performance. As a result, they have increased both focus and funding to address underperformance. To this end, our research-based intervention programs have demonstrated consistent success with at-risk and special education student populations and have established us as one of the most readily recognized companies exclusively serving this market. We operate in three business segments: Voyager, a comprehensive intervention business; Sopris, a supplemental solutions education business; and Cambium Learning Technologies (CLT), a technology-based education product business.

We were incorporated under the laws of the State of Delaware in June 2009. On December 8, 2009, we completed the mergers of Voyager Learning Company (VLCY) and VSS-Cambium Holdings II Corp. (Cambium) into two of our wholly owned subsidiaries, resulting in VLCY and Cambium becoming our wholly owned subsidiaries. The results of VLCY are included in the Company s operations beginning with the December 8, 2009 merger date; therefore, the 2009 financial information contained in this report consists of the results of the Company for the full year but only include VLCY for the last 23 days of that year.

The transaction was accounted for as an acquisition of VLCY by Cambium, as that term is used under U.S. Generally Accepted Accounting Principles (U.S. GAAP), for accounting and financial reporting purposes under the applicable accounting guidance for business combinations. In making this determination, management considered that (a) the newly developed entity did not have any significant pre-combination activity and, therefore, did not qualify to be the accounting acquirer, and (b) the former sole stockholder of Cambium is the majority holder of the combined entity, while the prior owners of VLCY became minority holders in the combined entity. As a result, the historical financial statements of Cambium have become the historical financial statements of the Company.

Cambium Learning, Inc., a subsidiary of Cambium (Cambium Learning) was founded in December 2002 to create a leading company focused on the at-risk and special student populations. In 2007, Cambium Learning was acquired by a consortium of equity sponsors led by Veronis Suhler Stevenson (VSS). A significant portion of Cambium Learning s growth has resulted from the acquisition and growth of companies acquired by Cambium Learning and from newly introduced programs developed by authors and researchers. In October 2003, Cambium Learning acquired Metropolitan Teaching & Learning, Inc. Metropolitan Teaching & Learning, Inc. was founded in 1998, and has developed culturally responsive instructional materials and customized programs for use in urban markets, with particular emphasis on mathematics. In February 2004, Cambium Learning acquired Sopris West Educational Services, Inc., a provider of intervention programs in literacy, mathematics, and behavior. In April 2005, Cambium Learning acquired Kurzweil Education Systems, Inc., which develops reading enabling technologies for struggling readers and individuals with visual impairments. In February 2006, Cambium Learning acquired IntelliTools, Inc., a provider of assistive hardware and software technologies for the special education and at-risk market segments in math and literacy.

VLCY s predecessor company, Bell & Howell Company, was incorporated in Delaware in 1907. On January 31, 2005, VLCY completed the acquisition of Voyager Expanded Learning, Inc., in support of its long-term strategy to grow its educational business for grades K-12. On June 30, 2007, ProQuest Company amended Article I of its certificate of incorporation solely to change the corporate name from ProQuest Company to Voyager Learning Company. The name change and amendment were completed pursuant to a merger of VLCY s wholly owned subsidiary with and into VLCY.

Strategy for Growth and Development

Our strategy for growth and development is based upon the following:

Continued Focus on the Pre-K Through 12th Grade Intervention Market: The intervention market is highly attractive and is characterized by favorable long-term growth trends and historically strong government support. We devote most of our resources to better serve this market and we believe that our concentrated focus positions us to capture a greater market share over time. We are a leading provider that offers comprehensive instructional material, professional development and learning technology solutions specifically designed for the intervention market. We also believe that this focus allows us to deliver better designed products to our customers, ultimately resulting in more favorable student outcomes. We plan to continue to employ a broad-based approach to compete across segments and build scale and market share.

Increased Offering of Technology-Based Learning Solutions: We have a wide range of technology-based learning solutions offered as either standalone tools or as part of our blended model (which integrates these technology-based learning solutions with our print-based products). Our standalone technology-based solutions include online supplemental reading, writing and vocabulary lessons and books as well as interactive simulations in math and science. Such solutions are employed by our customers for at-risk students and are more commonly used by, and are equally as effective for, on-track students to enhance their proficiency levels. Across much of our product offering, we utilize a comprehensive student data reporting system with multiple years of results. We believe this ability to assess, track and report results is crucial to providing educators with the tools required to achieve and provide accountability for student outcomes.

Leverage Nationally Recognized Brands, Sales Force and Scalable Platform: We believe our portfolio of premier brands and research-based products and services has consistently delivered superior learning outcomes for school districts. We plan to leverage our reputation for quality and our experienced sales force to generate new business and capture a greater share of business from existing customers across our national footprint. Further, we plan to utilize our portfolio of technology-driven products and services and an easily replicable implementation model to rapidly meet customer needs.

Invest in Key Growth Initiatives: In 2010, we made specific investments in certain key areas intended to facilitate growth in 2011 and beyond. In the Voyager business unit, we integrated two large sales forces (pre-combination Cambium and VLCY) into one national model and we consolidated the student reporting systems of the two previously separate companies. In the Sopris business unit, we built a nationwide field sales force, made significant investments in marketing and introduced two substantial new products. In the CLT unit, we have increased our investment in sales, marketing and product development to enhance continued growth products. Across all business units, we have substantially upgraded our e-commerce and e-marketing capabilities in order to facilitate greater demand pull for our products. We intend to increase market penetration and market share through these investments, enabling us to recognize greater revenues per student.

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Funding Sources and Industry Information

The intervention market is focused on administering supplemental education solutions to at-risk and special education students within the Pre-K through 12th grade student segment. At-risk and special education students are those students that are underperforming when evaluated against their peers and current academic standing, which is defined as the bottom 40% of learners. Students in need of intervention are often found in three distinct groups: English language learners (ELL), Special Education (SPED) and impoverished students. The ELL group is made up of those students whose first language is not English. SPED students are individuals with special needs, including learning and communication challenges, emotional and behavioral disorders, physical disabilities and developmental disorders. Impoverished students are from families with low socioeconomic status and are at an academic disadvantage due to their families financial hardships.

We believe that educating at-risk and special education students requires a different approach than relying on traditional instructional materials, as these intervention programs often require detailed implementation and training. Key federal and state programs, such as the Title 1 portion (Title 1) of the reauthorized Elementary Secondary Education Act (ESEA), the School Improvement Grants program (SIG), the Individuals with Disabilities Education Act (IDEA) and the Race to the Top Program enacted under the American Recovery and Reinvestment Act of 2009 (ARRA) have been key drivers in encouraging school districts to address the needs of this student population.

While school districts use a variety of government funding sources in order to procure our products and services, our industry receives proportionally more federally provided funds than education services and products as a whole, which tend to rely more heavily on state and local funding. Title 1 (and the Title 111 portion of the ESEA) and IDEA have existed for decades and have experienced steady increases since their inception. Further augmenting these traditional funding sources in 2009 and 2010 was the ARRA, which allocated an additional $10 billion for Title I and an additional $11.3 billion for IDEA over the fiscal years ending September 2010 and September 2011. Additional federal funds are also being made available through the ARRA s Race to the Top program, which is expected to provide over $4 billion in additional education funding.

Over the long-term, we expect growth in the overall intervention market will be driven by the following key factors:

Large and Growing Addressable Market: Total Pre-K through 12th grade enrollment was 56 million in 2008, with enrollments rising. It is estimated that at least 40% of these students require intervention and represent a large addressable market for us. Demand for intervention is expected to continue to increase since intervention is typically more cost effective than special education programs. We believe that, with more attention in general, increased analysis of U.S. student outcomes versus other countries, focus and likely inclusion of the graduation rate in the ESEA, and movement to national standards, the number of children deemed to need intervention is likely to increase from 40% to over 50%, as indicated by proficiency rates of the National Assessment of Educational Progress.

Historically Stable Federal Funding Landscape: The funding environment for Pre-K through 12th grade education has historically been stable across economic cycles. While the recent downturn has pressured state and local budgets, the primary sources of federal funding for education (Title I and IDEA) have been maintained at historically high levels. Traditional federal funding sources for education have been temporarily augmented by ARRA funding from 2009 to 2011, including the Race to the Top program.

Increasing Emphasis on Accountability and Measurement: The No Child Left Behind Act (NCLB) has been a key driver for increased accountability and a measurement of student performance. School districts are required to demonstrate adequate yearly progress (AYP) or risk a cut in funding. Intervention products help schools improve performance of the most challenged learners and allow schools to meet stringent AYP criteria. Furthermore, there is greater emphasis on evaluating educators based on the performance of their students. The combination of these factors will continue to drive the demand for intervention and professional development products.

Proven Return on Investment of Intervention Products: Numerous studies have demonstrated and quantified the benefits of intervention products for at-risk and special education students. We believe traditional educational materials are inadequate and not designed to meet their learning needs. Also, teachers are becoming better trained at utilizing intervention materials, which we expect will contribute to greater demand for such products.

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Product Overview

We operate as three reportable segments, with separate management teams and infrastructures that offer various products and services, as follows:

Voyager, our comprehensive intervention solutions;

Sopris, our supplemental solutions;

Cambium Learning Technologies(or CLT), our technology-based solutions

During 2010, net revenues were $117.9 million for Voyager, $24.7 million for Sopris and $38.6 million for CLT. Unallocated shared services such as accounting, legal, human resources and corporate-related items are recorded in a Shared Services category. Depreciation and amortization expense, goodwill impairment, interest income and expense, other income and expense, and taxes are also included in this category.

Voyager

Our Voyager unit offers reading, math and professional development programs targeted towards the at-risk and special education student populations. Voyager materials, offered in print form and increasingly in online format, are tailored to meet the needs of these students and differ considerably from traditional instructional materials in design, approach and intensity. Lessons are based on scientific research and are carefully designed to effectively and efficiently address each of the strategies and skills necessary to improve the abilities of struggling students.

Voyager Reading Programs. The reading programs in the Voyager business unit consist of: Voyager Passport®; LANGUAGE!; Passport Reading Journeys®; Read Well; Voyager Universal Literacy System®; Ticket to Read®; TimeWarp® Plus; Voyager Pasaporte®; and We Can!.

Voyager Passport is a comprehensive reading intervention system for grades K-5. Voyager Passport provides direct, systematic instruction in each of the five essential reading components (phonemic awareness, phonics, fluency, vocabulary, and comprehension) and is designed as an intervention program for grade K-5 students for whom a core reading program is not sufficient. The lessons are typically daily and run 30 to 40 minutes in duration. They are based on the latest scientific research regarding effective reading instruction and are carefully designed to effectively and efficiently address each of the strategies and skills necessary to improve the reading ability of struggling readers.

LANGUAGE!, our principal adolescent literacy offering, is a comprehensive literacy program that targets students in grades 3-12 achieving at or below the 20th percentile. The program consists of a 36-unit curriculum organized into six levels that cover phonemic awareness and phonics, word recognition and spelling, vocabulary and morphology, grammar and usage, listening and reading comprehension, and speaking and writing. LANGUAGE! is designed for special education students, as well as students learning to speak English. The curriculum is a mastery-based curriculum. Students exit as soon as they achieve grade-level proficiency, which will vary depending on the specific needs of the student and where the student enters the program.

Passport Reading Journeys is a targeted intervention program designed to accelerate reading for struggling readers in middle school and high school, grades 6-9. The lesson format integrates reading, comprehension, vocabulary, fluency and writing. Age-appropriate content, real-life journeys on DVDs, online interactive lessons, and captivating text are designed to hold student interest and motivate students to read for both information and enjoyment. The program targets the affective domain as much as the cognitive domain, as many struggling readers have lost confidence, are not engaged, and are close to dropping out. The program meets all of the instructional recommendations of the Reading Next Report, which is an industry research report outlining the key elements of effective literacy intervention for middle and high school students, and provides teachers with the tools necessary to help students become successful readers.

ReadWell is an alternative comprehensive core reading program that targets at-risk students in grades K-2. The program is a research-based and data-driven reading curriculum that addresses all five components of effective reading instruction phonemic awareness, phonics, vocabulary, comprehension and fluency as outlined by the National Reading Panel in 2000.

The Voyager Universal Literacy System is an alternative comprehensive core reading curriculum for grades K-3 that explicitly and systematically teaches the five essential components of reading instruction listed above.

Ticket to Read (www.tickettoread.com) is an interactive web-based program offered with Voyager s Passport, ReadWell and Universal Literacy System programs. Ticket to Read is designed to improve reading by allowing students to practice various aspects of reading skills. Instruction is leveled, self-paced and teacher-monitored. Students are motivated by a leader-board, a virtual clubhouse that includes earning online tickets and other rewards, games, and engaging self-selected passages on a variety of topics as they build vocabulary, fluency, phonics and reading comprehension skills. Approximately one-quarter of the use takes place after school hours, including weekends, further enabling students to reinforce what they have learned in the classroom and enabling parents and/or guardians to become more involved in their children s education.

TimeWarp Plus is a four-to-six week summer reading intervention program which immerses grade K-9 students in reading adventures to build essential reading skills that can prevent summer learning loss and prepare students for the coming year. TimeWarp Plus is a balanced, research-based reading program offered as a two-to-four hour daily reading instruction focused around exciting, adventure-based themes and hands-on learning experiences. Student engagement and maximizing teacher time are key components of the program.

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Voyager Pasaporte provides students in grades K-3 with targeted reading intervention in Spanish, using a similar scientifically-based reading research and framework as Voyager Passport. The lessons typically run daily for 30 to 40 minutes in duration. They are based on scientific research regarding effective reading instruction and are carefully designed to effectively and efficiently address each of the strategies and skills necessary to improve the reading ability of struggling Spanish-speaking children who cannot read effectively in any language. Built-in assessment and progress monitoring tools provide teachers with vital information about student learning so they can adjust instruction as needed.

We Can! is a multilingual early childhood program which is designed to develop both social and academic skills. The program offers flexible lesson plans for customized instruction, a classroom management system and learning center choices. We Can! also fits within a variety of Pre-K settings.

Voyager Math Programs. The math programs in the Voyager business unit consist of: Vmath®, Vmath Summer Adventure, TransMath, Inside Algebra and Voyages.

Vmath is a targeted, systematic intervention system that is aligned with the tenets of the National Council of Teachers of Mathematics and is designed to complement and enhance all major math programs by building upon and reinforcing the concepts, skills, and strategies of a core math program. Through 30 to 40 minutes of daily instruction, Vmath helps struggling students build a foundation in math and learn the skills and concepts crucial to achieving grade-level success. VmathLive is a standalone or complementary online math capability, targeting additional student practice for grades 2-8.

Vmath Summer Adventure targets math students who may need summer intervention to prevent summer learning loss in math as well as in reading. Vmath Summer Adventure combines explicit instruction in essential math concepts and skills and real-life adventures to stimulate student interest and understanding over a shortened summer school program for grades K-8.

TransMath targets students in the 25th percentile and below in grades 5-9. TransMath provides students with in-depth, sequential skill building of foundational math concepts through reform-based and procedural instruction. Multisensory strategies are designed to promote problem-solving proficiency, vocabulary development and mathematical discourse. VmathLive is offered with TransMath.

Inside Algebra targets students at risk of failure in algebra and teaches them a variety of core objectives through activities intended to make learning fun. Students may participate in Inside Algebra in small groups, as a supplement to basal curricula, or as a standalone algebra intervention program.

Voyages targets grades K-5 and is a core mathematics program designed by teachers, for teachers. Educators may utilize Voyages as a core program, as an intervention program or as part of a gifted and talented program.

Voyager Professional Development Programs. Professional development services provide customized, sustainable, product independent solutions for teachers and leadership to help our customers enhance their existing investments in curricula, textbooks, and learning resources. Specific topics include Reading, Math, Behavior, Response to Intervention, Instructional Audits, Coaching and Leadership, and support all tiers of student instruction. These services are provided via three delivery systems: consulting services and custom professional development, custom conferences and institutes, and distance learning.

Sopris

Our Sopris unit focuses on providing a diverse, yet comprehensive collection of printed and electronic supplemental education materials to complement core programs and to provide intense remediation aimed at specific skill deficits. When compared to products offered by our other business units, Sopris products tend to be more narrowly-tailored and target a smaller, more specific audience. Sopris primary products are Step Up to Writing; REWARDS; Dynamic Indicators of Basic Early Literacy Skills (DIBELS/IDEL); Language Essentials for Teachers of Reading and Spelling (LETRS); The Six Minute Solution; Algebra Ready; and RAVE-O. Through these offerings, we commercialize research of some of the most highly regarded authors in the field, including Drs. Louisa Moats, Anita Archer and Roland Good.

Step Up to Writing is a strategies-based program that spans grades K-12 and addresses students who score at or below the basic skill level in writing. Authored by Dr. Maureen Aumon, the program teaches students to write both narrative and expository pieces, actively engage with reading materials and develop study skills. Step Up to Writing is designed to fit alongside a school district s existing reading program and to be integrated into any standard curriculum or instructional system.

REWARDS is a research-based, reading intervention program designed for general and special education, remedial reading, summer school and after-school programs. Authored by Dr. Anita Archer, the program focuses on de-coding, fluency, vocabulary, comprehension, test-taking abilities and content-area reading and writing.

DIBELS/IDEL is a literary screening and progress monitoring tool. Authored by Drs. Roland Good and Ruth Kaminski, students from grades K-3 take benchmark assessments three times a year in order to measure the critical areas of early reading: awareness, phonics, fluency, comprehension and vocabulary. Students in grades 4-6 are assessed in the areas of fluency and comprehension. For those with reading difficulties, progress monitoring assessments are given to determine the effectiveness of the interventions being used. IDEL offers DIBELS materials for Spanish-speaking students.

LETRS is a stand-alone professional development program for educators. Authored by Dr. Louisa Moats, the training program is delivered through a combination of print materials, online courses, software and face-to-face training. LETRS Institutes are grouped into a series of three-day sessions presented by certified national LETRS trainers and engage educators through group activities and hands-on practice.

The Six Minute Solution targets grades K-12 and helps students improve reading fluency. This peer-mentoring and feedback system is designed to complement a reading curriculum.

Algebra Ready teaches students fundamental mathematics and is designed to prepare them for algebra and geometry. Students can utilize Algebra Ready during summer school, extended days, or as a supplement to a core math curriculum.

RAVE-O (Reading through Automaticity, Vocabulary, Engagement, and Orthography) is an intensive, multisensory, small group reading intervention for primary through intermediate grades. Authored by neuroscientist Dr. Maryanne Wolf, the program applies brain research to reading intervention.

Cambium Learning Technologies

Our CLT unit utilizes technology to deliver subscription-based websites, online libraries, software and equipment designed to help students reach their potential in grades K through 12 and beyond. CLT products are offered under four different industry leading brands: Learning A-Z, ExploreLearning, Kurzweil Educational Systems and IntelliTools.

Learning A-Z. Learning A-Z is a group of related websites known as Reading A-Z™, Raz-Kids™, Reading-Tutors™, Vocabulary A-Z™ and Writing A-Z™, which provide online supplemental reading, writing and vocabulary lessons, books, and other resources for students and teachers. Science A-Z™, a Learning A-Z website, is aimed at the supplemental science market.

We sell online supplemental reading, math and science products under the Learning A-Z brand. There are three free websites (LearningPage™, Sites for Teachers and Sites for Parents), which aid in directing interested parents, teachers, schools and districts to six subscription-based sites: Reading A-Z, Raz-Kids, Reading-Tutors, Vocabulary A-Z, Writing A-Z, and Science A-Z. Each of these websites offers products available for purchase through online subscriptions.

Reading A-Z offers thousands of research-based, printable teacher materials to teach guided reading, phonological awareness, phonics, comprehension, fluency, letter recognition and formation, high-frequency words, poetry and vocabulary. The teaching resources include professionally developed downloadable leveled books (27 levels), a systematic phonics program that includes decodable books, high-frequency word books, poetry books, nursery rhymes, vocabulary books, read-aloud books, lesson plans, worksheets, graphic organizers and reading assessments. All leveled books, worksheets, graphic organizers and quizzes are available as printable PDF files and as projectables for use on interactive and non-interactive whiteboards. The leveled books and a variety of other books are available in Spanish and French, as well as a version with UK spellings.

Raz-Kids is a student-centered online collection of interactive leveled books and quizzes designed to guide and motivate emergent and reluctant readers, as well as improve the skills of fluent readers. Students can listen to and read books as well as record their reading and then take an online quiz while receiving immediate feedback. Students earn stars for their reading activity. The stars can then be spent in each student s personal clubhouse-like environment for purchasing a catalog full of items that include aliens and other fun characters. The program currently consists of over 300 online books along with companion quizzes and worksheets spread over 27 levels of difficulty. A new feature is an online tool that allows teachers to place students at the appropriate reading level while capturing reading rate and fluency. The website also features a classroom management system for teachers to build rosters, assign books and review student reading activity.

Reading-Tutors is a low-cost, easy-to-use collection of research-based resource packets for tutors. Each of the 400 packets contains items tutors need to help emerging readers gain key literacy skills in the alphabet, phonological awareness, phonics, high-frequency words, fluency and comprehension. It also has all the resources needed to train tutors as well as set up and administer a successful tutoring program.

Vocabulary A-Z provides customized and pre-made vocabulary lessons for use by teachers to improve student vocabularies. Vocabulary A-Z has thousands of vocabulary words that can be used to generate custom vocabulary lessons and assessments. Word activities and worksheets are available based on the word lists the user generates. The Vocabulary A-Z lesson generator incorporates best practices from current educational research.

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Writing A-Z provides teachers with a comprehensive collection of resources to enhance the writing proficiency of students in grades K-6. The site provides core writing lessons grouped by genre, including student packets with leveled materials, mini-lessons that target key writing processes and skills, and writing tools for organizing and improving writing.

Science A-Z provides teachers with an online collection of resources to improve student skills in both science and reading. The website offers a collection of downloadable resources organized into thematic units aligned with state standards. The materials are categorized into four scientific domains: life, earth, physical and process science. The thematic units are organized into three grade-level groupings: K-2, 3-4, and 5-6. The themed packs include lessons, books, high-interest information sheets, career sheets, and process activities. Within each grade span, all books and information sheets are written to a high, medium and low level of difficulty. The website includes many other science resources, including science fair resources and a monthly Science In the News feature.

ExploreLearning. ExploreLearning™ is a subscription-based online library of interactive simulations in math and science for grades 3-12. ExploreLearning has won National Science Foundation funding, supports the tenets of the National Council of Teachers of Mathematics and has received positive mention in books published by the Association of Supervision and Curriculum Development and the National Science Teachers Association. ExploreLearning is also a perennial award winner recognized by industry peer groups, including the Association of Educational Publishers, Software Industry and Information Association, as well as publications such as *District Administration Magazine* and *Tech and Learning Magazine*. ExploreLearning materials are correlated to state standards and over 120 math and science textbooks. Like Learning A-Z, ExploreLearning is an online subscription-based business. REFLEX, ExploreLearning s newest adaptive software, is a game-based solution for grades 2-6 that teaches math fluency in the four operations. The program will launch in March 2011.

Kurzweil Educational Systems. Kurzweil Educational Systems is a program that primarily targets students in middle school through higher education struggling with reading and writing, specifically those students with ADHD, dyslexia and visual impairments. Kurzweil Educational Systems produces the following two software products for individuals with learning difficulties and for those who are visually impaired:

Kurzweil 3000. Kurzweil 3000 is a reading, writing and learning software package for students with dyslexia, attention deficit disorder or other learning difficulties, including physical impairments or language learning needs.

Kurzweil 1000. Kurzweil 1000 provides visually impaired users access to printed and electronic materials. Documents and digital files are converted from text to speech and read aloud in a variety of voices that can be modified to suit individual preferences. In addition, this software provides users with document creation and editing, studying and study skills for note-taking, summarizing and outlining text.

IntelliTools. IntelliTools offers hardware products that target students with physical, visual and cognitive disabilities that make using a standard keyboard and mouse difficult. IntelliTools also offers software products that target elementary and middle school special education students struggling with reading and math. IntelliTools products include:

IntelliKeys® USB, which is a programmable alternative keyboard with supporting software for students or adults who have difficulty using a standard keyboard.

IntelliTools Classroom Suite, which is an authoring and application tool intended to boost achievement on standards-based tests and help meet adequate yearly progress goals under the No Child Left Behind Act.

IntelliTools, which offers software products with a simple interface for students to use. The software includes lessons, activities and assessments that reinforce reading, writing and math skills with the capability to generate reports and provide detailed data tracking.

Marketing and Distribution

Curriculum Development

We continually seek to take advantage of new product and technology opportunities and view product development to be essential to maintaining and growing our market position. We have developed relationships with many industry-leading authors who are known for their expertise in improving the cognitive and behavioral performance of at-risk and special education students. Many authors are leaders in their respective fields, such as literacy, mathematics, cognitive reasoning, and behavioral sciences. These authors are engaged by us to develop content and then to refine that content once feedback is obtained from our customers. We also employ both in-house and contracted developers of curriculum and on-line content. We generally conduct an extensive refresh of our products every three to five years to incorporate the latest research, bring images current, and update factual content. The web-based products are enhanced continuously. Between the product refreshes, we often develop variations, expansions (i.e., more grade levels) and other basic enhancements of our products. As of December 31, 2010, we had 141 employees in curriculum development. Research and development expense, net of capitalization, was $10.6 million for 2010 and $5.6 million for 2009. In addition, we capitalize certain expenditures related to product development.

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Sales and Marketing

Sales Force Organization

We generally organize our marketing and sales force around our Voyager, Sopris and CLT business units. Within CLT, the sales forces are further divided to focus on reading, math/science, or special education areas. We have separate sales forces by unit and sales producers sell all available products in the unit and are general relationship managers. They are supported by product or subject matter experts as well as a corporate marketing team. As of December 31, 2010, our sales force consisted of 90 field and 31 inside sales producers for a total of 121 direct sales producers, excluding sales management and marketing. Where we elect to use both field and inside sales producers in a business unit, we tend to segment the customers primarily based on size of a territory, whereby larger territories are covered by field representatives and smaller territories are covered more effectively by inside sales employees. We also use direct marketing through catalogs and are increasingly making use of e-commerce and the Internet to sell our products. Sales and marketing expense was $46.0 million for 2010 and $23.4 million for 2009.

Competition

The market for our products is highly competitive. We compete with a wide range of companies from large publishers covering a broad array of products to small providers who specialize in very limited areas. We compete with:

Traditional text book suppliers, which often offer intervention products as part of their core reading and math programs, including Houghton Mifflin/Harcourt, Pearson, The McGraw-Hill Companies, and Scholastic;

Supplemental suppliers, a market segment that is quite fragmented, including the supplementary products divisions of the international textbook publishers named above, and others including Curriculum Associates, Teacher Created Materials, School Specialty, Haights Cross Communications and The Hampton-Brown Company;

Technology suppliers, including Scholastic (Read 180, MiniBooks), Adaptive Curriculum, Carnegie Learning, Renaissance Learning, Don Johnston and TextHelp; and

Service providers, including Americas Choice (recently purchased by Pearson), and research laboratories such as WestEd.

In addition, with greater use of virtual tools, we compete with a number of entities like K12 and Florida Virtual School.

Concentration Risk

We are not overly dependent upon any one customer or a few customers, the loss of which would have a material adverse effect on our business. We have a broad customer base; in the three years ended December 31, 2010 for both VLCY and the Company, no single customer accounted for more than 10% of our total net revenues in any one year. Additionally, our top ten customers accounted for approximately 20% of our net revenues in 2010.

Seasonality

Our quarterly operating results fluctuate due to a number of factors, including the academic school year, school procurement policies, funding cycles, the amount and timing of new products and spending patterns. In addition, customers experience cyclical funding issues that can impact revenue patterns. We generally expect our lowest revenues and earnings to be in the first and fourth fiscal quarters and our highest revenues and earnings to be in the second and third fiscal quarters.

Governmental Regulations

Our operations are governed by laws and regulations relating to equal employment opportunity, workplace safety, information privacy, and worker health, including the Occupational Safety and Health Act and regulations under that Act. Additionally, as a company that often bids on various state, local and federally funded programs, we are subject to various governmental procurement policies and regulations. We believe that we are in compliance in all material respects with applicable laws and regulations and that future compliance will not have a material adverse effect upon our consolidated operations or financial condition.

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Employees

Our future success is substantially dependent on the performance of our management team and our ability to attract and retain qualified technical and managerial personnel. As of December 31, 2010, we had a total of 564 employees. None of our employees are represented by collective bargaining agreements. We regard our relationship with our employees to be good.

Executive Officers

Ronald Klausner. Ronald Klausner, age 57, currently serves as a Class III director and our Chief Executive Officer. Mr. Klausner has served as one of our directors since December 8, 2009. Mr. Klausner served as President of Voyager Expanded Learning from October 2005 until December 8, 2009, when he became our Chief Executive Officer. Prior to that, Mr. Klausner served as President of ProQuest Information and Learning Company (a subsidiary of VLCY until it was sold in 2007) from April 2003 to October 2005. Mr. Klausner came to VLCY from D&B (formerly known as Dun & Bradstreet), a global business information and technology solutions provider, where he worked for 27 years. He most recently served as D&B s Senior Vice President, U.S. Sales, leading a segment with more than $900 million in revenue. Previously, Mr. Klausner led global data and operations, and customer service, providing business-to-business, credit, marketing and purchasing information in over 200 countries.

David F. Cappellucci. David F. Cappellucci, age 54, currently serves as a Class I director and our President. Mr. Cappellucci has served as one of our directors since December 8, 2009. Mr. Cappellucci served as the Chief Executive Officer of Cambium from April 2007 until December 8, 2009 and has 24 years of experience in the education industry. Before co-founding Cambium in December of 2002, Mr. Cappellucci spent 13 years with Houghton Mifflin Company, where he served in a variety of senior management positions, overseeing strategy, mergers and acquisitions, planning and operations at both the corporate level and within a number of business units, including the K-12 School Publishing Group and the Educational and Business Software Divisions. In 2000, Mr. Cappellucci co-founded Classwell Learning Group, an education company formed within the Houghton Mifflin organization. Through 2002, Mr. Cappellucci served as President and Chief Executive Officer of Classwell Learning Group, which was described as the best new brand in the education market by a major industry magazine in 2002. From 1992 to 1997, Mr. Cappellucci served as Senior Vice President of Elementary Education for Simon & Schuster. Prior to that, Mr. Cappellucci was Vice President of Finance, Planning and Operations for Houghton Mifflin s K-12 school and assessment businesses.

Bradley C. Almond. Bradley C. Almond, age 44, currently serves as our Senior Vice President and Chief Financial Officer. Mr. Almond served as Chief Financial Officer of VLCY since January 2009 and continues to serve as our subsidiary s Chief Financial Officer. Mr. Almond joined VLCY in November 2006 as Chief Financial Officer of the Voyager Expanded Learning operating unit. Before joining VLCY, Mr. Almond was Chief Financial Officer, Treasurer and Vice President of Administration at Zix Corporation, a publicly traded email encryption and e-prescribing service provider located in Dallas, Texas, since 2003. From 1998 to 2003, Mr. Almond worked at Entrust Inc., where he held a variety of management positions, including president of Entrust Japan, general manager of Entrust Asia and Latin America, vice president of finance and vice president of sales and customer operations. Mr. Almond is a licensed Certified Public Accountant.

John Campbell. John Campbell, age 50, currently serves as Senior Vice President and the President of the CLT business unit. Mr. Campbell served in the positions of Senior Vice President of Strategy & Business Development, Senior Vice President of K-12 and Chief Operating Officer of Voyager Expanded Learning since joining VLCY in January 2004 until December 8, 2009. Before joining VLCY, Mr. Campbell served as Chief Operating Officer and business unit head of a research based reading company (Breakthrough to Literacy) within McGraw-Hill. Prior to joining Breakthrough/McGraw-Hill, he served as Director of Technology for Tribune Education. Additionally, Mr. Campbell has experience as General Manager of a software start-up (Insight) and as Director of Applications and Technical Support for a hardware manufacturer (Commodore International).

George A. Logue. George A. Logue, age 60, currently serves as Executive Vice President and the President of the Supplemental Solutions business unit. Mr. Logue served as the Executive Vice President of Cambium from June 2003 until December 8, 2009 and has 35 years of education industry experience. Before joining Cambium, Mr. Logue spent 18 years in various leadership roles with Houghton Mifflin Company. At Houghton Mifflin, Mr. Logue served as

Executive Vice President of the School Division from 1996 to 2003. Prior to serving as Executive Vice President of Houghton Mifflin, Mr. Logue was Vice President for Sales and Marketing from 1994 to 1996.

Carolyn W. Getridge. Carolyn W. Getridge, age 66, currently serves as our Senior Vice President of Human Resources and Urban Development. She joined VLCY in 1997 as a member of the team that launched the company after a distinguished 30-year career in public education. Immediately prior to joining Voyager, Ms. Getridge was Superintendent of the Oakland Unified School District. Ms. Getridge also served as Associate Superintendent of Curriculum and Instruction in Oakland and as Director of Education Programs for the Alameda (CA) County Office of Education.

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Todd W. Buchardt. Todd W. Buchardt, age 51, currently serves as our Senior Vice President, General Counsel and Secretary. Mr. Buchardt served VLCY as Senior Vice President since November 2002, Vice President since March 2000, and General Counsel and Secretary since 1998. Before joining VLCY, Mr. Buchardt held various legal positions with First Data Corporation from 1986 to 1998.

Robert H. Pasternack, Ph.D. The Honorable Robert H. Pasternack, Ph.D., age 61, currently serves as our Senior Vice President of Special Education. Dr. Pasternack served VLCY in the same capacity from August 2006. Dr. Pasternack has over 40 years experience in public education. Before joining VLCY, Dr. Pasternack served as Assistant Secretary for the Office of Special Education and Rehabilitative Services (OSERS) at the U.S. Department of Education from 2001 to 2004. In addition, Dr. Pasternack served on the President s Commission on Excellence in Special Education and the President s Mental Health Commission and as the Chair of the Federal Interagency Coordinating Committee during his appointment as the Assistant Secretary. Prior to being appointed to this position, Dr. Pasternack was the State Director of Special Education for the State of New Mexico and also served as a Superintendent and first grade teacher. Dr. Pasternack is a nationally certified school psychologist, a certified educational diagnostician, a certified school administrator, and a certified teacher (K-12).

Proprietary Rights

We regard a substantial portion of our technologies and content as proprietary and rely primarily on a combination of patent, copyright, trademark and trade secret laws, and employee or vendor non-disclosure agreements, to protect our rights.

We have developed relationships with authors who are known for their expertise in improving the cognitive and behavioral performance of at-risk and special education students. Many authors are leaders in their respective fields, such as literacy, mathematics, and positive school climate. These authors are engaged by us to develop content and then to refine that content once feedback is obtained from our customers. We act as exclusive agents for and, in most instances, own the intellectual property from these well-known authors, whereby we publish their works under a royalty arrangement. We also derive a substantial amount of our curriculum content through in-house development efforts. To a much lesser degree, we also license from third parties published works, certain technology content or services upon which we rely to deliver certain products and services. Curriculum developed in-house or developed through the use of independent contractors is our proprietary property. Certain curriculum might be augmented or complemented with third party products, which may include printed materials, videos or photographs. This additional third party content may be sourced from various providers who retain the appropriate trademarks and copyrights to the material and agree to our use under a nonexclusive, fee-based arrangement.

We use U.S.-registered trademarks to identify various products which we develop. The trademarks survive as long as they are in use and the registration of these trademarks is renewed.

Website Access to Company Reports

We make available free of charge through our website, www.cambiumlearning.com, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, Forms 3, 4 and 5 filed on behalf of our directors, officers and other affiliated persons, and all amendments to those reports as soon as reasonably practical after such material is electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). We also will provide any of the foregoing information without charge upon written request to Cambium Learning Group, Inc., 17855 North Dallas Parkway, Suite 400, Dallas, Texas 75287, Attention: Investor Relations.

We are providing the address to our website solely for the information of our investors. Our website and the information contained therein or incorporated therein are not intended to be incorporated into this Annual Report on Form 10-K.

Code of Ethics

We have adopted a Senior Financial Officers Code of Ethics and a Code of Business Conduct to promote such standards as (1) honest and ethical conduct; (2) full, fair, accurate, timely and understandable disclosure in our periodic reports; and (3) compliance with applicable governmental rules and regulations. Amendments to, or waivers from, the code of ethics will be posted on our website. A copy of the code of ethics and the code of business conduct are posted on our website, www.cambiumlearning.com, within the Investor Relations section under the heading Corporate Governance . The code of ethics is also available in print to anyone who requests it by writing to the

Company at the following address: Cambium Learning Group, Inc., 17855 North Dallas Parkway, Suite 400, Dallas, Texas 75287, Attention: Investor Relations.

We have also implemented a whistleblower hotline, as required under the Sarbanes-Oxley Act of 2002, by engaging a third party service that provides anonymous reporting for serious workplace ethical issues via telephone and/or the Internet.

Item 1A. Risk Factors.

This section should be read in conjunction with the Consolidated Financial Statements of the Company and the notes thereto included in this Annual Report on Form 10-K for the year ended December 31, 2010.

Risks Related to our Business

Changes in funding for public schools could cause the demand for our products to decrease.

We derive a significant portion of our revenues from public schools, which are heavily dependent on federal, state and local government funding. Budget cuts, curtailments, delays, changes in leadership, shifts in priorities or general reductions in funding could reduce or delay our revenues. Funding difficulties experienced by schools, which have been exacerbated by the current economic downturn and state budget deficits (most state budget fiscal years end on June 30), could also cause those institutions to demand price reductions and could slow or reduce purchases of intervention products, which in turn could materially harm our business. Our business may be adversely affected by changes in educational funding at the federal, state or local level, resulting from changes in legislation, changes in state procurement processes, changes in government leadership, emergence of other funding or legislative priorities and changes in the condition of the local, state or U.S. economy. Some of our transaction opportunities have been related to ARRA stimulus funds available to our customers. Funds allocated by the ARRA will be spent by September 2011, this may hinder our ability to consummate certain transactions.

We receive significant revenues from certain states and reductions in public school education spending in those states could cause the demand for our products to decrease.

In 2010, we derived significant revenues from the following three states in the following approximate percentages: California 14%; Florida 8%; and Texas 8%. To some extent, we expect the economic situation faced by these states to continue to have a depressive effect on public school spending. If that is the case, our sales to these states could be materially reduced which could harm our business and financial condition.

Changes in school procurement policies may adversely affect our business.

The school appropriations process is often slow, unpredictable and subject to many factors outside of our control. School districts choose to procure educational materials in various ways which can change quickly necessitating a change in our sales strategy or sales investments. Districts and states may switch procurement decisions from a centralized (district-wide) to a decentralized (school by school) decision, states may switch from state-wide standard adoptions to flexible district level procurement, and customers could increasingly utilize competitive requests for proposals (RFP) or procurement via the Internet. Any of these changes could cause us to modify our sales strategy or cause us to expend greater sales effort to win business and if we are slow to respond the result could be a material loss of market share.

Our failure to maintain or expand our customer base could diminish incremental revenues from certain products.

We sell products that require customers to purchase certain replenishment materials year after year. Sales of these consumable items and replacement materials typically involve considerably less revenue than the initial sale. Furthermore, we provide products and services under arrangements that are terminable at will. Our ability to maintain and grow revenues and profitability will depend significantly upon the ability to maintain and grow our existing customer base and to acquire new customers. If we are not successful in continuing to acquire additional customers or maintaining our existing customers, our earnings may be adversely affected.

Our revenue growth and profitability will depend, in part, on our ability to attract and retain productive resellers.

Historically, we have used resellers as a sales channel for certain products, primarily Kurzweil Educational Systems and Intellitools. Entities that resell our products may discontinue selling the products or choose to substitute a competing product, or they may not dedicate sufficient attention and resources to our products that they are selling. Should any of our current or future resellers perform below our expectations, or should we lose one or more relationships with one of our current resellers, or fail to establish relationships with additional or replacement resellers, our revenues and profitability could be adversely affected.

Our revenues and profitability will depend on our ability to continue to develop new products and services that appeal to customers and end users and respond to changing customer preferences.

We operate in markets that are characterized by continuous and rapid change, including product introductions and enhancements, changes in customer demands and evolving industry standards. In a period of rapid change, the technological and curriculum life cycles of our products are difficult to estimate. The demand for some of our more "mature" products and services has begun to migrate to other, newer products and services. As a result, we will need to continuously reassess our product and service offerings. We could make investments in new products and services that may not be profitable, or whose profitability may be significantly lower than what we have experienced historically. If we are unable to anticipate trends and develop new products or services responding to changing customer preferences, our revenues and profitability could be adversely affected. Our business could be harmed if we are unable to develop new products and invest in existing products in an appropriate balance to keep our company competitive in the marketplace.

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Our business is anticipated to be seasonal and our operating results are anticipated to fluctuate seasonally.

Our business is likely to be subject to seasonal fluctuations. We generally expect revenue and income from operations to be higher during the second and third calendar quarters. In addition, the quarterly results of operations have fluctuated in the past, and our quarterly results of operations can be expected to continue to fluctuate in the future.

If we are unable to compete effectively, we may be unable to successfully attract and retain customers and our profitability could be materially harmed.

The market for our products and services is highly competitive and is characterized by frequent product developments and enhancements of existing products. Several of our competitors have substantially greater financial, research and development, manufacturing and marketing resources than us as well as greater name recognition and larger customer bases. Accordingly, our competitors may be able to respond more quickly to new technologies and changes in customer requirements, have more favorable access to suppliers and devote greater resources to the development and sale of their products and services. These competitors may be successful in developing products and services that are more effective or less costly than any products or services that we may provide currently or may develop in the future.

Our intellectual property protection may be inadequate, which may allow others to use our technologies and thereby reduce our ability to compete.

The technology underlying our services and products may be vulnerable to attack by our competitors. We rely on a combination of trademark, copyright and trade secret laws, employee and third party nondisclosure agreements and other contracts to establish and protect our technology and other intellectual property rights. The steps that we have taken in order to protect our proprietary technology may not be adequate to prevent misappropriation of our technology or to prevent third parties from developing similar technology independently.

Technology content licensed from third parties may not continue to be available.

We license from third parties technology content upon which we rely to deliver products and services to customers. This technology may not continue to be available to us on commercially reasonable terms or at all. Moreover, we may face claims from persons who claim that our licensed technologies infringe upon or violate those persons proprietary rights. These types of claims, regardless of the outcome, may be costly to defend and may divert management s efforts and resources.

Our products could infringe on the intellectual property of others, which may cause us to engage in costly litigation and to pay substantial damages or restrict or prohibit us from selling our products.

Third parties may assert infringement or other intellectual property claims against us based on their intellectual property rights. If any of these claims are successful, we may be required to pay substantial damages, possibly including treble damages, for past infringement. We also may be prohibited from selling our products or providing certain content without first obtaining a license from the third party, which, if available at all, may require us to pay additional fees or royalties to the third party. Even if infringement claims against us are without merit, defending a lawsuit takes significant time, is often expensive and may divert management attention away from other business concerns.

Our success will depend in part on our ability to attract and retain key personnel.

Our success depends in part on our ability to attract and retain highly qualified executives and management, as well as creative and technical personnel. Members of our senior management team have substantial industry experience that is critical to the execution of our business plan. If they or other key employees were to leave the Company, and we were unable to find qualified and affordable replacements for these individuals, our business could be harmed materially.

Increases in operating costs and expenses, many of which are beyond our control, could materially and adversely affect our operating performance.

We must control our costs and expenses to be profitable and to generate enough cash flow to service our indebtedness. Some of our costs are variable and subject to factors beyond our control; in particular, increases in paper, fuel, and employee compensation expenses could have a significant impact on our business.

Merger and acquisition activity could adversely affect our operations.
We may seek potential acquisitions of products, technologies and businesses in the education industry that could complement or expand our current product and service offerings and businesses. In the event that we identify appropriate acquisition candidates, we may not be able to successfully negotiate, finance or integrate the acquired products, technologies or businesses. Furthermore, such an acquisition could cause a diversion of management s time and resources. Any particular acquisition, if completed, may materially and adversely affect our business, results of operations, financial condition or liquidity.
We could experience system failures, software errors or capacity constraints, any of which would cause interruptions in the delivery of electronic content to customers and ultimately may cause us to lose customers.
Any significant delays, disruptions or failures in the systems, or errors in the software, that we use for the technology-based component of our products, as well as for internal operations, could harm our business materially. We have occasionally suffered computer and telecommunication outages or related problems in the past. The growth of our customer base, as well as the number of websites we provide, could strain our systems in the future and will likely magnify the consequences of any computer and telecommunications problems that we may experience. However, destruction or disruption of data center sites could cause a system-wide failure. Although we maintain property insurance on these premises, claims for any system failure could exceed our coverage. In addition, our products could be affected by failures associated with third party hosting providers or by failures of third party technology used in our products, and we may have no control over remedying these failures.
Our systems face security risks and we need to ensure the privacy of our customers.
Our systems and websites may be vulnerable to unauthorized access by hackers, computer viruses and other disruptive problems. Any security breaches or problems could lead to misappropriation of our customers information, our websites, our intellectual property and other rights, as well as disruption in the use of our systems and websites. Any security breach related to our websites could tarnish our reputation and expose us to damages and litigation. We also may incur significant costs to maintain our security precautions or to correct problems caused by security breaches. Furthermore, to maintain these security measures, we may be required to monitor our customers access to our websites, which may cause disruption to customers use of our systems and websites. These disruptions and interruptions could harm our business materially.
We have a single distribution center and could experience significant disruption of business and ultimately lose customers in the event it was damaged, destroyed or experienced technological failure.
We store and distribute the majority of our printed materials through a single warehouse in Frederick, Colorado. In the event that this distribution facility was damaged, destroyed or experienced technological failure, we would be delayed in responding to customer requests. Customers often purchase materials very close to the school year and such delivery delays could cause our customers to turn to competitors for products they need immediately. While we maintain adequate property insurance, the loss of customers could have a long-term, detrimental impact on our reputation and business.
Failure to efficiently and effectively manage our direct marketing initiatives could negatively affect our business.
The growth of several of our products depends on our ability to efficiently and effectively manage our direct marketing initiatives. We use various direct marketing strategies to market our products, including direct mailings, catalogs, online marketing, search engine optimization and telemarketing. In each case, we rely on a database containing information about our current and prospective customers to develop and implement direct marketing campaigns. We face the risk of unauthorized access to our customer database or the corruption of our database as a result of technology failure or otherwise. Failure to maintain, protect and properly utilize the available information in the database could lead to decreased revenues and could materially and adversely affect our results of operations, financial condition and liquidity.
Both Cambium and VLCY have been subjected to material accounting irregularities in recent years, which could result in enhanced regulatory scrutiny in the future and could undermine the confidence that some investors may have in the integrity of our financial statements.
During 2008, Cambium discovered certain irregularities relating to the control and use of cash and certain other general ledger items which revealed a substantial misappropriation of assets spanning fiscal 2004 through fiscal 2008.

These irregularities were perpetrated by a former employee, resulting in embezzlement losses, before the effect of income taxes, amounting to $14.0 million. See Note 3 to the consolidated financial statements. In early 2006, VLCY (then known as ProQuest Company) announced that it had identified potential material irregularities in its accounting that were to be investigated by VLCY s audit committee, with the assistance of outside experts. In July 2006, VLCY announced that its audit committee had completed its investigation and issued a statement that detailed the key findings, including that the evidence indicated that a single individual was responsible for the misstatements. After completion of that investigation, VLCY restated certain of its previously filed financial statements. The fact that both Cambium and VLCY have experienced material accounting irregularities within the past seven years could result in enhanced regulatory scrutiny and could impair the confidence of investors, financing sources, research analysts and potential acquirers in the integrity of our financial statements.

Risks Related to Debt and Ownership of our Common Stock

We do not foresee paying cash dividends in the foreseeable future and, as a result, our investors sole source of gain, if any, will depend on capital appreciation, if any.

We do not plan to declare or pay any cash dividends on our shares of common stock in the foreseeable future and currently intend to retain future earnings, if any, for future operation, debt reduction and expansion. Any decision to declare and pay dividends in the future will be made at the discretion of our board of directors and will depend on, among other things, our results of operations, financial condition, restrictions imposed by applicable law, business and investment strategy, contractual limitations and other factors that our board of directors may deem relevant. In addition, our ability to pay dividends may be limited by covenants of any existing and future indebtedness we or our subsidiaries incur, including the 9.75% senior secured notes (described below). As a result, our stockholders may not receive any return on an investment in our common stock unless they sell our common stock for a price greater than that which they paid for it. Moreover, investors may not be able to resell their shares of the Company at or above the price they paid for them.

Our majority stockholder has a contractual right to increase its percentage of ownership in our company which, if exercised, would dilute the ownership percentage of all other stockholders and could reduce the price of our common stock.

Our majority stockholder, VSS-Cambium Holdings III, LLC, the holding company through which VSS owns its interest in the Company, and funds managed or controlled by VSS, have the right to increase their percentage ownership of our company at a discount from market price. Under a stockholders agreement entered into in connection with the mergers, at any time and from time to time at or prior to December 8, 2011, VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS have the right to purchase from us, in cash, at a 10% discount from market price, up to the lesser of 7,500,000 shares of our common stock or shares of our common stock with an aggregate purchase price of $20 million. VSS-Cambium Holdings III, LLC also holds a warrant which was, or will become upon issuance, exercisable for up to 560,137 shares of our common stock at December 31, 2010 and may become exercisable for more shares in the future. If VSS-Cambium Holdings III, LLC decides to exercise its right to purchase shares of our common stock under the stockholders agreement or exercises its warrant, it could result in a reduction to the price of our common stock.

The existence of a majority stockholder may adversely affect the market price of our common stock and could delay, hinder or prevent a change in corporate control or result in the entrenchment of management and the board of directors, and our majority stockholder has a contractual right to maintain its percentage ownership in our company.

VSS-Cambium Holdings III, LLC, owns a majority of our outstanding common stock. Accordingly, VSS-Cambium Holdings III, LLC will likely have the ability to determine the outcome of matters submitted to our stockholders for approval, including the election and removal of directors and any merger, consolidation or sale of all or substantially all our assets. In addition, VSS-Cambium Holdings III, LLC will likely have the ability to control our management, affairs and operations. Accordingly, this concentration of ownership may harm the market price of our common stock by delaying, deferring or preventing a change in control or impeding a merger, consolidation, takeover or other business combination.

The ownership of a large block of stock by a single stockholder may reduce our market liquidity. Should VSS-Cambium Holdings III, LLC determine to sell any of its position in the future, sales of substantial amounts of our common stock on the market, or even the possibility of these sales, may adversely affect the market price of our common stock. These sales, or even the possibility of these sales, also may make it more difficult for us to raise capital through the issuance of equity securities at a time and at a price we deem appropriate.

Moreover, VSS-Cambium Holdings III, LLC has a contractual right to maintain its percentage ownership in our company. Specifically, under the terms of a stockholders agreement entered into in connection with the mergers, if we were to engage in a new issuance of our securities, VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS would have preemptive rights to purchase an amount of our securities that would enable them to maintain their same collective percentage of ownership in our company following the new issuance. VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS would have these preemptive rights for so long as those entities collectively beneficially own, in the aggregate, at least 25% of the outstanding shares of our common stock. Thus, while other holders of our securities would risk suffering a reduction in percentage ownership in connection with a new issuance of securities by us, VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS would, through this preemptive right, have the opportunity to avoid a reduction in percentage ownership.

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We are a controlled company within the meaning of the NASDAQ rules and, as a result, qualify for, and rely on, exemptions from various corporate governance standards, which limits the presence of independent directors on our board of directors and board committees.

Due to the fact that VSS-Cambium Holdings III, LLC owns a majority of our outstanding common stock, we are deemed a controlled company for purposes of NASDAQ Rule 5615(c)(2). Under this rule, a company of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company is a controlled company and is exempt from certain NASDAQ corporate governance requirements, including requirements that a majority of the board of directors consist of independent directors, that compensation of officers be determined or recommended to the board of directors by a majority of independent directors or by a compensation committee that is composed entirely of independent directors and that director nominees be selected or recommended for selection by a majority of the independent directors or by a nominating committee composed solely of independent directors. We intend to rely upon these exemptions. Accordingly, our stockholders may not have the same protections afforded to stockholders of other companies that are required to comply fully with the NASDAQ rules.

Since the controlled company exemption does not extend to the composition of audit committees, we are required to have an audit committee that consists of at least three directors, each of whom must be independent based on independence criteria set forth in Rule 10A-3 of the Securities Exchange Act of 1934 (the Exchange Act). Our board of directors has adopted an audit committee charter which will govern our audit committee. These three directors must also satisfy the requirements set forth in NASDAQ Rule 5605(a) and (c). The audit committee is currently composed entirely of independent directors.

Certain attributes of our stock may make the stock less liquid.

Certain attributes of our stock, including price, low trading volumes, and the existence of a majority stockholder, may make investments in our stock less liquid. These attributes could result in increased volatility in the price of our stock regardless of our performance, and could make it difficult to sell our shares in significant volumes at a favorable price. The liquidity of our stock could be further reduced if we repurchase shares.

We may seek to raise additional funds, finance additional acquisitions or develop strategic relationships by issuing additional securities, including capital stock.

In the future, we may seek to raise additional funds, finance additional acquisitions or develop or engage in strategic relationships by issuing equity or debt securities. The issuance of equity securities, including debt securities that are convertible into equity, would reduce the percentage ownership of our existing stockholders. Furthermore, any newly issued equity securities could have rights, preferences and privileges senior to those of the holders of our common stock. The issuance of new debt securities could also subject us to covenants which constrain our ability to grow or otherwise take steps that may be favored by our holders of common stock.

Under the terms of a stockholders agreement that we entered into on December 8, 2009 in compliance with the mergers, so long as our former sole stockholder and funds controlled by VSS beneficially own in the aggregate at least 25% of the outstanding shares of our common stock, they will have preemptive rights which generally give them the opportunity to purchase an amount of our securities in a new issuance of securities by us that would enable them to maintain their same collective percentage ownership in us following the new issuance. Thus, while other stockholders risk suffering a reduction in percentage ownership in connection with an issuance of securities by us, VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS will have the opportunity to avoid a reduction in percentage ownership. In addition, under the stockholders agreement, until December 8, 2011, VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS will have the right to purchase from us, in cash, at a 10% discount from market price, up to the lesser of 7,500,000 shares of our common stock or shares of our common stock with a discounted purchase price of $20 million. Any purchases of stock at a discount from the market price may dilute the ownership percentage and equity ownership of all other stockholders.

Provisions of our organizational documents and Delaware law may delay or deter a change of control.

Our organizational documents contain provisions that may have the effect of discouraging, delaying or preventing a change of control of, or unsolicited acquisition proposals for, our company. These include provisions that:

- vest our board of directors with the sole power to set the number of directors of our company;

provide that our board of directors will be elected on a staggered term basis, so that generally only one-third of the board will be elected at each annual meeting of stockholders;

limit the persons that may call special meetings of stockholders;

establish advance notice requirements for stockholder proposals and director nominations; and

limit stockholder action by written consent.

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Also, our board of directors has the authority to issue shares of preferred stock in one or more series and to fix the rights and preferences of these shares, all without stockholder approval. Any series of preferred stock is likely to be senior to our common stock with respect to dividends, liquidation rights and, possibly, voting rights. The ability of our board of directors to issue preferred stock also could have the effect of discouraging unsolicited acquisition proposals, thus adversely affecting the market price of our common stock.

In addition, Delaware corporate law makes it difficult for stockholders that recently have acquired a large interest in a corporation to cause the merger or acquisition of the corporation against the directors wishes. Under Section 203 of the Delaware General Corporate Law (the DGCL), a Delaware corporation such as the Company may not engage in any merger or other business combination with an interested stockholder or such stockholder s affiliates or associates for a period of three years following the date that such stockholder became an interested stockholder, except in limited circumstances, including by approval of the corporation s board of directors.

We have a significant amount of senior secured debt and will have the obligation to make interest payments and comply with restrictions contained in the credit agreements with our senior secured lenders.

In February 2011, we closed an offering of $175 million aggregate principal amount of 9.75% senior secured notes due 2017, as well as a new revolving credit facility. We are subject to risks associated with substantial indebtedness, including the risk that we will not be able to refinance existing indebtedness when it becomes due, the risk that we would not be able to secure alternative financing if we are unable to comply with the debt covenants or if we were to experience an event of default, and the risk that our cash flows from operations are insufficient to make scheduled interest payments. We are required to make interest payments semi-annually in arrears on each February 15 and August 15, commencing on August 15, 2011. If we are unable to generate sufficient cash flow from operations in the future to service our debt, we may be required to refinance all or a portion of our debt. However, we may not be able to obtain any such new or additional financing on favorable terms or at all.

The indenture governing the notes and the credit agreement governing our new revolving credit facility contain various covenants that limit our ability to, among other things, incur or guarantee additional indebtedness; pay dividends and make other restricted payments; incur restrictions on the payment of dividends or other distributions from our restricted subsidiaries; create or incur certain liens; make certain investments; transfer or sell assets; enter into operating leases; engage in transactions with affiliates; and merge or consolidate with other companies or transfer all or substantially all of our or their assets.

Further, upon the occurrence of specific types of change of control events, we will be required to offer to repurchase outstanding notes at 101% of their principal amount plus accrued and unpaid interest. The source of funds for any such purchase of the notes will be our available cash or cash generated from our and our subsidiaries operations or other sources, including borrowings, sales of assets or sales or equity. Our failure to repurchase the notes upon a change of control would cause a default under the indenture governing the notes and a cross default under our new revolving credit facility.

Borrowing capacity under Cambium Learning, Inc. s revolving credit facility may affect our ability to finance our operations.

In February 2011, our wholly owned subsidiary, Cambium Learning, Inc. entered into a new asset-backed revolving credit facility, consisting of a four-year $40.0 million revolving credit facility, which includes a $5.0 million subfacility for swing line loans and a $5.0 million subfacility for letters of credit. Our ability to borrow funds under this facility is limited by a borrowing base determined relative to the value, calculated periodically, of eligible accounts receivable and eligible inventory. Our ability to borrow funds under the revolving credit facility is also conditioned upon our compliance with a financial covenant that generally requires us to maintain, on a consolidated basis, either (i) excess availability of at least the greater of $8 million and 15% of the revolver commitment or (ii) a fixed charge coverage ratio of 1.1 to 1.0. Our business is seasonal and any inability to borrow funds under the revolving credit facility could affect our ability to finance our operations.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Our principal corporate office is located in Dallas, Texas. We lease office and warehouse facilities in Dallas, Texas; Charlottesville, Virginia; Tucson, Arizona; Frederick, Colorado; Natick, Massachusetts and Ann Arbor, Michigan. The Frederick, Colorado warehouse is under a build-to-suit lease and so is included in our land and building but is not considered owned for purposes of the table below.

The following table provides summary information in square feet with respect to these facilities as of December 31, 2010.

	Total (sq ft)
Owned	
Leased	327,543
Total	327,543

We believe the buildings and equipment used in our continuing operations generally to be in good condition and adequate for our current needs and that additional space will be available as needed.

Item 3. Legal Proceedings.

We are not presently engaged in any pending legal proceeding material to our financial condition, results of operations or liquidity.

Item 4. (Removed and Reserved).

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information: Our common stock is traded on the NASDAQ Global Market under the symbol ABCD. Below are the high and low sale prices for each quarter since our common stock commenced publicly trading on December 9, 2009.

	2010		2009	
Fiscal Quarter	**High**	**Low**	**High**	**Low**
First	$ 4.20	$ 3.41	N/A	N/A
Second	5.59	3.42	N/A	N/A
Third	3.76	2.77	N/A	N/A
Fourth (Since Dec 9, 2009)	3.55	2.67	$ 14.80	$ 3.62

Record Holders: As of March 4, 2011, there were 124 holders of record of our common stock.

Purchases Of Equity Securities: We made no repurchases of our equity securities in the fiscal year ended December 31, 2010.

Dividends: We have not declared or paid any cash dividends to our stockholders. Any future determination to pay dividends, if any, will be at the discretion of our board of directors. We do not presently expect to pay any dividends.

Securities Authorized for Issuance Under Equity Compensation Plans: We have securities authorized for issuance under the Cambium Learning Group, Inc. 2009 Equity Incentive Plan (Incentive Plan). In connection with the then pending merger with VLCY, on July 31, 2009, the Company s board of directors and sole stockholder approved the Incentive Plan. The general purposes of the Incentive Plan are to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentives to employees, directors and consultants, and to promote the success of the Company.

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Securities authorized for issuance under equity compensation plans at December 31, 2010 are as follows:
(in thousands, except per share amounts)

Plan Category	Number of securities to be issued upon exercise of outstanding options and rights	Weighted-average exercise price of outstanding options and rights	Number of securities remaining available for future issuance under equity incentive plan (a)
Equity compensation plans approved by security holders	3,957	$ 5.19	1,033
Equity compensation plans not approved by security holders			
Total	3,957	$ 5.19	1,033

(a) Excludes securities reflected in the first column, Number of securities to be issued upon exercise of outstanding options and rights, and outstanding restricted stock.

Recent Sales of Unregistered Securities: There were no Company securities that were issued or sold by the Company during the period covered by this report that were not registered under the Securities Act of 1933, as amended (the Securities Act).

Stock Performance Graph: The following graph compares the total cumulative shareholder return of the Company s common stock with the total cumulative return of the NASDAQ Composite Index and a customized Peer Group Index. Measurement points include December 9, 2009, the date that our stock began publicly trading, and the last trading day of the quarters ended December 31, 2009, March 31, 2010, June 30, 2010, September 30, 2010 and December 31, 2010. Total cumulative shareholder return assumes $100 invested on December 9, 2009 in the Company s common stock, the NASDAQ Composite Index and the Peer Group Index, respectively, and reinvestment of any dividends. Our Peer Group Index is composed of the following companies: K12, Inc., The McGraw-Hill Companies, Pearson PLC, Renaissance Learning, Scholastic, and School Specialty. Historical stock price performance should not be relied upon as an indication of future stock performance.

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Item 6. Selected Financial Data.

The tables below present summary selected historical consolidated financial data derived from our consolidated financial statements prepared in accordance with GAAP. You should read the information set forth below in conjunction with our consolidated financial statements and related notes, management s discussion and analysis of financial condition and results of operations and other financial information presented elsewhere herein.

The summary selected historical consolidated financial data for the year ended December 31, 2006, the period from January 1, 2007 through April 11, 2007 (the 2007 predecessor period), the period from January 29, 2007 through December 31, 2007 (the 2007 successor period), the year ended December 31, 2008, the year ended December 31, 2009 and the year ended December 31, 2010 have been derived from our audited consolidated financial statements.

On December 8, 2009, we completed the mergers of VLCY and Cambium into two of our wholly-owned subsidiaries, resulting in VLCY and Cambium becoming our wholly-owned subsidiaries. The transaction was accounted for as an acquisition of VLCY by Cambium, as that term is used under U.S. GAAP, for accounting and financial reporting purposes under the applicable accounting guidance for business combinations. As a result, the historical financial statements of Cambium have become the historical financial statements of the Company and the results of VLCY are included from the merger date.

(in thousands, except per share data)	**Year Ended December 31, 2010**	**Year Ended December 31, 2009**	**Year Ended 31, December 2008**	**Successor Period from January 29, 2007 (Inception) through December 31, 2007(1)**	**Predecessor Period from January 1, 2007 through April 11, 2007**	**Predecessor Year Ended December 31, 2006**
Statement of Operations Data:						
Product revenues	**$ 160,778**	**$ 90,385**	**$ 89,207**	**$ 71,266**	**$ 15,238**	**$ 92,882**
Service revenues	**20,482**	**10,663**	**10,524**	**9,581**	**3,176**	**13,542**
Net revenues	**181,260**	**101,048**	**99,731**	**80,847**	**18,414**	**106,424**
Total operating expenses, excluding in-process research and development, impairment, and embezzlement	**(181,528)**	**(115,108)**	**(104,648)**	**(81,305)**	**(32,179)**	**(97,955)**
Acquired in-process research and development				**(890)**		
Goodwill impairment(3)		**(9,105)**	**(75,966)**			
Embezzlement and related recoveries (expense)(2)	**353**	**(129)**	**(7,254)**	**(5,732)**	**(1,000)**	**(3,261)**
Income (loss) before interest, other income (expense), and income taxes	**85**	**(23,294)**	**(88,137)**	**(7,080)**	**(14,765)**	**5,208**
Gain from settlement with previous stockholders(4)			**30,202**			

Net (loss) income	**(15,950)**	**(35,765)**	**(69,560)**	**(13,931)**	**(11,812)**	**440**
Net (loss) income per common share basic and diluted	**$ (0.36)**	**$ (1.63)**	**$ (3.39)**	**$ (0.68)**	**$ (4.34)**	**$ 0.16**

			As of:		
(in thousands)	**December 31, 2010**	**December 31, 2009**	**December 31, 2008**	**December 31, 2007**	**December 31, 2006**
Balance Sheet Data:					
Cash and cash equivalents	$ 11,831	$ 13,345	$ 2,418	$ 1,206	$ 1,642
Total current assets	76,177	74,316	31,617	26,601	25,007
Total assets	383,062	393,841	270,477	369,138	138,028
Total current liabilities	66,774	58,366	16,360	16,849	26,871
Total long term debt, less current portion	150,850	150,487	153,787	176,402	17,500
Total liabilities	259,050	254,069	202,273	239,058	59,133
Total members interest and stockholders equity	124,012	139,772	68,204	130,080	78,895

Footnotes to the Selected Financial Data:

(1) On January 29, 2007, VSS-Cambium Holdings, LLC was formed for the purpose of acquiring all of the capital stock of Cambium Learning. That acquisition was completed on April 12, 2007. The consolidated financial statements present the Company as of December 31, 2007 (Successor basis reflecting activity of the Company from January 29, 2007 and including the results of Cambium Learning from April 12, 2007) and the period January 1, 2007 through April 11, 2007 (Predecessor basis for the period prior to Company s acquiring Cambium Learning).

(2) We discovered in 2008 that a former employee had perpetrated a significant misappropriation of assets during a period beginning in 2004 and extending through April 2008.

(3) Reflects the non-cash effect of the impairment write-down of goodwill during 2009 and 2008 resulting from a reduction in the fair value of assets.

(4) For fiscal 2008, we received a settlement from our previous stockholders relating to the embezzlement we suffered. For further information, see Note 3 to our Consolidated Financial Statements.

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

This section should be read in conjunction with the Consolidated Financial Statements of the Company and the notes thereto included in this Annual Report on Form 10-K for the year ended December 31, 2010.

Organization of Information

This section includes the following sections:

- Overview
- Results of Operations
- Year Ended December 31, 2010 Compared to Year Ended December 31, 2009
- Year Ended December 31, 2009 Compared to Year Ended December 31, 2008
- Liquidity and Capital Resources
- Non-GAAP Measures
- Capital Expenditures and Outlook
- Commitments and Contractual Obligations
- Off-Balance Sheet Arrangements
- Critical Accounting Policies and Estimates
- Recently Issued Financial Accounting Standards

Overview

On December 8, 2009, we completed the business combination of Cambium and VLCY as contemplated by the Agreement and Plan of Mergers, dated as of June 20, 2009, among us, VLCY, Vowel Acquisition Corp., our wholly-owned subsidiary, Cambium, a wholly-owned subsidiary of VSS-Cambium Holdings III, LLC, Consonant Acquisition Corp., our wholly owned subsidiary, and Vowel Representative, LLC, solely in its capacity as stockholders representative. We refer to this agreement and plan of mergers in this report as the merger agreement. Pursuant to the merger agreement, we acquired all of the common stock of each of Cambium and VLCY through the merger of Consonant Acquisition Corp. with and into Cambium, with Cambium continuing as the surviving corporation (the Cambium Merger), and the concurrent merger of Vowel Acquisition Corp. with and into VLCY, with VLCY continuing as the surviving corporation (the Voyager Merger). As a result of the effectiveness of the mergers, Cambium and VLCY became our wholly owned subsidiaries.

Under the terms of the merger agreement, each outstanding share of VLCY s common stock was converted in the Voyager Merger into the right to receive at the election of each stockholder, either (i) $6.50 in cash, without interest, or (ii) one share of our common stock, plus, regardless of the election made, additional consideration consisting of cash and a contingent value right, as described in the merger agreement. The amount of cash available to satisfy cash elections by the VLCY stockholders was limited to $67.5 million in the aggregate. The cash consideration payable to the former VLCY stockholders was insufficient to accommodate all of the cash elections that were made. Accordingly, the amount of cash paid to the former VLCY stockholders who elected to exchange shares of VLCY common stock for cash was reduced, pro rata, in accordance with agreed procedures set forth in the merger agreement. Pursuant to these procedures, we paid $67.5 million in cash to the former holders of VLCY s common stock and issued to those stockholders a total of 19.5 million shares of common stock. The cash consideration paid to the former VLCY stockholders consisted of $25 million contributed by VSS-Cambium Holdings III, LLC and $42.5 million contributed by VLCY. In exchange for its contribution of $25 million, VSS-Cambium Holdings III, LLC received 3.8 million shares of our common stock issued at the ascribed value of $6.50 per share. The shares of Cambium s common stock held by VSS-Cambium Holdings III, LLC, its sole stockholder, were converted in the Cambium Merger into the right to receive 20.5 million shares of the our common stock. In addition, as part of the merger consideration, VSS-Cambium Holdings III, LLC received a warrant to purchase a number of shares of our common stock determined by a formula set forth in the merger agreement, which is currently equal to 0.6 million shares. In connection with the consummation of this transaction we entered into a stockholders agreement pursuant to which we granted VSS-Cambium Holdings III, LLC and funds managed and controlled by VSS the right to purchase up to 7.5 million shares of our common stock as provided for in the stockholders agreement as well as certain preemptive rights set forth therein.

The merger transaction was accounted for as an acquisition of VLCY by Cambium, as that term is used under U.S. GAAP, for accounting and financial reporting purposes under the applicable accounting guidance for business combinations. In making this determination, management considered that (a) the newly developed entity did not have any significant pre-combination activity and, therefore, did not qualify to be the accounting acquirer, and (b) the former sole stockholder of Cambium is the majority holder of the combined entity, while the prior owners of VLCY became minority holders in the combined entity. As a result, the historical financial statements of Cambium have become the historical financial statements of the Company. The results of VLCY are included in the Company s operations beginning with the December 8, 2009 merger date; therefore, the 2009 financials include VLCY for the last 23 days of that year and the results of the Company for the full year.

Prior to the merger transaction completed on December 8, 2009, we had two reportable segments: Published Products and Learning Technologies. Subsequent to the merger transaction, we operate as three reportable segments with separate management teams and infrastructures that offer various products and services, as follows:

Voyager, our comprehensive intervention business;

Sopris, our supplemental solutions education business; and

Cambium Learning Technologies, our technology-based education product business.

Unallocated shared services, such as accounting, legal, human resources and corporate-related items, are recorded in a Shared Services category. Depreciation and amortization expense, interest income and expense, other income and expense, and taxes are included in this category.

Our historical segment reporting results have been adjusted for comparative purposes to reflect the current organizational structure. These reclassifications required certain assumptions and estimates. See Note 21 to the Consolidated Financial Statements for further information on our reportable segments. Also, as a result of the merger transaction and change in segments, we made a number of changes to personnel and processes as part of an overall departmental restructuring. As certain functions were consolidated, some resources were shifted to other areas of the business. In particular, some general and administrative functions were merged and, where appropriate, certain resources were shifted to customer facing functions, which are classified as cost of revenues. These changes may affect comparability of pre-merger and post-merger periods.

Results of Operations

Fiscal Year 2010 Compared to Fiscal Year 2009

Highlights

During 2010, we continued to experience adverse conditions in the education funding environment, including the elimination of Reading First funding and the continued depressed circumstance of certain state and local budgets. As school districts rely upon state and local budgets, some of our customers have found it more challenging to secure alternative funding sources in the midst of these market conditions. Additionally, potential customers are more frequently utilizing a request for proposal process to complete purchases, which elongates the time required to complete a sale.

We have experienced some positive impact, both directly and indirectly, from the ARRA passed in February 2009. The ARRA provides significant new federal funding for various education initiatives through September 2011. While the education funding is for a broad set of education initiatives, we believe that schools and districts have directed, and may continue to direct, some of the new funding for programs which use our products. In some instances, if ARRA funding is not used directly for programs using our products, we may still be receiving an indirect benefit. When the ARRA funding is used to assist schools to meet their overall financial needs, other funds may be freed up to use for our programs. In 2009 and 2010 we have had success in securing orders which we believe are directly funded by ARRA funds. We believe that we received more directly funded ARRA purchases in 2010 versus 2009. This increase allowed us to partially offset a decline in order volume we experienced due to the end of Reading First funding in 2009. Order volume is an internal metric of shipments of our products and orders for online subscriptions and it serves as a leading indicator of net revenues.

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The following trends have had or may have an impact on our net revenues, profitability and EBITDA:

- Declines have been realized in our internal order volume metric due to the elimination of the Reading First program and the economic crisis faced by many states and local entities. To some extent, we expect the crisis will continue throughout the following quarters and have a continued depressive effect on general spending and therefore make order volume growth challenging.

- The stimulus funds drove several large multi-year deals in 2009 and 2010 which helped offset the wind down of Reading First.

- We expect continued growth in our online subscription-based products.

- We have experienced success growing our portfolio to address the math needs of the market, including products such as Vmath, Transitional Math and Gizmos (ExploreLearning). While the Gizmos products have continued strong growth in 2010, our other math-based products have been flat. We expect that the market for these products will continue to be strong and will return to growth in the future.

- We believe our product diversification will strengthen our ability to sustain market share in a troubled market and capture market share when the market recovers.

- We believe our focus on student outcomes through product usage and an overall partnership approach with the customer to implement our solutions, in the manner that the program was designed, results in higher student success rates, and such success, if achieved, will lead to customer retention and growth through reference sales.

- We believe there is a trend of student accountability resulting in greater funding being directed to at-risk children in the United States with new funding sources, such as Race to the Top, which could provide additional funds for our products.

- Successful efforts to reduce the Company s cost structure were undertaken in 2009 by both VLCY and Cambium, to better align our cost structure to current market conditions. In 2010, we achieved significant cost savings as part of an effort to achieve merger related synergies, which included a reduction in force. The Company will continue to seek ways to operate more efficiently, but the magnitude of the reductions in 2009 and 2010 are not expected to be replicated.

- We invested in several key areas in 2010. These are improved student data management systems, a separate dedicated sales force and development of an ecommerce engine for Sopris and continued investment in CLT, primarily in product development, sales and marketing.

- We expect to benefit from continuity of our leadership team and sales organization, who have now worked together for more than a year.

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The following tables set forth information regarding Cambium s net revenues, costs and expenses, and other components of our statements of operations. The results and percentages for the years ended December 31, 2010, 2009 and 2008 are set forth in the tables below. Due to purchase accounting adjustments, some amounts may not be comparable between each period presented.

	Year Ended December 31, 2010		**Year Ended December 31, 2009**		**Year Ended December 31, 2008**	
(in thousands)	**Amount**	**% of Revenues**	**Amount**	**% of Revenues**	**Amount**	**% of Revenues**
Net revenues:						
Product revenues						
Voyager	$ 100,412	55.4%	$ 44,329	43.9%	$ 40,424	40.5%
Sopris	22,249	12.3%	23,431	23.2%	27,495	27.6%
Cambium Learning Technologies	38,117	21.0%	22,625	22.4%	21,288	21.3%
Service revenues						
Voyager	17,527	9.7%	8,594	8.5%	7,924	7.9%
Sopris	2,487	1.4%	1,754	1.7%	2,217	2.2%
Cambium Learning Technologies	468	0.3%	315	0.3%	383	0.4%
Total net revenues	181,260	100.0%	101,048	100.0%	99,731	100.0%
Cost of revenues:						
Cost of product revenues						
Voyager	29,340	16.2%	10,678	10.6%	11,214	11.2%
Sopris	6,514	3.6%	6,350	6.3%	6,003	6.0%
Cambium Learning Technologies	4,334	2.4%	2,537	2.5%	3,029	3.0%
Shared Services	1,395	0.8%	26	0.0%		0.0%
Cost of service revenues						
Voyager	16,455	9.1%	5,992	5.9%	5,721	5.7%
Sopris	1,225	0.7%	1,093	1.1%	1,489	1.5%
Cambium Learning Technologies	628	0.3%	172	0.2%	253	0.3%
Amortization expense	28,511	15.7%	17,527	17.3%	15,966	16.0%
Total cost of revenues	88,402	48.8%	44,375	43.9%	43,675	43.8%
Research and development expense	10,558	5.8%	5,611	5.6%	6,416	6.4%
Sales and marketing expense	45,987	25.4%	23,368	23.1%	24,600	24.7%
General and administrative expense	23,857	13.2%	30,519	30.2%	16,156	16.2%
Shipping costs	3,570	2.0%	1,512	1.5%	2,348	2.4%
Depreciation and amortization expense	9,154	5.1%	9,723	9.6%	11,453	11.5%

Goodwill impairment charge		0.0%	9,105	9.0%	75,966	76.2%
Embezzlement and related expense (recoveries)	(353)	(0.2)%	129	0.1%	7,254	7.3%
Income (loss) before interest, other income (expense) and income taxes	85	0.0%	(23,294)	(23.1)%	(88,137)	(88.4)%
Net interest expense	(17,292)	(9.5)%	(19,477)	(19.3)%	(18,434)	(18.5)%
Gain from settlement with previous stockholders					30,202	30.3%
Loss on extinguishment of debt					(5,632)	(5.6)%
Other income (expense), net	674	0.4%	(698)	(0.7)%	(981)	(1.0)%
Income tax benefit	583	0.3%	7,704	7.6%	13,422	13.5%
Net loss	$ (15,950)	(8.8)%	$ (35,765)	(35.4)%	$ (69,560)	(69.7)%

Year Ended December 31, 2010 Compared to Year Ended December 31, 2009
Net revenues

Net revenues for the year ended December 31, 2010 increased $80.3 million, or 79.4%, to $181.3 million from $101.0 million in the same period for 2009 due to the VLCY acquisition. VLCY s historical 2009 pre-merger net revenues of $98.7 million are not included in the Company s reported prior year revenues. Excluding the impact of the merger, our net revenues for 2010 were lower due to a decline in order volumes. Net revenues subsequent to the acquisition of VLCY include the impact of a purchase accounting adjustment to reduce deferred revenue balances to fair value at the time of the VCLY acquisition. These adjustments reduced the amount of deferred revenue recognized by approximately $12.9 million in 2010 and $1.4 million in 2009.

Voyager. The Voyager segment s net revenues in 2010 increased $65.0 million, or 122.9%, to $117.9 million from net revenues of $52.9 million in 2009 due to the VLCY acquisition, partially offset by lower order volumes. Product revenues increased $56.1 million, or 126.5%, to $100.4 million from net revenues of $44.3 million in 2009. Service revenues increased $8.9 million, or 103.9%, to $17.5 million from net revenues of $8.6 million in 2009. VLCY s historical 2009 pre-merger net revenues related to the Voyager segment of $77.8 million are not included in the Company s reported prior year revenues. Net revenues subsequent to the acquisition of VLCY include the impact of a purchase accounting adjustment to reduce deferred revenue balances to fair value at the time of the VCLY acquisition. These adjustments reduced the amount of deferred revenue recognized by approximately $4.7 million in 2010 and $0.5 million in 2009.

Sopris. The Sopris segment s net revenues in 2010 decreased $0.5 million, or 1.8%, to $24.7 million from net revenues of $25.2 million in 2009. Product revenues decreased $1.2 million, or 5.0%, to $22.2 million from net revenues of $23.4 million in 2009. Service revenues increased $0.7 million, or 41.8%, to $2.5 million from net revenues of $1.8 million in 2009. The decline in supplementary program sales was mainly due to a contract for the use of our assessment product under a licensing agreement, under which we recognized net revenues of $1.0 million in 2010 versus $1.7 million in 2009.

Cambium Learning Technologies. The CLT segment s net revenues in 2010 increased $15.7 million, or 68.2%, to $38.6 million from net revenues of $22.9 million in 2009 due to the VLCY acquisition. VLCY s historical 2009 pre-merger net revenues related to the CLT segment of $21.0 million are not included in the Company s reported prior year revenues. Net revenues subsequent to the acquisition of VLCY include the impact of a purchase accounting adjustment to reduce deferred revenue balances to fair value at the time of the VLCY acquisition. These adjustments reduced the amount of deferred revenue recognized by approximately $8.2 million in 2010 and $0.9 million in 2009. CLT has consistently experienced year on year order volume growth that is translating to growth in net revenues, although the impact of 2010 order volume is not fully reflected in net revenues as a large portion of these sales are recognized over a subscription period.

Cost of revenues

Cost of product revenues include expenses to print, purchase, handle and warehouse product, as well as royalty costs. Cost of service revenues include costs to provide services and support to customers. Total cost of revenues, excluding amortization, for the year ended December 31, 2010 increased $33.1 million, or 123.1%, to $59.9 million from $26.8 million in 2009 primarily due to the VLCY acquisition. VLCY s historical 2009 pre-merger cost of revenues of $30.8 million are not included in the Company s prior year results. Cost of revenues in 2010 benefited from efficiency gains from cost-cutting measures. Additionally, cost of revenues subsequent to the acquisition of VLCY include the impact of a purchase accounting adjustment to reduce deferred cost balances to fair value at the time of the VCLY acquisition. These adjustments reduced the amount of deferred costs recognized by approximately $1.2 million in 2010 and $0.1 million in 2009.

Voyager. The Voyager segment s cost of revenues in 2010 increased $29.1 million, or 174.7%, to $45.8 million from $16.7 million in 2009 due to the VLCY acquisition. Cost of product revenues increased $18.6 million, or 174.8%, to $29.3 million from $10.7 million in 2009. Cost of service revenues for the year ended December 31, 2010 increased $10.5 million, or 174.6%, to $16.5 million from $6.0 million in 2009.

Sopris. The Sopris segment s cost of revenues in 2010 increased $0.3 million, or 4.0%, to $7.7 million from $7.4 million in 2009. Cost of product revenues increased $0.1 million, or 2.6%, to $6.5 million from cost of product revenues of $6.4 million in 2009. Cost of service revenues increased $0.1 million, or 12.1%, to $1.2 million from cost of service revenues of $1.1 million in 2009.

Cambium Learning Technologies. The CLT segment s cost of revenues in 2010 increased $2.3 million, or 83.2%, to $5.0 million from cost of revenues of $2.7 million in 2009, primarily due to the VLCY acquisition.

Amortization expense

Amortization expense included in cost of revenues includes amortization for acquired pre-publication costs and technology, acquired publishing rights, and developed pre-publication and technology. Amortization for 2010 increased $11.0 million, or 62.7%, to $28.5 million from $17.5 million in 2009 due to the VLCY acquisition.

Research and development expenses

Research and development expenditures include costs to research, evaluate and develop educational products, net of capitalization. Research and development expenses for year ended December 31, 2010 increased $5.0 million, or 88.2%, to $10.6 million from $5.6 million in the same period of 2009. The increased expenditures relate primarily to the VLCY acquisition. VLCY s historical 2009 pre-merger research and development expenses of $4.3 million are not included in the Company s reported prior year results.

Sales and marketing expense

Sales and marketing expenditures include all costs to maintain our various sales channels, including the salaries and commission paid to our sales force, and costs related to our advertising and marketing efforts. Sales and marketing expenses for the year ended December 31, 2010 increased $22.6 million, or 96.8%, to $46.0 million from

$23.4 million in the same period of 2009 due to the VLCY acquisition. VLCY s historical 2009 pre-merger sales and marketing expenses of $28.8 million are not included in the Company s reported prior year expenses. Partially offsetting these charges, 2010 sales and marketing expense include the impact of a purchase accounting adjustment to write down deferred costs to zero at the time of the VCLY acquisition. These adjustments reduced the amount of expense recognized in 2010 by approximately $1.0 million. Additionally, the Company realized synergy savings as a result of the integration of the Company and VLCY.

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General and administrative expense

General and administrative expenses for the year ended December 31, 2010 decreased $6.6 million, or 21.8%, to $23.9 million from $30.5 million in the same period of 2009. VLCY s historical 2009 pre-merger general and administrative expenses of $24.7 million are not included in the Company s reported prior year expenses. General and administrative expenses for 2010 were lower than 2009 due to significant non-recurring merger transaction costs incurred in 2009, savings due to synergies resulting from the merger, and the reallocation of certain resources to cost of sales from general and administrative expenses as a result of the departmental restructuring. Additionally, we recorded a gain of $1.1 million in 2010 to reflect a decrease in the estimated fair value of the contingent value rights liability (CVR) issued in connection with the merger. These decreases are partially offset by the impact of the VLCY acquisition and by non-recurring integration costs of $3.8 million incurred in 2010.

Shipping costs

Shipping costs for the year ended December 31, 2010 increased $2.1 million, or 136.1%, to $3.6 million from $1.5 million in 2009. The increase in these shipping costs was due mainly to the VLCY acquisition. VLCY s historical 2009 pre-merger shipping costs of $1.9 million are not included in the Company s reported prior year expenses.

Depreciation and amortization expense

Depreciation and amortization expense for the year ended December 31, 2010 decreased $0.5 million, or 5.9%, to $9.2 million from $9.7 million in the same period of 2009. This decrease is due to the fact that the Company s intangible assets are amortized on an accelerated basis.

Goodwill impairment

We review the carrying value of goodwill for impairment at least annually and whenever certain triggering events occur. As a result of our annual impairment review for the year ended December 31, 2010, no impairment was indicated.

Embezzlement and related expenses

In 2008, we discovered certain irregularities relating to the control and use of cash and certain other general ledger items which revealed a misappropriation of assets over more than a three-year period beginning in 2004 and continuing through April 2008. These irregularities were perpetrated by a former Cambium Learning employee, resulting in substantial embezzlement losses and related expenses. Embezzlement and related expenses (recoveries) for the year ended December 31, 2010 were $(0.4) million compared to $0.1 million in the same period of 2009. The decrease in the embezzlement and related expenses was mainly due to a recovery during 2010 of approximately $0.5 million.

Net interest expense

Net interest expense for the year ended December 31, 2010 decreased $2.2 million, or 11.2%, to $17.3 million from $19.5 million in the same period of 2009. This decrease was mainly due to lower interest expense on our senior secured debt as a result of a credit rating increase in the first quarter of 2010, which reduced the applicable interest rate to 8%. See Note 14 to the Consolidated Financial Statements.

Income taxes

In 2010, we recorded an income tax benefit of $0.6 million. Pre-tax losses at statutory tax rates provided a federal tax benefit of approximately $5.8 million. We continue to maintain a valuation allowance against our deferred tax assets, which eliminated almost all of the deferred tax benefit generated.

In 2009, we recorded an income tax benefit of $7.7 million. Pre-tax losses at statutory tax rates provided a federal tax benefit of approximately $15.2 million. The impairment charge to non-deductible goodwill did not result in a tax benefit which is $3.2 million less than the amount expected based on the federal statutory tax rate. Certain merger costs are non-deductible and did not result in a tax benefit which is $4.7 million less than the amount expected based on the federal statutory tax rate. Furthermore, after the merger with VLCY, we established a valuation allowance on our net federal deferred tax assets.

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Year Ended December 31, 2009 Compared to Year Ended December 31, 2008

Net revenues

Net revenues for the year ended December 31, 2009 increased $1.3 million, or 1.3%, to $101.0 million from $99.7 million in the same period for 2008. Our net revenues for 2009 were impacted by several significant declines, such as the nationwide economic slowdown, which caused the amount of funding available to schools to decline, a decline in our Sopris segment related to our assessment product, and declines in key adoption states such as Alabama and Florida. Regarding the decline in adoption states, we enjoyed increased sales performance in 2008 in these states but the nature of the adoption leads to lower revenues in the year following the adoption. Offsetting these declines was the impact of the acquisition of VLCY, contributing an incremental $4.5 million in net revenues, and increases in sales of our math products as well as some growth in several new and existing customers.

Voyager. The Voyager segment s net revenues in 2009 increased $4.6 million, or 9.5%, to $52.9 million from net revenues of $48.3 million in 2008. Product revenues increased $3.9 million, or 9.7%, to $44.3 million from net revenues of $40.4 million in 2008. Service revenues increased $0.7 million, or 8.5%, to $8.6 million from net revenues of $7.9 million in 2008. The increase in year over year net revenues was due mainly to the impact of the acquisition of VLCY, contributing an incremental $3.0 million in product revenues and $0.8 million in service revenues. Additionally, Voyager was able to offset the decline in the state adoption sales in Alabama and Florida and overcome the general state and local funding crisis with increases in sales of our math products as well as some growth in several new and existing customers.

Sopris. The Sopris segment s net revenues in 2009 decreased $4.5 million, or 15.2%, to $25.2 million from net revenues of $29.7 million in 2008. The decline in supplementary program revenues was mainly due to a decrease in sales of DIBELS in Florida, as Florida developed its own assessment program. Additionally, we renegotiated and extended a relationship with a customer which uses our assessment product under an annual licensing fee arrangement. As a result of changes in terms with this customer, we recognized licensing fee revenue for two annual periods totaling $3.1 million in 2008. During the first quarter of 2009, we recognized additional revenue of $1.7 million related to this licensing agreement.

Cambium Learning Technologies. The CLT segment s net revenues in 2009 increased $1.2 million, or 5.9%, to $22.9 million from net revenues of $21.7 million in 2008. The increase in year over year net revenues was due mainly to the impact of the acquisition of VLCY, contributing an incremental $0.7 million in product revenues.

Cost of revenues

Cost of product revenues include expenses to print, purchase, handle and warehouse product, as well as royalty costs. Cost of service revenues include all costs to provide services and support to customers. Total cost of revenues, excluding amortization, for the year ended December 31, 2009 decreased $0.9 million, or 3.1%, to $26.8 million from $27.7 million in 2008. The decrease in cost of revenues was mainly due to efficiency gains from cost-cutting measures. As a percentage of net revenues, cost of revenues decreased 1.2 percentage points to 26.6% for the year ended December 31, 2009 from 27.8% in the same period in 2008.

Voyager. The Voyager segment s cost of revenues for the year ended December 31, 2009 decreased $0.2 million, or 1.6%, to $16.7 million from $16.9 million in 2008. Cost of product revenues for the year ended December 31, 2009 decreased $0.5 million, or 4.8%, to $10.7 million from $11.2 million in 2008. The decrease in cost of revenues was mainly due to improved cost management performance. Cost of service revenues for the year ended December 31, 2009 increased $0.3 million, or 4.7%, to $6.0 million from $5.7 million in 2008. The increase was driven by higher service revenues, partially offset by efficiency gains from cost-cutting measures.

Sopris. The Sopris segment s cost of revenues for the year ended December 31, 2009 decreased $0.1 million, or 0.7%, to $7.4 million from $7.5 million in 2008. Cost of product revenues for the year ended December 31, 2009 increased $0.4 million, or 5.8%, to $6.4 million from $6.0 million in 2008. The increase in cost of revenues was due to a change in product mix toward products with higher incremental costs. Cost of service revenues for the year ended December 31, 2009 decreased $0.4 million, or 26.6%, to $1.1 million from cost of service revenues of $1.5 million in 2008. The decrease was driven by lower service revenues and efficiency gains from cost-cutting measures.

Cambium Learning Technologies. The CLT segment s cost of revenues for the year ended December 31, 2009 decreased $0.6 million, or 17.5%, to $2.7 million from $3.3 million in 2008. Cost of product revenues for the year ended December 31, 2009 decreased $0.5 million, or 16.2%, to $2.5 million from cost of revenues of $3.0 million in 2008. The decrease in cost of revenues was mainly due to improved cost management performance. Cost of service revenues for the year ended December 31, 2009 remained relatively flat, decreasing $0.1 million, or 32.0%, to $0.2 million from $0.3 million in 2008.

Amortization expense

Amortization expense included in cost of revenues includes amortization for acquired pre-publication costs and technology, acquired publishing rights, and developed pre-publication and technology. Amortization for 2009 increased $1.6 million, or 9.8%, to $17.5 million from $16.0 million in 2008. Approximately $0.7 million of the increase is related to the acquired pre-publication costs and technology acquired in the VLCY acquisition. The remainder of the increase was mainly due to higher pre-publication amortization as a result of investments made in new programs.

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Research and development expenses

Research and development expenditures include costs to research, evaluate and develop educational products, net of capitalization. Research and development expenses for the year ended December 31, 2009 decreased $0.8 million, or 12.5%, to $5.6 million from $6.4 million in the same period of 2008, due to planned spending decreases as a result of weak economic conditions in 2009. As a percentage of revenues, research and development expenses decreased to 5.6% of revenues in 2009 compared to 6.4% in 2008.

Sales and marketing expense

Sales and marketing expenditures include all costs to maintain our various sales channels, including the salaries and commission paid to our sales force, and costs related to our advertising and marketing efforts. Sales and marketing expenses for the year ended December 31, 2009 decreased $1.2 million, or 5.0%, to $23.4 million from $24.6 million in the same period of 2008. As a percentage of revenues, selling and marketing expenses decreased to 23.1% of revenues in the 2009 compared to 24.7% in 2008. Selling costs decreased for the year ended December 31, 2009 in comparison to the same period in 2008 due to the costs incurred in 2008 to participate in several state adoption activities. We also experienced lower catalog and mailing costs due to a lower volume of catalogs mailed in 2009 compared to 2008.

General and administrative expense

General and administrative expenses for year ended December 31, 2009 increased $14.4 million, or 88.9%, to $30.5 million from $16.2 million in the same period of 2008. The increase was primarily due to the incurrence of $15.5 million in merger-related transaction and integration expenses in 2009 with only immaterial amounts incurred in 2008. Excluding these costs, general and administrative expenses were down $1.1 million, or 6.9%, in 2009 compared to 2008, primarily as a result of cost-cutting measures.

Shipping costs

Shipping costs for the year ended December 31, 2009 decreased $0.8 million, or 35.6%, to $1.5 million from $2.3 million in 2008. The decrease in these shipping costs was due mainly to cost containment and efficiencies.

Depreciation and amortization expense

Depreciation and amortization expense for the year ended December 31, 2009 decreased $1.7 million, or 15.1%, to $9.7 million from $11.5 million in the same period of 2008. The decrease in this amortization was due mainly to lower contract and reseller network intangible amortization, partially offset by the depreciation and amortization related to assets acquired in the VLCY acquisition.

Goodwill impairment

We review the carrying value of goodwill for impairment at least annually and whenever certain triggering events occur. As a result of the signing of the merger agreement, we assessed the carrying values of our reporting units as of June 30, 2009. The first step of impairment testing showed that the carrying value of our Published Products segment exceeded its fair value and that a step two analysis was needed. Step two impairment testing determined that the goodwill balance as of the measurement date was partially impaired and a $9.1 million impairment charge was recorded.

Due to the weakening of the economy and the impact that economic conditions were having on our customers and business in the latter portion of fiscal 2008, we identified deterioration in the expected future financial performance of our Published Products segment. As a result, we recorded an impairment loss of $76.0 million for this segment in 2008, reflecting the difference between the fair value and recorded value for goodwill.

Under the new segment structure, both the 2008 and the 2009 goodwill impairment charges were assigned to the Voyager segment.

Embezzlement and related expenses

In 2008, we discovered certain irregularities relating to the control and use of cash and certain other general ledger items which revealed a misappropriation of assets over more than a three-year period beginning in 2004 and continuing through April 2008. These irregularities were perpetrated by a former Cambium Learning employee, resulting in substantial embezzlement losses and related expenses. Embezzlement and related expenses for the year ended December 31, 2009 were $0.1 million compared to $7.3 million in the same period of 2008. The decrease in the embezzlement and related expenses was mainly due to the non-recurring nature of the embezzlement loss and related expenses that were incurred in the year ended December 31, 2008.

Net interest expense

Net interest expense in the year ended December 31, 2009 increased $1.0 million, or 5.7%, to $19.5 million from $18.4 million in the same period of 2008. This increase was mainly due to higher interest expense on both our senior secured and senior unsecured debt as a result of the permanent waiver and amendments to the credit agreement we signed on August 22, 2008 following the embezzlement loss described above. Under the terms and conditions of the permanent waiver and amendment, the interest rates on Cambium s senior secured and senior unsecured debt were increased. See Note 14 to the Consolidated Financial Statements.

Income taxes

In 2009, we recorded an income tax benefit of $7.7 million. Pre-tax losses at statutory tax rates provided a federal tax benefit of approximately $15.2 million. The impairment charge to non-deductible goodwill did not result in a tax benefit which is $3.2 million less than the amount expected based on the federal statutory tax rate. Certain merger costs are non-deductible and did not result in a tax benefit which is $4.7 million less than the amount expected based on the federal statutory tax rate. Furthermore, after the merger with VLCY, we established a valuation allowance on our net federal deferred tax assets.

In 2008, we recorded an income tax benefit of $13.4 million. Pre-tax losses at statutory rates provided a federal tax benefit of approximately $29.0 million. The impairment charge to non-deductible goodwill did not result in a tax benefit which is approximately $26.6 million less than the amount expected based on the federal statutory rate. We also recorded non-taxable book income related to a purchase adjustment, which resulted in a tax benefit of $10.2 million.

Gain from settlement with previous stockholders

For fiscal 2008, we received a total settlement from previous stockholders of $30.2 million relating to the embezzlement we suffered. The total settlement consisted of $20 million in escrowed funds, together with additional payments of $9.3 million and interest income of $0.9 million. The total settlement amount of $30.2 million was used to cover costs and to pay down a portion of a senior secured credit facility. Because the embezzlement was discovered after the initial purchase allocation was made in connection with the 2007 acquisition of Cambium Learning, the entire settlement amount was recorded on our consolidated statement of operations as a gain from settlement with the previous stockholders.

Loss on extinguishment of debt

For fiscal 2008, we recorded a loss on the extinguishment of debt of $5.6 million related to the modification of our senior secured credit facility and senior unsecured promissory notes resulting from the execution of an amendment of those documents and the delivery by the lenders of a permanent waiver. The associated unamortized deferred financing costs as of August 22, 2008 of $4.6 million and amendment fees of $1.0 million related to the permanent waiver were recorded as a loss on extinguishment of debt.

Liquidity and Capital Resources

Because sales seasonality affects operating cash flow, we normally incur a net cash deficit from all of our activities through the early part of the third quarter of the year. We typically fund these seasonal deficits through the drawdown of cash, supplemented by borrowings on a revolving credit facility. The primary source of liquidity is cash flow from operations and the primary liquidity requirements relate to debt service, pre-publication costs, capital investments and working capital. We believe that based on current and anticipated levels of operating performances, cash flow from operations and availability under a revolving credit facility, we will be able to make required interest payments on our debt and fund our working capital and capital expenditure requirements for the next 12 months.

Long-term debt

9.75% Senior Secured Notes. On February 17, 2011, we completed the offering (the Offering) of $175 million aggregate amount of 9.75% Senior Secured Notes (the Notes). After the issuance discount, we received proceeds of 99.442%. The notes will mature on February 15, 2017. The Offering was a private placement exempt from the registration requirements under the Securities Act. We used a portion of the net proceeds from the sale of the Notes to repay in full outstanding indebtedness under our existing secured credit facility and senior unsecured notes and to pay related fees and expenses, and intend to use the remaining net proceeds for general corporate purposes. Interest on the Notes will accrue at a rate of 9.75% per annum from the date of original issuance and will be payable semi-annually in arrears on each February 15 and August 15, commencing on August 15, 2011, to the holders of record of the Notes on the immediately preceding February 1 and August 1. Pursuant to a Registration Rights Agreement entered into in connection with the Offering, we have agreed to file a registration statement with the SEC that would enable holders of the Notes to exchange the privately placed Notes for publicly registered notes with substantially identical terms.

The Notes are secured by (i) a first priority lien on substantially all of our assets (other than inventory and accounts receivable and related assets of the ABL Credit Parties in connection with the ABL Facility (each as defined and discussed below) and subject to certain exceptions), including capital stock of the Guarantors (the Company and certain of its subsidiaries), and (ii) a second-priority lien on substantially all of the inventory and accounts receivable and related assets of the ABL Credit Parties, in each case, subject to certain permitted liens. The Notes also contain customary covenants, including limitations on our ability to incur debt, and events of default as defined by the indenture governing the Notes. We may, at our option, redeem the Notes prior to their maturity based on the terms included in the indenture governing the Notes.

Registration Rights Agreement. In connection with the Offering, we entered into a Registration Rights Agreement that requires us to (i) file with the SEC within 180 days after the issue date of the Notes (or February 17, 2011), a registration statement under the Securities Act (the Exchange Offer Registration Statement), relating to an offer to exchange the Notes (the Exchange Offer) for new notes (the Exchange Notes) on terms substantially identical to the Notes, except that the Exchange Notes will not be subject to the same restrictions on transfer; (ii) use commercially reasonable efforts to cause the Exchange Offer Registration Statement to become effective within 270 days after the date of the Notes; and (iii) within 60 days of the Exchange Offer Registration Statement becoming effective, complete the Exchange Offer and issue the Exchange Notes in exchange for all Notes validly tendered in the Exchange Offer. If we fail to meet these obligations set forth in the Registration Rights Agreement (a Registration Default), then we will be required to pay additional interest to the holders of the Notes. The rate of the additional interest will be 0.25% per annum for the first 90-day period immediately following the occurrence of a Registration Default. Thereafter, the rate of additional interest will increase by an additional 0.25% per annum with respect to each subsequent 90-day period until all Registration Defaults have been cured, up to a maximum additional interest rate of 1.0% per annum. We will pay such additional interest until all the Registration Defaults relating to the Notes are cured. At such time, the interest rate on the Notes will revert to the original interest rate on the Notes.

New Credit Facility (ABL Facility). On February 17, 2011, our wholly owned subsidiary, Cambium Learning, Inc. (together with its wholly owned subsidiaries, the ABL Credit Parties), entered into a new asset-backed revolving credit facility (the ABL Facility) pursuant to a Loan and Security Agreement (the ABL Loan Agreement), by and among the ABL Credit Parties, Harris N.A., individually and as Agent for any ABL Lender (as hereinafter defined) which is or becomes a party to said ABL Loan Agreement, certain other lenders party thereto (together with Harris N. A. in its capacity as a lender, the ABL Lenders), Barclays Bank PLC, individually and as Collateral Agent, and BMO Capital Markets and Barclays Capital, as Joint Lead Arrangers and Joint Book Runners. The ABL Facility consists of a four-year $40.0 million revolving credit facility, which includes a $5.0 million subfacility for swing line loans and a $5.0 million subfacility for letters of credit. In addition, the ABL Facility provides that the ABL Credit Parties may increase the aggregate principal amount of the ABL Facility by up to an additional $20.0 million, subject to the consent of the Agent (whose consent shall not be unreasonably withheld) and subject to the satisfaction of certain other conditions specified in the ABL Facility.

As the ABL Facility s borrowing base is determined by eligible inventory and eligible accounts receivable, seasonality will cause the available amount to fluctuate. We estimate normal borrowing availability during 2011 of between $20 and $30 million.

The interest rate for the ABL Facility will be, at the ABL Credit Parties option, either an amount to be determined (ranging from 2.75% to 3.25%, depending upon the ABL Credit Parties fixed charge coverage ratio at the time) above the London Interbank Offered Rate or at an amount to be determined (ranging from 1.75% to 2.25%, depending upon the ABL Credit Parties fixed charge coverage ratio at the time) above the base rate. On any day, the base rate will be the greatest of (i) the Agent s then-effective prime commercial rate, (ii) an average federal funds rate plus 0.50% and (iii) the LIBOR quoted rate plus 1.00%. The ABL Facility will, subject to certain exceptions, be secured by a first-priority lien on the ABL Credit Parties inventory and accounts receivable and related assets and a second-priority lien (junior to the lien securing the ABL Credit Parties obligations with respect to the Notes) on substantially all of the ABL Credit Parties other assets.

Revolving loans under the ABL Facility may be used solely for (i) the satisfaction of existing indebtedness of the ABL Credit Parties under their prior senior secured credit facility and outstanding pursuant to their prior existing senior unsecured notes, (ii) general operating capital needs of the ABL Credit Parties in a manner consistent with the provisions of the ABL Facility and all applicable laws, (iii) working capital and other general corporate purposes in a manner consistent with the provisions of the ABL Facility and all applicable laws, (iv) the payment of certain fees and expenses incurred in connection with the ABL Facility and/or the Notes, and (v) other purposes permitted under the ABL Loan Agreement.

The ABL Facility contains a financial covenant that generally requires the ABL Credit Parties to maintain, on a consolidated basis, either (i) excess availability of at least the greater of $8 million and 15% of the revolver commitment or (ii) a fixed charge coverage ratio of 1.1 to 1.0. The ABL Credit Parties will be required to pay, quarterly in arrears, an unused line fee equal to the product of (x) either 0.375% or 0.50% (depending upon the ABL Credit Parties fixed charge coverage ratio at the time) and (y) the average daily unused amount of the revolver.

Cash flows

Cash from operations is seasonal with more cash generated in the second half of the year than in the first half of the year. Cash is historically generated during the second half of the year because the buying cycle of school districts generally starts at the beginning of each new school year in the fall. Cash provided by (used in) our operating, investing and financing activities is summarized as follows:

(in thousands)	2010	2009	2008
Operating activities	$ 20,161	$ 1,934	$ (13,855)
Investing activities	(14,441)	(13,092)	26,889
Financing activities	(7,234)	22,085	(11,822)

Operating activities. Cash provided by (used in) operating activities was $20.2 million, $1.9 million and $(13.9) million for the years ended December 31, 2010, 2009 and 2008, respectively. In 2010, cash flows from normal operations were partially offset by a payment of $5.2 million for a tax indemnification obligation to the state of Michigan and approximately $4.2 million in non-recurring integration costs. Additionally, our accounts receivable balance was $12.5 million higher at year end 2010 versus year end 2009 due to the timing of several significant transactions. In 2009, cash flows from normal operations were partially offset by $11.6 million of transaction costs related to the merger transaction.

Investing activities. Cash provided by (used in) investing activities was $(14.4) million, $(13.1) million and $26.9 million for the years ended December 31, 2010, 2009 and 2008, respectively. Expenditures related to property, equipment, software and pre-publications costs were $13.3 million, $3.4 million and $3.2 million for the years ended December 31, 2010, 2009 and 2008, respectively. The increase in expenditures for 2010 is attributable to the merger with VLCY in late 2009. Cash payments of $9.7 million were made in 2009 for the VLCY acquisition (net of cash acquired), and another $1.1 million was paid in 2010 for the first distribution to the holders of the CVR. Cash inflows for 2008 included $30.2 million related to the embezzlement settlement from the previous stockholders as discussed in Note 3 to the Consolidated Financial Statements.

Financing activities. Cash provided by (used in) financing activities was $(7.2) million, $22.1 million and $(11.8) million for the years ended December 31, 2010, 2009 and 2008, respectively. Net principal payments for debt, revolving credit facilities and capital leases were $7.2 million, $5.9 million, and $19.5 million for the years ended December 31, 2010, 2009 and 2008, respectively. Other significant cash inflows for 2009 included $25.0 million of capital contributed by Cambium s stockholders related to the VLCY acquisition and $3.0 million of capital contributed by Cambium s stockholders to fund the cure to a senior secured credit agreement financial covenant. Other significant cash inflows for 2008 included $7.0 million in unsecured loans from affiliates related to the permanent waiver of the financial reporting defaults related to our senior secured credit facility and the senior unsecured notes as described in Note 14 to the Consolidated Financial Statements.

Non-GAAP Measures

Our historical financial statements presented in accordance with GAAP include VLCY results only for the periods subsequent to the December 8, 2009 acquisition date. Further, the net losses for both the Company and VLCY as reported on a GAAP basis include material non-recurring and non-operational items. We believe that earnings (loss) from operations before interest and other income (expense), income taxes, and depreciation and amortization, or EBITDA, and Adjusted EBITDA, which further excludes non-recurring and non-operational items, provide useful information for investors to assess the results of the ongoing business of the combined company.

EBITDA and Adjusted EBITDA are not prepared in accordance with GAAP and may be different from similarly named, non-GAAP financial measures used by other companies. Non-GAAP financial measures should not be considered a substitute for, or superior to, measures of financial performance prepared in accordance with GAAP. We believe that Adjusted EBITDA provides useful information to investors because it reflects the underlying performance of the ongoing operations of the combined company and provides investors with a view of the combined company s operations from management s perspective. Adjusted EBITDA removes significant one-time or certain non-cash items from earnings. We use Adjusted EBITDA to monitor and evaluate the operating performance of the combined company and as the basis to set and measure progress towards performance targets, which directly affect compensation for employees and executives. We generally use these non-GAAP measures as measures of operating performance and not as measures of liquidity. Our presentation of EBITDA and Adjusted EBITDA should not be construed as an indication that our future results will be unaffected by unusual or nonrecurring items.

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Below is a reconciliation between net loss and Adjusted EBITDA for the years ended December 31, 2010 and 2009.

Reconciliation Between Net Revenues to Adjusted Net Revenues and Between Net Income (Loss) and Adjusted EBITDA
for the Years Ended December 31, 2009 and 2010

	Cambium	VLCY Pre-Merger Results (342 days)	Pro Forma Adjustments [(a)]	Pro Forma Combined	Cambium Learning Group
	2009				2010
	(In thousands) (Unaudited)				
Total net revenues	$ 101,048	$ 98,728	$ (11,565)	$ 188,211	$ 181,260
Non-recurring and non-operational costs included in net revenues but excluded from adjusted net revenues:					
Adjustments related to purchase accounting [(g)]	1,392		11,565	12,957	12,937
Adjusted net revenues	$ 102,440	$ 98,728	$	$ 201,168	$ 194,197
Net loss	$ (35,765)	$ (34,375)	$ 8,870	$ (61,270)	$ (15,950)
Reconciling items between net loss and EBITDA:					
Depreciation and amortization	27,250	18,301	(5,772)	39,779	37,665
Net interest expense	19,477	558	71	20,106	17,292
Other (income) expense	698	(3,279)		(2,581)	(674)
Income tax	(7,704)	(190)	7,894		(583)
Income (loss) from operations before interest and other income (expense), income taxes, and depreciation and amortization (EBITDA)	3,956	(18,985)	11,063	(3,966)	37,750
Non-recurring and non-operational costs included in EBITDA but excluded from Adjusted EBITDA:					
Transaction costs [(b)]	13,570	9,937	(23,507)		
Integration and merger-related costs [(c)]	2,133	120	1,864	4,117	5,963
Legacy VLCY corporate [(d)]	57	2,247		2,304	968
Stock-based compensation expense [(e)]	37	179	552	768	1,085

Embezzlement and related expenses (recoveries) [(f)]	129			129	(353)
Adjustments related to purchase accounting [(g)]	1,136		10,028	11,164	10,748
Goodwill impairment [(h)]	9,105	27,175		36,280	
Adjustments to CVR liability [(i)]					(1,124)
Adjusted EBITDA	$ 30,123	$ 20,673	$	$ 50,796	$ 55,037

(a) On December 8, 2009, we acquired VLCY. The acquisition was accounted for as a purchase transaction. Our consolidated financial statements include the results of VLCY from December 8, 2009, the date of acquisition. Therefore, the historical results of the Company have been adjusted to show the effect on our statement of operations if the transaction had been completed at the beginning of 2009. The combined historical net loss includes the following pro forma adjustments:

the pro forma impact of the amortization of intangible assets and the reduction in deferred revenue and related deferred costs based on the purchase price allocation;

the pro forma impact of reduced interest income lost as a result of the $58.0 million of cash used in the purchase price consideration (net of $25.0 million contributed by the sole stockholder of the Company at the time of the merger);

the pro forma impact of certain employment agreements and stock option grants entered into on the effective date of the merger;

the elimination of merger transaction costs incurred by the Company and VLCY; and

the pro forma tax effect of the merger, which was estimated using a combined company effective tax rate of 0%.

(b) External incremental costs incurred by the Company and VLCY that are directly related to the merger.

(c) Costs directly associated with the integration of the Company and VLCY, including severance and other costs incurred to achieve synergies and the cost of retention and change in control agreements directly related to the merger. The cost for retention and change in control agreements included was $0.8 million for the year ended December 31, 2009 and $1.7 million for the year ended December 31, 2010.

(d) Legacy VLCY corporate costs representing corporate costs related to legacy VLCY liabilities such as pension and severance costs for former VLCY employees. For the year ended December 31, 2009, these also include internal costs related to VLCY s strategic alternative process, corporate overhead costs related to the restatement of VLCY s financial statements and the related activities for VLCY to become current with its SEC filings, and costs to transition VLCY s corporate office from Ann Arbor, Michigan to Dallas, Texas.

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(e) Stock-based compensation expense is related to our outstanding options, restricted stock awards, warrants, and stock appreciation rights (SARs).

(f) During 2008, we discovered certain irregularities relating to the control and use of cash and certain other general ledger items which resulted from a substantial misappropriation of assets over more than a three-year period beginning in 2004 and continuing through April 2008. These irregularities were perpetrated by a former employee, resulting in embezzlement losses, net of recoveries.

(g) Under applicable accounting guidance for business combinations, an acquiring entity is required to recognize all of the assets acquired and liabilities assumed in a transaction at the acquisition date fair value. Net revenues have been reduced by $1.4 million and $12.9 million, respectively, for the years ended December 31, 2009 and December 31, 2010 in the historical financial statements due to the write-down of deferred revenue to its estimated fair value as of the merger date and in the pro forma adjustments to reflect the impact of the write-down assuming the merger occurred on January 1, 2009. The write-down was determined by estimating the cost to fulfill the related future customer obligations plus a normal profit margin. Partially offsetting this impact, cost of revenues and sales and marketing expenses were reduced for other purchase accounting adjustments, primarily a write-down of deferred costs to zero at the acquisition date. During the years ended December 31, 2009, and December 31, 2010, the historical cost of revenues was reduced by $0.2 million and $1.2 million, respectively, and the historical sales and marketing expenses were reduced by $0.1 million and $1.0 million, respectively, and the related pro forma adjustments reflect the impact of the write-down assuming the merger occurred on January 1, 2009. The adjustment of deferred revenue and deferred costs to fair value is required only at the purchase accounting date; therefore, its impact on net revenues, cost of revenues, and sales and marketing expense is non-recurring.

(h) Goodwill impairment charges of $9.1 million for the year ended December 31, 2009 and pre-merger VLCY goodwill impairment charges of $27.2 million for the year ended December 31, 2009.

(i) Adjustments to the CVR liability as a result of the amendments of the merger agreement and the related escrow agreement, the expiration of the statute of limitations on potential tax liabilities and changes in likelihood of collecting potential tax receivables included in the estimate of the fair value of the CVRs.

Our historical financial statements include VLCY deferred revenue only as of period ends subsequent to the December 8, 2009 acquisition date. Therefore, the historical balance sheets reported on a GAAP basis include the deferred revenue balance of VLCY beginning with the year ended December 31, 2009.

Further, the deferred revenue balances as reported on a GAAP basis as of December 31, 2009 and 2010 include material purchase accounting adjustments related to the VLCY acquisition. We believe that the combined deferred revenue balances and adjusted deferred revenue balances, which exclude the effect of the purchase accounting adjustment, provide useful information for investors to assess the results of the ongoing business of the combined company.

Adjusted deferred revenue is not prepared in accordance with GAAP and may be different from non-GAAP financial measures used by other companies. Non-GAAP financial measures should not be considered a substitute for, or superior to, measures of financial performance prepared in accordance with GAAP. We believe that adjusted deferred revenue provides useful information to investors for assessing the impact of deferred revenue changes on our reported GAAP and adjusted revenues.

Change in Adjusted Deferred Revenue for the Years Ended December 31, 2009 and 2010

	As of: *(in thousands)* *(Unaudited)*

	December 31, 2008	December 31, 2009	December 31, 2010
Cambium deferred revenue	$ 1,910	$ 24,181	$ 37,556
Legacy VLCY deferred revenue	29,507		
Total combined deferred revenue	31,417	24,181	37,556
Purchase accounting fair value adjustment		14,374	1,437
Adjusted deferred revenue	31,417	38,555	38,993
Change in adjusted deferred revenue		**$ 7,138**	**$ 438**

Capital Expenditures and Outlook

(Dollars in millions)	Year Ended December 31, 2010	Year Ended December 31, 2009	Year Ended December 31, 2008
Pre-publication costs	$ 4.8	$ 2.4	$ 2.2
Property, equipment and software	8.5	1.0	1.0
Total expenditures for property, equipment, and pre-publication costs	$ 13.3	$ 3.4	$ 3.2

Capital spending in 2011 is expected to be $14.1 to $15.1 million and will be concentrated primarily on ongoing and new product development, which management believes will generate future sales growth.

We believe that current cash, cash equivalents and short term investment balances, expected income tax refunds, and cash generated from operations will be adequate to fund the working capital and capital expenditures necessary to support our currently expected sales for the foreseeable future.

Commitments and Contractual Obligations

We have various contractual obligations which are recorded as liabilities in our Consolidated Financial Statements. Other items, such as certain purchase commitments and other executory contracts, are not recognized as liabilities in our Consolidated Financial Statements but are required to be disclosed.

The following table summarizes our significant operational and contractual obligations and commercial commitments at December 31, 2010 showing the future periods in which such obligations are expected to be settled in cash:

(in millions)	Total	2011	2012 & 2013	2014 & 2015	After 2015
Senior secured notes as of December 31, 2010	$ 112.4	$ 8.9	$ 103.5	$	$
Senior unsecured notes as of December 31, 2010	64.2			64.2	
Build-to-suit lease obligations as of December 31, 2010	6.5	1.0	2.2	2.3	1.0
Other capital lease obligations as of December 31, 2010	0.1	0.1			
Operating lease obligations as of December 31, 2010	9.1	1.5	3.8	1.8	2.0
Contingent value rights as of December 31, 2010	7.4	1.6	5.8		

As described in Liquidity and Capital Resources and in Note 23 to the Consolidated Financial Statements, in February 2011, we closed an offering of $175 million aggregate principal amount of Notes due 2017 and entered into

a new $40 million asset-based revolving credit facility. We used a portion of the net proceeds from the offering to repay in full outstanding indebtedness under the secured credit facility and senior unsecured notes that existed as of December 31, 2010.
We have letters of credit outstanding as of December 31, 2010 in the amount of $2.9 million to support workers compensation insurance coverage, certain of our credit card programs, the build-to-suit lease, and performance bonds for certain contracts. We maintain a $1.1 million certificate of deposit as collateral for the workers compensation insurance and credit card program letters of credit and for our Automated Clearinghouse (ACH) programs. We also maintain a $0.9 million money market fund investment as collateral for our travel card program. The certificate of deposit and money market fund investment are recorded in other assets.
As of December 31, 2010, we have $12.0 million in obligations with respect to our pension plan. For further information, see Note 15 to our Consolidated Financial Statements included herein.
As of December 31, 2010, we have approximately $0.8 million of long-term income tax liabilities that have a high degree of uncertainty regarding the timing of the future cash outflows. We are unable to reasonably estimate the years when settlement will occur with the respective tax authorities.

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on the Company s financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies and Estimates

Our Consolidated Financial Statements are prepared in accordance with U.S. GAAP, which require management to make estimates and assumptions that affect the reported amount of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities.

On an ongoing basis, we evaluate our estimates, including those related to accounting for revenue recognition, impairment, capitalization and depreciation, allowances for doubtful accounts and sales returns, inventory reserves, income taxes, and other contingencies. We base our estimates on historical experience and other assumptions we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that may not be readily available from other sources. Actual results may differ from these estimates, which could have a material impact on our financial statements.

Certain accounting policies require higher degrees of judgment than others in their application. We consider the following to be critical accounting policies due to the judgment involved in each. For a detailed discussion of our significant accounting policies, see Note 2 to our Consolidated Financial Statements included herein.

Revenue Recognition. In October 2009, new guidance was issued regarding multiple-deliverable revenue arrangements and certain arrangements that include software elements. This guidance requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The guidance eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. In addition to requiring that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method, the guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which includes (1) vendor-specific objective evidence (VSOE), if available, (2) third party evidence (TPE), if vendor-specific objective evidence is not available, and (3) best estimate of selling price (BESP), if neither VSOE nor TPE is available. The objective of BESP is to determine the price at which we would transact a sale if the product or service were sold on a stand-alone basis. It also removes tangible products from the scope of software revenue guidance and provides guidance on determining whether software deliverables in an arrangement that includes a tangible product are covered by the scope of the software revenue guidance. This guidance must be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early adoption permitted. Effective January 1, 2010, we adopted this guidance on a prospective basis for all new or materially modified arrangements entered into after the adoption date.

Revenues are derived from sales of reading, math and science, and professional development solutions to school districts primarily in the United States. Sales include printed materials and often online access to educational materials for individual students, teachers, and classrooms. Revenue from the sale of printed materials for reading and math products is recognized when the product is shipped to or received by the customer, depending on the shipping terms of the arrangement. Revenue for product support, training and implementation services, and online subscriptions is recognized over the period services are delivered. Revenue for the online content sold separately or included with certain curriculum materials is recognized ratably over the subscription period, typically a school year. Revenue for our professional development courses, which can include an Internet delivery component, is recognized over the contractual delivery period. ExploreLearning and Learning A-Z derive revenue exclusively from sales of online subscriptions to their reading, math and science teaching websites and related training and professional development. Typically, the subscriptions are for a twelve- to twenty-four-month period and the revenue is recognized ratably over the period the online access is available to the customer.

The division of revenue between shipped materials, online materials, and ongoing support and services was determined in accordance with the new accounting guidance for revenue arrangements with multiple deliverables. We are not able to establish VSOE for each of our deliverables. Whenever VSOE cannot be established, we review the offerings of our competitors to determine whether TPE can be established. TPE is determined based on the prices charged by our competitors for a similar deliverable when sold separately. It may be difficult for us to obtain sufficient information on competitor pricing to substantiate TPE and therefore we may not always be able to use TPE. We also use BESP to determine the selling price of certain of deliverables. BESP was primarily used for the printed materials for product lines acquired in the VLCY acquisition, which have historically been priced on a bundled basis with the related online materials. Our determination of BESP considers the anticipated margin on that deliverable, the selling price and profit margin for similar parts or services, and our ongoing pricing strategy and policies.

We plan to analyze the selling prices used in the allocation of arrangement consideration at least annually. Selling prices will be analyzed on a more frequent basis if a significant change in our business necessitates a more timely analysis or if we experience significant variances in our selling prices.

Our software products often include maintenance, support or on-line services. Maintenance and support services include telephone support, bug fixes, and, for certain products, rights to upgrades and enhancements on a when-and-if available basis. On-line services include storage, assignment, scoring and reporting. These services are recognized on a straight-line basis over the period they are provided. Revenues under multiple-element software license arrangements, which may include several different software products and services sold together, are allocated to each element based on the residual method in accordance with accounting guidance for software revenue recognition. In certain instances, telephone support and software repairs are provided for free within the first year of licensing the software. The cost of providing this service is insignificant, and is accrued at the time of revenue recognition.

We enter into agreements to license certain publishing rights and content. We recognize the revenue from these agreements when the license amount is fixed and determinable, collection is reasonably assured, and the license period has commenced. For those license agreements that require us to deliver additional materials as part of the license agreement, the revenue is recognized when the product is received by the customer. Shipments to school book depositories are on consignment and revenue is recognized based on shipments from the depositories to the schools.

Impairment of Goodwill. We review the carrying value of goodwill for impairment at least annually. The annual analysis is performed as of December 1 or when certain triggering events occur. The applicable accounting guidance requires that a two-step impairment test be performed on goodwill. In the first step, the fair value of each reporting unit is compared to its carrying value. If the fair value of a reporting unit exceeds the carrying value of that unit, goodwill is not impaired and no further testing is required. If the carrying value of the reporting unit exceeds the fair value of that unit, then a second step must be performed to determine the implied fair value of the reporting entity s goodwill. If the carrying value of a reporting unit s goodwill exceeds its implied fair value, then an impairment loss equal to the difference is recorded.

Determining the fair value of a reporting unit is judgmental in nature, and involves the use of significant estimates and assumptions. These estimates and assumptions may include revenue growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates, future economic and market conditions, and determination of appropriate market comparables. In addition, we make certain judgments and assumptions in allocating shared assets and liabilities to determine the carrying values of our reporting units.

We performed the 2010 yearend impairment analysis using four reporting units: Voyager; Sopris; the Learning A-Z and ExploreLearning subscription businesses from the CLT segment (LAZEL); and the Kurzweil and IntelliTools businesses from the CLT segment (KI). The following table details the goodwill balance by reporting unit at December 31, 2010:

	Goodwill balance as of December 31, 2010	
Voyager	$	76,085
Sopris		17,300
LAZEL		19,724
KI		38,806
Total	$	151,915

In the first step of the impairment test for fiscal year 2010, the fair market value of each reporting unit was determined using an income approach and was dependent on multiple assumptions and estimates, including future cash flow projections with a terminal value multiple and the discount rate used to determine the expected present value of the estimated future cash flows. Future cash flow projections were based on management s best estimates of economic and market conditions over the projected period, including industry fundamentals such as the state of educational funding, revenue growth rates, future costs and operating margins, working capital needs, capital and other expenditures, and tax rates. The discount rate applied to the future cash flows was a weighted-average cost of capital and took into consideration market and industry conditions, returns for comparable companies, the rate of return an outside investor would expect to earn, and other relevant factors. The first step of impairment testing for fiscal 2010 showed that the fair value of each reporting unit exceeded its carrying value by at least 10%; therefore, no second step of testing was required.

The adverse developments in the education funding environment that affected our operations during fiscal year 2009 and 2010 may continue to have an impact, and potentially increase the impact, on our future revenues, profits, cash flows and carrying value of assets. Although management has included its best estimates of the impact of these and other factors in our cash flow projections, the projection of future cash flows is inherently uncertain and requires a significant amount of judgment. Actual results that are significantly different than these cash flow projections or a change in the discount rate could significantly affect the fair value estimates used to value our reporting units in step one of the goodwill analysis or the fair values of our other asset and liability balances used in step two of the goodwill analysis, and could result in future goodwill impairments.

Impairment of Long Lived Assets. We review the carrying value of long lived assets for impairment whenever events or changes in circumstances indicate net book value may not be recoverable from the estimated undiscounted future cash flows. If our review indicates any assets are impaired, the impairment of those assets is measured as the amount by which the carrying amount exceeds the fair value as estimated by discounted cash flows. Assets to be disposed of are reported at the lower of the carrying amount or fair value less cost of disposal. For fiscal year 2010, no impairment was indicated.

The determination whether our definite-lived intangible assets are impaired involves significant assumptions and estimates, including projections of future cash flows, the percentage of future revenues and cash flows attributable to the intangible assets, asset lives used to generate future cash flows, and royalty charges attributable to trademarks. The impairment calculations are most sensitive to the future cash flow assumptions. Future cash flow projections are based on management s best estimates of economic and market conditions over the projected period, including industry fundamentals such as the state of educational funding, revenue growth rates, future costs and operating margins, working capital needs, and capital and other expenditures. Adverse developments in the education funding environment, including the reductions in available state and local funds as property taxes decline, have affected our operations during 2010 and may continue to have an impact, and potentially increase the impact, on our future revenues, profits, cash flows and carrying value of assets.

*Pre-Publication Costs.*We capitalize certain pre-publication costs of our curriculum, including art, prepress, editorial, and other costs incurred in the creation of the master copy of our curriculum products. Pre-publication costs are amortized over the expected life of the education program, generally on an accelerated basis over a period of five years. The amortization methods and periods chosen reflect the expected revenues generated by the education programs. We periodically review the recoverability of the capitalized costs based on expected net realizable value.

Accounts Receivable. Accounts receivable are stated net of allowances for doubtful accounts and estimated sales returns. The allowance for doubtful accounts is based on a review of the outstanding balances and historical collection experience. The reserve for sales returns is based on historical rates of returns as well as other factors that in our judgment could reasonably be expected to cause sales returns to differ from historical experience. Actual bad debt write-offs and returns could differ from our estimates.

Inventory. Inventory is stated at the lower of cost, determined using the first-in, first-out (FIFO) method, or market, and consists of finished goods. We reduce slow-moving or obsolete inventory to net realizable value. Inventory values are maintained at an amount that management considers appropriate based on factors such as the inventory aging, historical usage of the product, future sales forecasts, and product development plans. These factors involve management s judgment and changes in estimates could result in increases or decreases to the inventory values. Inventory values are reviewed on a periodic basis.

Income Taxes. Provision is made for the expense, or benefit, associated with taxes based on income. The provision for income taxes is based on laws currently enacted in every jurisdiction in which we do business and considers laws mitigating the taxation of the same income by more than one jurisdiction. Significant judgment is required in determining income tax expense, current tax receivables and payables, deferred tax assets and liabilities, and valuation allowance recorded against the net deferred tax assets. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, taxable income in prior carryback years, loss carryforward limitations, and tax planning strategies in assessing whether deferred tax assets will be realized in future periods. If, after consideration of these factors, management believes it is more likely than not that a portion of the deferred tax assets will not be realized, a valuation allowance is established. The amount of the deferred tax asset considered realizable could be reduced if estimates of future taxable income during the carryforward period are reduced.

We recognize liabilities for uncertain tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if available evidence indicates that it is more likely than not that the position will be sustained on audit. The second step requires us to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. It is inherently difficult and subjective to estimate these amounts, since this requires management to determine the probability of various possible outcomes. We reevaluate our uncertain tax positions on a periodic basis, based on factors such as changes in facts and circumstances, changes in tax law, effectively settled issues under audit and new audit activity.

Contingent Value Rights (CVRs). CVRs were issued to VLCY stockholders as part of the merger. Each CVR represents the right to receive a cash amount equal to the sum of the following amounts (minus specified agreed-upon liabilities, including agreed contingencies, potential working capital adjustments and expenses of the stockholders representative) under the merger agreement:

- specified VLCY tax refunds received after the effective time of the merger, plus

- the lesser of $4.0 million *or* the amount of specified post-signing tax refunds of VLCY received after the date of the merger agreement and on or prior to the date of the closing, which was $1.6 million, plus

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a portion of funds held for a potential tax indemnity obligation, if such obligation is not paid to its beneficiary, plus

other amounts specified in the escrow agreement,

divided by the total number of shares of VLCY common stock outstanding as of the effective time of the merger.

The first CVR payment date was in September 2010 and $1.1 million was distributed to the escrow agent at that time for distribution to holders of the CVRs. A second CVR distribution will be made in June 2011 and the final distribution, if any, with respect to a potential tax indemnity obligation will be in October 2013. Additionally, as described in Other Contingencies below, any amounts due to CVR holders as a result of refunds received related to the Michigan tax payment will be distributed upon the final resolution of this agreed contingency.

The fair value of the liability for the CVRs is determined using a probability-weighted cash flow analysis which takes into consideration the likelihood, amount and timing of cash flows of each element of the pool of assets and liabilities included in the CVR. The determination of fair value of the CVRs involves significant assumptions and estimates, which are reviewed at each quarterly reporting date. As of December 31, 2010, a fair value of $7.4 million has been recorded as a liability for the remaining CVR payments. During the year ended December 31, 2010, a gain of $1.1 million was recorded in general and administrative expense to reflect a decrease in the estimated fair value of the CVR liability. The ultimate value of the CVRs is not known at this time; however, it is not expected to be more than $11 million and could be as low as the $1.1 million already distributed. Future changes in the estimate of the fair value of the CVRs will impact results of operations and could be material. As of December 31, 2010, restricted assets in an escrow account for the benefit of the CVRs were $4.2 million. The escrow account includes $3.0 million for a potential tax indemnity obligation, which, if such obligation is not triggered, will benefit the CVRs by $1.9 million with the remainder reverting back to the general cash of the Company. Further information regarding the fair value of the CVRs is included in Note 13 to the Consolidated Financial Statements.

Other Contingencies. Other contingencies are recorded when it is probable that a liability exists and the value can be reasonably estimated.

The Company had a potential indemnification liability related to state income taxes and related interest that had been assessed against ProQuest Information and Learning (PQIL). On August 27, 2010, PQIL received a decision and order of determination from the Michigan taxing authority. According to the determination of the Michigan taxing authority, PQIL was liable to the State of Michigan for unpaid taxes and interest in the amount of approximately $10.4 million. In order to expedite resolution of this matter and access the Michigan Court of Claims, the Company paid this indemnification liability to the state of Michigan on behalf of PQIL on September 7, 2010. The Company has filed an action in the Michigan Court of Claims to pursue a refund of the assessment. Management believes it is more likely than not that the Company s position will be upheld in the Court of Claims and a $10.4 million tax receivable for the expected refund is recorded in other assets on the consolidated balance sheet as of December 31, 2010.

This indemnification liability was identified as an agreed contingency for purposes of the CVRs issued as part of the VLCY merger consideration. In accordance with the terms of the merger agreement, dated June 20, 2009, fifty percent (50%) of any amount that is paid or due and payable with respect to each agreed contingency would offset payments due under the CVRs from an amount held for such payments by Wells Fargo Bank, N.A., as escrow agent, in an escrow account. Upon payment of the approximately $10.4 million, the Company requested a disbursement to the Company from the escrow account in an amount equal to fifty percent (50%) of the payment, or approximately $5.2 million. This cash disbursement was received by the Company during the third quarter of 2010. On September 20, 2010, the Company amended the merger agreement and the escrow agreement to extend the term of the escrow agreement until the later of the full distribution of the escrow funds or the final resolution of the agreed contingency. The final resolution of the tax litigation or potential settlement could result in a refund ranging from zero to approximately $10.4 million. As of December 31, 2010, the fair value of the CVR includes a reduction of approximately $1.0 million related to this state income tax issue. This calculated reduction amount uses management assumptions related to the likelihood of any ultimate cash outflows for this agreed-upon contingency. However, the actual impact on the CVR could be up to one-half of the $10.4 million if PQIL s position is not ultimately upheld. Additionally, if PQIL s position is not ultimately upheld, the Company could incur up to $10.4 million of indemnification expense in future periods on its Statements of Operations, partially offset by any reduction to the CVRs liability.

Recently Issued Financial Accounting Standards

Information regarding recently issued accounting standards is included in Note 2 to the Consolidated Financial Statements, which is included in Item 8 of this Annual Report on Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk

We had outstanding at yearend $95.4 million of indebtedness under Cambium Learning s senior secured credit facility (excluding the $2.9 million in outstanding letters of credit) and had outstanding at yearend $56.7 million of the senior unsecured notes due on April 11, 2014, which were issued on April 12, 2007. With the expiration of our interest rate swap on June 30, 2010, all of the indebtedness under Cambium Learning s variable rate facilities would result in the interest rates under these facilities being limited by the maximum interest rate applicable to the facilities. Assuming an applicable tax rate of 38.5%, we expect that our annual earnings would decrease by approximately $0.6 million for each one percentage point increase in the rates applicable to Cambium Learning s variable debt, and by $5.9 million for a ten percent increase in the variable component used in determining the interest rates applicable to Cambium Learning s variable debt.

As described in Liquidity and Capital Resources and in Note 23 to the Consolidated Financial Statements, in February 2011, we closed an offering of $175 million aggregate principal amount of Notes (fixed rate) due 2017 and entered into a new $40 million asset-based revolving credit facility. We used a portion of the net proceeds from the offering to repay in full outstanding indebtedness under the secured credit facility and senior unsecured notes that existed as of December 31, 2010.

Foreign Currency Risk

We do not have material exposure to changes in foreign currency rates. As of December 31, 2010, we do not have any outstanding foreign currency forwards or option contracts.

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Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Cambium Learning Group, Inc.

We have audited the accompanying consolidated balance sheets of Cambium Learning Group, Inc. and subsidiaries (the Company), as of December 31, 2010 and 2009, and the related consolidated statements of operations, shareholders equity and comprehensive income (loss), and cash flows for the years then ended. The Company s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company, as of December 31, 2010 and 2009, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 10, 2011 expressed an unqualified opinion.

/s/ Whitley Penn LLP
Dallas, Texas
March 10, 2011

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Cambium Learning Group, Inc.

We have audited Cambium Learning Group, Inc. and subsidiaries (the Company) internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying *Management s Report on Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders equity and comprehensive income (loss), and cash flows for the years then ended, and our report dated March 10, 2011, expressed an unqualified opinion on those consolidated financial statements.

/s/ Whitley Penn LLP

Dallas, Texas

March 10, 2011

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Report of Independent Registered Public Accounting Firm

To the Board of Managers and Members of VSS-Cambium Holdings, LLC:

We have audited the accompanying consolidated balance sheet of VSS-Cambium Holdings, LLC (a Delaware limited liability company) and subsidiaries (the Company) as of December 31, 2008, and the related consolidated statements of operations, members equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of VSS-Cambium Holdings, LLC and subsidiaries as of December 31, 2008, and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ Grant Thornton LLP
Boston, Massachusetts
October 8, 2009 except for
Note 21, as to which the date
is October 29, 2009 and except for
Note 1 (Segments), as to which the date is March 26, 2010

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Cambium Learning Group, Inc. and Subsidiaries
Consolidated Statements of Operations

(In thousands, except per share data)	For the Years Ended December 31, 2010	2009	2008
Net revenues:			
Product revenues	$ 160,778	$ 90,385	$ 89,207
Service revenues	20,482	10,663	10,524
Total net revenues	181,260	101,048	99,731
Cost of revenues:			
Cost of product revenues	41,583	19,591	20,246
Cost of service revenues	18,308	7,257	7,463
Amortization expense	28,511	17,527	15,966
Total cost of revenues	88,402	44,375	43,675
Research and development expense	10,558	5,611	6,416
Sales and marketing expense	45,987	23,368	24,600
General and administrative expense	23,857	30,519	16,156
Shipping and handling costs	3,570	1,512	2,348
Depreciation and amortization expense	9,154	9,723	11,453
Goodwill impairment		9,105	75,966
Embezzlement and related expense (recoveries)	(353)	129	7,254
Total costs and expenses	181,175	124,342	187,868
Income (loss) before interest, other income (expense) and income taxes	85	(23,294)	(88,137)
Net interest income (expense):			
Interest income	19	10	86
Interest expense	(17,311)	(19,487)	(18,520)
Net interest income (expense)	(17,292)	(19,477)	(18,434)
Gain from settlement with previous stockholders			30,202
Loss on extinguishment of debt			(5,632)
Other income (expense), net	674	(698)	(981)
Loss before income taxes	(16,533)	(43,469)	(82,982)
Income tax benefit	583	7,704	13,422

Net loss	$	(15,950)	$	(35,765)	$	(69,560)
Net loss per common share:						
Basic net loss per common share	$	(0.36)	$	(1.63)	$	(3.39)
Diluted net loss per common share	$	(0.36)	$	(1.63)	$	(3.39)
Average number of common shares and equivalents outstanding:						
Basic		44,322		21,994		20,493
Diluted		44,322		21,994		20,493

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries
Consolidated Balance Sheets

(In thousands, except per share data)	As of December 31, 2010	2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 11,831	$ 13,345
Accounts receivable, net	31,627	19,127
Inventory	22,015	19,812
Deferred tax assets	3,703	6,267
Restricted assets, current	3,064	9,755
Other current assets	3,937	6,010
Total current assets	76,177	74,316
Property, equipment and software at cost	32,944	24,951
Accumulated depreciation and amortization	(7,838)	(4,294)
Property, equipment and software, net	25,106	20,657
Goodwill	151,915	151,915
Acquired curriculum and technology intangibles, net	33,063	44,695
Acquired publishing rights, net	38,707	52,312
Other intangible assets, net	22,132	28,133
Pre-publication costs, net	7,834	5,464
Restricted assets, less current portion	12,641	14,930
Other assets	15,487	1,419
Total assets	$ 383,062	$ 393,841

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries
Consolidated Balance Sheets

	As of December 31, 2010	2009
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Notes payable line of credit	$	$ 5,000
Current portion of long-term debt	1,280	1,280
Current portion of capital lease obligations	378	443
Accounts payable	6,465	2,308
Contingent value rights, current	1,623	3,950
Accrued expenses	22,888	23,920
Deferred revenue, current	34,140	21,465
Total current liabilities	66,774	58,366
Long-term liabilities:		
Long-term debt, less current portion	150,850	150,487
Capital lease obligations, less current portion	12,317	12,695
Deferred revenue, less current portion	3,416	2,716
Contingent value rights, less current portion	5,746	5,649
Other liabilities	19,947	24,156
Total long-term liabilities	192,276	195,703
Commitments and contingencies (See Note 19)		
Stockholders equity:		
Preferred stock ($.001 par value, 15,000 shares authorized, zero shares issued and outstanding at December 31, 2010 and 2009)		
Common stock ($.001 par value, 150,000 shares authorized, 43,869 and 43,859 shares issued and outstanding at December 31, 2010 and 2009)	44	44
Capital surplus	259,887	258,789
Accumulated deficit	(135,218)	(119,268)
Other comprehensive income (loss):		
Pension and postretirement plans	(702)	206
Net unrealized gain on securities	1	1
Accumulated other comprehensive income (loss)	(701)	207
Total stockholders equity	124,012	139,772

Total liabilities and stockholders equity	$ 383,062	$ 393,841

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

	For the Years Ended December 31,		
(in thousands)	**2010**	**2009**	**2008**
Operating activities:			
Net loss	$ (15,950)	$ (35,765)	$ (69,560)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization expense	37,665	27,250	27,419
Goodwill impairment		9,105	75,966
Gain from settlement with previous stockholders			(30,202)
Gain from recovery of property held for sale			(1,578)
Loss on extinguishment of debt unamortized debt issuance costs			4,594
Non-cash interest expense	2,124	2,309	1,701
Amortization of deferred financing costs			604
Loss (gain) on derivative instruments	(992)	(1,390)	848
Change in fair value of contingent value rights obligation	(1,124)		
Loss on disposal of assets	89	2	
Stock-based compensation and expense	1,085	37	(618)
Issuance of subscription rights		2,222	
Deferred income taxes	(1,063)	(7,975)	(13,526)
Changes in operating assets and liabilities:			
Accounts receivable, net	(12,500)	2,306	(1,041)
Inventory	(2,203)	4,725	(3,152)
Other current assets	2,073	3,022	(355)
Other assets	(14,068)	1,579	(15)
Restricted assets	8,980	(7,948)	
Accounts payable	4,157	(1,812)	(2,941)
Accrued expenses	(40)	4,980	(2,651)
Deferred revenue	13,375	497	480
Other long-term liabilities	(1,447)	(1,115)	172
Other, net		(95)	
Net cash provided by (used in) operating activities	20,161	1,934	(13,855)
Investing activities:			
Cash paid for acquisitions, net of cash acquired	(1,106)	(9,697)	(112)
Expenditures for property, equipment, software and pre-publication costs	(13,335)	(3,395)	(3,201)
Settlement proceeds from previous stockholders			30,202
Net cash provided by (used in) investing activities	(14,441)	(13,092)	26,889
Financing activities:			

Repayment of debt		(1,761)		(5,585)		(24,280)
Principal payments under capital lease obligations		(443)		(289)		(226)
Borrowings under revolving credit agreement		19,000		10,000		5,000
Payment of revolving credit facility		(24,000)		(10,000)		
Proceeds from capital contributions		(30)		2,959		684
Proceeds from issuance of common stock in connection with the merger				25,000		
Borrowings from affiliates						7,000
Net cash provided by (used in) financing activities		(7,234)		22,085		(11,822)
Increase (decrease) in cash and cash equivalents		(1,514)		10,927		1,212
Cash and cash equivalents, beginning of year		13,345		2,418		1,206
Cash and cash equivalents, end of year	$	11,831	$	13,345	$	2,418
Supplemental disclosure of cash flow information:						
Income taxes paid (refunded)	$	15	$	(3,080)	$	742
Interest paid		12,002		16,936		16,215
Supplemental disclosure of noncash investing and financing activities:						
Non-cash acquisition costs paid				86,546		
Conversion of unsecured notes payable affiliates						7,000
Assets received in settlement property held for sale						1,578

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries
Consolidated Statements of Stockholders and Members Equity and Comprehensive Income (Loss)

(Dollars and shares in thousands)	Common Stock Shares	Par Value	Additional Paid in Capital	Members Interest	Accumulated Other Comprehensive Income	Accumulated Deficit	Total
Balance at December 31, 2007		$	$	$ 144,023	$	$ (13,943)	$ 130,080
Capital contribution by members				7,684			7,684
Net loss						(69,560)	(69,560)
Balance at December 31, 2008				151,707		(83,503)	68,204
Capital contribution by members				2,959			2,959
Conversion of members interests to common shares in connection with the merger (a)	20,493	20	154,646	(154,666)			
Issuance of common stock to members in exchange for a $25 million capital contribution in connection with the merger	3,846	4	24,996				25,000
Issuance of common stock to Voyager stockholders in connection with the merger	19,520	20	76,888				76,908
Issuance of subscription rights in connection with the merger			2,222				2,222
Stock-based compensation and expense			37				37
Comprehensive income (loss):							
Net loss						(35,765)	(35,765)
Pension plan					206		206
Unrealized gain on securities					1		1
Total comprehensive income (loss)							(35,558)
Balance at December 31, 2009	43,859	44	258,789		207	(119,268)	139,772
Issuance of restricted stock	10		25				25
Stock-based compensation and expense			1,103				1,103
Distribution of former members interest			(30)				(30)

Comprehensive income (loss):							
Net loss						(15,950)	(15,950)
Pension plan					(908)		(908)
Total comprehensive income (loss)							(16,858)
Balance at December 31, 2010	43,869	$ 44	$ 259,887	$	$ (701)	$ (135,218)	$ 124,012

(a) As the previous members are also majority stockholders in Cambium Learning Group, Inc., the common shares issued on December 8, 2009 in connection with the merger will be considered outstanding for all periods presented for purposes of calculating earnings per share.

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

Cambium Learning Group, Inc. and Subsidiaries
Notes to the Consolidated Financial Statements
Note 1 Basis of Presentation

Cambium Learning Group, Inc. Cambium Learning Group, Inc. (the Company) was incorporated under the laws of the State of Delaware in June 2009. On December 8, 2009, the Company completed the mergers of Voyager Learning Company (VLCY) and VSS-Cambium Holdings II Corp. (Cambium) into two of its wholly-owned subsidiaries, resulting in VLCY and Cambium becoming wholly-owned subsidiaries. Following the completion of the mergers, all of the outstanding capital stock of VLCY s operating subsidiaries, Voyager Expanded Learning, Inc. and LAZEL, Inc., was transferred to Cambium Learning, Inc., Cambium s operating subsidiary (Cambium Learning).

The results of VLCY are included in the Company s operations beginning with the December 8, 2009 merger date; therefore the 2009 financials include VLCY for the last 23 days of 2009 and the results of the Company for that full year. The transaction was accounted for as an acquisition of VLCY by Cambium, as that term is used under U.S. GAAP, for accounting and financial reporting purposes under the applicable accounting guidance for business combinations. In making this determination, management considered that (a) the newly developed entity did not have any significant pre-combination activity and, therefore, did not qualify to be the accounting acquirer and (b) the former sole stockholder of Cambium is the majority holder of the combined entity, while the prior owners of VLCY became minority holders in the combined entity. As a result, the historical financial statements of Cambium have become the historical financial statements of the Company.

Fiscal Year. The consolidated financial statements present the Company as of a calendar year ending on December 31.

Nature of Operations. The Company operates in three business segments: Voyager, a comprehensive intervention business; Sopris, a supplemental solutions education business; and Cambium Learning Technologies, a technology-based education product business.

Voyager offers reading, math and professional development programs targeted towards the at-risk and special education student populations. Voyager materials, offered online and via print, are tailored to meet the needs of these students and differ considerably from traditional instructional materials in design, approach and intensity. Lessons are based on scientific research and are carefully designed to effectively and efficiently address each of the strategies and skills necessary to improve the abilities of struggling students.

Sopris focuses on providing a diverse, yet comprehensive collection of printed and electronic supplemental education materials to complement core programs and to provide intense remediation aimed at specific skill deficits. When compared to products offered by the Company s other business units, Sopris products tend to be more narrowly-tailored and target a smaller, more specific audience.

Cambium Learning Technologies leverages technology to deliver subscription-based websites, online libraries, software and equipment designed to help students reach their potential in grades K through 12 and beyond. Cambium Learning Technologies products are offered under four different industry leading brands: Learning A-Z, ExploreLearning, Kurzweil Educational Systems and IntelliTools.

Segments. The Company operates as three reportable segments with separate management teams and infrastructures that offer various products and services: Voyager, the Company s comprehensive intervention business; Sopris, the Company s supplemental solutions education business; and Cambium Learning Technologies, the Company s technology-based education product business. Prior to the merger transaction completed on December 8, 2009, the Company had two reportable segments: Published Products and Learning Technologies. See Note 21 for further information on the Company s reportable segments.

Note 2 Significant Accounting Policies

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles 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 date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Subsequent actual results may differ from those estimates.

Principles of Consolidation. The consolidated financial statements of the Company include the accounts of the Company and its wholly owned subsidiaries: Voyager Learning Company, Cambium Education, Inc., LAZEL, Inc., Cambium Learning, Inc., and Kurzweil/IntelliTools, Inc. All inter-company accounts and transactions are eliminated in consolidation.

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Revenue Recognition. In October 2009, new guidance was issued regarding multiple-deliverable revenue arrangements and certain arrangements that include software elements. This guidance requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The guidance eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. In addition to requiring that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method, the guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which includes (1) vendor-specific objective evidence (VSOE), if available, (2) third party evidence (TPE), if vendor-specific objective evidence is not available, and (3) best estimate of selling price (BESP), if neither VSOE nor TPE is available. The objective of BESP is to determine the price at which the Company would transact a sale if the product or service were sold on a stand-alone basis. It also removes tangible products from the scope of software revenue guidance and provides guidance on determining whether software deliverables in an arrangement that includes a tangible product are covered by the scope of the software revenue guidance. This guidance must be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early adoption permitted. Effective January 1, 2010, the Company adopted this guidance on a prospective basis for all new or materially modified arrangements entered into after the adoption date. As a result of this change in methodology, revenues were approximately $0.5 million higher than they would have been under the prior guidance.

Revenues are derived from sales of reading, math and science, and professional development solutions to school districts primarily in the United States. Sales include printed materials and often online access to educational materials for individual students, teachers, and classrooms. Revenue from the sale of printed materials for reading and math products is recognized when the product is shipped to or received by the customer, depending on the shipping terms of the arrangement. Revenue for product support, training and implementation services, and online subscriptions is recognized over the period services are delivered. Revenue for the online content sold separately or included with certain curriculum materials is recognized ratably over the subscription period, typically a school year. Revenue for the Company s professional development courses, which can include an Internet delivery component, is recognized over the contractual delivery period. ExploreLearning and Learning A-Z derive revenue exclusively from sales of online subscriptions to their reading, math and science teaching websites and related training and professional development. Typically, the subscriptions are for a twelve- to twenty-four-month period and the revenue is recognized ratably over the period the online access is available to the customer.

The division of revenue between shipped materials, online materials, and ongoing support and services was determined in accordance with the new accounting guidance for revenue arrangements with multiple deliverables. The Company is not able to establish VSOE for each deliverable. Whenever VSOE cannot be established, the Company reviews the offerings of competitors to determine whether TPE can be established. TPE is determined based on the prices charged by the Company s competitors for a similar deliverable when sold separately. It may be difficult to obtain sufficient information on competitor pricing to substantiate TPE and therefore the Company may not always be able to use TPE.

The Company also uses BESP to determine the selling price of certain deliverables. BESP was primarily used for the printed materials for product lines acquired in the VLCY acquisition, which have historically been priced on a bundled basis with the related online materials. The determination of BESP considers the anticipated margin on that deliverable, the selling price and profit margin for similar parts or services, and the Company s ongoing pricing strategy and policies.

The Company plans to analyze the selling prices used in the allocation of arrangement consideration at least annually. Selling prices will be analyzed on a more frequent basis if a significant change in the business necessitates a more timely analysis or if the Company experiences significant variances in selling prices.

The Company s software products often include maintenance, support or on-line services. Maintenance and support services include telephone support, bug fixes, and, for certain products, rights to upgrades and enhancements on a when-and-if available basis. On-line services include storage, assignment, scoring and reporting. These services are recognized on a straight-line basis over the period they are provided. Revenues under multiple-element software license arrangements, which may include several different software products and services sold together, are allocated to each element based on the residual method in accordance with accounting guidance for software revenue recognition. In certain instances, telephone support and software repairs are provided for free within the first year of licensing the software. The cost of providing this service is insignificant, and is accrued at the time of revenue recognition.

The Company enters into agreements to license certain publishing rights and content. The Company recognizes the revenue from these agreements when the license amount is fixed and determinable, collection is reasonably assured, and the license period has commenced. For those license agreements that require delivery of additional materials as part of the license agreement, the revenue is recognized when the product is received by the customer. Shipments to school book depositories are on consignment and revenue is recognized based on shipments from the depositories to the schools.

Accounts Receivable. Accounts receivable are stated net of allowances for doubtful accounts and estimated sales returns. The allowance for doubtful accounts and estimated sales returns totaled $0.6 million at yearend 2010 and $0.3 million at yearend 2009. The allowance for doubtful accounts is based on a review of the outstanding balances and historical collection experience. The reserve for sales returns is based on historical rates of returns as well as other factors that in the Company s judgment could reasonably be expected to cause sales returns to differ from historical experience. A reconciliation of the accounts receivable reserve is shown in the table below for the periods indicated:

(in thousands)	**2008**	**2009**	**2010**
Beginning accounts receivable reserve	$ 695	$ 706	$ 316
Charged to costs and expenses	18	5	62
Charged to other accounts [1]	(5)	12	218
Recoveries		11	2
Write-offs	(2)	(418)	(41)
Other			
Ending accounts receivable reserve	$ 706	$ 316	$ 557

[1] **Charges to other accounts include sales returns**

Net Earnings (Loss) per Common Share. Basic net earnings (loss) per common share is computed by dividing net earnings (loss) by the weighted average number of common shares outstanding during the period. Diluted net earnings (loss) per common share is computed by dividing net earnings (loss) by the weighted average number of common shares outstanding during the period, including the potential dilution that could occur if all of the Company s outstanding stock awards that are in-the-money were exercised, using the treasury stock method. A reconciliation of the weighted average number of common shares and equivalents outstanding used in the calculation of basic and diluted net earnings per common share are shown in the table below for the periods indicated:

	For the Years Ended December 31,		
(in thousands)	**2010**	**2009**	**2008**
Basic	44,322	21,994	20,493
Dilutive effect of awards			
Diluted	44,322	21,994	20,493
Antidilutive securities:			
Options	3,757	2,256	
Warrants	105	72	
Subscription rights	6,509	4,711	

As the previous members of VSS-Cambium Holdings, LLC are also majority stockholders in Cambium Learning Group, Inc., 20.5 million of common shares issued on December 8, 2009 in connection with the merger were considered outstanding for the periods from January 1, 2009 to the merger date and the year ended December 31, 2008. The 20.5 million shares reflect the number of shares issued to the sole stockholder of Cambium at the merger date in consideration of its pre-merger equity interest. The weighted-average shares outstanding for the year ended December 31, 2009 includes an additional 3.8 million shares issued to the sole stockholder in exchange for a $25 million contribution made at the time of the merger and 19.5 million shares issued to VLCY stockholders, as well as 0.4 million shares related to a warrant issued to the sole stockholder for which all contingencies have been resolved and that requires little consideration to exercise. The weighted-average shares outstanding for the year ended

December 31, 2010 includes an additional 10 thousand shares of restricted stock. See Note 17 for further information on these awards.

Cash and Cash Equivalents. The Company considers all highly liquid investments with maturities of three months or less (when purchased) to be cash equivalents. The carrying amount reported in the Consolidated Balance Sheets approximates fair value.

Inventory. Inventory is stated at the lower of cost, determined using the first-in, first-out (FIFO) method, or market, and consists of finished goods. The Company reduces slow-moving or obsolete inventory to net realizable value.

Restricted Assets. Restricted assets consist of funds placed in a rabbi trust pursuant to the merger agreement for the purpose of funding certain obligations acquired in the VLCY merger, mostly deferred compensation, pension, and severance obligations, and an escrow of funds subject to the Contingent Value Rights (CVRs) described in Note 4.

Property and Equipment. Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed over the assets estimated useful lives using the straight-line method. Estimated lives are as follows.

	Estimated Useful Life
Building	35 years
Land improvements	19 years
Machinery and equipment	8 - 15 years
Furniture and fixtures	8 years
Computer equipment and software	3 - 5 years
Leasehold improvements	Lesser of useful life or lease term

Expenditures for maintenance and repairs, as well as minor renewals, are charged to operations as incurred, while improvements and major renewals are capitalized.

Purchased and Developed Software. Purchased and developed software includes the costs to purchase third party software and to develop internal-use software. The Company follows applicable guidance for the costs of computer software developed or obtained for internal use for capitalizing software projects. Software costs are amortized over the expected economic life of the product, generally three to five years. At December 31, 2010 and 2009, unamortized capitalized software was $7.3 million and $3.4 million, respectively, which included amounts of software under development of $1.2 million and $0.6 million, respectively.

Acquired Curriculum and Technology. Acquired curriculum and technology represents curriculum and developed technology acquired in the acquisitions of VLCY in 2009, certain assets of Tobii Assistive Technology, Inc. in 2008 and Cambium Learning in 2007 and is the initial purchase accounting value placed on the past development and refinement of the core methodologies, processes, measurement techniques, and technologies by which the Company structures curriculum. Acquired curriculum and technology is being amortized using an accelerated method over six to seven years, as it has an economic benefit declining over the estimated useful life. Acquired curriculum and technology is presented net of accumulated amortization of $16.0 million and $4.3 million as of yearend 2010 and 2009, respectively.

Acquired Publishing Rights. A publishing right allows the Company to publish and republish existing and future works, as well as transform, adapt, or create new works based on previously published materials. The Company determines the fair market value of the publishing rights arising from business combinations by discounting the after-tax cash flows projected to be derived from the publishing rights and titles to their net present value using a rate of return that accounts for the time value of money and the appropriate degree of risk. The useful life of the publishing rights is based on the lives of the various titles involved, which is generally ten years. The Company calculates amortization using either the straight-line method or the percentage of the projected discounted cash flows derived from the titles in the current year as a percentage of the total estimated discounted cash flows over the remaining useful life. The Company periodically reviews the recoverability of the publishing rights based on expected net realizable value, and generally retires the assets once fully depreciated. Acquired publishing rights are presented net of accumulated amortization of $51.6 million and $38.0 million as of yearend 2010 and 2009, respectively.

Pre-Publication Costs. The Company capitalizes certain pre-publication costs of its curriculum including art, prepress, editorial, and other costs incurred in the creation of the master copy of its curriculum products. Pre-publication costs are amortized over the expected life of the education program, generally on an accelerated basis over a period of five years. The amortization methods and periods chosen reflect the expected sales generated by the education programs. The Company periodically reviews the recoverability of the capitalized costs based on expected net realizable value, and generally retires the assets once fully depreciated. Pre-publication costs are presented net of accumulated amortization of $5.3 million and $2.9 million as of yearend 2010 and 2009, respectively.

Goodwill and Other Intangible Assets. Goodwill and other intangible assets are related to the acquisitions of VLCY in 2009, certain assets of Tobii Assistive Technology, Inc. in 2008 and Cambium Learning in 2007. Other intangible assets include tradenames/trademarks, reseller networks, customer relationships/lists, and conference attendee relationships, which are being amortized on a straight-line basis over estimated lives ranging from six to sixteen years.

Other intangible assets are presented net of accumulated amortization of $27.5 million and $26.2 million as of yearend 2010 and 2009, respectively.

See Note 7 herein for further discussion of the Company s review of goodwill and the related impairment charge recognized in the year ended December 31, 2009.

Depreciation and Amortization. Depreciation and amortization for the years ended December 31, 2010, December 31, 2009, and December 31, 2008 was broken out as follows:

	For the Years Ended December 31,		
(in thousands)	2010	2009	2008
Acquired publishing rights	$ 13,605	$ 13,949	$ 13,566
Acquired curriculum and technology	11,632	1,852	1,328
Pre-publication costs	2,450	1,707	1,072
Internally developed software related to product	824	19	
Total amortization included in cost of revenues	28,511	17,527	15,966
Tradenames and trademarks	1,467	1,349	1,330
Other intangible assets	4,534	6,555	8,650
Property, equipment and software	3,153	1,819	1,473
Total depreciation and amortization included in operating expenses	9,154	9,723	11,453
Total depreciation and amortization	$ 37,665	$ 27,250	$ 27,419

Impairment of Long Lived Assets. The Company reviews the carrying value of long lived assets for impairment whenever events or changes in circumstances indicate net book value may not be recoverable from the estimated undiscounted future cash flows. If the review indicates any assets are impaired, the impairment of those assets is measured as the amount by which the carrying amount exceeds the fair value as estimated by either quoted market prices or discounted cash flows. Assets to be disposed of are reported at the lower of the carrying amount or fair value less cost of disposal. The determination whether the Company s definite-lived intangible assets are impaired involves significant assumptions and estimates, including projections of future cash flows, the percentage of future revenues and cash flows attributable to the intangible assets, asset lives used to generate future cash flows, and royalty relief savings attributable to trademarks. For the years ended December 31, 2010, 2009 and 2008, no impairment was indicated.

Deferred Costs. Certain up-front costs associated with completing the sale of the Company s products are deferred and recognized as the related revenue is recognized.

Advertising Costs. The Company, from time to time, ships products to prospective customers as samples. Samples costs are expensed to sales and marketing expense upon shipment and totaled $3.2 million, $1.5 million, and $1.6 million for the years ended December 31, 2010, 2009 and 2008, respectively. Other costs of advertising, which include advertising, print, and photography expenses, are expensed as incurred and totaled $1.3 million, $2.9 million, and $4.5 million for the years ended December 31, 2010, 2009 and 2008, respectively. The Company recognizes catalog expense when the catalog is mailed to potential customers. The cost to print the catalog is recorded in prepaid expenses on the Consolidated Balance Sheets until such time that the catalog is mailed.

Income Taxes. Provision is made for the expense, or benefit, associated with taxes based on income. The provision for income taxes is based on laws currently enacted in every jurisdiction in which the Company does business and considers laws mitigating the taxation of the same income by more than one jurisdiction. Significant judgment is required in determining income tax expense, current tax receivables and payables, deferred tax assets and liabilities, and valuation allowance recorded against the net deferred tax assets. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, taxable income in prior carryback years, loss carryforward limitations, and tax planning strategies in assessing whether deferred tax assets will be realized in future periods. If, after consideration of these factors, management believes it is more likely than not that a portion of the deferred tax assets will not be realized, a valuation allowance is established. The amount of the deferred tax asset considered realizable could be reduced if estimates of future taxable income during the carryforward period are reduced.

The Company recognizes liabilities for uncertain tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if available evidence indicates that it is more likely than not that the position will be sustained on audit. The second step requires the Company to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. The Company reevaluates its uncertain tax positions on a periodic basis, based on factors such as changes in facts and circumstances, changes in tax law, effectively settled issues under audit and new audit activity. The Company accrues interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense.

Royalty Advances. Royalty advances to authors are capitalized and represent amounts paid in advance of the sale of an author s product. These costs are then expensed as the related publication is sold. The Company evaluates advances periodically to determine if they are expected to be utilized and reserves any portion of a royalty advance that is not expected to be recovered.

Sales Taxes. The Company reports sales taxes collected from customers and remitted to governmental authorities on a net basis. Sales tax collected from customers is excluded from revenues. Collected but unremitted sales tax is included as part of accrued expenses in the accompanying Consolidated Balance Sheets.

Stock-Based Compensation. The Company accounts for its stock-based compensation in accordance with applicable accounting guidance for share-based payments. This guidance requires all share-based payments to be recognized in the Consolidated Statement of Operations based on their fair values. Compensation costs for awards with graded vesting are recognized on a straight-line basis over the anticipated vesting period.

Recently Issued Financial Accounting Standards.

In October 2009, new guidance was issued regarding multiple-deliverable revenue arrangements and certain arrangements that include software elements. See Revenue Recognition above for disclosures related to the Company s adoption of this guidance.

In January 2010, new guidance was issued regarding improving disclosures about fair value measurements. This standard amends the disclosure guidance with respect to fair value measurements for both interim and annual reporting periods. Specifically, this standard requires new disclosures for significant transfers of assets or liabilities between Level 1 and Level 2 in the fair value hierarchy; separate disclosures for purchases, sales, issuance and settlements of Level 3 fair value items on a gross, rather than net, basis; and more robust disclosure of the valuation techniques and inputs used to measure Level 2 and Level 3 assets and liabilities. Except for the detailed disclosures of changes in Level 3 items, which will be effective for the Company as of January 1, 2011, the remaining new disclosure requirements were effective for the Company as of January 1, 2010. The Company has included these new disclosures, as applicable, in Note 13 to the Consolidated Financial Statements.

In December 2010, new guidance was issued regarding the disclosure of supplementary pro forma information for business combinations. This guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The guidance also expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. This guidance is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010 with early adoption permitted. The Company will make the required disclosures for any business combination that closes on or after January 1, 2011.

Note 3 Embezzlement

On April 26, 2008, the Company began an internal investigation that revealed irregularities over the control and use of cash and certain other general ledger accounts of the Company, revealing a misappropriation of assets (the Embezzlement Matter). These irregularities were perpetrated by a former employee over more than a three-year period beginning in 2004 and continuing through April 2008. The embezzlement loss incurred in each year, before the effect of income taxes, is as follows:

Year/Period		Amount *(in thousands)*
2007 and prior		12,196
2008		1,800
Total Embezzlement Loss	$	13,996

In addition to these losses, the Company has incurred fees and expenses as a result of the embezzlement totaling $5.5 million in 2008, net of recoveries. In 2008, the Company took possession of five boats which were purchased by the former employee using the embezzled funds. As of December 31, 2008, the boats had an appraised value of

$1.6 million and were netted against the fees and expenses incurred as a result of the embezzlement. In the year ended December 31, 2009, the Company incurred fees and expenses as a result of the embezzlement totaling $0.1 million, net of recoveries. In the year ended December 31, 2010, the Company received net recoveries of ($0.4) million.
When the Company acquired Cambium Learning and its subsidiaries on April 12, 2007, $20.0 million of the purchase price was held in escrow. Pursuant to an agreement dated July 10, 2008 by and between the former stockholders of the predecessor company and the members of the successor company, the remaining escrow amount was distributed in its entirety to VSS-Cambium Settlement Fund, LLC (Settlement Fund), acting as an agent for Cambium Learning. Also, the former stockholders of the predecessor company agreed to contribute an additional $9.3 million to the Settlement Fund. The total settlement of $30.2 million, including interest income of $0.9 million, was distributed to Cambium Learning and used to cover costs and pay down a portion of the senior credit facility. Since the embezzlement was discovered after the initial purchase allocation, the entire settlement amount was recorded as a gain from settlement with previous stockholders on the accompanying Consolidated Statements of Operations. The former stockholders also agreed to forego any claims or rights to any amount held in escrow in exchange for which the members of VSS-Cambium Holdings, LLC indemnified the former stockholders from any claims in connection with the Embezzlement Matter.

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Note 4 Acquisitions

Acquisition of VLCY

On December 8, 2009, the Company acquired VLCY and its subsidiaries. The Company determined that the merger could capitalize upon potential strategic, operational and financial synergies to generate significant cash flow and strengthen the leadership position of Cambium and VLCY in education solutions for the pre-K-12 market. In reaching its decision to acquire VLCY, which resulted in the recognition of $44.6 million of goodwill, there were a number of reasons why the Company believed the acquisition would be beneficial. These potential benefits include:

- Capitalizing on the complementary nature of the companies products to enhance certain products with minimal development costs, achieve critical mass in certain markets, facilitate the cross-selling of each other s products to established customers, and expand sales and marketing reach.

- Leveraging the companies combined implementation services and robust technological capabilities.

- Combining two experienced management teams to spread best practices , attract leading authors and programs, and acquire additional product lines and business as opportunities arise.

- Increasing sales into existing and new markets of certain products through complementary sales channels.

The acquisition was accounted for as a purchase transaction. The consolidated financial statements of the Company include the results of VLCY from December 8, 2009, the date of acquisition. The purchase price was allocated among tangible and intangible assets acquired and liabilities assumed based on fair values at the transaction date. The excess of the purchase price over the acquired tangible and intangible assets and liabilities was recorded as goodwill. The Company acquired the stock of VLCY and, therefore, the additional goodwill resulting from this transaction is not expected to be tax deductible. Acquisition costs of zero, $13.6 million, and $26,000 are included in general and administrative expenses in the Consolidated Statements of Operations for the years ended December 31, 2010, 2009, and 2008, respectively.

Consideration to the VLCY shareholders consisted of:

- at the election of the stockholder, either,
  - one share of Company common stock, or

  - $6.50 in cash, limited to a maximum of $67.5 million in the aggregate and prorated in accordance with the merger agreement;
- plus, regardless of the election made,
  - an amount in cash equal to the amount of certain tax refunds specified in the merger agreement and received by VLCY prior to the closing of the mergers (reduced by the amount of the VLCY tax refunds contractually required to be placed in escrow at closing), divided by the total number of shares of VLCY common stock outstanding immediately prior to the effective time of the mergers; plus

  - a Contingent Value Right (CVR) to receive cash in an amount equal to the aggregate amount of specified tax refunds received after the closing of the mergers and various other amounts deposited in escrow on or after the closing date, reduced by any payments to be made under the escrow agreement entered into in connection with the mergers, with respect to agreed contingencies, a potential working capital adjustment and allowed expenses, divided by the total number of shares of VLCY common stock outstanding immediately prior to the effective time of the mergers.

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Additionally, pursuant to the merger, a share-based award held by the Chief Executive Officer of VLCY was required to be converted into rights or options for shares of the Company with the same terms and conditions that were applicable to the rights or options for VLCY shares. Therefore, in accordance with applicable accounting guidance for business combinations, the fair value, prior to conversion, of replacement equity awards issued for pre-combination services at the date of acquisition is included in the calculation of the purchase price.
The following represents the components of the purchase price:

(in thousands)		
Cash paid to shareholders making the cash election	$	67,499
Cash paid to shareholders for specified tax refunds		15,523
Fair value of shares of Company issued to shareholders		76,907
Fair value of equity awards converted at acquisition		22
Fair value of the Contingent Value Rights		9,617
Total consideration	$	169,568

The fair value of Company shares issued to VLCY shareholders of $76.9 million was determined using a per share value of $3.94 multiplied by the 19.5 million shares issued. The $3.94 fair value per share was determined using a volume-weighted average of the five days before and after the end of a settling in period that the Company determined began as of the date trading began on December 9, 2009 and continued through December 31, 2009.
The first CVR payment date was in September 2010 and $1.1 million was distributed to the escrow agent at that time for distribution to holders of the CVRs. A second CVR distribution will be made in June 2011 and the final distribution, if any, with respect to a potential tax indemnity obligation will be in October 2013. Additionally, as described in Note 19, any amounts due to CVR holders as a result of refunds received related to the Michigan tax payment will be distributed upon the final resolution of this agreed contingency.
The fair value of the liability for the CVRs is determined using a probability weighted cash flow analysis which takes into consideration the likelihood, amount and timing of cash flows of each element of the pool of assets and liabilities included in the CVR. The determination of fair value of the CVRs involves significant assumptions and estimates, which are reviewed at each quarterly reporting date. As of December 31, 2010, a fair value of $7.4 million has been recorded as a liability for the remaining CVR payments. During 2010, a gain of $1.1 million was recorded in general and administrative expense to reflect a decrease in the estimated fair value of the CVR liability. The ultimate value of the CVRs is not known at this time; however, it is not expected to be more than $11 million and could be as low as the $1.1 million already distributed. Future changes in the estimate of the fair value of the CVRs will impact results of operations and could be material. As of December 31, 2010, restricted assets in an escrow account for the benefit of the CVRs were $4.2 million. See Note 13 for further information on the fair value of the CVRs and related escrow trust.

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The following represents the allocation of the purchase price:

(in thousands)		
Cash and cash equivalents	$	73,325
Accounts receivable		10,883
Income tax receivable		4,713
Inventory		11,687
Other current assets		11,919
Property, plant and equipment		3,216
Intangible assets		50,249
Curriculum in development		909
Other assets		11,891
Accounts payable and accrued expenses		(14,835)
Deferred revenue		(21,774)
Capital lease obligations		(187)
Other liabilities		(17,075)
Goodwill		44,647
Total net assets acquired	$	169,568

Other identified intangibles acquired consist of the following:

	Voyager	Cambium Learning Technologies	Useful Life
	(in thousands)		
Curriculum and technology	$ 23,700	$ 19,000	7 years
Customer relationships	3,880	1,500	7 years
Tradenames and trademarks	1,610	559	15 years

Goodwill purchased in the acquisition has been allocated to the Company s Voyager and Cambium Learning Technologies reporting units as $24.9 million and $19.7 million, respectively. Valuations were established giving consideration to the three basic approaches to value with the method or methods applied for each asset depending on the nature of the asset and the type and reliability of information available for the analysis and were based upon the Company s projected revenue growth assumptions through each asset s estimated useful life. Discounted cash flows were based upon the Company s weighted-average cost of capital of 25% and an estimated effective tax rate of 38% at the time of the mergers. Curriculum and technology and customer relationships were valued using a form of the income approach known as the excess earnings method. Tradenames and trademarks were valued using a form of the income approach known as the relief-from-royalty method.

Supplemental Pro Forma Information

After the December 8, 2009 acquisition date, the VLCY acquisition contributed $4.5 million of net revenues and a pretax loss of $1.5 million to the Company s consolidated 2009 results. The following unaudited supplemental pro forma information presents the results of operations as if the VLCY acquisition had occurred at the beginning of the reporting period:

(in thousands) (unaudited)	Year Ended December 31, 2009
Net revenues	$ 188,211

Loss before income taxes		(61,270)
Net loss		(61,270)
Net loss per share basic and diluted	$	(1.38)

The supplemental pro forma information has been adjusted to include:

the pro forma impact of the amortization of intangible assets and the reduction in deferred revenue and related deferred costs based on the purchase price allocation;

the pro forma impact of reduced interest income lost as a result of the $58.0 million of cash used in the purchase price consideration (net of $25.0 million contributed by the sole stockholder of the Company at the time of the merger);

the pro forma impact of certain employment agreements and stock option grants entered into on the effective date of the merger, as well as the impact of certain contractual obligations, severance, retention, and other payments that became payable as a result of the merger;

the elimination of merger transaction costs incurred by the Company and VLCY; and

the pro forma tax effect of the merger, which was estimated using a combined company effective tax rate of 0%.

Basic and diluted loss per share is calculated using share equivalents outstanding at the merger date of 44.3 million. The pro forma results are presented for illustrative purposes only and do not reflect the realization of potential cost savings, or any integration costs. These pro forma results do not purport to be indicative of the results that would have actually been obtained if the acquisition occurred at the beginning of the respective reporting periods, nor is the pro forma data intended to be a projection of future results.

Acquisition of Certain Assets of Tobii Assistive Technology, Inc.

On July 25, 2008, Cambium acquired certain intellectual property rights and an inventory of titles with related author agreements of Tobii Assistive Technology, Inc., a Massachusetts corporation, for $112,003. The cash used to fund this acquisition came from the Company s general working capital. The purchase price was allocated as follows: $52,003 to goodwill (deductible for tax purposes), $39,000 to customer lists and $21,000 to developed technology. The customer lists and developed technology are amortized on a straight-line basis over their useful lives of two years and three years, respectively.

Note 5 Income Taxes

Losses before income taxes for the years ended December 31, 2010, 2009 and 2008 were all attributable to the United States.

Income tax benefit attributable to income included the following:

	Years Ended December 31,		
(in thousands)	**2010**	**2009**	**2008**
Current income tax expense (benefit):			
United States federal	$ 1	$	$
State and local	888	272	103
Current income tax expense	889	272	103
Deferred income tax benefit			
United States federal		(5,571)	(11,951)
State and local	(1,472)	(2,405)	(1,574)
Deferred income tax benefit	(1,472)	(7,976)	(13,525)
Income tax benefit	$ (583)	$ (7,704)	$ (13,422)

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Reconciliation of income tax benefit and the domestic federal statutory income tax benefit is as follows:

	Years Ended December 31,		
(in thousands)	**2010**	**2009**	**2008**
Statutory federal income tax benefit	$ (5,787)	$ (15,214)	$ (29,044)
Increase (reduction) from:			
State taxes (net of federal benefit)	(584)	(1,378)	(1,057)
Goodwill impairment		3,187	26,588
Purchase price adjustment			(10,244)
Merger transaction expenses		4,745	
Change in valuation allowance	6,436	625	122
Other	(648)	331	213
Income tax benefit	$ (583)	$ (7,704)	$ (13,422)

Deferred income taxes are primarily provided for temporary differences between the financial reporting basis and the tax basis of the Company s assets and liabilities. The tax effects of each type of temporary difference and carryforward that give rise to a significant portion of deferred tax assets (liabilities) at the end of fiscal 2010 and 2009 were as follows:

(in thousands)	**2010**	**2009**
Deferred tax assets are attributable to:		
Net operating loss carryforwards	**$ 18,682**	**$ 25,916**
Tax credit carryforwards	**7,673**	**7,670**
Reserves	**4,940**	**7,164**
Inventory	**5,697**	**4,435**
Deferred financing costs	**1,569**	**2,317**
Embezzlement loss	**1,404**	**1,528**
Fixed assets	**1,472**	**1,039**
Other	**728**	**738**
Total gross deferred tax assets	**42,165**	**50,807**
Valuation allowance	**(18,645)**	**(14,312)**
Net deferred tax assets	**23,520**	**36,495**
Deferred tax liabilities are attributable to:		
Intangibles	**(24,308)**	**(33,981)**
Deferred revenue	**(38)**	**(4,403)**
Total gross deferred tax liabilities	**(24,346)**	**(38,384)**
Net deferred tax liability	**$ (826)**	**$ (1,889)**

The deferred tax asset (liability) is classified as follows:

(in thousands)		2010		2009
Short-term deferred tax asset	**$**	**3,703**	**$**	**6,267**
Long-term deferred tax liability		**(4,529)**		**(8,156)**
Net deferred tax asset (liability)	**$**	**(826)**	**$**	**(1,889)**

The net increase in the valuation allowance in 2010 was $4.3 million. The valuation allowance increased during 2010 primarily because it offset the increase in the deferred tax asset derived from pre-tax losses. As of December 31, 2010, there is no amount of the valuation allowance for which subsequently recognized benefits will be allocated to reduce goodwill.

The net increase in the valuation allowance in 2009 was $11.5 million. The valuation allowance increased during 2009 primarily because of the acquisition of VLCY. VLCY had established a valuation allowance of $12.1 million as of the date of acquisition against all of its Federal and unitary state net deferred tax assets. The inclusion of Cambium s net deferred tax liabilities decreased VLCY s valuation allowance approximately $1.8 million. Post acquisition, increases in the Company s deferred tax assets were offset by increases in the valuation allowance. As of December 31, 2009, there is not any amount of the valuation allowance for which subsequently recognized benefits will be allocated to reduce goodwill.

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At December 31, 2010, the amounts and expiration dates of loss and tax credit carryforwards were as follows:

(in thousands)	Amount as of December 31, 2010	Expire or start expiring at the end of:
U.S. net operating loss [(1)]	$ 49,908	2028
State net operating loss carryforward (net):		
State tax net operating losses	1,214	2012-2028
Tax credits:		
Minimum tax credit	7,254	Carry forward indefinitely
Research and development tax credit	419	2014-2021
Total tax credits	7,673	

(1) **$35.7 million of the U.S net operating loss (NOL) above is related to the VLCY acquisition. The utilization of this NOL is subject to an annual limitation of $7.1 million.**

Income taxes paid, net of tax refunds, were $15 thousand for fiscal year 2010. Income taxes refunded, net of tax payments, were $3.1 million for fiscal year 2009. $3.4 million of the income taxes received during 2009 were deposited into escrow pursuant to the CVR obligation in connection with the merger agreement. Income taxes paid, net of refunds, for fiscal year 2008 were $0.7 million.

VLCY was formerly known as ProQuest Company. Under sale agreements with Snap-On Incorporated and Cambridge Scientific Abstracts, LP (CSA), the Company is liable to indemnify Snap-On Incorporated or CSA for any income taxes assessed against ProQuest Business Solutions (PQBS) or ProQuest Information and Learning (PQIL) for periods prior to VLCY s sale of PQBS or PQIL in 2006 and 2007, respectively. The Company has established a contingent liability for those matters where it is not probable that the position will be sustained and a tax receivable for those matters where it is deemed more likely than not that the position will be sustained. The amounts of the liability and receivable are based on management s best estimate given the Company s history with similar matters and interpretations of current laws and regulations in accordance with applicable accounting guidance for income tax positions.

Uncertain Tax Positions

The Company recognizes the financial statement impacts of a tax return position when it is more likely than not, based on technical merits, that the position will ultimately be sustained. For tax positions that meet this recognition threshold, the Company applies judgment, taking into account applicable tax laws, experience managing tax audits and relevant GAAP, to determine the amount of tax benefits to recognize in the financial statements. For each position, the difference between the benefit realized on the Company s tax return and the benefit reflected in the financial statements is recorded on the Consolidated Balance Sheets as an unrecognized tax benefit (UTB). The Company updates its UTBs at each financial statement date to reflect the impacts of audit settlements and other resolution of audit issues, expiration of statutes of limitation, developments in tax law and ongoing discussions with tax authorities. A reconciliation of the change in the UTB balance from January 1, 2010 to December 31, 2010, and January 1, 2009 to December 31, 2009, is as follows:

(in thousands)	2010	2009
Balance at the beginning of the year	$ 15,437	$
Increases for acquisitions during the period		14,685

Increases for tax positions taken during the period		752
Decreases for expiration of the statute of limitations	(5,058)	
Decreases relating to settlements	(3,181)	
Balance at the end of the year	$ 7,198	$ 15,437

The Company estimates it is reasonably possible that approximately $0.1 million in unrecognized tax benefits will be recognized in 2011 due to the statute of limitations expiring. Of this amount and included in the balance of unrecognized tax benefits at December 31, 2010 are approximately $0.8 million of tax benefits that, if recognized, would affect the effective tax rate. The recognition of the remaining uncertain tax positions would not affect the effective tax rate, but would instead increase or would have increased available tax attributes. However, the recognition of the tax attribute would be offset by an increase in the deferred tax asset valuation allowance resulting in no net impact in the effective tax rate.

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The Company recognizes interest accrued related to unrecognized tax benefits and penalties as income tax expense. Related to the unrecognized tax benefits noted above, the Company recognized no penalties and immaterial amounts for interest (gross) during 2010 and, as of December 31, 2010, has a liability for interest (gross) of approximately $0.1 million.

The Company files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. All U.S. tax years prior to 2008 related to the VLCY acquired entities have been audited by the Internal Revenue Service. Cambium and its subsidiaries have been examined by the Internal Revenue Service through the end of 2006. Various state tax authorities are in the process of examining income tax returns for various tax years through 2007.

Note 6 Property, Equipment and Software

Balances of major classes of assets and accumulated depreciation and amortization consist of the following:

	Year Ended December 31, 2010	2009
Land and building	$ 13,360	$ 13,360
Furniture and fixtures	1,187	775
Machinery, computers and equipment	6,947	5,867
Software	10,431	4,619
Leasehold improvements	1,019	330
Total	32,944	24,951
Less accumulated depreciation and amortization	7,838	4,294
Property,equipment and software, net	$ 25,106	$ 20,657

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Note 7 Goodwill and Other Intangible Assets

The changes in the carrying amount of goodwill for the years ended December 31, 2010 and December 31, 2009 are as follows:

(in thousands)	Publishing	Voyager	Sopris	CLT	Total
Balance as of December 31, 2008					
Goodwill	$ 153,533	$	$	$ 38,806	$ 192,339
Accumulated impairment losses	(75,966)				(75,966)
	77,567			38,806	116,373
Goodwill impairment	(9,105)				(9,105)
Allocation of Publishing goodwill among Voyager and Sopris segments	(68,462)	51,162	17,300		
Goodwill from acquisitions		24,923		19,724	44,647
Balance as of December 31, 2009					
Goodwill		161,156	17,300	58,530	236,986
Accumulated impairment losses		(85,071)			(85,071)
		76,085	17,300	58,530	151,915
Goodwill impairment					
Goodwill from acquisitions					
Balance as of December 31, 2010					
Goodwill		161,156	17,300	58,530	236,986
Accumulated impairment losses		(85,071)			(85,071)
	$	$ 76,085	$ 17,300	$ 58,530	$ 151,915

In accordance with applicable accounting guidance, goodwill and other indefinite-lived intangible assets are not amortized but are instead reviewed for impairment at least annually and if a triggering event is determined to have occurred in an interim period. The Company s annual impairment testing is performed as of December 1 of each year. The Company performed the 2010 yearend impairment analysis using four reporting units: Voyager; Sopris; the Learning A-Z and ExploreLearning subscription businesses from the Cambium Learning Technologies segment; and the Kurzweil and IntelliTools businesses from the Cambium Learning Technologies segment. As noted in the table above, the goodwill balances reported by the Voyager and Sopris reporting units at December 31, 2010 were $76.1 million and $17.3 million, respectively. Of the December 31, 2010 goodwill balance recorded in the Cambium Learning Technologies segment, $38.8 million is attributable to the Kurzweil and Intellitools reporting unit and $19.7 million is attributable to the Learning A-Z and Explore Learning reporting unit. In the first step of the impairment test for fiscal year 2010, the fair market value of each reporting unit was determined using an income approach and was dependent on multiple assumptions and estimates, including future cash flow projections with a terminal value multiple and the discount rate used to determine the expected present value of the estimated future cash flows. Future cash flow projections were based on management s best estimates of economic and market conditions over the projected period, including industry fundamentals such as the state of educational funding, revenue growth rates, future costs and operating margins, working capital needs, capital and other expenditures, and tax rates. The discount rate applied to the future cash flows was a weighted-average cost of capital and took into consideration market and industry conditions, returns for comparable companies, the rate of return an outside investor would expect to earn, and other relevant factors. The first step of impairment testing for fiscal 2010 showed that the fair value of each reporting unit exceeded its carrying value by at least 10%; therefore, no second step of testing was required.

In June 2009, the Company determined that the signing of the merger agreement was a triggering event requiring it to review goodwill for impairment. At the time of this review, the Company had two reporting units: Published Products and Learning Technologies. The first step of impairment testing as of June 30, 2009 showed that the carrying value of the Published Products unit exceeded its fair value and that the second step of testing was required for this unit. The second step requires the allocation of fair value of a reporting unit to all of the assets and liabilities of that reporting unit as if the reporting unit had been acquired in a business combination. The fair value was determined using an income approach based on forecasted operating results. As a result of the second step of the Company s second quarter 2009 impairment test, the goodwill balance for the reporting unit as of the measurement date was determined to be partially impaired, and an impairment charge of $9.1 million was recorded as of June 30, 2009. As of the second quarter 2009, the estimated fair market value of the reporting unit was estimated to have fallen below the book value as a result of worsening and prolonged adverse developments in the overall education funding environment, including the reductions in Reading First funding effective 2008 and the reductions in available state and local funds.

In conducting the annual goodwill impairment testing for fiscal 2008, the Company compared the book value of goodwill attributed to the Published Products and Learning Technologies segments with the estimated fair market values of these segments. As of yearend 2008, the estimated fair market value of the Published Products segment was estimated to be less than the book value as a result of lower future cash flow projections, driven by adverse developments in the education funding environment at the federal and local level. An impairment charge of $76.0 million related to Published Products was recorded in 2008 as a result of these factors. These estimates of fair market are dependent on multiple assumptions and inputs, including industry fundamentals such as the state of educational funding and the actual performance and future projections of the Company.

The Company s definite lived intangible assets and related accumulated amortization at the end of fiscal 2010 and 2009 consist of the following:

(in thousands)	Balance at December 31, 2008	Additions	Disposals	Balance at December 31, 2009	Additions	Disposals	Balance at December 31, 2010
Other intangible assets gross book value:							
Publishing rights	$ 90,300	$	$	$ 90,300	$	$	$ 90,300
Trademark	15,580	2,169		17,749			17,749
Customer relationships	13,739	5,380		19,119		(39)	19,080
Contracts	2,100			2,100		(2,100)	
Acquired curriculum and technology	6,321	42,700		49,021			49,021
Reseller network	12,300			12,300			12,300
Conference attendees	500			500			500
Non-compete	2,600			2,600		(2,600)	
Total other intangibles gross book value	143,440	50,249		193,689		(4,739)	188,950
Other intangible assets accumulated amortization:							
Publishing rights	(24,039)	(13,949)		(37,988)	(13,605)		(51,593)
Trademark	(2,460)	(1,349)		(3,809)	(1,467)		(5,276)
Customer relationships	(7,175)	(2,915)		(10,090)	(2,585)	39	(12,636)
Contracts	(1,487)	(555)		(2,042)	(58)	2,100	
Acquired curriculum and technology	(2,474)	(1,852)		(4,326)	(11,632)		(15,958)
Reseller network	(5,426)	(2,132)		(7,558)	(1,595)		(9,153)
Conference attendees	(293)	(86)		(379)	(53)		(432)

Non-compete	(1,490)	(867)		(2,357)	(243)	2,600	
Total other intangibles accumulated amortization	(44,844)	(23,705)		(68,549)	(31,238)	4,739	(95,048)
Other intangible assets, net	$ 98,596	$ 26,544	$	$ 125,140	$ (31,238)	$	$ 93,902

Estimated aggregate amortization expense expected for each of the next five years related to intangibles subject to amortization is as follows:

(in thousands)	Amortization - Cost of Revenues	Amortization - Operating Expense	Total Amortization
2011	$ 21,785	$ 4,296	$ 26,081
2012	17,519	3,440	20,959
2013	12,710	2,779	15,489
2014	8,978	2,436	11,414
2015	5,972	2,175	8,147
Thereafter	4,806	7,006	11,812
	$ 71,770	$ 22,132	$ 93,902

Note 8 Other Current Assets

Other current assets at the end of fiscal 2010 and 2009 consist of the following:

(in thousands)	**2010**	**2009**
Deferred costs	$ 2,163	$ 269
Prepaid expenses	1,463	2,019
Income taxes receivable	249	1,322
Other current assets	62	
Settlement receivable		2,400
Total	$ 3,937	$ 6,010

The settlement receivable amount relates to an amount due from a subsidiary sold by VLCY in the years prior to the merger with Cambium. The receivable was allocated a portion of the purchase price at the acquisition date and was also included in the CVRs obligation created in the merger with VLCY, as described in Note 4.

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Note 9 Other Assets

Other assets at the end of fiscal 2010 and 2009 consist of the following:

(in thousands)	2010	2009
Tax receivables	$ 11,168	$
Deferred financing costs	1,542	
Collateral investments	1,964	1,061
Other	813	358
Total	$ 15,487	$ 1,419

Tax receivables include the $10.4 million receivable from the state of Michigan as discussed in Note 19 to the Consolidated Financial Statements. The deferred financing costs represent costs incurred in connection with the issuance of the $175 million aggregate principal amount of 9.75% senior secured notes as described in Note 23 to the Consolidated Financial Statements.

Note 10 Accrued Expenses

Accrued expenses at the end of fiscal 2010 and 2009 consist of the following:

(in thousands)	2010	2009
Salaries, bonuses and benefits	$ 10,183	$ 12,428
Accrued royalties	3,220	1,770
Pension and post-retirement medical benefits	1,209	1,293
Deferred compensation	525	633
Interest rate swap		992
Other	7,751	6,804
Total	$ 22,888	$ 23,920

Salaries, bonuses and benefits accrued as of December 31, 2009 include severance and other amounts owed to employees and former employees that are related to the merger agreement between the Company and VLCY. As of the merger date, funds related to these obligations, as well as obligations related to certain deferred compensation and pension liabilities, were placed in a rabbi trust pursuant to the merger agreement. As of December 31, 2010, the funds in this rabbi trust totaled $11.5 million. See Note 15 for further description of the Company s pension benefits.

Note 11 Other Liabilities

Other liabilities at the end of fiscal 2010 and 2009 consist of the following:

(in thousands)	2010	2009
Pension and post-retirement medical benefits, long-term portion	$ 10,847	$ 10,509
Long-term deferred tax liability	4,529	8,156
Long-term income tax payable	847	1,255
Long-term deferred compensation	613	1,179
Other	3,111	3,057
Total	$ 19,947	$ 24,156

See Note 15 for further description of the Company s pension benefits.

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Note 12 Leases

Capital Lease Obligations

The Company leases a warehouse, office space and certain administrative equipment under capital lease agreements with original lease terms up to 10 years. Capital leases that exist as of year-end 2010 expire no later than 2016.

The Company has a build-to-suit lease for warehouse and office space in Frederick, Colorado. The lease requires minimum monthly rents that expire on October 31, 2016. The lease is renewable at the Company s option for two additional periods of five years each. The Company has an outstanding letter of credit in the amount of $1.0 million to secure the lease. The Company evaluated the provisions of the accounting guidance relating to the effect of a lessee s involvement in an asset construction and concluded that due to the Company s collateral to the landlord, in the form of the $1.0 million letter of credit, that it is deemed the owner of the land and building for accounting purposes. As a result, the related capitalized costs for the warehouse space in Frederick, Colorado are classified as land and building and are included in property, plant and equipment, net, in the accompanying Consolidated Balance Sheets. A corresponding liability is included in the current portion of capital lease obligations and capital lease obligations, less current portion. [Due to the acquisition of Cambium, the Company recorded an increase of $4.8 million in purchase accounting related to the fair market value of land, land improvements, and building for the warehouse space on the date of acquisition. The related liability has been adjusted accordingly.] The cost of the building is being depreciated over a 35-year useful life. The amount of the depreciation expense was $0.4 million for each year presented. Additionally, the obligation will be reduced over the life of the lease at an interest rate of 5.54%. At the end of the original lease term, the land and building, net of accumulated depreciation, and the remaining liability will equal $9.8 million. The gross value of assets leased under the build-to-suit lease was $13.4 million at December 31, 2010 and December 31, 2009, which is included in the Land and Building category in Property, Equipment and Software. The accumulated amortization of these leased capital assets was $1.4 million and $1.0 million at December 31, 2010 and December 31, 2009, respectively.

The gross value of other leased capital assets used for administrative purposes was $0.1 million and $0.4 million at December 31, 2010 and December 31, 2009, respectively, which are included in the Machinery, Computers and Equipment category in Property, Equipment and Software. The accumulated amortization of leased capital assets was $0.1 million and $0.1 million at December 31, 2010 and December 31, 2009, respectively. Amortization of capital lease assets is recognized over the term of the lease on a straight line basis and included in depreciation and amortization expense.

Operating Leases

The Company leases certain facilities and equipment for production, selling and administrative purposes under agreements with original lease periods up to 10 years. Leases generally include provisions requiring payment of taxes, insurance, and maintenance on the leased property. Some leases include renewal options and rent escalation clauses, and certain leases include options to purchase the leased property during or at the end of the lease term.

Rent holidays and rent escalation provisions are considered in determining straight-line rent expense to be recorded over the lease term. The lease term begins on the date of initial term of the lease. Lease renewal periods are considered on a lease-by-lease basis and are generally not included in the initial lease term. Operating rent expense was $2.4 million, $1.1 million and $1.2 million, for the years ended December 31, 2010, 2009 and 2008, respectively.

Future minimum build-to-suit and capital lease payments under long-term non-cancelable leases, and the related present value of capital lease payments at December 31, 2010 are as follows:

(in thousands)		
2011	$	1,073
2012		1,110
2013		1,092
2014		1,138
2015		1,160
Thereafter		967

Total minimum lease payments		6,540
Less: Amount representing interest		(3,692)
Present value of net minimum lease payments		2,848
Less: Current portion		(378)
Add: Remaining liability at end of build-to-suit lease		9,847
Capital lease obligations, less current portion	$	12,317

Future minimum payments under all remaining non-cancelable operating leases are payable as follows:

(in thousands)

2011	$	1,460
2012		2,175
2013		1,632
2014		1,014
2015		774
Thereafter		2,061
Total minimum lease payments	$	9,116

Note 13 Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability (exit price), in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques are based on observable or unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company s market assumptions. These two types of inputs have created the following fair value hierarchy:

Level 1 Quoted prices for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which significant value drivers are observable.

Level 3 Valuations derived from valuation techniques in which significant value drivers are unobservable.

Applicable guidance requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

As of December 31, 2010, financial instruments include $11.8 million of cash and cash equivalents, restricted assets of $15.7 million, collateral investments of $2.0 million, the $95.4 million senior secured credit facility, the $56.7 million senior unsecured notes, $0.4 million of warrants, and $7.4 million in CVRs. As of December 31, 2009, financial instruments include $13.3 million of cash and cash equivalents, restricted assets of $24.7 million, collateral investments of $1.1 million, the $5.0 million revolver, the $97.2 million senior secured credit facility, the $54.6 million senior unsecured notes, $0.3 million of warrants, $9.6 million in CVRs, and the $1.0 million interest rate swap contract. The fair market values of cash equivalents and the restricted assets are equal to their carrying value as these investments are recorded based on quoted market prices and/or other market data for the same or comparable instruments and transactions as of the end of the reporting period. The fair value of the revolver is equal to its carrying value due to the short-term nature of the instrument and the interest rate being variable. The fair market value of the senior credit facility and senior unsecured notes are subject to market conditions; however, a limited trading market restricts the ability to freely trade the debt. The senior credit facility bears interest at a variable rate and management believes that the carrying value of the senior credit facility approximates its fair value.

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Assets and liabilities measured at fair value on a recurring basis are as follows:

(in thousands) **Description**	**As of December 31, 2010**	**Fair Value at Reporting Date Using** Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	**Total Gains (Losses)**
Restricted Assets:					
Money Market	$ 15,705	$ 15,705	$	$	$
Collateral Investments:					
Money Market	901	901			
Certificate of Deposit	1,063	1,063			
Warrant	360		360		23
Interest rate swap					992
CVRs	7,369			7,369	1,124

(in thousands) **Description**	**As of December 31, 2009**	**Fair Value at Reporting Date Using** Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	**Total Gains (Losses)**
Restricted Assets:					
Money Market	$ 24,686	$ 24,686	$	$	$
Collateral Investments:					
Certificate of Deposit	1,061	1,061			
Warrant	280		280		1
Interest rate swap	992		992		1,390
CVRs	9,617			9,617	

The warrant was valued as described in Note 17 below.

In accordance with the provisions in the accounting guidance for intangibles goodwill and other, for the year ended December 31, 2009, goodwill with a carrying amount of $161.0 million was written down to its implied fair value of $151.9 million, resulting in an impairment charge of $9.1 million, which was included in earnings for the period. As described in Note 7 above, no goodwill impairment was indicated upon completion of the Company s 2010 annual impairment analysis.

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The fair value of the liability for the CVRs is determined using a probability weighted cash flow analysis which takes into consideration the likelihood, amount and timing of cash flows of each element of the pool of assets and liabilities included in the CVR. The determination of fair value of the CVRs involves significant assumptions and estimates, which are reviewed at each quarterly reporting date. As of December 31, 2010, a fair value of $7.4 million has been recorded as a liability for the remaining CVR payments. During the year ended December 31, 2010, a gain of $1.1 million was recorded in general and administrative expense to reflect a decrease in the estimated fair value of the CVR liability. The ultimate value of the CVRs is not known at this time; however, it is not expected to be more than $11 million and could be as low as the $1.1 million already distributed. Future changes in the estimate of the fair value of the CVRs will impact results of operations and could be material. A detail of the elements included in the CVR is as follows:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) CVRs *(In thousands)*			
		Loss (Gain) for Changes in Estimated CVR Liability		
Components of CVR Liability:	**Estimated Fair Value as of Merger Date**	**2009**	**2010**	**Estimated Fair Value as of December 31, 2010**
Tax refunds received before closing of the merger	$ 1,583	$	$	$ 1,583
Other specified tax refunds	5,932		(1,431)	4,501
Tax indemnity obligation	1,717			1,717
Legal receivable	2,400			2,400
Michigan state tax liability	(900)		(140)	(1,040)
Other specified tax related liabilities	(579)		447	(132)
Costs incurred to collect tax refunds and by stockholders representative	(536)	(18)		(554)
Estimated fair value of CVR liability	**9,617**	**(18)**	**(1,124)**	**8,475**
Payments to holders of CVRs				1,106
Remaining estimated CVR liability				**$ 7,369**

As of December 31, 2010, restricted assets in an escrow account for the benefit of the CVRs were $4.2 million, with activity as follows. The escrow account includes $3.0 million for a potential tax indemnity obligation, which, if such obligation is not triggered, will benefit the CVRs by $1.9 million with the remainder reverting back to general cash of the Company.

	CVR Escrow Trust (In thousands)
Balance as of December 31, 2008	$
Funding of potential tax indemnity obligation	3,000
Tax refunds received	4,964

Costs incurred to collect tax refunds and by stockholders representative		(18)
Balance as of December 31, 2009		**7,946**
Tax refunds received		370
Funds received for legal receivable		2,400
Payments of specified liabilities		(5,280)
Payments to holders of CVRs		(1,106)
Costs incurred to collect tax refunds and by stockholders representative		(152)
Interest income		1
Balance as of December 31, 2010	**$**	**4,179**

Note 14 Debt

Long-term debt consists of the following at December 31 2010 and 2009:

(in thousands)	**2010**	**2009**
$128.0 million of floating rate senior secured notes due April 11, 2013, interest payable quarterly	$ 95,408	$ 97,169
$64.2 million of 13.75% senior unsecured notes due April 11, 2014, interest payable quarterly	56,722	54,598
	152,130	151,767
Less: Current portion of long-term debt	(1,280)	(1,280)
Total long-term debt	$ 150,850	$ 150,487

Permanent Waiver

As a result of the Embezzlement Matter and the relevant investigation, the Company was unable to issue its 2007 financial statements until after April 14, 2008, causing a financial reporting default under the senior secured credit facility (the Senior Facility) and Senior Unsecured Notes Agreement. Pursuant to waivers entered into among the Company, the administrative agent under the Senior Facility, and the required lenders, and waivers entered into among the Company, the administrative agent under the Senior Unsecured Notes Agreement, and the required noteholders on May 20, 2008, the required lenders under the Senior Facility and the required noteholders under the Senior Unsecured Note Agreement each temporarily waived the financial reporting defaults, and extended the date upon which the Company was required to deliver the relevant financial reports until August 15, 2008. During the period of temporary waiver, interest on the senior secured loans made pursuant to the Senior Facility and Senior Unsecured Notes was calculated at 2% higher than the original rate, as called for in the agreements. The additional interest for the Senior Unsecured Notes was added to the principal of the notes and is payable at maturity.

While in default, including the period of temporary waiver, the Company was prohibited from borrowing against the revolving loans made pursuant to the Senior Facility. In order to assist the Company in meeting its seasonal, short-term financing requirements, three members of the Company made unsecured loans to the Company totaling $7.0 million, payable October 11, 2014, with interest at 14% per year, payable quarterly beginning June 30, 2008.

On August 22, 2008, the Company entered into a Permanent Waiver and Amendment (Permanent Waiver) with its Senior Facility and Senior Unsecured Notes lenders. Under the terms and conditions of the Permanent Waiver, the lenders waived the default arising from the embezzlement and resulting financial reporting default, and agreed to other terms and conditions further described in this note.

The EBITDA definition in the credit agreement, as amended, was modified to include adjustments related to losses and expenses incurred as a result of the Embezzlement Matter.

The Permanent Waiver required the Company to pay an amendment fee and increased the interest rate on the Senior Facility and Senior Unsecured Notes.

In connection with the Permanent Waiver, the $7.0 million in unsecured loans described above were converted to capital stock on June 30, 2008.

Deferred financing costs were capitalized in other assets, net of accumulated amortization, and were amortized over the term of the related debt using the effective interest method. In connection with the successor financings above, the Company incurred $5.9 million in financing costs. Capitalized deferred financing costs at August 22, 2008 (date of Permanent Waiver) were $4.6 million.

In accordance with the accounting guidance for modifications or exchanges of debt instruments, the modifications to the Senior Facility and Senior Unsecured Notes resulting from the Permanent Waiver were analyzed to determine whether the refinancing would be recorded as an extinguishment of debt or a modification of debt. Based upon this analysis, it was determined that the modification qualified as extinguishment of debt, with associated unamortized deferred financing costs and amendment fees included in debt extinguishment gain or loss. The Company recognized a total pre-tax charge of $5.6 million consisting of deferred financing costs of $4.6 million and amendment fees of $1.0 million, recorded as loss on extinguishment of debt during fiscal year 2008 in the accompanying Consolidated Statement of Operations.

Senior Secured Credit Facility

On April 12, 2007, Cambium Learning entered into a $158 million credit agreement consisting of a $30 million revolving credit facility and a $128 million term loan facility. The credit agreement requires quarterly principal payments of $0.3 million in respect of the term loan facility. The senior notes are secured by substantially all of Cambium Learning s personal property. Under the original agreement, the interest rate on the Senior Facility was based upon either the one-, three- or six-month LIBOR rate plus 2.75%.

Due to the Permanent Waiver, the interest rate on the Senior Facility is now based on one-, three- or six-month LIBOR or Alternative Base Rate (ABR) plus a spread as determined by Cambium Learning s credit ratings, subject to a floor on each of the two rates. Based on ratings as of yearend 2010, the spread is LIBOR plus 5.0%. The LIBOR rate cannot be less than 3.0%, and the ABR cannot be less than 4.0%. As of December 31, 2010, the interest rate on the senior secured notes and the revolving credit facility was 8.0%. As of December 31, 2010, the Company had $95.4 million of principal outstanding under the term loan facility and no borrowings under the revolving credit facility, and subject to certain borrowing base capacity limitations for outstanding letters of credit, had $27.1 million available to borrow under the revolving credit facility.

On August 27, 2008, in accordance with the terms of the Permanent Waiver, $23.0 million was used to prepay the Tranche B Loans of the Senior Facility. In addition, proceeds from the recovery of the embezzled funds have been used to make prepayments on the Senior Facility.

Senior Unsecured Notes

On April 12, 2007, Cambium Learning entered into a Note Purchase Agreement and sold 11.75% notes due April 11, 2014 (the Senior Unsecured Notes), generating gross proceeds of $50 million, in a private placement. The Senior Unsecured Notes are guaranteed by the Company and pay cash interest equal to 10.0% on a quarterly basis. Any additional interest beyond the 10% rate is added to the principal of the notes and is not payable until April 11, 2014. The initial interest rate on the senior unsecured notes was 11.75% per annum. That rate was increased by 200 basis points in connection with the negotiation of the Permanent Waiver and credit agreement amendments in 2008 and was increased by an additional 50 basis points as of March 31, 2009 by virtue of Cambium s total leverage ratio (as defined under the senior unsecured notes) exceeding 5.5 to 1 as of March 31, 2009; however, as a result of the merger with VLCY, the total leverage ratio fell below 5.5 to 1 and the rate was decreased by 50 basis points. Thus, as of December 31, 2009, the interest rate on the subordinated notes became 13.75% per annum. Assuming the all-in interest rate on the senior unsecured notes had remained at 13.75% until April 11, 2010, the value of the notes, including accrued interest, would have been $64.2 million.

Covenants under the Senior Facility and Senior Unsecured Notes

The Senior Facility includes a financial covenant which is a total leverage ratio. The ratio is calculated quarterly using an adjusted EBITDA, which is defined as earnings before interest paid, taxes, depreciation, and amortization, and other adjustments allowed under the terms of the agreement, on a rolling 12-month basis. It also contains customary covenants, including limitations on Cambium Learning s ability to incur debt, and events of default as defined by the agreement. The Senior Facility also limits Cambium Learning s ability to pay dividends, to make advances, and otherwise engage in inter-company transactions. The Senior Facility required the total leverage ratio to be no greater than 5.5:1 for fiscal 2010.

The Senior Unsecured Notes include a financial covenant which requires that beginning with the quarter ended March 31, 2009, Cambium Learning maintains as of the end of each fiscal quarter consolidated adjusted EBITDA of not less than $25.0 million, which is defined as earnings before interest paid, taxes, depreciation, and amortization, and other adjustments allowed under the terms of the agreement, on a rolling 12-month basis. The Senior Unsecured Notes also contain customary covenants, including limitations on Cambium Learning s ability to incur debt.

In the event that Cambium Learning fails to comply with these financial covenants, the Company has the right to make a cash contribution to the capital of Cambium Learning, the aggregate amount not to be in excess of the minimum amount necessary to cure the relevant failure to comply with the financial covenant. Upon receipt by Cambium Learning of such cash, the financial covenant will be recalculated giving effect to the pro forma adjustments. EBITDA shall be increased by the amount of cash contributed, solely for the purpose of measuring the financial covenant. This right to make a cash contribution is available for no more than one fiscal quarter in a fiscal year. For the fiscal quarter ended June 30, 2009, Cambium Learning s total leverage ratio was greater than the maximum permitted 6.5:1, and Cambium Learning s adjusted EBITDA was less than the minimum required $25 million. As of August 14, 2009, Cambium Learning was in non-compliance with these covenants. On August 14, 2009, the Company notified both its senior secured lenders and senior unsecured note holders that VSS-Cambium Holdings, LLC intended to cure the non-compliance. On August 17, 2009, $3.0 million of capital was contributed to Cambium Learning by its stockholder to fund the cure. On August 20, 2009, the $3.0 million was paid to the senior secured lenders and reduced the principal amount outstanding on Cambium Learning s senior secured credit agreement.

Amendments to the Senior Facility and Senior Unsecured Notes

Cambium Learning entered into an amendment to each of its credit agreements on October 29, 2009. Since the Senior Facility and the Senior Unsecured Notes Agreement are substantially similar agreements, each of the amendments is substantially similar to the other. The amendments were permitted under the terms of the merger agreement, and provide for the following important modifications to the credit agreements:

Change in Control Definition. Prior to the amendment, the original investors in Cambium Learning were required to own or control a majority of the outstanding economic or voting interests of Cambium Learning. This majority threshold was reduced to 35%.

VSS Funds Ownership. VSS is not permitted to sell or otherwise transfer any of the Company s common stock that it directly or indirectly owns, unless it continues to directly or indirectly own or control at least 35% of the outstanding Company common stock, and it has not sold or otherwise transferred, in the aggregate, more than 15% of its Company common stock.

Increase in Material Indebtedness. An event of default would occur if a change in control occurred under any of Cambium Learning s other material indebtedness. The term material indebtedness includes the Senior Unsecured Notes, as well as any other debt, the principal amount of which exceeds a specified threshold. The $5 million threshold was increased under the amendment to $7.5 million.

Exceptions to Restricted Payments. Cambium Learning is prohibited from paying dividends, unless the specific type of payment is permitted. Additional types of payments were permitted to allow the following:

- Up to $3.0 million to fund public company, administrative, overhead, franchise tax and related costs incurred by the Company; and
- Up to $750,000 in annual board of director compensation and expenses.

The annual monitoring fee previously payable to VSS was eliminated.

Permitted Acquisition Basket Reset. The amount of consideration payable in an acquisition is limited under the credit agreements, and the limitations were reset after giving effect to the acquisition of Voyager Expanded Learning by Cambium Learning in connection with the mergers. The limitation was reset to a cumulative $150 million amount, but any single acquisition is limited to $20 million until the ratio of senior secured debt to EBITDA (as calculated under the credit agreements) does not exceed 2.50 to 1.0, and the ratio of total leverage to EBITDA (as calculated under the credit agreements) does not exceed 3.50 to 1.0, at which time the single acquisition limit will be increased to $100 million.

Definition of Consolidated EBITDA. The definition of Consolidated EBITDA, which is used for calculating leverage ratios under the senior secured credit agreement, and the minimum EBITDA covenant under the Senior Unsecured Notes Agreement was modified to allow additional add-backs for the following items:

- Deferred revenue associated with a permitted acquisition;
- Up to $24.0 million in M&A costs related to the mergers;
- Up to $2.0 million in costs incurred in closing of locations or lease terminations in connection with the mergers;
- Up to $5.0 million in severance costs incurred in connection with the mergers;

Up to $3.0 million in integration costs incurred connection with the mergers; and

Merger and acquisition costs for future transactions (whether or not completed) of up to $5.0 million for closed transactions and $0.5 million for failed transactions in any calendar year, and $2.0 million in the aggregate.

In addition, the amendments ratified and approved the mergers and the related transactions.

Each of the lenders who executed the amendment on or before October 28, 2009 received a fee equal to 20 basis points of the amount of its loans and commitments under the credit agreements, for an aggregate fee payable to all lenders equal to approximately $0.3 million, which is included in other income (expense) in the Consolidated Statements of Operations.

At December 31, 2010, the future minimum repayments under long-term debt, including paid-in-kind interest of $7.5 million in 2014, were payable as follows:

(in thousands)	**2010**
2011	1,280
2012	1,280
2013	92,848
2014	64,223
2015	
Thereafter	
Total debt repayment	$ 159,631

As described in Note 23 to the Consolidated Financial Statements, during February 2011, Cambium Learning used a portion of the net proceeds from the sale of $175 million aggregate amount of 9.75% Senior Notes to repay in full its existing Senior Facility and Senior Unsecured Notes. The Senior Notes are due in 2017.

In June 2007, the Company entered into an interest rate swap contract, with a notional amount of $39.0 million, which expired in June 2010. Under the agreement, to the extent that LIBOR exceeded a fixed maximum rate, the Company received payments on the notional amount. The total fair value of this financial instrument at December 31, 2009 amounted to a liability of approximately $1.0 million and is included in accrued expenses in the accompanying Consolidated Balance Sheets. The Company recognized a gain of $1.0 million, a gain of $1.4 million, and a loss of $0.8 million for the years ended December 31, 2010, 2009 and 2008, respectively, on changes in fair market value of the interest rate swap, which have been included in other income (expense) in the accompanying Consolidated Statements of Operations.

Note 15 Profit-Sharing, Pension, and Other Postretirement Benefit Plans

Defined Contribution Plans

On January 1, 2010, the Company s 401(k) plan was consolidated with VLCY s plan. Under this plan, the Company provides matching contributions of 50% of participant contributions up to 4%. Additionally, the Company may make discretionary contributions based upon exceeding company performance targets of up to 2% of eligible earnings for all employees regardless of participation. The 401(k) matching contribution expense was $0.7 million in 2010.

Prior to 2010, Cambium had a defined contribution retirement plan, the Cambium Learning 401(k) Savings Plan, which conformed to Section 401(k) of the Internal Revenue Code and covered substantially all of Cambium s eligible employees. Participants elected to contribute a percentage of their compensation subject to an annual limit. Cambium provided a matching contribution in amounts up to 4.5% of employee compensation. The 401(k) matching contribution expense was $0.6 million and $0.7 million for the years ended December 31, 2009 and December 31, 2008, respectively.

As a result of the acquisition of VLCY, the Company also has contractual obligations under a frozen replacement benefit plan (RBP) for a small number of terminated and retired executives and one current employee. Because the RBP is frozen, no participant can make or is entitled to additional contributions. Instead, the Company has accrued a liability totaling $1.0 million as of yearend 2010 to reflect its estimated future obligation for the RBP. The current portion of the RBP liability, which was $0.4 million at yearend 2010, is included on the line Deferred compensation in Note 10 of the Consolidated Financial Statements. The long-term portion of the RBP liability, which was $0.6 million at yearend 2010, is included on the line Long-term deferred compensation in Note 11 of the Consolidated Financial Statements.

Defined Benefit Plan

As a result of the acquisition of VLCY, the Company also has a frozen defined benefit pension plan covering certain terminated and retired former domestic employees. The benefits are primarily based on years of service and/or compensation during the years immediately preceding retirement. The Company uses a measurement date of December 31 for its pension plan.

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Applicable accounting guidance for employers accounting for defined benefit pension and other postretirement plans requires reporting of the funded status of defined benefit postretirement plans as an asset or liability in the statement of financial position, recognizing changes in the funded status due to gains or losses, prior service costs, and net transition assets or obligations in other comprehensive income in the year the changes occur, adjusting other comprehensive income when the gains or losses, prior service costs, and net transition assets or obligations are recognized as components of net period benefit cost through amortization, and measuring the funded status of a plan as of the date of the statement of financial position, with limited exceptions.

The net costs of the Company s defined benefit pension plan for the years ended December 31, 2010 and 2009 are as follows:

(in thousands)	**2010**	**2009**
Service cost	$	$
Interest cost	584	36
Recognized net actuarial loss/(gain)	908	(206)
Net pension and other postretirement benefit cost (income)	$ 1,492	$ (170)

Obligation and Funded Status

The funded status of the Company s U.S. defined benefit pension plan at the end of fiscal 2010 and 2009 is as follows:

(in thousands)	**2010**	**2009**
Change in Benefit Obligation		
Benefit obligation, beginning of period	$ 11,734	$ 12,010
Service cost		
Interest cost	584	36
Actuarial (gain)/loss	908	(206)
Benefits paid	(1,212)	(106)
Benefit obligation, end of year	$ 12,014	$ 11,734
Change in Plan Assets		
Fair value, beginning of period	$	$
Company contributions	1,212	106
Benefits paid	(1,212)	(106)
Fair value, end of year	$	$
Funded/(unfunded) status	$ (12,014)	$ (11,734)
Accrued benefit cost	$ (12,014)	$ (11,734)
Amounts Recognized in the Consolidated Balance Sheets		
Current accrued benefit liability	(1,182)	(1,266)

Non-current accrued benefit liability		(10,832)		(10,468)
Net amount recognized	$	(12,014)	$	(11,734)

At December 31, 2010, the Company had a net actuarial loss of $0.9 million for its U.S. pension plan, compared to a net actuarial gain of $0.2 million in 2009. These amounts are included in Accumulated Other Comprehensive Income (Loss) in the Consolidated Balance Sheets. Of this amount, the Company expects immaterial amounts to be recognized as a component of net pension cost (income) during 2011.

Plan Assumptions

	2010	**2009**
Discount rate	**4.75%**	**5.25%**

The discount rate is determined by analyzing the average returns of high-quality fixed income investments defined as AA-rated or better. The Company also utilizes an interest rate yield curve for instruments with maturities corresponding to the benefit obligations.

Additional Information

For the Company s U.S. defined benefit pension plan, the projected benefit obligation and accumulated benefit obligation at the end of fiscal 2010 and 2009 are as follows:

(in thousands)	**2010**	**2009**
Projected benefit obligation	$ 12,014	$ 11,734
Accumulated benefit obligation	12,014	11,734

Future Contributions

Total contributions expected to be paid under the Company s frozen U.S. retirement plans or to the beneficiaries thereof during fiscal 2011 are $1.6 million, consisting of $1.2 million to its U.S. defined benefit plan and $0.4 million to the RBP.

Gross benefit payment obligations under the Company s continuing defined benefit plans for the next ten years are anticipated to be as follows:

(in thousands)	**U.S. Retirement Plans (Pension Plan and RBP)**
2011	$ 1,556
2012	1,211
2013	1,173
2014	1,104
2015	1,066
2016 - 2020	4,733

Note 16 Stockholders /Members Equity

Common Stock

Shares Authorized and Outstanding. The Company is authorized to issue 150,000,000 shares of common stock, par value $0.001 per share. As of December 31, 2010, there were 43,868,676 shares of common stock outstanding and an additional 5,000,000 shares of common stock reserved for issuance pursuant to the 2009 Equity Incentive Plan. Shares of the Company s common stock are not convertible into or exchangeable for shares of any other class of capital stock. There are no redemption or sinking fund provisions applicable to the common stock.

At the time of the merger between the Company and VLCY:

20.5 million shares were issued to the former sole stockholder in consideration of its pre-merger interest;

3.8 million shares were issued to the former sole stockholder as consideration for a $25.0 million capital contribution made in conjunction with the merger; and

19.5 million shares were issued to the former VLCY stockholders as part of the purchase price consideration for the acquisition.

Voting Rights. Each holder of shares of the Company s common stock is entitled to one vote for each share held of record on the applicable record date on all matters submitted to a vote of stockholders, including the election of directors.

Dividend Rights. Holders of the Company s common stock are entitled to receive dividends when, as and if declared by the board of directors out of funds legally available for payment, subject to the rights of holders of the Company s preferred stock, if any. The Company does not expect to pay dividends in the short term.

Rights Upon Liquidation. In the event of a voluntary or involuntary liquidation, dissolution or winding up, the holders of the Company s common stock will be entitled to share equally in any of the assets available for distribution after payment in full of all debts and after the holders of all series of the Company s outstanding preferred stock, if any, have received their liquidation preferences in full.

Preemptive Rights; Subscription Rights. In general, holders of the Company s common stock have no preemptive rights to purchase, subscribe for or otherwise acquire any unissued or treasury shares or its other securities. However, under the terms of the stockholders agreement, entered into in connection with the mergers (the Stockholders Agreement) except with respect to specified exempt issuances, for so long as VSS-Cambium Holdings III, LLC and funds managed or controlled by VSS (collectively VSS) beneficially own in the aggregate at least 25% of the outstanding shares of the Company s common stock, VSS has preemptive rights to purchase the Company s common stock (or other securities that may be approved by the audit committee of the board of directors), in connection with any proposed securities offering by the Company. These preemptive rights generally give VSS the opportunity to purchase an amount of common stock (or such other securities as may be approved by the audit committee) in the new issuance sufficient to enable VSS to maintain their same collective percentage ownership following the new issuance. In addition, under the Stockholders Agreement, the Company granted VSS a subscription right that would permit them to purchase, at any time and from time to time until December 8, 2011, a number of shares of the Company s common stock up to the lesser of: (i) 7,500,000 shares of common stock (subject to adjustment in the event of any dividend, stock split, combination or similar recapitalization event); or (ii) the number of shares of common stock that VSS may purchase from time to time during the 24-month subscription period for an aggregate purchase price of $20 million. The purchase price per share in connection with the subscription rights is equal to 90% of the volume weighted average price of the Company s common stock measured over the ten-trading-day period immediately preceding the issuance and sale of the shares of the common stock.

Preferred Stock

Shares Authorized and Outstanding. The Company is authorized to issue 15,000,000 shares of preferred stock, par value $0.001 per share. As of December 31, 2010, there are no shares of preferred stock issued or outstanding.

Blank Check Preferred Stock. Under the certificate of incorporation, without further stockholder action, the board of directors is authorized to provide for the issuance of shares of preferred stock in one or more series, to establish from time to time the number of shares to be included in each such series, and to fix the designation, powers, preferences and rights of the shares of each such series and any qualifications, limitations or restrictions on such shares. The board of directors may authorize the issuance of preferred stock with voting or conversion rights that could adversely affect the voting power or other rights of the holders of the Company s common stock.

Members Interest

VSS-Cambium Holdings, LLC. VSS-Cambium Holdings, LLC was formed on January 29, 2007, and on that date entered into a stock purchase agreement that provided for the purchase by VSS-Cambium Holdings, LLC of all of the outstanding stock of Cambium Learning. Each Investor and Executive Member (Member) contributed capital which totaled $144.0 million, including cash and carryover interest, and was issued a membership interest in the Company. The capital contributed was then used to purchase the outstanding stock of Cambium Learning on April 12, 2007. On January 15, 2008, $0.8 million of capital was contributed by a new investor for a membership interest in the Company. $7 million in unsecured loans (see Note 14), were converted to equity of the Company s sole stockholder in late August 2008. A capital stock issuance fee of $0.1 million was paid by the Company. In August 2009, the Company s sole stockholder made a capital contribution of $3.0 million to fund a cure for a debt covenant violation (see Note 14). No future capital contribution is required to the Company by its former Members. At the time of the merger between the Company and VLCY, all membership interests were converted to 20.5 million shares of common stock.

VSS-Cambium Management, LLC. VSS-Cambium Management, LLC (Management LLC) is a Delaware limited liability company formed on February 7, 2007. Management LLC was a member and held up to a $50,000 equity interest in VSS-Cambium Holdings, LLC. Its members were individuals admitted as Management Members including some which were also Members of the Company. Management Members could include employees of and consultants to the Company. Management LLC was authorized to sell a total of 100,000 Management LLC units. As of December 8, 2009 and December 31, 2008, 65,762 units for a total of $32,881 have been sold and distributed to certain employees of Cambium. The units were valued at $0.50 per unit and reflect the fair value at the date of purchase as determined by the Company s Board of Managers. There are no further obligations related to these units.

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Note 17 Stock-Based Compensation and Expense

The total amount of pre-tax expense for stock-based compensation recognized in the years ended December 31, 2010, 2009 and 2008 was $1.1 million, $2.3 million, and zero, respectively. The stock-based compensation expense was allocated as follows:

(in thousands)	2010	2009
Cost of sales	$ 58	$
Research and development expense	123	
Sales and marketing expense	136	
General and administrative expense	768	2,259
Total	$ 1,085	$ 2,259

As of December 31, 2010, the Company has one stock-based compensation plan, which is described below. The total income tax expense recognized for book purposes in the consolidated statement of operations related to stock-based compensation was zero, zero and $0.2 million for the years ended December 31, 2010, 2009 and 2008, respectively. The total tax benefit realized was zero for all years presented.

Stock Option Plan

In fiscal 2009, the Company adopted the Cambium Learning Group, Inc. 2009 Equity Incentive Plan (Incentive Plan). Under the Incentive Plan, 5,000,000 shares of common stock were reserved for issuance. The Incentive Plan is administered by the board of directors which has the authority to establish the terms and conditions of awards granted under the Incentive Plan. Under the Incentive Plan, the Company can grant incentive stock options, non-statutory stock options, stock appreciation rights (SARs), restricted stock, restricted stock units, conversion stock options, conversion SARs, and other stock or cash awards.

Warrant

In connection with the completion of the merger with VLCY on December 8, 2009, the Company issued to VSS-Cambium Holdings III, LLC a warrant to purchase shares of the Company s common stock (the Holdings Warrant). As of December 31, 2010, the Holdings Warrant was exercisable for 560,137 shares of the Company s common stock at an exercise price of $0.01 per share. The Holdings Warrant expires on December 8, 2014. The number of shares of common stock issuable pursuant to the Holdings Warrant may increase in the future upon the occurrence of certain events described below. The number of shares of the Company s common stock issuable under the Holdings Warrant is based upon the calculation of three separate amounts, described herein as the Cambium Specified Asset Recoupment Amount, the Additional Share Amount and the Formula Amount. The 560,137 shares that are exercisable, or will be exercisable upon issuance, represent 104,907 shares originating from the Cambium Specified Asset Recoupment Amount and 455,230 shares originating from the Formula Amount, which are summarized as follows:

The Cambium Specified Asset Recoupment Amount is based upon the net amount of recoveries that the Company receives or received on and after June 1, 2009, including periods after the effective time of the mergers, with respect to the embezzlement matter that was discovered in April 2008. As of December 31, 2010, the Company has received net recoveries of approximately $1.5 million with respect to this matter, although the actual amount of net recoveries that the Company will ultimately receive is not known at this time. The Cambium Specified Asset Recoupment Amount equals 0.45 multiplied by the quotient of the aggregate net recoveries divided by $6.50. Therefore as of December 31, 2010, 104,907 shares are exercisable, or will be exercisable upon issuance, under the Holdings Warrant related to the Cambium Specified Asset Recoupment Amount. In accordance with applicable accounting guidance for distinguishing liabilities from equity, this award is recorded as a liability in the other liabilities line on the Consolidated Balance Sheets and measured at fair value. The initial recording and any subsequent increases in the value of the award attributable to embezzlement recoveries is recorded to embezzlement loss on the income statement. Subsequent changes in fair value are recorded to general and administrative expense. The warrant was valued at $0.4 million on December 31, 2010 with the Black-Scholes pricing model. Due to the low exercise price of the warrants, the model assumptions do not significantly impact the valuation.

The Additional Share Amount is calculated over a period commencing at the effective time of the mergers with VLCY and Cambium and ending two years thereafter. The Additional Share Amount will equal the number of shares of VLCY common stock, if any, that are surrendered upon consummation of the VLCY merger in excess of the sum of the 29,874,145 shares that were known to be outstanding plus the number of shares of VLCY common stock that are issued upon the exercise of options known to be outstanding, provided that the maximum Additional Share Amount is capped at a maximum of 145,000 shares and provided, further, that an adjustment to the number of shares VSS-Cambium Holdings III, LLC received in connection with the merger of Cambium was not already made under the terms of the merger agreement. Following completion of the merger with VLCY, 29,999 shares of VLCY common stock in excess of 29,874,145 shares were surrendered and, pursuant to the merger agreement, the number of shares of the Company s common stock issuable to VSS-Cambium Holdings III, LLC was adjusted to increase the number of shares it received. At the effective time of the merger with VLCY all outstanding stock options were terminated. Thus, the Company does not believe that the Holdings Warrant shall be issuable with respect to any shares relating to the Additional Share Amount.

The Formula Amount adds shares to the Holdings Warrant only if, prior to completion of the mergers with Cambium and VLCY, equity cure payments were made under Cambium s existing credit agreements, debt was retired under those agreements or payments were made to obtain default-related waivers under those agreements. The only applicable event was an equity cure payment of $3.0 million made in August 2009 (see Note 14). The Formula Amount equals the equity cure payment of $3.0 million divided by $6.50, or 455,230 shares. Thus, 455,230 shares of the Company s common stock are currently exercisable under the Holdings Warrant with respect to the Formula Amount. In accordance with applicable accounting guidance for distinguishing liabilities from equity, this award is recorded to equity with the offset going against the capital contribution made to affect the debt cure.

Subscription Right

In connection with the merger with VLCY, the Company granted VSS a subscription right that permits them to purchase, at any time and from time to time until December 8, 2011, a number of shares of common stock up to the lesser of:

7,500,000 shares of common stock (subject to adjustment in the event of any dividend, stock split, combination or similar recapitalization event); or

the number of shares of common stock that VSS may purchase from time to time during the 24-month subscription period for an aggregate purchase price of $20.0 million (based upon the per share purchase price described below).

The purchase price per share in connection with the subscription rights is equal to 90% of the volume weighted average price of the common stock measured over the ten-trading-day period immediately preceding the issuance and sale of the shares of common stock. These rights are accounted for as equity with the offsetting grant date fair value of $2.2 million recorded to general and administrative expense during 2009.

Fair Value of Stock Option and SAR Grants

The fair value of each stock-based compensation award granted is estimated on the date of grant using the Black-Scholes option-pricing model.

In connection with the merger with VLCY, the Company issued conversion stock options to purchase 105,910 shares and conversion SARs with respect to 200,000 shares. These were issued in replacement of share-based awards held by employees of VLCY that were required to be converted into rights or options for shares of the Company with the same terms and conditions that were applicable to the rights or options for VLCY shares, including exercise prices ranging from $8.55 to $36.00 per share. The conversion SARs are recorded as a liability at December 31, 2010 and 2009 in other liabilities on the Consolidated Balance Sheets. For more information see Note 4. The following assumptions were used during 2009 to estimate the fair value of conversion awards:

	2009
Expected stock volatility	35.00%
Risk-free interest rate	1.02%
Expected years until exercise	0.10 - 2.56
Dividend yield	0.00%

The following assumptions were used during 2009 to estimate the fair value of other awards:

	2009
Expected stock volatility	35.00%
Risk-free interest rate	2.69%
Expected years until exercise	6.25
Dividend yield	0.00%

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During the year ended December 31, 2010, the Company granted 1,754,762 options under the Incentive Plan with a total grant date fair value, net of forecasted forfeitures, of $2.0 million. Of these options 82,500 have a per-share exercise price equal to $4.81, 1,233,572 have a per-share exercise price equal to $4.50 and 438,690 of these options have an exercise price equal to $6.50. These options vest equally over a four year service period and the term of the options is ten years from the date of grant. The following assumptions were used in the Black-Scholes option-pricing model to estimate the fair value of these awards:

	2010
Expected stock volatility	35.00%
Risk-free interest rate	2.40% - 2.87%
Expected years until exercise	6.25
Dividend yield	0.00%

Due to a lack of exercise history or other means to reasonably estimate future exercise behavior, the Company used the simplified method as described in applicable accounting guidance for stock-based compensation to estimate the expected years until exercise on new awards.

Restricted common stock awards of 6,000 and 4,000 shares were issued during the first and second quarters of 2010, respectively. The restrictions on the common stock awards will lapse one year from the anniversary of the grant date or upon a change in control of the Company for the 6,000 share grant and equally over a four-year period on the anniversary of the grant date or upon a change in control of the Company for the 4,000 share grant. These awards were valued based on the Company s closing stock price on the date of grant. Expense of $25 thousand was recorded to general and administrative expense for the year ended December 31, 2010.

During 2010, 105,910 conversion stock options, which had been issued in replacement of share-based awards held by employees of VLCY, were cancelled. Additionally, 139,216 of the options granted on January 27, 2010 and 8,493 of the options granted on May 25, 2010 were forfeited during the year. There was no impact to expense during the period as a result of these forfeitures.

Summary of Stock Option and SAR Activity

A summary of the stock option, stock appreciation right and restricted stock transactions for the year ended December 31, 2010 is as follows:

	Stock Option Grantees		SAR Grantee		Restricted Stock	
	Shares (000s)	Weighted Average Exercise Price	Shares (000s)	Weighted Average Exercise Price	Shares (000s)	Weighted Average Grant Date Fair Value
Awards outstanding at December 31, 2009	2,256	$ 6.03	200	$ 8.55		$
For the year ended December 31, 2010:						
Granted	1,755	5.01			10	3.90
Exercised/Restricted Stock Vested						