HOLLY ENERGY PARTNERS LP
Form S-3
December 07, 2018
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**As filed with the Securities and Exchange Commission on December 7, 2018**

**Registration No. 333-**

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

# Form S-3

**REGISTRATION STATEMENT**

***UNDER***

***THE SECURITIES ACT OF 1933***

**Holly Energy Partners, L.P.**

**Holly Energy Finance Corp.***

**(Exact Name of Registrant as Specified in Their Charters)**

| **Delaware** | **20-0833098** |
|---|---|

| **Delaware**<br>**(State or Other Jurisdiction of Incorporation or Organization)** | **20-2263311**<br>**(I.R.S. Employer Identification No.)** |
|---|---|
| | **Denise C. McWatters**<br><br>**Senior Vice President, General Counsel and Secretary**<br><br>**Holly Energy Partners, L.P.** |
| **2828 N. Harwood, Suite 1300**<br><br>**Dallas, Texas 75201**<br><br>**(214) 871-3555**<br>**(Address, Including Zip Code, and Telephone Number, Including Area Code, of each of the Registrants Principal Executive Offices)** | **2828 N. Harwood, Suite 1300**<br><br>**Dallas, Texas 75201**<br><br>**(214) 871-3555**<br>**(Name, Address, Including Zip Code, and Telephone Number, Including Area Code, of each of the Registrants Agent for Service)** |

***Copy to:***

**Alan J. Bogdanow**

**Katherine Terrell Frank**

**Vinson & Elkins L.L.P.**

**Trammell Crow Center**

**2001 Ross Avenue, Suite 3900**

**Dallas, Texas 75201**

**(214) 220-7700**

**Approximate date of commencement of proposed sale to the public:** From time to time after this registration statement becomes effective.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest

reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box.

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If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box.

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

| | | |
|---|---|---|
| Large accelerated filer | | Accelerated filer |
| Non-accelerated filer | (Do not check if a smaller reporting company) | Smaller reporting company |

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act

**CALCULATION OF REGISTRATION FEE**

| Title of Each Class of Securities to be Registered | Amount to be Registered | Proposed Maximum Offering Price per Unit | Proposed Maximum Aggregate Offering Price | Amount of Registration Fee |
|---|---|---|---|---|
| **Primary Offering** | | | | |
| Common units representing limited partner interests(1) | | | | |
| Preferred units representing limited partner interests | | | | |
| Debt securities(2) | | | | |
| Guarantees of debt securities(3) | | | | |
| Total Primary Offering | (4) | (6) | $2,000,000,000.00(8) | $9,975.17(10) |
| **Secondary Offering** | | | | |
| Common units representing limited partner interests | 59,630,030(5) | (7) | $1,692,896,551.70(9) | $128,172.34(11) |
| **Total (Primary and Secondary)** | | | | $138,147.51 |

(1) There are being registered hereunder an indeterminate number of common units of Holly Energy Partners, L.P. ( Holly Energy Partners ) that may be issued upon conversion of preferred units or debt securities registered

hereunder. No separate consideration will be received for common units that are issued upon conversion of preferred units or debt securities registered hereunder.

(2) If any debt securities are issued at an original issue discount, then the offering price of such debt securities shall be in such amount as shall result in an aggregate initial offering price not to exceed $2,000,000,000, less the dollar amount of any registered securities previously issued.

(3) Each of the subsidiaries of Holly Energy Partners identified on the following pages may guarantee any series of debt securities issued under this Registration Statement. No separate consideration will be paid in respect of any guarantees. Pursuant to Rule 457(n) under the Securities Act of 1933 (the Securities Act ), no separate registration fee will be paid with respect to any guarantees of any debt securities registered hereby.

(4) The amount of securities registered in the primary offering consists of $2,000,000,000 of a presently indeterminate number or amount of common units of Holly Energy Partners, preferred units of Holly Energy Partners, debt securities of Holly Energy Partners, which may be co-issued by its subsidiary, Holly Energy Finance Corp., and guarantees of such debt securities as set forth in Note 3 above.

(5) Pursuant to Rule 416(a) under the Securities Act, the number of common units being registered on behalf of the selling unitholders shall be adjusted to include any additional common units that may become issuable as a result of any distribution, split, combination or similar transaction.

(6) With respect to the primary offering, the proposed maximum aggregate offering price for each class of securities to be registered in the primary offering is not specified pursuant to General Instruction II.D. of Form S-3.

(7) With respect to the secondary offering, the proposed maximum offering price per common unit will be determined from time to time in connection with, and at the time of, the sale by the selling unitholder.

(8) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(o) under the Securities Act of 1933. With respect to the primary offering, in no event will the aggregate initial offering price of all securities offered from time to time pursuant to this Registration Statement exceed $2,000,000,000.

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(9) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(c) under the Securities Act on the basis of the average of the high and low sale prices of the common units on December 4, 2018, as reported on the New York Stock Exchange.

(10) The $2,000,000,000 of securities registered in the primary offering includes $1,917,696,610.00 of common units of Holly Energy Partners, preferred units of Holly Energy Partners, debt securities of Holly Energy Partners, which may be co-issued by its subsidiary, Holly Energy Finance Corp., and guarantees of such debt securities (the Primary Unsold Securities ) registered pursuant to Registration Statement No. 333-204609 (the Prior Registration Statement ), originally filed with the Securities and Exchange Commission on June 1, 2016, and declared effective on December 14, 2016, that have not been issued and sold by us. Pursuant to Rule 415(a)(6) under the Securities Act, $219,768.03 of filing fees previously paid in connection with the Primary Unsold Securities (which includes $219,768.03 of filing fees previously paid in connection with unsold securities registered pursuant to Registration Statement No. 333-178304 filed by the Registrant on December 2, 2011, and declared effective on June 4, 2012) will continue to be applied to the Primary Unsold Securities. The Registrants are also including $82,303,390.00 of newly registered common units of Holly Energy Partners, preferred units of Holly Energy Partners, debt securities of Holly Energy Partners, which may be co-issued by its subsidiary, Holly Energy Finance Corp., and guarantees of such debt securities (the New Securities ). A filing fee of $9,975.17, calculated in accordance with Rule 457(o) under the Securities Act, is paid herewith in connection with the New Securities. To the extent that, after the filing date hereof and prior to the effectiveness of this registration statement, the Registrants sell any Primary Unsold Securities pursuant to the Prior Registration Statement, the Registrants will identify in a pre-effective amendment to this registration statement the updated amount of Primary Unsold Securities from the Prior Registration Statement to be included in this registration statement pursuant to Rule 415(a)(6) and the updated amount of New Securities to be registered on this registration statement. In accordance with Rule 415(a)(6), the offering of Primary Unsold Securities on the Prior Registration Statement will be deemed terminated as of the effective date of this registration statement.

(11) The 59,630,030 common units registered hereunder for sale by certain selling unitholders include 22,380,030 common units of Holly Energy Partners (the Secondary Unsold Units ) registered pursuant to the Prior Registration Statement. Pursuant to Rule 415(a)(6) under the Securities Act, $68,437.07 of filing fees previously paid in connection with the Secondary Unsold Units (which includes $67,709.92 of filing fees previously paid in connection with unsold securities registered pursuant to Registration Statement No. 333-178304 filed by the Registrant on December 2, 2011, and declared effective on June 4, 2012) will continue to be applied to the Secondary Unsold Units. A filing fee of $128,172.34, calculated in accordance with Rule 457(c) under the Securities Act, is paid herewith in connection with the 37,250,000 new secondary common units registered hereunder (the New Secondary Units ). In accordance with Rule 415(a)(6), the offering of Secondary Unsold Units on the Prior Registration Statement will be deemed terminated as of the effective date of this registration statement.

**The Registrants hereby amend this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrants shall file a further amendment that specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

* Additional Registrants are identified on the following pages.

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## ADDITIONAL REGISTRANTS

The additional Registrants listed below are subsidiaries of Holly Energy Partners and may guarantee the debt securities registered hereby.

| | |
|---|---|
| **Cheyenne Logistics LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **45-3541447**<br>*(I.R.S. Employer Identification Number)* |
| **El Dorado Logistics LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **45-3541520**<br>*(I.R.S. Employer Identification Number)* |
| **El Dorado Operating LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **47-4613468**<br>*(I.R.S. Employer Identification Number)* |
| **El Dorado Osage LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **61-1771654**<br>*(I.R.S. Employer Identification Number)* |
| **Frontier Aspen LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **47-4934328**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Cheyenne LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **81-2771127**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Cheyenne Shortline LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **30-0997573**<br>*(I.R.S. Employer Identification Number)* |
| **HEP El Dorado LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |

| | |
|---|---|
| **Delaware** | **46-4027645** |
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |

**HEP Fin-Tex/Trust-River, L.P.**
*(Exact Name of Registrant As Specified In Its Charter)*

| | |
|---|---|
| **Texas** | **20-2161011** |
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |

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| **HEP Logistics GP, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **51-0504692**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Mountain Home, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **71-0968300**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Navajo Southern, L.P.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **57-1207829**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Oklahoma LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **82-5321261**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Pipeline Assets, Limited Partnership**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **51-0512050**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Pipeline GP, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **72-1583767**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Pipeline, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **71-0968296**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Refining Assets, L.P.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **51-0512052**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Refining GP, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware** | **71-0968297**<br>*(I.R.S. Employer Identification Number)* |

*(State or Other Jurisdiction of Incorporation or Organization)*

**HEP Refining, L.L.C.**
*(Exact Name of Registrant As Specified In Its Charter)*

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|---|---|
| **Delaware** | **71-0968299** |

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| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |
| **HEP Tulsa LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **27-0497982**<br>*(I.R.S. Employer Identification Number)* |
| **HEP UNEV Holdings LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **90-0868553**<br>*(I.R.S. Employer Identification Number)* |
| **HEP UNEV Pipeline LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **26-1123552**<br>*(I.R.S. Employer Identification Number)* |
| **HEP Woods Cross, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **72-1583768**<br>*(I.R.S. Employer Identification Number)* |
| **Holly Energy Holdings LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **30-0997569**<br>*(I.R.S. Employer Identification Number)* |
| **Holly Energy Partners Operating, L.P.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **51-0504696**<br>*(I.R.S. Employer Identification Number)* |
| **Holly Energy Storage Lovington LLC**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **27-2245181**<br>*(I.R.S. Employer Identification Number)* |
| **Lovington-Artesia, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |
| **Delaware**<br>*(State or Other Jurisdiction of Incorporation or Organization)* | **26-1583770**<br>*(I.R.S. Employer Identification Number)* |
| **Roadrunner Pipeline, L.L.C.**<br>*(Exact Name of Registrant As Specified In Its Charter)* | |

| | |
|---|---|
| **Delaware** | **26-2758381** |
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |

**SLC Pipeline LLC**
*(Exact Name of Registrant As Specified In Its Charter)*

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|---|---|
| **Delaware** | **27-0385778** |
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |

**Woods Cross Operating LLC**
*(Exact Name of Registrant As Specified In Its Charter)*

| | |
|---|---|
| **Delaware** | **81-2995600** |
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification Number)* |

(1) The address, telephone number and primary standard industrial classification code number of each additional registrant is the same as Holly Energy Partners. The name, address and telephone number for the agent for service for each additional registrant is the same as Holly Energy Partners agent for service.

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**The information in this prospectus is not complete and may be changed. Securities may not be sold pursuant to this prospectus until a registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell securities, and it is not soliciting an offer to buy securities, in any jurisdiction where the offer or sale is not permitted.**

**SUBJECT TO COMPLETION, DATED , 2018**

**PROSPECTUS**

**Holly Energy Partners, L.P.**

**Holly Energy Finance Corp.**

**COMMON UNITS**

**PREFERRED UNITS**

**DEBT SECURITIES**

**GUARANTEES**

We may from time to time, in one or more offerings, offer and sell (i) common units representing limited partner interests in Holly Energy Partners, L.P. ( common units ); (ii) preferred units representing limited partner interests in Holly Energy Partners, L.P. ( preferred units ); and (iii) debt securities of Holly Energy Partners, L.P., which may be co-issued by Holly Energy Finance Corp. and may be guaranteed by certain other subsidiaries of Holly Energy Partners, L.P. The aggregate initial offering price of all securities sold by us under this prospectus will not exceed $2,000,000,000.

The selling unitholders named in this prospectus may from time to time, in one or more offerings, offer and sell up to 59,630,030 common units. We will not receive any proceeds from the sale of these common units by the selling unitholders. The selling unitholders, as affiliates of ours, may be deemed to be underwriters within the meaning of the Securities Act of 1933 (the Securities Act ), and, as a result, may be deemed to be offering securities, indirectly, on our behalf. For a more detailed discussion of the selling unitholders, please read Selling Unitholders.

We or the selling unitholders may offer and sell these securities in amounts, at prices and on terms to be determined by market conditions and other factors at the time of the offering. This prospectus provides you with only a general description of these securities and the manner in which we or the selling unitholders will offer these securities. The specific terms of any securities that we or the selling unitholders offer will, if not included in this prospectus or information incorporated by reference herein, be included in a supplement to this prospectus. Any prospectus

supplement may also add, update or change information contained in this prospectus.

Our common units are listed on the New York Stock Exchange under the trading symbol HEP. We will provide information in the prospectus supplement for the expected trading market, if any, for any preferred units or debt securities that we offer.

**Limited partnerships are inherently different from corporations, and investing in our securities involves risk. Before you make an investment in our securities, you should read Risk Factors beginning on page 6 and carefully read and consider the risk factors incorporated herein by reference.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.**

**The date of this prospectus is .**

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Our, we, us and Holly Energy Partners as used in this prospectus refer to Holly Energy Partners, L.P. or to Holly Energy Partners, L.P. and its subsidiaries collectively, including its subsidiary Holly Energy Finance Corp., as the context requires. References in this prospectus to our general partner refer to HEP Logistics Holdings, L.P. and/or Holly Logistic Services, L.L.C., the general partner of HEP Logistics Holdings, L.P., as appropriate.

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## ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission (the Commission ) using a shelf registration process. Under this shelf registration process, we may offer and sell from time to time up to $2,000,000,000 of our securities. In addition, the selling unitholders may from time to time offer and sell up to 59,630,030 of our common units.

This prospectus provides you with a general description of the securities that are registered hereunder that may be offered by us or the selling unitholders. Each time we offer securities, we will provide you with a prospectus supplement that will describe, among other things, the specific amounts and prices of the securities being offered and the terms of the offering. Because the selling unitholders may be deemed to be underwriters under the Securities Act, each time a selling unitholder sells any common units offered by this prospectus, such selling unitholder is required to provide you with this prospectus and any related prospectus supplement containing specific information about the selling unitholder and the terms of the common units being offered in the manner required by the Securities Act.

Any prospectus supplement may add, update or change information contained in this prospectus. Any statement that we make in this prospectus will be modified or superseded by any inconsistent statement made by us in any prospectus supplement. The information in this prospectus is accurate as of its date. Additional information, including our financial statements and the notes thereto, is incorporated in this prospectus by reference to our reports filed with the Commission. Therefore, before you invest in our securities, you should carefully read this prospectus and any prospectus supplement relating to the securities offered to you together with the additional information incorporated by reference in this prospectus and any prospectus supplement (including the documents described under the heading Where You Can Find More Information in both this prospectus and any prospectus supplement).

**You should rely only on the information contained in or incorporated by reference in this prospectus or any prospectus supplement. We have not authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. Neither we nor anyone acting on our behalf is making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should not assume that the information incorporated by reference or provided in this prospectus or any prospectus supplement is accurate as of any date other than the date on the front of those documents.**

## WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, and other information with the Commission (File No. 001-32225). Our SEC filings are available to the public through the Internet at the Commission s website at *http://www.sec.gov*. You can also obtain information about us at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

We make available free of charge on our Internet website at *http://www.hollyenergypartners.com* all of the documents that we file with the Commission as soon as reasonably practicable after we electronically file those documents with the Commission. Information on our website or any other website is not incorporated by reference into this prospectus and does not constitute part of this prospectus unless specifically so designated and filed with the Commission.

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## DOCUMENTS INCORPORATED BY REFERENCE

The Commission allows us to incorporate by reference into this prospectus the information we file with it, which means that we can disclose important information to you by referring you to the documents we file with it. The information incorporated by reference is considered to be part of this prospectus, and later information that we file with the Commission will automatically update and supersede information in this prospectus and information previously filed with the Commission. Therefore, before you decide to invest in a particular offering under this shelf registration, you should always check for reports we may have filed with the Commission after the date of this prospectus.

We incorporate by reference the documents listed below and any future filings made by us with the Commission under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 (the Exchange Act ) before the filing of a post-effective amendment to the registration statement of which this prospectus is a part that indicates that all securities offered hereunder have been sold or that deregisters all securities then remaining unsold (other than information furnished and not filed with the Commission):

- our Annual Report on Form 10-K for the year ended December 31, 2017, filed on February 21, 2018;
- our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2018, June 30, 2018, and September 30, 2018, as filed on May 2, 2018, August 2, 2018, and October 31, 2018, respectively;
- the Current Reports on Form 8-K filed on January 26, 2018, February 7, 2018, February 8, 2018, February 22, 2018, and November 1, 2018;
- the description of our common units contained in our Registration Statement on Form 8-A, filed on June 21, 2004, and any subsequent amendment thereto filed for the purpose of updating such description.

All filings filed by us pursuant to the Exchange Act after the date of the initial filing of this registration statement and prior to the effectiveness of such registration statement (excluding information furnished pursuant to Items 2.02 and 7.01 of Form 8-K) shall also be deemed to be incorporated by reference to this prospectus.

We will provide without charge to each person, including any beneficial owner, to whom a prospectus is delivered, upon written or oral request, a copy of any document incorporated by reference in this prospectus and any exhibit specifically incorporated by reference in those documents. Requests for such documents or exhibits should be directed to:

Holly Energy Partners, L.P.

Attn: Senior Vice President, General Counsel and Secretary

2828 N. Harwood, Suite 1300

Dallas, Texas 75201

Telephone number: (214) 871-3555

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## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This prospectus and some of the documents we incorporate by reference contain various forward-looking statements within the meaning of federal securities laws. These forward-looking statements are identified as any statement that does not relate strictly to historical or current facts. When used in this prospectus or the documents we have incorporated herein or therein by reference, words such as anticipate, project, expect, plan, goal, forecast, in should, would, could, believe, may and similar expressions and statements regarding our plans and objectives for future operations are intended to identify forward-looking statements. These forward-looking statements are based on our beliefs and assumptions and those of our general partner, using currently available information and expectations as of the date on which such statements were made, are not guarantees of future performance and involve certain risks and uncertainties. Although we and our general partner believe that such expectations reflected in such forward-looking statements are reasonable, neither we nor our general partner can give assurance that our expectations will prove to be correct. All statements concerning our expectations for future results of operations are based on forecasts for our existing operations and do not include the potential impact of any future acquisitions. Our forward-looking statements are subject to a variety of risks, uncertainties and assumptions. If one or more of these risks or uncertainties materialize, or if underlying assumptions prove incorrect, our actual results may vary materially from those anticipated, estimated, projected or expected. Certain factors could cause actual results to differ materially from results anticipated in the forward-looking statements. These factors include, but are not limited to:

- risks and uncertainties with respect to the actual quantities of petroleum products and crude oil shipped on our pipelines and/or terminalled, stored or throughput in our terminals;
- the economic viability of HollyFrontier Corporation ( HollyFrontier ), Delek US Holdings, Inc. ( Delek ) and our other customers;
- the demand for refined petroleum products in markets we serve;
- our ability to purchase and integrate future acquired operations;
- our ability to complete previously announced or contemplated acquisitions;
- the availability and cost of additional debt and equity financing;
- the possibility of reductions in production or shutdowns at refineries utilizing our pipeline and terminal facilities;
- the effects of current and future government regulations and policies;

our operational efficiency in carrying out routine operations and capital construction projects;

the possibility of terrorist or cyber attacks and the consequences of any such attacks;

general economic conditions;

the impact of recent changes in the tax laws and regulations that affect master limited partnerships; and

other financial, operational and legal risks and uncertainties detailed from time to time in our filings with the Commission.

All forward-looking statements included in this prospectus and all subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. Other factors described herein, or factors that are unknown or unpredictable, could also have a material adverse effect on future results. You should not put undue reliance on any forward-looking statements. Please read Risk Factors on page 7 of this prospectus and the Risk Factors section in our Annual Report on Form 10-K for the year ended December 31, 2017. The forward-looking statements speak only as of the date made and, other than as required by securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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## WHO WE ARE

### General

We are a Delaware limited partnership engaged principally in the business of operating a system of petroleum product and crude pipelines, storage tanks, distribution terminals, loading rack facilities and refinery processing units in West Texas, New Mexico, Utah, Nevada, Oklahoma, Wyoming, Kansas, Idaho and Washington. We generate revenues by charging tariffs for transporting petroleum products and crude oil through our pipelines, by charging fees for terminalling and storing refined products and other hydrocarbons, providing other services at our storage tanks and terminals and charging a tolling fee per barrel or thousand standard cubic feet of feedstock throughput in our refinery processing units. We do not take ownership of products that we transport, terminal, store or process, and therefore, we are not directly exposed to changes in commodity prices.

We own and operate petroleum product and crude pipelines, terminal, tankage and loading rack facilities, and refinery processing units that support the refining and marketing operations of HollyFrontier in the Mid-Continent, Southwest and Northwest regions of the United States and Delek s refinery in Big Spring, Texas. HollyFrontier owns approximately 57% of our outstanding common units as well as a non-economic general partner interest. Our assets are categorized into a Pipelines and Terminals segment and a Refinery Processing Unit segment.

### Partnership Structure and Management

As is common with publicly traded limited partnerships and in order to maximize operational flexibility, we conduct our operations through subsidiaries. We have five direct subsidiaries: (i) Holly Energy Finance Corp. ( Holly Energy Finance ), (ii) Holly Energy Partners Operating, L.P. ( Holly Energy Partners Operating ), a limited partnership that conducts our operations, (iii) HEP Logistics GP, L.L.C., the general partner of Holly Energy Partners Operating, (iv) HEP UNEV Holdings LLC, a limited liability company that serves as a holding company of HEP UNEV Pipeline LLC, which holds our interests in the UNEV Pipeline, and (v) Holly Energy Holdings LLC ( Holly Energy Holdings ), a limited liability company that serves as the holding company of its subsidiaries. Holly Energy Holdings owns directly or indirectly 100% of the membership or partnership interests in its subsidiaries, other than Osage Pipe Line, in which it indirectly owns a 50% interest, and Cheyenne Pipeline, in which it indirectly owns a 50% interest. HEP UNEV Holdings LLC owns directly 100% of the membership interest in HEP UNEV Pipeline LLC, which owns a 75% membership interest in UNEV Pipeline, LLC. Holly Energy Finance was organized for the sole purpose of co-issuing certain of our debt securities, does not have any operations of any kind, and does not generate any revenue other than as may be incidental to its activities as a co-issuer of any of our debt securities.

Holly Logistic Services, L.L.C., as the general partner of HEP Logistics Holdings, L.P., our general partner, manages our operations and activities. Neither our general partner nor the board of directors of Holly Logistic Services, L.L.C. are elected by our unitholders. Unlike shareholders in a publicly traded corporation, our unitholders are not entitled to elect the directors of Holly Logistic Services, L.L.C.

The address and phone number of our principal executive offices is 2828 N. Harwood, Suite 1300, Dallas, Texas 75201; telephone number (214) 871-3555. Our website is located at *http://www.hollyenergypartners.com*. Information on our website or any other website is not incorporated by reference into this prospectus and does not constitute a part of this prospectus unless specifically so designated and filed with the Commission.

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## THE SUBSIDIARY GUARANTORS

Throughout this prospectus, we refer to each of the following subsidiaries of Holly Energy Partners as the Subsidiary Guarantors : Cheyenne Logistics LLC, El Dorado Logistics LLC, El Dorado Operating LLC, El Dorado Osage LLC, Frontier Aspen LLC, HEP Cheyenne LLC, HEP Cheyenne Shortline LLC, HEP El Dorado LLC, HEP Fin-Tex/Trust-River, L.P., HEP Logistics GP, L.L.C., HEP Mountain Home, L.L.C., HEP Navajo Southern, L.P., HEP Oklahoma LLC, HEP Pipeline Assets, Limited Partnership, HEP Pipeline GP, L.L.C., HEP Pipeline, L.L.C., HEP Refining Assets, L.P., HEP Refining GP, L.L.C., HEP Refining, L.L.C., HEP Tulsa LLC, HEP UNEV Holdings LLC, HEP UNEV Pipeline LLC, HEP Woods Cross, L.L.C., Holly Energy Holdings LLC, Holly Energy Partners Operating, L.P, Holly Energy Storage Lovington LLC, Lovington-Artesia, L.L.C., Roadrunner Pipeline, L.L.C., SLC Pipeline LLC and Woods Cross Operating LLC. Each of the Subsidiary Guarantors may jointly and severally and unconditionally guarantee our payment obligations under any series of debt securities offered by this prospectus and any prospectus supplement.

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## RISK FACTORS

An investment in our securities involves risks. Before you invest in our securities, you should carefully consider those risk factors included in our most recent Annual Report on Form 10-K, as supplemented by our Quarterly Reports on Form 10-Q, each of which is incorporated herein by reference, and those risk factors that may be included in the applicable prospectus supplement together with all of the other information included in this prospectus, any prospectus supplement and the documents we incorporate by reference in evaluating an investment in our securities. This prospectus also contains forward-looking statements that involve risks and uncertainties. Please read Cautionary Statement Regarding Forward-Looking Statements. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of certain factors, including the risks described in the foregoing documents and the other information included in, or incorporated by reference into, this prospectus. If any of these risks occur, our business, financial condition or results of operations could be adversely affected. In that case, we may be unable to pay distributions to our unitholders, or to pay interest on, or the principal of, any debt securities. In that event, the trading price of our securities could decline and you could lose all or part of your investment. When we offer and sell any securities pursuant to a prospectus supplement, we may include additional risk factors relevant to such securities in the prospectus supplement.

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## USE OF PROCEEDS

Except as otherwise provided in the applicable prospectus supplement, we will use the net proceeds from any sale of securities described in this prospectus for general partnership purposes, which may include, among other things, funding acquisitions of assets or businesses, working capital, capital expenditures, investments in subsidiaries, the repayment or retirement of existing debt and/or the repurchase of common units or other securities. The prospectus supplement for any particular offering of securities using this prospectus will disclose the actual use of the net proceeds from the sale of such securities. The exact amounts to be used and when the net proceeds will be applied to partnership purposes will depend on a number of factors, including our funding requirements and the availability of alternative funding sources.

We will not receive any of the proceeds from the sale of common units by the selling unitholders.

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## DESCRIPTION OF DEBT SECURITIES

Holly Energy Partners may issue debt securities in one or more series, and Holly Energy Finance may be a co-issuer of one or more series of such debt securities. When used in this section, references to we, us and our refer to Holly Energy Partners and, if Holly Energy Finance co-issues any debt securities, Holly Energy Finance. References to an Indenture refer to the particular Indenture under which we issue a series of debt securities.

The following description sets forth the general terms and provisions that will apply to any of our debt securities. Each prospectus supplement will state the particular terms that will apply to any debt securities included in the supplement.

### General

#### *The Indentures*

We will issue our debt securities under either a Senior Indenture or a Subordinated Indenture, among us, a trustee that we will name in the related prospectus supplement and, as applicable, any Subsidiary Guarantors. The term Trustee as used in this prospectus shall refer to the trustee under any Indenture. Any debt securities will be governed by the applicable provisions of the Indenture and those made part of the Indenture by reference to the Trust Indenture Act of 1939. We, the Trustee and, as applicable, the Subsidiary Guarantors, may enter into supplements to the applicable Indenture from time to time. The debt securities will be either senior debt securities or subordinated debt securities.

Neither Indenture contains provisions that would afford holders of debt securities protection in the event of a sudden and significant decline in our credit quality or a takeover, recapitalization or highly leveraged or similar transaction. Accordingly, we could in the future enter into transactions that could increase the amount of indebtedness outstanding at that time or otherwise adversely affect our capital structure or credit rating.

This description is a summary of the material provisions of the debt securities and the Indentures. We urge you to read the forms of Senior Indenture and Subordinated Indenture filed as exhibits to the registration statement of which this prospectus is a part because those Indentures, and not this description, govern your rights as a holder of our debt securities.

#### *The Debt Securities*

Any series of debt securities that we issue:

- will be the general obligations of Holly Energy Partners and Holly Energy Finance, if Holly Energy Finance co-issues such debt securities;
- will be general obligations of the Subsidiary Guarantors, if guaranteed by them; and
- may be subordinated to our Senior Indebtedness and that of any Subsidiary Guarantors.

The Indenture does not limit the total amount of debt securities that we may issue. We may issue debt securities under the Indenture from time to time in separate series, up to the aggregate amount authorized for each such series.

**Specific Terms of Each Series of Debt Securities to be Described in the Prospectus Supplement**

We will prepare a prospectus supplement and either a supplemental indenture, or authorizing resolutions of the board of directors of our general partner s general partner, accompanied by the officers certificate, relating to

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any series of debt securities that we offer, which will include specific terms relating to some or all of the following:

- the form and title of the debt securities;
- the total principal amount of the debt securities;
- the date or dates on which the debt securities may be issued;
- whether the debt securities are senior or subordinated debt securities;
- the currency or currencies in which principal and interest will be paid, if not in U.S. dollars;
- the portion of the principal amount which will be payable if the maturity of the debt securities is accelerated;
- any right we may have to defer payments of interest by extending the dates payments are due and whether interest on those deferred amounts will be payable;
- the dates on which the principal and premium, if any, of the debt securities will be payable;
- the interest rate or rates which the debt securities will bear, or by which the debt securities will accrete in value, and the interest payment dates for the debt securities;
- any conversion or exchange provisions;
- any optional redemption provisions;
- any sinking fund or other provisions that would obligate us to repurchase or otherwise redeem the debt securities;
- whether the debt securities are (i) to be co-issued by Holly Energy Finance and (ii) entitled to the benefits of any guarantees by the Subsidiary Guarantors;
- whether the debt securities may be issued in amounts other than $1,000 each or multiples thereof;

any changes to or additional events of default or covenants;

any changes to the defeasance or discharge provisions of the Indenture;

the subordination, if any, of the debt securities and any changes to the subordination provisions of the Subordinated Indenture; and

any other terms of the debt securities.

This description of debt securities will be deemed modified, amended or supplemented by any description of any series of debt securities set forth in a prospectus supplement related to that series.

The prospectus supplement also will describe any material United States federal income tax consequences or other special considerations regarding the applicable series of debt securities, including, without limitation, those relating to:

debt securities with respect to which payments of principal, premium or interest are determined with reference to an index or formula, including changes in prices of particular securities, currencies or commodities;

debt securities with respect to which payments of interest may be made in kind in lieu of, or in addition to, cash;

debt securities with respect to which principal, premium or interest is payable in a foreign or composite currency;

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debt securities that are issued at a discount below their stated principal amount, bearing no interest or interest at a rate that at the time of issuance is below market rates; and

variable rate debt securities that are exchangeable for fixed rate debt securities.

At our option, we may make cash interest payments by check mailed to the registered holders of debt securities or, if so stated in the applicable prospectus supplement, at the option of a holder by wire transfer to an account designated by the holder.

Unless otherwise provided in the applicable prospectus supplement, fully registered securities may be transferred or exchanged at the office of the Trustee at which its corporate trust business is principally administered in the United States, subject to the limitations provided in the Indenture, without the payment of any service charge, other than any applicable tax or governmental charge.

Any funds we pay to a paying agent for the payment of amounts due on any debt securities that remain unclaimed for two years will be returned to us, and the holders of the debt securities must look only to us for payment after that time.

**The Subsidiary Guarantees**

Our payment obligations under any series of debt securities may be jointly and severally, fully and unconditionally guaranteed by any of the Subsidiary Guarantors. If a series of debt securities is so guaranteed, the Subsidiary Guarantors will execute a notation of guarantee as further evidence of their guarantee. The applicable prospectus supplement will describe the terms of any guarantee by the Subsidiary Guarantors.

The obligations of each Subsidiary Guarantor under its guarantee of the debt securities will be limited to the maximum amount that will not result in the obligations of the Subsidiary Guarantor under the guarantee constituting a fraudulent conveyance or fraudulent transfer under federal or state law, after giving effect to:

all other contingent and fixed liabilities of the Subsidiary Guarantor; and

any collections from or payments made by or on behalf of any other Subsidiary Guarantors in respect of the obligations of the Subsidiary Guarantor under its guarantee.

The guarantee of any Subsidiary Guarantor may be released under certain circumstances. If we exercise our legal or covenant defeasance option with respect to debt securities of a particular series, or satisfy and discharge the Indenture with respect to that series, as described below under Defeasance and Discharge, then any Subsidiary Guarantor will be released with respect to that series. Further, if no default has occurred and is continuing under the Indenture, and to the extent not otherwise prohibited by the Indenture, a Subsidiary Guarantor will be unconditionally released and discharged from its guarantee:

automatically upon any sale, exchange or transfer, whether by way of merger or otherwise, to any person that is not our affiliate, of all of our direct or indirect limited partnership or other equity interests in the Subsidiary Guarantor;

automatically upon the merger of the Subsidiary Guarantor into us or any other Subsidiary Guarantor or the liquidation and dissolution of the Subsidiary Guarantor; or

following delivery of a written notice by us to the Trustee, upon the discharge or release of all guarantees by the Subsidiary Guarantor of any debt of ours under any credit facility, except discharge or release by or as a result of payment under such guarantee.

If a series of debt securities is guaranteed by the Subsidiary Guarantors and is designated as subordinate to our Senior Indebtedness, then the guarantees by the Subsidiary Guarantors will be subordinated to the Senior Indebtedness of the Subsidiary Guarantors to substantially the same extent as the series is subordinated to our Senior Indebtedness. See Subordination.

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**Specific Covenants**

The prospectus supplement applicable to any particular series of debt securities will contain a description of the important financial and other covenants that apply to us and our subsidiaries that are added to the Indenture specifically for the benefit of holders of a particular series.

The Indenture will contain the following covenants for the benefit of the holders of all series of debt securities:

***Reports***

So long as any debt securities are outstanding, we will:

- for as long as we are required to file information with the Commission pursuant to the Exchange Act, file with the Trustee, within 15 days after we file the same with the Commission, copies of the annual reports and of the information, documents and other reports which we are required to file with the Commission pursuant to the Exchange Act;

- if we are not required to file information with the Commission pursuant to the Exchange Act, file with the Trustee, within 15 days after we would have been required to file the same with the Commission, financial statements and a Management s Discussion and Analysis of Financial Condition and Results of Operations, both comparable to what we would have been required to file with the Commission had we been subject to the reporting requirements of the Exchange Act; and

- if we are required to furnish annual or quarterly reports to our unitholders pursuant to the Exchange Act, file with the Trustee and mail to the holders any annual report or other reports sent to unitholders generally.

The availability to the public of the foregoing materials on the Commission s website or on our website shall be deemed to satisfy the foregoing delivery obligations.

***Merger, Consolidation or Sale of Assets***

We may, without the consent of the holders of any of the debt securities, consolidate with or sell, lease, convey or otherwise dispose of all or substantially all of our assets to, or merge with or into, any partnership, limited liability company or corporation if:

- the entity surviving any such consolidation or merger or to which such assets shall have been transferred (the successor ) is us or the successor is a domestic partnership, limited liability company or corporation and expressly assumes all of our obligations and liabilities under the Indenture and the debt securities; provided that Holly Energy Finance may not consolidate or amalgamate with or merge into any entity other than a domestic corporation so long as we are not a corporation;

immediately after giving effect to the transaction, no default or Event of Default (as defined below) has occurred and is continuing;

if we are not the continuing entity, then any Subsidiary Guarantor has confirmed that its guarantee will continue to apply to the debt securities; and

we have delivered to the Trustee an officers certificate and an opinion of counsel, each stating that such consolidation, merger or disposition complies with the Indenture.

The successor will be substituted for us in the Indenture with the same effect as if it had been an original party to the Indenture. Thereafter, the successor may exercise the rights and powers of us under the Indenture, in our name or in its own name. If we dispose of all or substantially all of our assets, we will be released from all liabilities and obligations under the Indenture and under the debt securities except that no such release will occur in the case of a lease of all or substantially all of our assets.

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**Events of Default, Remedies and Notices**

***Events of Default***

Each of the following events will be an Event of Default under the Indenture with respect to a series of debt securities, except as set forth in any prospectus supplement:

- default in any payment of interest on any debt securities of that series when due that continues for 30 days;
- default in the payment of principal of or premium, if any, on any debt securities of that series when due at its stated maturity, upon redemption, by declaration, upon required repurchase or otherwise;
- default in the payment of any sinking fund payment on any debt securities of that series when due;
- failure by us or, if the series of debt securities is guaranteed by any Subsidiary Guarantor, by such Subsidiary Guarantor, for 60 days (or 180 days in the case of a failure to deliver to the Trustee the reports described under Specific Covenants Reports above) after written notice to comply with any of the other agreements contained in the Indenture, any supplement to the Indenture or any board resolution authorizing the issuance of that series;
- certain events of bankruptcy, insolvency or reorganization of us or, if the series of debt securities is guaranteed by any Subsidiary Guarantor, of any such Subsidiary Guarantor that is a Significant Subsidiary Guarantor (as defined below) or any group of Subsidiary Guarantors that, taken together, would constitute a Significant Subsidiary Guarantor; or
- if the series of debt securities is guaranteed by any Subsidiary Guarantor:
  - any of the guarantees ceases to be in full force and effect, except as otherwise provided in the Indenture;
  - any of the guarantees is declared null and void in a judicial proceeding; or
  - any Subsidiary Guarantor denies or disaffirms its obligations under the Indenture or its guarantee.

A Significant Subsidiary Guarantor means any Subsidiary Guarantor that would be a significant subsidiary as defined in Article 1, Rule 1-02 of Regulation S-X, promulgated pursuant to the Securities Act, as such Regulation is in effect on the date of the Indenture.

***Exercise of Remedies***

If an Event of Default, other than an Event of Default described in the fifth bullet point above, occurs and is continuing, the Trustee or the holders of at least 25% in principal amount of the outstanding debt securities of that series may declare the entire principal of, premium, if any, and accrued and unpaid interest, if any, on all the debt securities of that series to be due and payable immediately.

A default under the fourth bullet point above will not constitute an Event of Default until the Trustee or the holders of 25% in principal amount of the outstanding debt securities of that series notify us and, if the series of debt securities is guaranteed by any Subsidiary Guarantor, any such Subsidiary Guarantor, of the default and such default is not cured within 60 days (or 180 days in the case of a failure to deliver to the Trustee the reports described under Specific Covenants Reports above) after receipt of notice.

If an Event of Default described in the fifth bullet point above occurs and is continuing, the principal of, premium, if any, and accrued and unpaid interest on all outstanding debt securities of all series will become immediately due and payable without any declaration of acceleration or other act on the part of the Trustee or any holders.

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The holders of a majority in principal amount of the outstanding debt securities of a series may rescind any declaration of acceleration by the Trustee or the holders with respect to the debt securities of that series but only if:

- rescinding the declaration of acceleration would not conflict with any judgment or decree of a court of competent jurisdiction; and
- all existing Events of Default have been cured or waived, other than the nonpayment of principal, premium or interest on the debt securities of that series that has become due solely by the declaration of acceleration.

If an Event of Default occurs and is continuing, the Trustee will be under no obligation, except as otherwise provided in the Indenture, to exercise any of the rights or powers under the Indenture at the request or direction of any of the holders unless such holders have offered to the Trustee reasonable indemnity or security against any costs, liability or expense. No holder may pursue any remedy with respect to the Indenture or the debt securities of any series, except to enforce the right to receive payment of principal, premium, if any, or interest when due, unless:

- such holder has previously given the Trustee notice that an Event of Default with respect to that series is continuing;
- holders of at least 25% in principal amount of the outstanding debt securities of that series have requested that the Trustee pursue the remedy;
- such holders have offered the Trustee reasonable indemnity or security against any cost, liability or expense;
- the Trustee has not complied with such request within 60 days after the receipt of the request and the offer of indemnity or security; and
- the holders of a majority in principal amount of the outstanding debt securities of that series have not given the Trustee a direction that, in the opinion of the Trustee, is inconsistent with such request within such 60-day period.

The holders of a majority in principal amount of the outstanding debt securities of a series have the right, subject to certain restrictions, to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee or of exercising any right or power conferred on the Trustee with respect to that series of debt securities. The Trustee, however, may refuse to follow any direction that:

- conflicts with law;
- is inconsistent with any provision of the Indenture;

the Trustee determines is unduly prejudicial to the rights of any other holder; or

would involve the Trustee in personal liability.

***Notice of an Event of Default***

Within 30 days after the occurrence of any default (meaning an event that is, or after the notice or passage of time would be, an Event of Default) or Event of Default, we are required to give written notice to the Trustee and indicate the status of the default or Event of Default and what action we are taking or propose to take to cure it. In addition, we are required to deliver to the Trustee, within 120 days after the end of each fiscal year, a compliance certificate indicating that we have complied with all covenants contained in the Indenture or whether any default or Event of Default has occurred during the previous year.

If a default occurs and is continuing, the Trustee must mail to each holder a notice of the default by the later of 90 days after the default occurs or 30 days after the Trustee knows of the default. Except in the case of a

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default in the payment of principal, premium, if any, or interest with respect to any debt securities, the Trustee may withhold such notice, but only if and so long as the board of directors, the executive committee or a committee of directors or responsible officers of the Trustee in good faith determines that withholding such notice is in the interests of the holders.

**Amendments and Waivers**

Without the consent of any holder of debt securities affected, we, the Trustee and any Subsidiary Guarantors, as applicable, may amend or supplement the Indenture to:

cure any ambiguity, omission, defect or inconsistency;

convey, transfer, assign, mortgage or pledge any property to or with the Trustee;

provide for the assumption by a successor of our obligations under the Indenture;

add any Subsidiary Guarantor with respect to the debt securities;

change or eliminate any restriction on the payment of principal of, or premium, if any, on, any debt securities;

add covenants for the benefit of the holders or surrender any right or power conferred upon us or any Subsidiary Guarantor;

make any change that does not adversely affect the interests of any holder;

add or appoint a successor or separate Trustee;

comply with any requirement of the Commission in connection with the qualification of the Indenture under the Trust Indenture Act of 1939;

to conform the text of the Indenture or any guarantee to any provision of the Description of Debt Securities section of the related prospectus or any prospectus supplement;

issue of additional debt securities in accordance with the limitations set forth in the Indenture; or

establish the form or terms of debt securities of any series to be issued under the Indenture.

In addition, we, the Trustee and any Subsidiary Guarantors, may amend the Indenture if the holders of a majority in principal amount of all debt securities of each series that would be affected then outstanding under such Indenture consent to it. We, the Trustee and any Subsidiary Guarantors, as applicable, may not, however, without the consent of each holder of outstanding debt securities of each series that would be affected, amend the Indenture to:

reduce the percentage in principal amount of debt securities of any series whose holders must consent to an amendment;

reduce the rate of or extend the time for payment of interest on any debt securities;

reduce the principal of or extend the stated maturity of any debt securities;

reduce the premium payable upon the redemption of any debt securities or change the time at which any debt securities may or shall be redeemed;

make any debt securities payable in other than U.S. dollars;

impair the right of any holder to receive payment of premium, principal or interest with respect to such holder s debt securities on or after the applicable due date;

impair the right of any holder to institute suit for the enforcement of any payment with respect to such holder s debt securities;

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in the case of any subordinated debt securities, make any changes to the subordination provisions that adversely affects any holder of such securities;

release any security that has been granted in respect of the debt securities, other than in accordance with the Indenture;

make any change in the amendment provisions which require each holder s consent;

make any change in the waiver provisions; or

except as provided in the Indenture, release any Subsidiary Guarantor or modify the guarantee of any Subsidiary Guarantor in any manner adverse to the holders.

The consent of the holders is not necessary under the Indenture to approve the particular form of any proposed amendment. It is sufficient if such consent approves the substance of the proposed amendment. After an amendment under the Indenture requiring the consent of any holders becomes effective, we are required to mail to the holders of each series affected a notice briefly describing the amendment. The failure to give, or any defect in, such notice, however, will not impair or affect the validity of the amendment.

The holders of a majority in aggregate principal amount of the outstanding debt securities of each affected series, on behalf of all such holders, and subject to certain rights of the Trustee, may waive:

compliance by us or a Subsidiary Guarantor with certain restrictive provisions of the Indenture; and

any past default or Event of Default under the Indenture;

except that such majority of holders may not waive a default:

in the payment of principal, premium or interest; or

in respect of a provision that under the Indenture cannot be amended without the consent of all holders of the series of debt securities that is affected.

**Defeasance and Discharge**

At any time, we may terminate, with respect to debt securities of a particular series, all our obligations under such series of debt securities and the Indenture, which we call a legal defeasance. If we decide to make a legal defeasance, however, we may not terminate our obligations:

relating to the defeasance trust;

to register the transfer or exchange of the debt securities;

to replace mutilated, destroyed, lost or stolen debt securities; or

to maintain a registrar and paying agent in respect of the debt securities.

At any time we may also effect a covenant defeasance, which means we have elected to terminate our obligations under:

covenants applicable to a series of debt securities, including any covenant that is added specifically for such series and is described in a prospectus supplement;

the bankruptcy provisions with respect to any Significant Subsidiary Guarantor or group of Subsidiary Guarantors that, taken together, constitute a Significant Subsidiary Guarantor; and

the guarantee provision described under Events of Default, Remedies and Notices Events of Default above with respect to a series of debt securities, if applicable, and any Events of Default that is added specifically for such series and described in a prospectus supplement.

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We may exercise our legal defeasance option notwithstanding our prior exercise of our covenant defeasance option. If we exercise our legal defeasance option, payment of the affected series of debt securities may not be accelerated because of an Event of Default with respect to that series. If we exercise our covenant defeasance option, payment of the defeased series of debt securities may not be accelerated because of an Event of Default with respect to that series specified in the fourth, fifth (with respect only to a Subsidiary Guarantor (if any)) or sixth bullet points under Events of Default, Remedies and Notices Events of Default above or an Event of Default that is added specifically for such series and described in a prospectus supplement.

In order to exercise either defeasance option, we must:

- irrevocably deposit in trust with the Trustee money or certain U.S. government obligations for the payment of principal of, premium, if any, and interest on the series of debt securities to redemption or stated maturity, as the case may be;

- comply with certain other conditions, including that no default has occurred and is continuing after the deposit in trust; and

- deliver to the Trustee of an opinion of counsel to the effect that holders of the series of debt securities will not recognize income, gain or loss for federal income tax purposes as a result of such defeasance and will be subject to federal income tax on the same amount and in the same manner and at the same times as would have been the case if such deposit and defeasance had not occurred. In the case of legal defeasance only, such opinion of counsel must be based on a ruling of the Internal Revenue Service (the IRS ) or other change in applicable federal income tax law.

If we exercise either our legal defeasance option or our covenant defeasance option, any guarantee by a Subsidiary Guarantor will terminate with respect to the defeased series of debt securities.

In addition, we may satisfy and discharge all our obligations under the Indenture with respect to debt securities of a particular series, other than our obligation to register the transfer of and exchange such debt securities, provided that we either:

- deliver all outstanding debt securities of such series to the Trustee for cancellation; or

- all such debt securities not so delivered for cancellation have either become due and payable or will become due and payable at their stated maturity within one year or are called for redemption within one year, and in the case of this bullet point, we have deposited with the Trustee in trust an amount of cash sufficient to pay the entire indebtedness of such debt securities, including interest to the stated maturity or applicable redemption date.

**No Personal Liability of Directors, Officers, Employees and Unitholders**

No past, present or future director, officer, partner, member, employee, incorporator, manager or unitholder or other owner of any equity interest in us, our general partner or any Subsidiary Guarantors, as applicable, will have any

liability for any obligations of us or any Subsidiary Guarantors under any debt securities, any Indenture, any guarantee of any debt securities or for any claim based on, in respect of, or by reason of, such obligations or their creation. Each holder of any debt security accepting such debt security waives and releases all such liability. The waiver and release are part of the consideration for issuance of any debt securities and any guarantee. The waiver may not be effective to waive liabilities under the federal securities laws.

**Subordination**

Debt securities of a series may be subordinated to our Senior Indebtedness, which we define generally to include any obligation created or assumed by us (or, if the series is guaranteed, any Subsidiary Guarantors) for the repayment of borrowed money and any guarantee thereof, whether outstanding or hereafter issued, unless, by

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the terms of the instrument creating or evidencing such obligation, it is provided that such obligation is subordinate or not superior in right of payment to the subordinated debt securities (or, if the series is guaranteed, the guarantee of any Subsidiary Guarantor), or to other obligations which are pari passu with or subordinated to the subordinated debt securities (or, if the series is guaranteed, the guarantee of any Subsidiary Guarantor). Subordinated debt securities will be subordinate in right of payment, to the extent and in the manner set forth in the Indenture and the prospectus supplement relating to such series, to the prior payment of all of our indebtedness and that of any Subsidiary Guarantor that is designated as Senior Indebtedness with respect to the series.

The holders of Senior Indebtedness of ours or, if applicable, any Subsidiary Guarantor, will receive payment in full of the Senior Indebtedness before holders of any subordinated debt securities will receive any payment of principal, premium or interest with respect to the subordinated debt securities upon any payment or distribution of our assets or, if applicable to any series of outstanding debt securities, the Subsidiary Guarantors assets, to creditors:

- upon a liquidation or dissolution of us or, if applicable to any series of outstanding debt securities, the Subsidiary Guarantors; or
- in a bankruptcy, receivership or similar proceeding relating to us or, if applicable to any series of outstanding debt securities, to the Subsidiary Guarantors.

Until the Senior Indebtedness is paid in full, any distribution to which holders of subordinated debt securities would otherwise be entitled will be made to the holders of Senior Indebtedness, except that the holders of subordinated debt securities may receive units representing limited partner interests and any debt securities that are subordinated to Senior Indebtedness to at least the same extent as the subordinated debt securities.

If we do not pay any principal, premium or interest with respect to Senior Indebtedness within any applicable grace period (including at maturity), or any other default on Senior Indebtedness occurs and the maturity of the Senior Indebtedness is accelerated in accordance with its terms, we may not:

- make any payments of principal, premium, if any, or interest with respect to subordinated debt securities;
- make any deposit for the purpose of defeasance or discharge of the subordinated debt securities; or
- repurchase, redeem or otherwise retire any subordinated debt securities, except that in the case of subordinated debt securities that provide for a mandatory sinking fund, we may deliver subordinated debt securities to the Trustee in satisfaction of our sinking fund obligation, unless, in any case,
  - the default has been cured or waived and any declaration of acceleration has been rescinded;
  - the Senior Indebtedness has been paid in full in cash; or

we and the Trustee receive written notice approving the payment from the representative of each issue of Designated Senior Indebtedness.

During the continuance of any default, other than a default described in the immediately preceding paragraph, that may cause the maturity of any Designated Senior Indebtedness to be accelerated immediately without further notice, other than any notice required to effect such acceleration, or the expiration of any applicable grace periods, we may not pay the subordinated debt securities for a period called the Payment Blockage Period. Generally, Designated Senior Indebtedness will include:

any specified issue of Senior Indebtedness of at least $100 million; and

any other Senior Indebtedness that we may designate in respect of any series of subordinated debt securities.

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A Payment Blockage Period will commence on the receipt by us and the Trustee of written notice of the default, called a Blockage Notice, from the representative of any Designated Senior Indebtedness specifying an election to effect a Payment Blockage Period and will end 179 days thereafter.

The Payment Blockage Period may be terminated before its expiration:

- by written notice to us and to the Trustee from the person or persons who gave the Blockage Notice;
- by repayment in full in cash of the Designated Senior Indebtedness with respect to which the Blockage Notice was given; or
- if the default giving rise to the Payment Blockage Period is no longer continuing.

Unless the holders of the Designated Senior Indebtedness or their representatives have accelerated the maturity of the Designated Senior Indebtedness, we may resume payments on the subordinated debt securities after the expiration of the Payment Blockage Period.

Generally, not more than one Blockage Notice may be given in any period of 360 consecutive days. The total number of days during which any one or more Payment Blockage Periods are in effect, however, may not exceed an aggregate of 179 days during any period of 360 consecutive days.

After all Senior Indebtedness is paid in full and until the subordinated debt securities are paid in full, holders of the subordinated debt securities shall be subrogated to the rights of holders of Senior Indebtedness to receive distributions applicable to Senior Indebtedness.

As a result of the subordination provisions described above, in the event of insolvency, the holders of Senior Indebtedness, as well as certain of our general creditors, may recover more, ratably, than the holders of the subordinated debt securities.

**Book-Entry System**

We may issue debt securities of a series in the form of one or more global certificates, each of which we refer to as a global security, registered in the name of a depositary or a nominee of a depositary. We expect that The Depository Trust Company, New York, New York, ( DTC ), will act as depositary. If we issue debt securities of a series in book-entry form, we will issue one or more global certificates that will be deposited with or on behalf of DTC and will not issue physical certificates to each holder. A global security may not be transferred unless it is exchanged in whole or in part for a certificated security, except that DTC, its nominees and their successors may transfer a global security as a whole to one another.

Beneficial interests in global debt securities will be shown on, and transfers of global debt securities will be made only through, records maintained by DTC and its participants.

DTC has advised us as follows:

DTC is a limited-purpose trust company organized under the New York Banking Law, a banking organization within the meaning of the New York Banking Law, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code, and a clearing agency registered pursuant to the provisions of Section 17A of the Exchange Act.

DTC holds and provides asset servicing for securities that its participants (known as direct participants) deposit with DTC. DTC also facilitates the post-trade settlement among direct participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between direct participants accounts, thereby eliminating the need for physical movement of securities certificates.

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Direct participants in DTC include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations.

Access to the DTC system is also available to others, known as indirect participants, such as U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a direct participant, either directly or indirectly.

The rules applicable to DTC participants are on file with the Commission.

Any purchases of debt securities under the DTC system must be made by or through direct participants, which will receive a credit for the debt securities on DTC s records. The ownership interest of each actual purchaser of debt securities is in turn to be recorded on the direct and indirect participants records. Beneficial owners of the debt securities will not receive written confirmation from DTC of their purchase, but beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the direct or indirect participants through which the beneficial owner entered into the transaction. Transfers of ownership interests in the debt securities are to be accomplished by entries made on the books of direct and indirect participants acting on behalf of beneficial owners. Beneficial owners will not receive certificates representing their ownership interests in the debt securities, except in the event that use of the book-entry system for the debt securities is discontinued.

Because DTC can only act on behalf of direct participants, who in turn act on behalf of indirect DTC participants and certain banks, the ability of a person having a beneficial interest in a security held in DTC to transfer or pledge that interest to persons or entities that do not participate in the DTC system, or otherwise take actions in respect of that interest, may be affected by the lack of a physical certificate of that interest. The laws of some states of the United States require that certain persons take physical delivery of securities in definitive form in order to transfer or perfect a security interest in those securities. Consequently, the ability to transfer beneficial interests in a security held in DTC to those persons may be limited.

DTC has advised us that it will take any action permitted to be taken by a holder of debt securities (including, without limitation, the presentation of debt securities for exchange) only at the direction of one or more of the participants to whose accounts with DTC interests in the relevant debt securities are credited, and only in respect of the portion of the aggregate principal amount of the debt securities as to which that participant or those participants has or have given the direction. However, in certain circumstances, DTC will exchange the global securities held by it for certificated debt securities, which it will distribute to its participants.

To facilitate subsequent transfers of ownership interests in the debt securities, all debt securities deposited by direct participants with DTC are registered in the name of DTC s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of debt securities with DTC and their registration in the name of Cede & Co. or such other nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual beneficial owners of the debt securities; DTC s records reflect only the identity of the direct participants to whose accounts such debt securities are credited, which may or may not be the beneficial owners. The direct and indirect participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to direct participants, by, direct participants to indirect participants, and by direct participants and indirect participants to beneficial owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the global securities. Under its usual procedures, DTC mails an omnibus proxy to the issuer as soon as possible after the record date. The omnibus proxy assigns Cede & Co. s consenting or voting rights to those direct participants to whose accounts the debt securities are credited on the record date (identified in the listing attached to the omnibus proxy).

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All payments on the global securities will be made to Cede & Co., as holder of record, or such other nominee as may be requested by an authorized representative of DTC. DTC s practice is to credit direct participants accounts upon DTC s receipt of funds and corresponding detail information from us or the Trustee on payment dates in accordance with their respective holdings shown on DTC s records. Payments by participants to beneficial owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in street name, and will be the responsibility of such participant and not of DTC, us, the Trustee or any Subsidiary Guarantor, as applicable, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, premium, if any, and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) shall be the responsibility of us or the Trustee. Disbursement of such payments to direct participants shall be the responsibility of DTC, and disbursement of such payments to the beneficial owners shall be the responsibility of direct and indirect participants.

Neither we, the Trustee nor any Subsidiary Guarantor, as applicable, will have any responsibility or obligation to direct or indirect participants, or the persons for whom they act as nominees, with respect to the accuracy of the records of DTC, its nominee, any other depositary or its nominee, or any participant with respect to any ownership interest in any debt securities, or payments to, or the providing of notice to participants or beneficial owners.

**The Trustee**

We may appoint a separate trustee for any series of debt securities. We may maintain banking and other commercial relationships with the Trustee and its affiliates in the ordinary course of business, and the Trustee may own debt securities.

**Governing Law**

The Indenture and any series of debt securities will be governed by, and construed in accordance with, the laws of the State of New York.

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## DESCRIPTION OF OUR COMMON UNITS AND PREFERRED UNITS

### Common Units

Our common units represent limited partner interests that entitle the holders to participate in our cash distributions and to exercise the rights and privileges available to limited partners under our partnership agreement. For a description of the relative rights and preferences of holders of our common units and our general partner in and to cash distributions, please carefully review this section and the section titled How We Make Cash Distributions in this prospectus.

Our outstanding common units are listed on the New York Stock Exchange (the NYSE ) under the symbol HEP. Any additional common units we issue will also be listed on the NYSE.

The transfer agent and registrar for our common units is EQ Shareowner Services.

#### *Number of Units*

As of December 3, 2018, we had 105,440,201 common units outstanding.

#### *Status as Limited Partner or Assignee*

Except as described below under Limited Liability, our common units will be fully paid, and unitholders will not be required to make additional capital contributions to us.

#### *Limited Liability*

Assuming that a limited partner does not participate in the control of our business within the meaning of the Delaware Revised Uniform Limited Partnership Act (the Delaware Act ) and that he otherwise acts in conformity with the provisions of our partnership agreement, his liability under the Delaware Act will be limited, subject to some possible exceptions, generally to the amount of capital he is obligated to contribute to us in respect of his units plus his share of any undistributed profits and assets wrongfully distributed to it, as described below. If it were determined, however, that the right of, or exercise of the right by, the limited partners as a group:

- to remove or replace our general partner;
- to approve some amendments to our partnership agreement; or
- to take other action under our partnership agreement;

constituted participation in the control of our business for the purposes of the Delaware Act, then the limited partners could be held personally liable for our obligations under the laws of Delaware to the same extent as our general partner. This liability would additionally extend to persons who transact business with us who reasonably believe that the limited partner is a general partner based on the conduct of the limited partner. Neither our partnership agreement nor the Delaware Act specifically provides for legal recourse against our general partner if a limited partner were to lose limited liability through any fault of our general partner.

Under the Delaware Act, a limited partnership may not make a distribution to a partner to the extent that at the time of the distribution, after giving effect to the distribution, all liabilities of the partnership, other than liabilities to partners on account of their partnership interests and liabilities for which the recourse of creditors is limited to specific property of the partnership, exceed the fair value of the assets of the limited partnership.

For the purposes of determining the fair value of the assets of a limited partnership, the Delaware Act provides that the fair value of the property subject to liability of which recourse of creditors is limited shall be

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included in the assets of the limited partnership only to the extent that the fair value of that property exceeds the nonrecourse liability. The Delaware Act provides that a limited partner who receives a distribution and knew at the time of the distribution that the distribution was in violation of the Delaware Act is liable to the limited partnership for the amount of the distribution for three years from the date of the distribution. Under the Delaware Act, an assignee who becomes a substituted limited partner of a limited partnership is liable for the obligations of its assignor to make contributions to the limited partnership, excluding any obligations of the assignor with respect to wrongful distributions, as described above, except the assignee is not obligated for liabilities unknown to it at the time it became a limited partner and that could not be ascertained from the partnership agreement.

We currently own property and conduct business in Texas, New Mexico, Utah, Nevada, Oklahoma, Wyoming, Kansas, Idaho, and Washington. We may own property or conduct business in other states in the future. Maintenance of our limited liability as a limited partner of our operating partnership may require compliance with legal requirements in the jurisdictions in which our operating partnership owns property or conducts business, including qualifying our subsidiaries to do business there.

Limitations on the liability of limited partners for the obligations of a limited partnership have not been clearly established in many jurisdictions. If, by virtue of our limited partner interest in our operating partnership or otherwise, it were determined that we were conducting business in any state without compliance with the applicable limited partnership or limited liability company statute, or that the right of, or exercise of the right by, the limited partners as a group, to remove or replace our general partner, to approve some amendments to our partnership agreement, or to take other action under our partnership agreement constituted participation in the control of our business for purposes of the statutes of any relevant jurisdiction, then the limited partners could be held personally liable for our obligations under the law of that jurisdiction to the same extent as our general partner under the circumstances. We will operate in a manner that our general partner considers reasonable and necessary or appropriate to preserve the limited liability of the limited partners.

***Voting Rights***

Our general partner manages and operates us. Unlike the holders of common stock in a corporation, our unitholders have only limited voting rights on matters affecting our business and, therefore, limited ability to influence management s decisions regarding our business. Our unitholders did not elect our general partner or the board of directors of our general partner s general partner and have no right to elect our general partner or the board of directors of our general partner s general partner on an annual or other continuing basis. The board of directors of our general partner s general partner is chosen by the members of our general partner s general partner. Furthermore, if unitholders are dissatisfied with the performance of our general partner, they will have little ability to remove our general partner. As a result of these limitations, the price at which the common units trade could be diminished because of the absence or reduction of a takeover premium in the trading price.

The vote of the holders of at least 66 $^{2}/_{3}$% of all outstanding units voting together as a single class is required to remove the general partner. Our unitholders will be unable to remove the general partner without its consent because the general partner and its affiliates own sufficient units to prevent its removal. Our unitholders voting rights are further restricted by the partnership agreement provision providing that any units held by a person or group that owns 20% or more of any class of units then outstanding, other than the general partner, its affiliates, their transferees, and persons who acquired such units with the prior approval of the board of directors of the general partner s general partner, cannot vote on any matter. Our partnership agreement also contains provisions limiting the ability of unitholders to call meetings or to acquire information about our operations, as well as other provisions limiting the unitholders ability to influence the manner or direction of management.

In voting its common units, the general partner and its affiliates will have no fiduciary duty or obligation whatsoever to us or the limited partners.

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Our unitholders will not have voting rights except with respect to the following matters which require the unitholder vote specified below:

| | |
|---|---|
| Issuance of additional units | No approval required. |
| Amendment of the partnership agreement | Certain amendments may be made by the general partner without the approval of the unitholders. Other amendments generally require the approval of a majority of the outstanding units. |
| Merger of our partnership or the sale of all or substantially all of our assets | Approval of a majority of the outstanding units. |
| Amendment of the partnership agreement of our operating partnership and other action taken by us as a limited partner of the operating partnership | Approval of a majority of the outstanding units if such amendment or other action would adversely affect our limited partners (or any particular class of limited partners) in any material respect. |
| Dissolution of our partnership | Approval of a majority of the outstanding units. |
| Reconstitution of our partnership upon dissolution | Approval of a majority of the outstanding units. |
| Withdrawal of the general partner | No approval right. Please read Description of Our Partnership Agreement Withdrawal or Removal of our General Partner. |
| Removal of the general partner | Not less than 66 2/3% of the outstanding units, voting as a single class, including units held by our general partner and its affiliates. |
| Transfer of the general partner interest | No approval right. Please read Description of Our Partnership Agreement Transfer of General Partner Interests. |
| Transfer of ownership interests in the general partner | No approval required at any time. |

***Transfer of Common Units***

The purchase of any of our common units offered by this prospectus and any prospectus supplement is accomplished through the completion, execution and delivery of a transfer application. Additionally, any later transfers of our

common units will not be recorded by the transfer agent or recognized by us unless the transferee executes and delivers a transfer application. By executing and delivering a transfer application, a purchaser or transferee of our common units:

becomes the record holder of our common units and is an assignee until admitted into our partnership as a substituted limited partner;

automatically requests admission as a substituted limited partner in our partnership;

agrees to be bound by the terms and conditions of, and executes, our partnership agreement;

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represents and warrants that such transferee has the capacity, power and authority to enter into the partnership agreement;

grants powers of attorney to our general partner and any liquidator of us as specified in the partnership agreement; and

gives the consents and approvals contained in our partnership agreement.

An assignee will become a substituted limited partner of our partnership for the transferred common units upon admission by our general partner and the recording of the name of the assignee on our books and records. Our general partner intends to admit assignees as substituted limited partners on a quarterly basis.

A transferee s broker, agent or nominee may complete, execute and deliver a transfer application. We are entitled to treat the nominee holder of a common unit as the absolute owner. In that case, the beneficial holder s rights are limited solely to those that it has against the nominee holder as a result of any agreement between the beneficial owner and the nominee holder.

Common units are securities and are transferable according to the laws governing transfer of securities. In addition to other rights acquired upon transfer, the transferor gives the transferee the right to request admission as a substituted limited partner in our partnership for the transferred common units. A purchaser or transferee of our common units who does not execute and deliver a transfer application obtains only:

the right to assign the common unit to a purchaser or other transferee; and

the right to transfer the right to seek admission as a substituted limited partner in our partnership for the transferred common units.

Thus, a purchaser or transferee of our common units who does not execute and deliver a transfer application:

will not receive cash distributions or federal income tax allocations, unless the common units are held in a nominee or street name account and the nominee or broker has executed and delivered a transfer application; and may not receive some federal income tax information or reports furnished to record holders of our common units.

The transferor of our common units has a duty to provide the transferee with all information that may be necessary to transfer the common units. The transferor does not have a duty to insure the execution of the transfer application by the transferee and has no liability or responsibility if the transferee neglects or chooses not to execute and forward the transfer application to the transfer agent. Until a common unit has been transferred on our books, we and the transfer agent may treat the record holder of the unit as the absolute owner for all purposes, except as otherwise required by law or stock exchange regulations.

***Reports and Records***

As soon as practicable, but in no event later than 120 days after the close of each fiscal year, our general partner will furnish or make available to each unitholder of record (as of a record date selected by our general partner) an annual report containing our audited financial statements and a report on those financial statements by our independent public accountants. These financial statements will be prepared in accordance with generally accepted accounting principles. Except for our fourth quarter, we will also furnish or make available summary financial information within 90 days after the close of each quarter.

We will also furnish each unitholder of record with information reasonably required for tax reporting purposes within 90 days after the close of each calendar year. This information is expected to be furnished in summary form so that some complex calculations normally required of partners can be avoided. Our ability to

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furnish this summary information to unitholders will depend on the cooperation of unitholders in supplying us with specific information. Every unitholder will receive information to assist such unitholder in determining his federal and state tax liability and filing his federal and state income tax returns, regardless of whether he supplies us with information.

A limited partner can, for a purpose reasonably related to the limited partner s interest as a limited partner, upon reasonable demand and at his own expense, have furnished to such unitholder:

- a current list of the name and last known address of each partner;
- a copy of our tax returns;
- information as to the amount of cash and a description and statement of the agreed value of any other property or services, contributed or to be contributed by each partner and the date on which each became a partner;
- copies of our partnership agreement, our certificate of limited partnership, amendments to either of them and powers of attorney which have been executed under our partnership agreement;
- information regarding the status of our business and financial condition; and
- any other information regarding our affairs as is just and reasonable.

Our general partner may, and intends to, keep confidential from the limited partners trade secrets and other information the disclosure of which our general partner believes in good faith is not in our best interest or which we are required by law or by agreements with third parties to keep confidential.

**Preferred Units**

Except as set forth below, our partnership agreement authorizes us to issue an unlimited number of additional limited partner interests and other equity securities for the consideration and with the rights, preferences and privileges established by our general partner in its sole discretion without the approval of any of our limited partners.

In accordance with Delaware law and the provisions of our partnership agreement, we may also issue additional partnership interests that, in the sole discretion of our general partner, have special voting rights to which our common units are not entitled. As of the date of this prospectus, we have no preferred units outstanding.

Should we offer preferred units under this prospectus, a prospectus supplement relating to the particular series of preferred units offered will include the specific terms of those preferred units, including the following:

the designation, stated value and liquidation preference of the preferred units and the number of preferred units offered;

the initial public offering price at which the preferred units will be issued;

the conversion or exchange provisions of the preferred units;

any redemption or sinking fund provisions of the preferred units;

the distribution rights of the preferred units, if any;

a discussion of material federal income tax considerations, if any, regarding the preferred units; and

any additional rights, preferences, privileges, limitations and restrictions of the preferred units.

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## HOW WE MAKE CASH DISTRIBUTIONS

*We have not issued any preferred units and the discussion below assumes that no preferred units are outstanding. A description of the material terms of our cash distribution policy as it applies to any preferred units will be set forth in the prospectus supplement relating to the offering of such preferred units.*

### Distributions of Available Cash

#### *General*

Our partnership agreement provides that we will distribute all of our available cash to unitholders of record on the applicable record date within 45 days after the end of each quarter.

In October 2017, our general partner agreed to waive $2.5 million of limited partner cash distributions for each of twelve consecutive quarters beginning with the quarter ending September 30, 2017.

#### *Definition of Available Cash*

Available cash generally means, for each fiscal quarter, all cash and cash equivalents on hand at the end of the quarter:

less the amount of cash reserves established by our general partner to:

provide for the proper conduct of our business;

comply with applicable law, any of our debt instruments, or other agreements; or

provide funds for distributions to our unitholders and to our general partner for any one or more of the next four quarters;

plus all cash and cash equivalents on hand on the date of determination of available cash for the quarter resulting from working capital borrowings made after the end of the quarter. Working capital borrowings are generally borrowings that are made under our credit facility and in all cases are used solely for working capital purposes or to pay distributions to partners.

### Distributions of Cash upon Liquidation

#### *General*

If we dissolve in accordance with the partnership agreement, we will sell or otherwise dispose of our assets in a process called liquidation. We will first apply the proceeds of liquidation to the payment of our creditors. We will distribute any remaining proceeds to the unitholders and the general partner, in accordance with their capital account balances, as adjusted to reflect any gain or loss upon the sale or other disposition of our assets in liquidation.

***Manner of Adjustments for Income***

The manner of the adjustment for gain is set forth in the partnership agreement. We will allocate any gain to the partners in the following manner:

*First*, to the general partner to the extent of any residual loss allocations; and

*Second*, the balance, if any, to the common unitholders, pro rata.

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***Manner of Adjustments for Losses***

We will generally allocate any loss to the general partner and the unitholders in the following manner:

*First*, to the holders of common units pro rata in proportion to the positive balances in their capital accounts until the capital accounts of the common unitholders have been reduced to zero; and

*Thereafter*, the balance, if any, 100% to the general partner.

***Adjustments to Capital Accounts***

We will make adjustments to capital accounts upon the issuance of additional units. In doing so, we will allocate any unrealized and, for tax purposes, unrecognized gain or loss resulting from the adjustments to the unitholders and the general partner in the same manner as we allocate gain or loss upon liquidation. In the event that we make positive adjustments to the capital accounts upon the issuance of additional units, we will allocate any later negative adjustments to the capital accounts resulting from the issuance of additional units or upon our liquidation in a manner which results, to the extent possible, in the general partner s capital account balances equaling the amount which they would have been if no earlier positive adjustments to the capital accounts had been made.

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## DESCRIPTION OF OUR PARTNERSHIP AGREEMENT

The following is a summary of the material provisions of our partnership agreement. Our second amended and restated partnership agreement, as amended, has been filed with the Commission. The following provisions of our partnership agreement are summarized elsewhere in this prospectus:

distributions of our available cash are described under How We Make Cash Distributions;

allocations of taxable income and other matters are described under Material U.S. Federal Tax Consequences;

rights of holders of our common units are described under Description of Our Common Units; and

fiduciary duties of our general partner are described under Conflicts of Interest and Fiduciary Duties.

### Purpose

Our purpose under our partnership agreement is to serve as the limited partner of our operating partnership and to engage in any business activities that may be engaged in by our operating partnership or that are approved by our general partner. The partnership agreement of our operating partnership provides that the operating partnership may, directly or indirectly, engage in any activity approved by the general partner but only to the extent that the general partner determines that, as of the date of the acquisition or commencement of the activity, the activity generates qualifying income as this term is defined in Section 7704 of the Internal Revenue Code of 1986, as amended, or any activity that enhances the operations of an activity that is described above.

### Power of Attorney

Each limited partner, and each person who acquires a unit from a unitholder and executes and delivers a transfer application, grants to our general partner and, if appointed, a liquidator, a power of attorney to, among other things, execute and file documents required for our qualification, continuance or dissolution. The power of attorney also grants the authority for the amendment of, and to make consents and waivers under, our partnership agreement.

### Reimbursements of Our General Partner

Our general partner does not receive any compensation for its services as our general partner. It is, however, entitled to be reimbursed for all of its costs incurred in managing and operating our business. Our partnership agreement provides that our general partner will determine the expenses that are allocable to us in any reasonable manner determined by our general partner in its sole discretion.

### Issuance of Additional Securities

Our partnership agreement authorizes us to issue an unlimited number of additional partnership securities and rights to buy partnership securities for the consideration and on the terms and conditions determined by our general partner in its sole discretion without the approval of the unitholders. It is possible that we will fund acquisitions through the

issuance of additional common units or other equity securities. Holders of any additional common units or other equity securities we issue may be entitled to share with the then-existing holders of our common units or other equity securities in our cash distributions. In addition, the issuance of additional partnership interests may dilute the value of the interests of the then-existing holders of common units in our net assets. In accordance with Delaware law and the provisions of our partnership agreement, we may also issue additional partnership interests that, in the sole discretion of our general partner, may have special voting rights to which common units are not entitled.

Moreover, the general partner will have the right, which it may from time to time assign in whole or in part to any of its affiliates, to purchase common units or other equity securities whenever, and on the same terms that,

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we issue those securities to persons other than the general partner and its affiliates, to the extent necessary to maintain its and its affiliates percentage interest, including its interest represented by common units, that existed immediately prior to each issuance. The holders of common units do not have preemptive rights to acquire additional common units or other partnership securities.

**Amendments to Our Partnership Agreement**

Amendments to our partnership agreement may be proposed only by our general partner, which consent may be given or withheld at its option. Any amendment that materially and adversely affects the rights or preferences of any type or class of limited partner interests in relation to other types or classes of limited partner interests or our general partner interest will require the approval of at least a majority of the type or class of limited partner interests or general partner interests so affected. However, in some circumstances, more particularly described in our partnership agreement, our general partner may make amendments to our partnership agreement without the approval of our limited partners or assignees.

**Withdrawal or Removal of Our General Partner**

Our general partner may withdraw as general partner without first obtaining approval of any unitholder by giving 90 days written notice, and that withdrawal will not constitute a violation of the partnership agreement.

Upon withdrawal of our general partner under any circumstances, other than as a result of a transfer by the general partner of all or a part of its general partner interest in us, the holders of a majority of the outstanding common units may select a successor to that withdrawing general partner. If a successor is not elected, or is elected but an opinion of counsel regarding limited liability and tax matters cannot be obtained, we will be dissolved, wound up, and liquidated, unless within a specified period of time after that withdrawal, the holders of a unit majority agree in writing to continue our business and to appoint a successor general partner.

Our general partner may not be removed unless that removal is approved by the vote of the holders of not less than $66\,^2/_3\%$ of our outstanding units, voting together as a single class, including units held by the general partner and its affiliates, and we receive an opinion of counsel regarding limited liability and tax matters. Any removal of our general partner is also subject to the approval of a successor general partner by the vote of the holders of a majority of the outstanding common units.

In the event of removal of our general partner under circumstances where cause exists or withdrawal of the general partner where that withdrawal violates the partnership agreement, a successor general partner will have the option to purchase the general partner interest of the departing general partner for a cash payment equal to the fair market value of such interest. Under all other circumstances where the general partner withdraws or is removed by the limited partners, the departing general partner will have the option to require the successor general partner to purchase the general partner interest of the departing general partner for its fair market value. In each case, this fair market value will be determined by agreement between the departing general partner and the successor general partner. If no agreement is reached, an independent investment banking firm or other independent expert selected by the departing general partner and the successor general partner will determine the fair market value. Or, if the departing general partner and the successor general partner cannot agree upon an independent investment banking firm or other independent expert, then an independent investment banking firm or other independent expert chosen by agreement of the firms or experts selected by each of them will determine the fair market value.

If the option described above is not exercised by either the departing general partner or the successor general partner, the departing general partner s general partner interest will automatically convert into common units equal to the fair

market value of those interests as determined by an investment banking firm or other independent expert selected in the manner described in the preceding paragraph.

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In addition, we will be required to reimburse the departing general partner for all amounts due the departing general partner, including, without limitation, all employee-related liabilities, including severance liabilities, incurred for the termination of any employees employed by the departing general partner or its affiliates for our benefit.

**Liquidation and Distribution of Proceeds**

Upon our dissolution, unless we are reconstituted and continued as a new limited partnership, the person authorized to wind up our affairs (the liquidator) will, acting with all the powers of our general partner that the liquidator deems necessary or desirable in its good faith judgment, liquidate our assets and apply the proceeds of the liquidation as provided in How We Make Cash Distributions Distributions of Cash upon Liquidation. The liquidator may defer liquidation or distribution of our assets for a reasonable period or distribute assets to partners in kind if it determines that a sale would be impractical or would cause undue loss to the partners.

**Transfer of General Partner Interests**

At any time, our general partner may transfer all or any part of its general partner interest in us to another person without the approval of our common unitholders. As a condition of this transfer, the transferee must, among other things, assume the rights and duties of the general partner, agree to be bound by the provisions of the partnership agreement, and furnish an opinion of counsel regarding limited liability and tax matters.

Subject to certain exceptions, our general partner and its affiliates may at any time transfer units to one or more persons, without unitholder approval.

**Transfer of Ownership Interests in Our General Partner and in Our General Partner s General Partner**

At any time, the partners of our general partner and the members of Holly Logistic Services, L.L.C., the general partner of our general partner, may sell or transfer all or part of their respective partnership or membership interests in our general partner or Holly Logistic Services, L.L.C. to an affiliate or a third party without the approval of our unitholders.

**Change of Management Provisions**

Our partnership agreement contains specific provisions that are intended to discourage a person or group from attempting to remove HEP Logistics Holdings, L.P. as our general partner or otherwise change management. If any person or group other than the general partner and its affiliates acquires beneficial ownership of 20% or more of any class of units, that person or group loses voting rights on all of its units. This loss of voting rights does not apply to any person or group that acquires the units from our general partner or its affiliates and any transferees of that person or group approved by our general partner or to any person or group who acquires the units with the prior approval of the board of directors.

The partnership agreement also provides that if the general partner is removed under circumstances where cause does not exist and units held by the general partner and its affiliates are not voted in favor of that removal, the general partner will have the right to convert its general partner interest into common units or to receive cash in exchange for those interests.

**Limited Call Right**

If at any time the general partner and its affiliates hold more than 80% of the then-issued and outstanding partnership securities of any class, the general partner will have the right, which it may assign in whole or in part to any of its affiliates or to us, to acquire all, but not less than all, of the remaining partnership securities of the class held by unaffiliated persons as of a record date to be selected by the general partner, on at least ten but not

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more than 60 days notice. The purchase price in the event of this purchase is the greater of: (1) the highest cash price paid by either of the general partner or any of its affiliates for any partnership securities of the class purchased within the 90 days preceding the date on which the general partner first mails notice of its election to purchase those partnership securities; and (2) the current market price as of the date three days before the date the notice is mailed.

As a result of the general partner s right to purchase outstanding partnership securities, a holder of partnership securities may have his partnership securities purchased at an undesirable time or price. The tax consequences to a unitholder of the exercise of this call right are the same as a sale by that unitholder of his common units in the market. Please read Material U.S. Federal Tax Consequences Disposition of Common Units.

**Indemnification**

Under our partnership agreement, in most circumstances, we will indemnify the following persons, to the fullest extent permitted by law, from and against all losses, claims, damages, or similar events:

- our general partner;
- the general partner of our general partner;
- any departing general partner;
- any person who is or was an affiliate of our general partner or the general partner of our general partner or any departing general partner;
- any person who is or was a member, partner, officer, director, fiduciary or trustee of any entity described above;
- any person who is or was serving as a director, officer, member, partner, fiduciary or trustee of another person at the request of our general partner, the general partner of our general partner or any departing general partner; or
- any person designated by our general partner.

Any indemnification under these provisions will only be out of our assets. Unless it otherwise agrees, the general partner will not be personally liable for, or have any obligation to contribute or loan funds or assets to us to enable us to effectuate, indemnification. We may purchase insurance against liabilities asserted against and expenses incurred by persons for our activities, regardless of whether we would have the power to indemnify the person against liabilities under the partnership agreement.

**Registration Rights**

Under our partnership agreement, we have agreed to register for resale under the Securities Act and applicable state securities laws any common units or other partnership securities proposed to be sold by our general partner or any of its affiliates if an exemption from the registration requirements is not otherwise available. These registration rights continue for two years following any withdrawal or removal of HEP Logistics Holdings, L.P. as our general partner. We are obligated to pay all expenses incidental to the registration, excluding underwriting discounts and commissions.

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## CONFLICTS OF INTEREST AND FIDUCIARY DUTIES

### Conflicts of Interest

Conflicts of interest exist and may arise in the future as a result of the relationships between our general partner and its affiliates, including HollyFrontier, on the one hand, and us and our limited partners, on the other hand. The directors and officers of the general partner of our general partner, Holly Logistic Services, L.L.C., have fiduciary duties to manage the general partner in a manner beneficial to its owners, which are affiliates of HollyFrontier. At the same time, our general partner has a fiduciary duty to manage us in a manner beneficial to us and our unitholders.

Our partnership agreement contains provisions that modify and limit our general partner s fiduciary duties to the unitholders. Our partnership agreement also restricts the remedies available to unitholders for actions taken that, without those limitations, might constitute breaches of fiduciary duty.

Our general partner will not be in breach of its obligations under the partnership agreement or its duties to us or our unitholders if the resolution of the conflict is:

- approved by a majority of the conflicts committee, although our general partner is not obligated to seek such approval;
- approved by the vote of a majority of the outstanding common units, excluding any common units owned by our general partner or any of its affiliates;
- on terms no less favorable to us than those generally being provided to or available from unrelated third parties; or
- fair and reasonable to us, taking into account the totality of the relationships between the parties involved, including other transactions that may be particularly favorable or advantageous to us.

Our general partner may, but is not required to, seek the approval of such resolution from the conflicts committee of the board of directors of Holly Logistic Services, L.L.C., the general partner of our general partner. If our general partner does not seek approval from the conflicts committee and the board of directors of Holly Logistic Services, L.L.C. determines that the resolution or course of action taken with respect to the conflict of interest satisfies either of the standards set forth in the third and fourth bullet points above, then the resolution or course of action taken by the general partner will be permitted and deemed approved by the unitholders and will not constitute a breach of its obligations under the partnership agreement or its duties to us or the unitholders. Unless the resolution of a conflict is specifically provided for in our partnership agreement, our general partner or the conflicts committee may consider any factors it determines in good faith to consider when resolving a conflict. When our partnership agreement requires someone to act in good faith, it requires that person to reasonably believe that he is acting in the best interests of the partnership, unless the context otherwise requires.

Conflicts of interest could arise in the situations described below, among others.

***Actions taken by our general partner may affect the amount of cash available for distribution to unitholders.***

The amount of cash that is available for distribution to unitholders is affected by decisions of our general partner regarding such matters as:

- amount and timing of asset purchases and sales;
- cash expenditures;
- borrowings;
- issuance of additional units; and
- the creation, reduction, or increase of reserves in any quarter.

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For example, in the event we have not generated sufficient cash from our operations to pay the minimum quarterly distribution on our common units, our partnership agreement permits us to borrow funds, which would enable us to make this distribution on all outstanding units.

Our partnership agreement provides that we and our subsidiaries may borrow funds from our general partner and its affiliates.

***We do not have any officers or employees and rely solely on officers and employees of Holly Logistic Services, L.L.C. and its affiliates.***

Affiliates of Holly Logistic Services, L.L.C. conduct businesses and activities of their own in which we have no economic interest. If these separate activities are significantly greater than our activities, there could be material competition for the time and effort of the officers and employees who provide services to Holly Logistic Services, L.L.C. Several of the officers of Holly Logistic Services, L.L.C. do not work full time on our affairs. These officers are required to devote time to the affairs of HollyFrontier or its affiliates and are compensated by them for the services rendered to them.

***We will reimburse the general partner and its affiliates for expenses.***

We will reimburse the general partner and its affiliates for costs incurred in managing and operating us, including costs incurred in rendering corporate staff and support services to us. Our partnership agreement provides that the general partner will determine the expenses that are allocable to us.

***Our general partner intends to limit its liability regarding our obligations.***

Our general partner intends to limit its liability under contractual arrangements so that the other party has recourse only to our assets and not against the general partner or its assets or any affiliate of the general partner or its assets. Our partnership agreement provides that any action taken by our general partner to limit its or our liability is not a breach of the general partner s fiduciary duties, even if we could have obtained terms that are more favorable without the limitation on liability.

***Unitholders will have no right to enforce obligations of our general partner and its affiliates under agreements with us.***

Any agreements between us, on the one hand, and our general partner and its affiliates, on the other, will not grant to the unitholders, separate and apart from us, the right to enforce the obligations of our general partner and its affiliates in our favor.

***Contracts between us, on the one hand, and our general partner and its affiliates, on the other, may not be the result of arm s-length negotiations.***

Our partnership agreement allows our general partner to determine any amounts to pay itself or its affiliates for any services rendered to us. Our general partner may also enter into additional contractual arrangements with any of its affiliates on our behalf. Neither our partnership agreement nor any of the other agreements, contracts, and arrangements between us and the general partner and its affiliates are or will be the result of arm s-length negotiations. However, any of these transactions are to be on terms that are fair and reasonable to us.

Our general partner and its affiliates will have no obligation to permit us to use any facilities or assets of the general partner and its affiliates, except as may be provided in contracts entered into specifically dealing with that use. There is no obligation of our general partner and its affiliates to enter into any contracts of this kind.

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***Our units are subject to our general partner s limited call right.***

Our general partner may exercise its right to call and purchase our units as provided in the partnership agreement or assign this right to one of its affiliates or to us. Our general partner may use its own discretion, free of fiduciary duty restrictions, in determining whether to exercise this right. As a result, a common unitholder may have his common units purchased from him at an undesirable time or price.

***We may not choose to retain separate counsel for ourselves or for unitholders.***

The attorneys, independent accountants, and others who perform services for us have been retained by our general partner. Attorneys, independent accountants, and others who perform services for us are selected by our general partner or the conflicts committee and may perform services for our general partner and its affiliates. We may retain separate counsel for ourselves or the unitholders in the event of a conflict of interest between our general partner and its affiliates, on the one hand, and us or the unitholders, on the other, depending on the nature of the conflict. We do not intend to do so in most cases.

***Our general partner s affiliates may compete with us.***

Our partnership agreement provides that our general partner will be restricted from engaging in any business activities other than those incidental to its ownership of interests in us and certain services the employees of our general partner are currently providing to HollyFrontier and its affiliates. Except as provided in our partnership agreement and the omnibus agreement among us, HollyFrontier and our general partner, affiliates of our general partner are not prohibited from engaging in other businesses or activities, including those that might be in direct competition with us.

**Fiduciary Duties**

Our general partner is accountable to us and our unitholders as a fiduciary. Fiduciary duties owed to unitholders by our general partner are prescribed by law and the partnership agreement. The Delaware Revised Uniform Limited Partnership Act, which we refer to in this prospectus as the Delaware Act, provides that Delaware limited partnerships may, in their partnership agreements, restrict or eliminate the fiduciary duties owed by a general partner to limited partners and the partnership.

Our partnership agreement contains various provisions replacing the fiduciary duties that might otherwise be owed by our general partner. These modifications are detrimental to the unitholders because they restrict the remedies available to unitholders for actions that, without those limitations, might constitute breaches of fiduciary duty, as described below. The following is a summary of the material restrictions of the fiduciary duties owed by our general partner to the limited partners:

| | |
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| State law fiduciary duty standards | Fiduciary duties are generally considered to include an obligation to act in good faith and with due care and loyalty. The duty of care, in the absence of a provision in a partnership agreement providing otherwise, would generally require a general partner to act for the partnership in the same manner as a prudent person would act on his own behalf. The duty of loyalty, in the absence of a provision in a partnership agreement providing otherwise, would generally require that any action taken or transaction engaged in where a conflict of interest is present be entirely |

fair to the partnership.

The Delaware Act generally provides that a limited partner may institute legal action on behalf of the partnership to recover damages from a third party where a general partner has refused to institute the action or where an effort to cause a general partner to do so is not

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| | likely to succeed. In addition, the statutory or case law of some jurisdictions may permit a limited partner to institute legal action on behalf of himself and all other similarly situated limited partners to recover damages from a general partner for violations of its fiduciary duties to the limited partners. |
| Partnership agreement modified standards | Our partnership agreement contains provisions that waive or consent to conduct by our general partner and its affiliates that might otherwise raise issues as to compliance with fiduciary duties or applicable law. For example, our partnership agreement provides that when our general partner is acting in its capacity as our general partner, as opposed to in its individual capacity, it must act in good faith and will not be subject to any other standard under applicable law. In addition, when our general partner is acting in its individual capacity, as opposed to in its capacity as our general partner, it may act without any fiduciary obligation to us or the unitholders whatsoever. These standards reduce the obligations to which the general partner would otherwise be held.<br><br>Our partnership agreement generally provides that affiliated transactions and resolutions of conflicts of interest not involving a vote of unitholders and that are not approved by the conflicts committee of the board of directors of our general partner s general partner must be:<br><br>on terms no less favorable to us than those generally being provided to or available from unrelated third parties; or<br><br>fair and reasonable to us, taking into account the totality of the relationships between the parties involved (including other transactions that may be particularly favorable or advantageous to us).<br><br>If our general partner does not seek approval from the conflicts committee and the board of directors of our general partner s general partner determines that the resolution or course of action taken with respect to the conflict of interest satisfies either of the standards set forth in the bullet points above, then the resolution or course of action taken by the general partner will be permitted and deemed approved by the unitholders and will not constitute a breach of its obligations under the partnership agreement or its duties to us or the unitholders. These standards reduce the obligations to which our general partner would otherwise be held. |

In addition to the other more specific provisions limiting the obligations of our general partner, our partnership agreement further provides that our general partner, its general partner and its officers and directors will not be liable for monetary damages to us, our limited partners, or assignees for any acts or omissions unless there has been a final and non-appealable judgment by a court of competent jurisdiction determining that the general partner or its officers and directors acted in bad faith or engaged in fraud, willful misconduct or gross negligence.

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In order to become one of our limited partners, a common unitholder is required to agree to be bound by the provisions in the partnership agreement, including the provisions discussed above. This is in accordance with the policy of the Delaware Act favoring the principle of freedom of contract and the enforceability of partnership agreements. The failure of a limited partner or assignee to sign a partnership agreement does not render the partnership agreement unenforceable against that person.

We must indemnify our general partner and the general partner of our general partner, Holly Logistic Services, L.L.C., and their officers, directors, and managers, to the fullest extent permitted by law, against liabilities, costs and expenses incurred by the general partner, Holly Logistic Services, L.L.C. or these other persons. We must provide this indemnification unless there has been a final and non-appealable judgment by a court of competent jurisdiction determining that these persons acted in bad faith or engaged in fraud, willful misconduct or gross negligence. We also must provide this indemnification for criminal proceedings unless our general partner, Holly Logistic Services, L.L.C. or these other persons acted with knowledge that their conduct was unlawful. Thus, our general partner and Holly Logistic Services, L.L.C. could be indemnified for their negligent acts if they met requirements set forth above. To the extent that these provisions purport to include indemnification for liabilities arising under the Securities Act, in the opinion of the Securities and Exchange Commission, such indemnification is contrary to public policy and therefore unenforceable.

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## MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES

This section summarizes the material U.S. federal income tax consequences that may be relevant to prospective unitholders and is based upon current provisions of the U.S. Internal Revenue Code of 1986, as amended (the Code ), existing and proposed U.S. Treasury regulations thereunder (the Treasury Regulations ), and current administrative rulings and court decisions, all of which are subject to change. Changes in these authorities may cause the U.S. federal income tax consequences to a prospective unitholder to vary substantially from those described below, possibly on a retroactive basis. Unless the context otherwise requires, references in this section to we us or the Partnership are references to Holly Energy Partners, L.P. and our operating partnership. This section should be read in conjunction with the risk factors included under the caption Tax Risks to Common Unitholders beginning on page 33 of our Annual Report on Form 10-K for the year ended December 31, 2017.

Legal conclusions contained in this section, unless otherwise noted, are the opinion of Vinson & Elkins L.L.P. and are based on the accuracy of representations made by us to them for this purpose. However, this section does not address all federal income tax matters that may affect us or our unitholders, such as the application of the alternative minimum tax. This section also does not address local taxes, state taxes, non-U.S. taxes, or other taxes that may be applicable, except to the limited extent that such tax considerations are addressed below under State, Local and Other Tax Considerations. Furthermore, this section focuses on unitholders who are individual citizens or residents of the United States (for federal income tax purposes), who have the U.S. dollar as their functional currency, who use the calendar year as their taxable year, who purchase units in this offering, who do not materially participate in the conduct of our business activities and who hold such units as capital assets (typically, property that is held for investment). This section has limited applicability to corporations (including other entities treated as corporations for federal income tax purposes), partnerships (including other entities treated as partnerships for federal income tax purposes), estates, trusts, non-resident aliens or other unitholders subject to specialized tax treatment, such as tax-exempt entities, non-U.S. persons, individual retirement accounts ( IRAs ), employee benefit plans, real estate investment trusts or mutual funds. ***Accordingly, we encourage each prospective unitholder to consult such unitholder s own tax advisor in analyzing the federal, state, local and non-U.S. tax consequences that are particular to that unitholder resulting from ownership or disposition of its units and potential changes in applicable tax laws.***

We are relying on the opinions and advice of Vinson & Elkins L.L.P. with respect to the matters described herein. An opinion of counsel represents only that counsel s best legal judgment and does not bind the IRS or a court. Accordingly, the opinions and statements made herein may not be sustained by a court if contested by the IRS. Any such contest of the matters described herein may materially and adversely impact the market for our common units and the prices at which such common units trade. In addition, our costs of any contest with the IRS will be borne indirectly by the general partner and our unitholders because the costs will reduce our cash available for distribution. Furthermore, the tax consequences of an investment in us may be significantly modified by future legislative or administrative changes or court decisions, which may be retroactively applied.

For the reasons described below, Vinson & Elkins L.L.P. has not rendered an opinion with respect to the following federal income tax issues:

- the treatment of a unitholder whose common units are the subject of a securities loan (e.g., a loan to a short seller to cover a short sale of common units) (please read Tax Consequences of Common Unit Ownership Treatment of Securities Loans );

whether our monthly convention for allocating taxable income and losses is permitted by existing Treasury Regulations (please read Disposition of Common Units Allocations Between Transferors and Transferees ); and

whether our method for taking into account Section 743 adjustments is sustainable in certain cases (please read Tax Consequences of Common Unit Ownership Section 754 Election and Uniformity of Common Units ).

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whether our use of simplifying conventions for making adjustments to book basis and relevant allocations is permitted by existing Treasury Regulations (please read Tax Consequences of Common Unit Ownership Allocation of Income, Gain, Loss and Deduction and Uniformity of Common Units ).

**Taxation of the Partnership**

***Partnership Status***

We are treated as a partnership for U.S. federal income tax purposes and, therefore, subject to the discussion below under Administrative Matters Information Returns and Audit Procedures, generally will not be liable for entity-level federal income taxes. Instead, as described below, each of our unitholders will take into account its respective share of our items of income, gain, loss and deduction in computing its federal income tax liability as if the unitholder had earned such income directly, even if we make no cash distributions to the unitholder. Distributions we make to a unitholder will not give rise to income or gain taxable to such unitholder, unless the amount of cash distributed exceeds the unitholder s adjusted tax basis in its units. Please read Tax Consequences of Common Unit Ownership Treatment of Distributions and Disposition of Common Units.

Section 7704 of the Code generally provides that publicly traded partnerships will be treated as corporations for federal income tax purposes. However, if 90% or more of a partnership s gross income for every taxable year it is publicly traded consists of qualifying income, the partnership may continue to be treated as a partnership for federal income tax purposes (the Qualifying Income Exception ). Qualifying income includes income and gains derived from the gathering, transportation, storage, refining, processing and marketing of certain natural resources, including oil, natural gas and products thereof. Other types of qualifying income include interest (other than from a financial business), dividends, gains from the sale of real property and gains from the sale or other disposition of capital assets (or property described in Section 1231(b) of the Code) held for the production of qualifying income. We estimate that less than 5% of our current gross income is not qualifying income; however, this estimate could change from time to time.

No ruling has been or will be sought from the IRS with respect to our classification as a partnership for federal income tax purposes or as to the classification of our partnership and limited liability company operating subsidiaries. Instead, we have relied on the opinion of Vinson & Elkins L.L.P. that, based upon the Code, existing Treasury Regulations, published revenue rulings and court decisions and representations described below, the Partnership and our partnership and limited liability company operating subsidiaries, other than those that have been identified as corporations to Vinson & Elkins L.L.P., will be classified as partnerships or disregarded as entities separate from us for federal income tax purposes.

In rendering its opinion, Vinson & Elkins L.L.P. has relied on factual representations made by us and our general partner, including, without limitation:

(a) Neither we nor any of our partnership or limited liability company operating subsidiaries, other than those that have been identified as corporations to Vinson & Elkins L.L.P., has elected or will elect to be treated as a corporation for federal income tax purposes; and

(b) For each taxable year since and including the year of our initial public offering, more than 90% of our gross income has been and will be income of a character that Vinson & Elkins L.L.P. has opined is qualifying income within the meaning of Section 7704(d) of the Code.

We believe that these representations are true and will be true in the future.

If we fail to meet the Qualifying Income Exception, other than a failure that is determined by the IRS to be inadvertent and that is cured within a reasonable time after discovery (in which case the IRS may also require us

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to make adjustments with respect to our unitholders or pay other amounts), we will be treated as transferring all of our assets, subject to all of our liabilities, to a newly formed corporation on the first day of the year in which we fail to meet the Qualifying Income Exception, in return for stock in that corporation and then as distributing that stock to our unitholders in liquidation of their interests in us. This deemed contribution and liquidation should not result in the recognition of taxable income by our unitholders or us so long as the aggregate amount of our liabilities does not exceed the adjusted tax basis of our assets. Thereafter, we would be treated as an association taxable as a corporation for federal income tax purposes.

The present U.S. federal income tax treatment of publicly traded partnerships, including us, or an investment in our units, may be modified by administrative or legislative action or judicial interpretation at any time. From time to time, members of the U.S. Congress have proposed and considered substantive changes to the existing federal income tax laws that would affect publicly traded partnerships. One such legislative proposal would have eliminated the Qualifying Income Exception upon which we rely for our treatment as a partnership for federal income tax purposes.

In addition, on January 24, 2017, final regulations regarding which activities give rise to qualifying income (the Final Regulations ) within the meaning of Section 7704 of the Code were published in the Federal Register. The Final Regulations are effective as of January 19, 2017, and apply to taxable years beginning on or after January 19, 2017. We do not believe the Final Regulations affect our ability to qualify as a publicly traded partnership. It is possible that a change in law could affect us and may be applied retroactively. Any such changes could negatively impact the value of an investment in our units. If for any reason we are taxable as a corporation in any taxable year, our items of income, gain, loss and deduction would be taken into account by us in determining the amount of our liability for federal income tax, rather than being passed through to our unitholders.

At the state level, several states have been evaluating ways to subject partnerships to entity-level taxation through the imposition of state income, franchise, or other forms of taxation. Imposition of a similar tax on us in the jurisdictions in which we operate or in other jurisdictions to which we may expand could substantially reduce our cash available for distribution to our unitholders.

Our taxation as a corporation would materially reduce the cash available for distribution to unitholders and thus would likely substantially reduce the value of our units. Any distribution made to a unitholder at a time when we are treated as a corporation would be (i) a taxable dividend to the extent of our current or accumulated earnings and profits, then (ii) a nontaxable return of capital to the extent of the unitholder s adjusted tax basis in its units (determined separately for each unit), and thereafter (iii) taxable capital gain.

The remainder of this discussion is based on the opinion of Vinson & Elkins L.L.P. that we will be treated as a partnership for federal income tax purposes.

**Tax Consequences of Common Unit Ownership**

***Limited Partner Status***

Unitholders who are admitted as limited partners of Holly Energy Partners, as well as unitholders whose common units are held in street name or by a nominee and who have the right to direct the nominee in the exercise of all substantive rights attendant to the ownership of their common units, will be treated as partners of Holly Energy Partners for federal income tax purposes. For a discussion related to the risks of losing partner status as a result of securities loans, please read Treatment of Securities Loans. Unitholders who are not treated as partners in us as described above are urged to consult their own tax advisors with respect to the tax consequences applicable to them under their particular circumstances.

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***Flow-Through of Taxable Income***

Subject to the discussion below under Entity-Level Collections of Unitholder Taxes and Administrative Matters Information Returns and Audit Procedures, and assuming our general partner does not make an election for us to be taxed as a corporation as a result of a change in tax law, with respect to payments we may be required to make on behalf of our unitholders, we will not pay any federal income tax. Rather, each unitholder will be required to report on its federal income tax return each year its share of our income, gains, losses and deductions for our taxable year or years ending with or within its taxable year. Consequently, we may allocate income to a unitholder even if that unitholder has not received a cash distribution.

***Basis of Common Units***

A unitholder s tax basis in its common units initially will be the amount paid or treated as paid for those common units increased by the unitholder s initial allocable share of our liabilities. That basis generally will be (i) increased by the unitholder s share of our income and any increases in such unitholder s share of our liabilities, and (ii) decreased, but not below zero, by the amount of all distributions to the unitholder, the unitholder s share of our losses, any decreases in its share of our liabilities, and the amount of any excess business interest allocated to the unitholder. The IRS has ruled that a partner who acquires interests in a partnership in separate transactions must combine those interests and maintain a single adjusted tax basis for all of those interests.

***Treatment of Distributions***

Distributions made by us to a unitholder generally will not be taxable to the unitholder, unless such distributions are of cash or marketable securities that are treated as cash and exceed the unitholder s tax basis in its common units, in which case the unitholder generally will recognize gain taxable in the manner described below under Disposition of Common Units.

Any reduction in a unitholder s share of our nonrecourse liabilities (liabilities for which no partner bears the economic risk of loss) will be treated as a distribution by us of cash to that unitholder. A decrease in a unitholder s percentage interest in us because of our issuance of additional common units may decrease such unitholder s share of our nonrecourse liabilities. For purposes of the foregoing, a unitholder s share of our nonrecourse liabilities generally will be based upon such unitholder s share of the unrealized appreciation (or depreciation) in our assets, to the extent thereof, with any excess nonrecourse liabilities allocated based on the unitholder s share of our profits. Please read Disposition of Common Units.

A non-pro rata distribution of money or property (including a deemed distribution as a result of the reallocation of our nonrecourse liabilities described above) may cause a unitholder to recognize ordinary income, if the distribution reduces the unitholder s share of our unrealized receivables, including depreciation recapture and substantially appreciated inventory items, both as defined in Section 751 of the Code ( Section 751 Assets ). To the extent of such reduction, the unitholder would be deemed to receive its proportionate share of the Section 751 Assets and exchange such assets with us in return for a portion of the non-pro rata distribution. This deemed exchange will generally result in the unitholder s recognition of ordinary income in an amount equal to the excess of (1) the non-pro rata portion of that distribution over (2) the unitholder s tax basis (typically zero) in the Section 751 Assets deemed to be relinquished in the exchange.

***Limitations on Deductibility of Losses***

A unitholder may not be entitled to deduct the full amount of loss we allocate to it because its share of our losses will be limited to the lesser of (i) the unitholder s adjusted tax basis in its common units, and (ii) in the case of a unitholder that is an individual, estate, trust or certain types of closely-held corporations, the amount for

which the unitholder is considered to be at risk with respect to our activities. A unitholder will be at risk to the extent of its adjusted tax basis in its common units, reduced by (1) any portion of that basis attributable to the unitholder s share of our nonrecourse liabilities, (2) any portion of that basis representing amounts otherwise protected against loss because of a guarantee, stop loss agreement or similar arrangement and (3) any amount of money the unitholder borrows to acquire or hold its common units, if the lender of those borrowed funds owns an interest in us, is related to another unitholder or can look only to the common units for repayment.

A unitholder subject to the at risk limitation must recapture losses deducted in previous years to the extent that distributions (including distributions deemed to result from a reduction in a unitholder s share of nonrecourse liabilities) cause the unitholder s at risk amount to be less than zero at the end of any taxable year. Losses disallowed to a unitholder or recaptured as a result of the basis or at risk limitations will carry forward and will be allowable as a deduction in a later year to the extent that the unitholder s adjusted tax basis or at risk amount, whichever is the limiting factor, is subsequently increased. Upon a taxable disposition of common units, any gain recognized by a unitholder can be offset by losses that were previously suspended by the at risk limitation but not losses suspended by the basis limitation. Any loss previously suspended by the at risk limitation in excess of that gain can no longer be used, and will not be available to offset a unitholder s salary or active business income.

In addition to the basis and at risk limitations, passive activity loss limitations limit the deductibility of losses incurred by individuals, estates, trusts, some closely-held corporations and personal service corporations from passive activities (generally, trade or business activities in which the taxpayer does not materially participate). The passive loss limitations are applied separately with respect to each publicly traded partnership. Consequently, any passive losses we generate will be available to offset only passive income generated by us. Passive losses that exceed a unitholder s share of the passive income we generate may be deducted in full when a unitholder disposes of all of its common units in a fully taxable transaction with an unrelated party. The passive activity loss rules are applied after other applicable limitations on deductions, including the at risk and basis limitations.

For taxpayers other than corporations in taxable years beginning after December 31, 2017, and before January 1, 2026, an excess business loss limitation further limits the deductibility of losses by such taxpayers. An excess business loss is the excess (if any) of a taxpayer s aggregate deductions for the taxable year that are attributable to the trades or businesses of such taxpayer (determined without regard to the excess business loss limitation) over the aggregate gross income or gain of such taxpayer for the taxable year that is attributable to such trades or businesses plus a threshold amount. The threshold amount is equal to $250,000 or $500,000 for taxpayers filing a joint return. Disallowed excess business losses are treated as a net operating loss carryover to the following tax year. Any losses we generate that are allocated to a unitholder and not otherwise limited by the basis, at risk, or passive loss limitations will be included in the determination of such unitholder s aggregate trade or business deductions. Consequently, any losses we generate that are not otherwise limited will only be available to offset a unitholder s other trade or business income plus an amount of non-trade or business income equal to the applicable threshold amount. Thus, except to the extent of the threshold amount, our losses that are not otherwise limited may not offset a unitholder s non-trade or business income (such as salaries, fees, interest, dividends and capital gains). This excess business loss limitation will be applied after the passive activity loss limitation.

***Limitations on Interest Deductions***

In general, we are entitled to a deduction for interest paid or accrued on indebtedness properly allocable to our trade or business during our taxable year. However, our deduction for this business interest is limited to the sum of our business interest income and 30% of our adjusted taxable income. For the purposes of this limitation, our adjusted taxable income is computed without regard to any business interest or business interest income, and in the case of taxable years beginning before January 1, 2022, any deduction allowable for depreciation, amortization, or depletion.

This limitation is first applied at the partnership level and any deduction

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for business interest is taken into account in determining our non-separately stated taxable income or loss. Then, in applying this business interest limitation at the partner level, the adjusted taxable income of each of our unitholders is determined without regard to such unitholder s distributive share of any of our items of income, gain, deduction, or loss and is increased by such unitholder s distributive share of our excess taxable income, which is generally equal to the excess of 30% of our adjusted taxable income over the amount of our deduction for business interest for a taxable year.

To the extent our deduction for business interest is not limited, we will allocate the full amount of our deduction for business interest among our unitholders in accordance with their percentage interests in us. To the extent our deduction for business interest is limited, the amount of any disallowed deduction for business interest will also be allocated to each unitholder in accordance with their percentage interest in us, but such amount of excess business interest will not be currently deductible. Subject to certain limitations and adjustments to a unitholder s basis in its common units, this excess business interest may be carried forward and deducted by a unitholder in a future taxable year. Further, a unitholder s basis in its common units will generally be increased by the amount of any excess business interest upon a disposition of such common units.

In addition to this limitation on the deductibility of a partnership s business interest, the deductibility of a non-corporate taxpayer s investment interest expense is generally limited to the amount of that taxpayer s net investment income. Investment interest expense includes:

- interest on indebtedness allocable to property held for investment;
- interest expense allocated against portfolio income; and

| | | |
|---|---|---|
| Nanning | 1 | 751 |
| Wuxi | 1 | 382 |
| Suzhou | 1 | 518 |
| Ningbo | 1 | 601 |
| Shijiazhuang | 1 | 544 |
| Fuzhou | 1 | 446 |
| Xi an | 2 | 822 |
| Zhuhai | 1 | 405 |
| Daqing | 1 | 290 |
| Yan Tai | 1 | 392 |
| Xiamen | 2 | 533 |
| Dongguan | 1 | 310 |
| Taiyuan | 1 | 415 |
| Haikou* | 1 | 0 |
| Guiyang* | 1 | 0 |

| | | |
|---|---|---|
| Weifang | 1 | 44 |

Notes:

currently offered
- not currently offered
* established in December 2014

***Online learning modules***

Our live distance instruction and classroom-based tutoring are supplemented by our proprietary online learning modules featured on our TTS platform. TTS has the following five core functions:

*Course content*. TTS contains lecture slides, key lecture video recordings, case studies, practice exercises and supplemental reading materials. In addition to recordings of past lectures, TTS also features exclusive online videos on key course materials. Students may view lecture videos using the computers at our learning centers. To foster effective learning of our course lecture materials, especially theoretical knowledge points, TTS features software development case studies and practice exercises. TTS contains supplemental reading materials on areas in which we have historically received frequent questions from students. TTS also allows students to download coding materials and study notes that they have prepared for reference in their future jobs.

*Self-assessment exams*. TTS features daily and weekly interactive mock examinations to measure learning outcomes. Students use the mock exams to assess their learning results and gauge their grasp of course content. After students complete a self-assessment exam, TTS automatically provides students with detailed explanations on each of the exam questions.

*Student and teaching staff interaction*. TTS allows students to interact with instructors and teaching assistants. In class, students may raise questions for instructors and teaching assistants using the messaging tools on TTS. After class, students can post questions to the teaching assistants through the online question and answer board in TTS. Teaching assistants are able to provide timely and accurate responses typically within 30 minutes after a question is submitted. To ensure the accuracy of responses and to identify questions of common interest, our instructors also actively review questions posted on TTS and regularly provide answers. Students are given the opportunity to provide feedback for each answer or tutorial service provided by teaching assistants using the evaluation functions on TTS.

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*Student management tools*. TTS allows instructors to receive daily ratings and feedback from students. Instructors may then adjust their lecture pace and coverage of course materials each day. TTS enables teaching assistants to evaluate each student s academic performance. The teaching assistant interface of TTS contains each student s monthly performance test scores, as well as each student s ranking within the class and nationally. Teaching assistants are required to follow-up with underperforming students regarding their academic status and to adopt concrete action plans with such students to improve their future performance. TTS also allows teaching assistants to monitor each student s attendance and to log their daily tutoring activities.

*Online student community*. TTS serves as an online student community that fosters academic collaboration among students. We encourage students to post course-related articles and comments sharing their study experiences on the bulletin board forum.

In addition to our TTS platform, we launched TMOOC.CN in March 2015 to cover a broader customer base. TMOOC.CN offers two types of online learning products: continuing education courses and job placement training courses. Continuing education courses, composed of a library of video clips that focus on on-the-job practical skills, target working professionals and others with continuing education needs. Job placement training courses are full length programs that target job seekers. These recruitment-oriented courses are carefully chosen from existing courses at our learning centers and redesigned to be more suitable for online learning environment. Students who finish all modules in a placement training course and pass the relevant Tarena certification examination will receive the same job placement services that we offer to other students at learning centers.

**Our Course Offerings**

Our courses provide students with practical education to prepare them for jobs in industries with significant growth potential and strong hiring demand. We currently offer courses in nine IT subjects and three non-IT subjects.

We generally offer the following two types of classes in order to accommodate the different scheduling and training needs of our students:

*Full-time class*. The term for a full-time class is typically four months and includes approximately 1,000 learning hours. Full-time classes meet from Monday to Saturday. In 2014, approximately 82% of our enrolled students attended our full-time classes.

*Part-time class*. Part-time classes typically have terms of four to five months. We allow students to attend part-time classes either exclusively during weekends or on a combination of weekday nights and weekends, as these students typically have full-time jobs. In 2014, approximately 18% of our enrolled students attended our part-time classes.

We have adopted stringent quality control procedures to ensure that we produce high quality graduates. We use entrance exams to assess the level of our students. Prospective full-time students with low entrance exam scores are recommended to enroll in preparatory training camps. We have a total of four monthly closed-book performance tests to evaluate the learning status of our students. For underperforming students who have failed the first monthly performance test, we offer them the opportunity to re-take the first month classes at no extra cost. We believe physical class attendance is important, and students with attendance rates below 90% are generally not given graduation certificates at the end of our program.

Our full-time classes also include short term, project-based training programs designed for college students to gain practical IT experience, which are not material for our business as a whole.

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***IT education courses***

We offer education courses covering the following nine IT subjects:

| Subject | Year of Launch | Student Enrollment in 2014 | Forces of Course Content |
|---|---|---|---|
| Java | 2002 | 21,610 | Programming for Windows and Linux-based desktop software and web-based software |
| C++ | 2009 | 3,181 | Programming for Windows and Linux-based desktop software |
| Software testing | 2009 | 2,481 | Practical software testing and quality assurance training |
| PHP | 2010 | 2,131 | Web-based software development for e-commerce industries |
| Embedded | 2009 | 2,114 | Development of software to control machines and devices |
| Android | 2011 | 2,534 | Programming for Android-based applications |
| .NET | 2007 | 528 | Development of software based on the .NET framework that runs primarily on Windows |
| iOS | 2012 | 1,874 | Programming for iOS-based applications |
| Linux and network engineering | 2013 | 889 | Linux operating system and network management technology |

Graduates of our IT education courses receive *Tarena Certified Software Developer* certificates, or TCSD certificates. Holders of TCSD certificates are qualified to obtain the intermediate-advanced software engineer certificate issued by the Ministry of Industry and Information Technology of China, or the MIIT, for their respective field of study, subject to such graduates passing our internal examination. Graduates of our Java courses are granted *ORACLE Certified Java Programmer certificates by* ORACLE Corporation after passing the relevant exams. Graduates of our Linux and Network engineering courses are awarded the international network engineer certificate issued by CompTIA upon passing the relevant exams, and our Linux and network engineering course graduates may also sign up for Red Hat certification exams at our learning centers. Graduates of our embedded course are awarded the *Embedded Engineer Certificate* issued by ARM upon passing the relevant exams.

***Non-IT education courses***

We began offering courses in non-IT subjects in 2013. We launched our digital art course in February 2013, our online sales and marketing course in November 2013 and our accounting course in October 2014. The following table describes the three non-IT courses that we currently offer:

| Subject | Year of Launch | Student Enrollment in 2014 | Focus of Course Content |
|---|---|---|---|
| Digital art | 2013 | 18,895 | Latest Adobe user interface design technology for graphic, webpage and mobile sites design |
| Online sales and marketing | 2013 | 3,404 | Search engine marketing, search engine optimization, and other Internet based marketing, including microblog marketing |
| Accounting | 2014 | 247 | Accounting certificate, and chief accountant practice |

Graduates of our online sales and marketing courses are awarded the *SEM Certificate* issued by Baidu without additional examination.

Since its launch in February 2013, our digital art course has registered strong growth in student enrollments and has become the second largest course in terms of net revenue contribution in 2014. Our accounting course is mainly designed for prospective students of age groups similar to our existing students, and such course helps us target a broader student base and further increase our overall enrollments.

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**Our Teaching Staff**

***Our instructors***

As of December 31, 2014, we employed 117 full-time instructors based in Beijing. Most of our instructors for IT education courses have industry backgrounds in global and domestic technology companies. Instructors for non-IT education courses are typically experts or veterans in their respective specialized fields. Our instructors also provide us with unique access to a large pool of experts on industry trends that is especially valuable in our decision-making and development process for new courses. We believe we attract highly qualified instructors by virtue of our respected brand, our well-established teaching infrastructure and sales team and our competitive compensation.

We believe that developing and maintaining highly capable and motivated instructors is critical to our success. We seek qualified instructor candidates who have extensive industry experience or come from other professional education service providers. These candidates are subject to multiple rounds of interviews conducted by our director of teaching, vice-president for teaching and the chief executive officer. All instructors are required to undergo training in teaching skills and techniques. We require our instructors to regularly update their course materials to remain current with evolving employer needs, industry developments and other key trends necessary to teach effectively. We typically have a back up instructor assigned to each course to meet any emergency needs.

To align incentives, instructors receive bonuses based on students ratings and the number of class sessions taught, in addition to their base compensation.

***Our teaching assistants***

We believe that our dedicated teaching assistants are essential to the success of our education model. Our teaching assistants interact with and tutor our students on a daily basis, and are instrumental in facilitating a disciplined and focused learning environment. Each classroom is staffed with one or two teaching assistants, who attends lectures together with students. Teaching assistants are available during class hours to answer student questions in person, and after class hours to address inquiries online via TTS. Teaching assistants are also responsible for offering focused tutoring services to underperforming students and continuously monitoring their academic results. We have adopted a comprehensive set of key performance indicators, or KPIs, to evaluate the performance of our teaching assistants. Such KPIs include student satisfaction, exam scores of students on monthly performance tests, the improvement of underperforming students and employment results after graduation, among other indicators.

We primarily seek teaching assistant candidates from our graduates who have demonstrated strong command of materials in the relevant subject areas. We provide necessary training to newly hired teaching assistants to tutor effectively. Our teaching assistants are frequently evaluated by students on the quality of their assistance. We had a total of 866 teaching assistants as of December 31, 2014.

**Course Content Development**

In addition to teaching, our instructors also develop the course content in their respective subject areas. We regularly update our existing programs, typically every six months, to stay abreast of the latest technology developments and industry trends. Our instructors are also responsible for producing practice exercises and exam questions for monthly performance tests to evaluate the effectiveness of our student self-assessment tests in TTS.

We regularly engage in new course development in order to capture demands created by evolving job market and industry trends. We have a set of procedures for new course development. Prior to developing a new course, we gather

market intelligence by collecting job market demand information to ensure that we are developing relevant and up-to-date courses. We conduct a series of surveys, each with clear parameters, to determine various aspects of the proposed new course. Once we gather enough market intelligence, we recruit, or identify from within Tarena, instructors with the appropriate industry and academic background to form a course-specific development task team. We generally require four or five instructors for each new course, and we historically have been able to recruit or identify such instructors within three months. We have generally been able to complete the teaching material development process for a new course in three months after we have finished instructor recruitment. All of our new courses are then pilot tested in selected learning centers in Beijing for student satisfaction, training practicality and employment outcomes. The time frame between our identification of a new course area and pilot testing is typically three to six months. We typically pilot test new courses for three to five months, and new courses that have passed our pilot tests are then introduced nationally. In 2014, we launched one new course in accounting, which began in October 2014.

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Our software research and development department is tasked with improving the technical performance and user experience of TTS. Since introducing TTS student version 1.0 in 2006, we have produced seven upgrades to TTS. The current version that our students use is TTS student version 8.0.

**Our Students**

The majority of our students are college students and graduates. In 2014, approximately 85% of our enrolled students were either studying towards, or already held, a post-secondary degree. We have experienced significant growth in student enrollment in recent years. Our student enrollment reached 59,960 in 2014.

***Student recruitment***

We rely primarily on Internet-based marketing to attract students and increase enrollments. We advertise on the Internet using search engine keywords on leading search engines. We also use banners and other advertising placements on targeted sites, such as education portals, career sites and industry-specific websites. We actively monitor the effectiveness of our advertising and adjust marketing spending accordingly.

As part of our online marketing efforts, we operate a promotional website *www.it211.com.cn*. Our *www.it211.com.cn* website features sample lecture videos and class materials covering the vast majority of our course subjects, as well as subjects beyond our current course offerings. We provide prospective students with prepaid study cards to purchase sample content on our *www.it211.com.cn* website.

Student recruitment generally occurs at the learning center level. Our learning centers host seminars, information sessions and preparatory training camps for prospective students, and distribute print and Internet-based advertising materials, including prepaid study cards for *www.it211.com.cn*. When a prospective student responds to our advertisements and contacts a learning center, an enrollment advisor generates a prospective student profile and advises the candidate, either online or in a face-to-face meeting, on various aspects of our courses and educational experience. As of December 31, 2014, we had a total of 981 enrollment advisors nationally.

To promote brand awareness, we place advertisements in industry trade publications and present at industry trade seminars and conventions. We also began to host our annual *Tarena-Discovery Cup Chinese University Students Software Design Competition* in April 2012.

In addition to our marketing efforts, we recruit a significant portion of our students directly from universities and colleges. As of December 31, 2014, we have cooperated with over 550 universities and colleges in China under one of the three following modes of cooperation:

*Joint-majors*. We offer joint-majors with 15 universities and colleges in China, namely Harbin Guangsha College, Harbin Cambridge University, Harbin International University, Hebei United University, Huaihai Institute of Technology, Huaiyin Institute of Technology, Jiangsu Normal University, Northeast Forestry University, Northeast Petroleum University, Qiqihar Institute of Technology, Kunming University of Science and Technology City College, Taihu University of Wuxi, Xuhai College of China University of Mining and Technology, Yangzhou University and Zhejiang Haiyang University. These universities offer students the option to major in one of the subject areas that we teach and include our selected courses in their standard undergraduate curriculum. Students in selected majors at these universities take our courses full-time for one semester and receive academic credits from these universities and colleges after

successfully completing our courses.

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*On-campus learning sites*. We have established on-campus learning sites with over 220 universities and colleges in China to offer our courses, without live broadcast, to students attending these universities and colleges. Students enrolled in our on-campus learning sites typically attend part of our course in the on-campus learning sites and part of the course at our learning centers. We pay universities and colleges for the cost of classroom facilities used in the learning sites but do not share revenue with these universities and colleges.

*Enrollment cooperation*. We have enrollment cooperation with over 340 universities and colleges in China. These universities and colleges allow us to organize marketing and promotional events on campus in order to attract students.

We had a total of 172 university cooperation representatives as of December 31, 2014. Our university cooperation representatives are responsible for establishing new and maintaining current cooperative relationships between us and universities in China. In 2014, we enrolled approximately 18% of our students from universities and colleges with which we cooperated.

***Student job placement services***

We have an effective job placement program for our students. Each learning center retains full-time career counselors who meet with students on the first day of class to discuss their career goals and to build an employment profile for each student. Our career counselors host a series of mandatory career development seminars for students throughout the term. During the final weeks of each course, our career counselors meet with students one-on-one to offer training on interview and résumé preparation. In addition to the scheduled career service activities, our career counselors are generally available to meet with students one-on-one during office hours. Our career counselors also monitor the employment results of our students and actively offer personalized assistance to students facing difficulties in securing job offers. We had a total of 231 career counselors as of December 31, 2014.

Each learning center also retains full-time employer cooperation representatives who routinely collaborate with employers, alumni, human resources websites and other employment recruiters to maximize opportunities for job placements. We had a total of 164 employer cooperation representatives as of December 31, 2014. We invite corporate employers to host recruiting events and interviews at our learning centers and offer students with interview opportunities across the country.

In January 2015, we launched a self-developed job search website called Job Show *(*www.jobshow.cn*)*, which serves as a dedicated open platform for our students and other job-seeking candidates to connect with corporate employers more effectively. Through Job Show, we source and list job opportunities from both IT and non-IT employers in China.

**Our Network of Employers**

We have a track record of producing job-ready and highly qualified candidates for many corporate employers. Since our inception, our network of potential employers for our students covered approximately 50,000 corporate employers, including Global *Fortune 500* companies, and leading technology, IT services and Internet companies in China.

We offer the following recruiting services to corporate employers:

*General recruiting services*. We offer corporate employers candidate referral services and other recruitment-related services. Once an employer communicates its hiring needs to us, we direct the relevant learning centers to produce a list of student candidates that meet the hiring criteria of such employer, and refer such candidates to the employer for interviews and assessments. We also offer space at our learning centers for employers to host recruiting events targeting our students and to conduct interviews.

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*Customized courses*. We offer customized courses targeting specific employers with large demands for trained professionals. Prospective students for our customized courses generally undergo interviews conducted by the employers before the start of classes. In addition to our standard curriculum, students enrolled in customized courses must participate in additional training provided by employers at our learning centers. Such additional training is tailored according to the particular skill requirements of the employers. Successful graduates of our customized courses who have passed the relevant qualifying exams are granted job offers by the employers.

While we currently do not generate revenue from any of our recruiting services for corporate employers, we believe such services enhance our brand recognition and are instrumental in our ability to help students achieve high job placement rates.

**Tuition Fees**

For our full-time and part-time classes, our standard tuition fees generally range from RMB16,800 (US$2,708) to RMB17,800 (US$2,869) per course. We increased our tuition fees for most of our full-time classes by approximately RMB1,000 (US$161) in 2012, further increased such tuition fees by RMB1,000 (US$161) in 2013 and again increased such tuition fees by RMB1,000 (US$161) in 2014. We also increased our tuition fees for part-time classes by RMB1,000 (US$161) to RMB3,000(US$483) per course in 2014. In March 2015, we increased tuition fees for selected courses by another RMB1,000 (US$161).

We primarily offer two payment options for our students, including one-time full payment upon enrollment and multiple payments within two months of enrollment. We also offer an option whereby qualified students can pay our tuition fees within a period of time after graduation.

To assist our students in paying our tuition fees, we offered the following three credit sources to provide financing services for our students to make one-time, up-front tuition payments in 2014:

*CreditEase*. CreditEase, a credit management and microfinancing company in China, assists our students in obtaining loans to pay for their tuition. CreditEase utilizes a person-to-person lending method to enable qualified students to borrow unsecured loans from unrelated individuals without using a bank as an intermediary. Under this person-to-person lending method, CreditEase identifies third-party individual lenders and matches their lending needs with the loan demands of our students. CreditEase began to offer this service to our students in July 2013. Approximately 73.9% of our students who obtained financing for tuition fees in 2014 obtained funding sourced by CreditEase.

*Bank of China Consumer Finance Co., Ltd*. We launched the BOC CFC student loan program in April 2014. Approximately 14.6% of our students who obtained financing for tuition fees in 2014 elected BOC CFC as the lender.

*Bank of Beijing Consumer Financing Company.* We launched the BOB CFC student loan program in September 2012. Approximately 11.5% of our students who obtained financing for tuition fees in 2014 elected BOB CFC as the lender.

Approximately 55% of our students enrolled in 2014 obtained financing from one of the three abovementioned sources. Such financing arrangements are bilateral in nature, and are carried out between our students and the

respective financing institution directly. We do not take any credit risk or liability in such arrangements.

Our cooperative agreement with BOB CFC expired in February 2015, and we are in the process of renewing such agreement with BOB CFC. In Janurary 2015, we began to cooperate with Renrendai, a third-party person-to-person lending service provider, in arranging loans for our students to pay for our tuition fees.

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We historically also cooperated with Chuanbang to provide financing services to our students. Chuanbang utilized a person-to-person lending method similar to the one used by CreditEase to assist our students in obtaining loans to pay for their tuition. Chuanbang is owned by Mr. Shaoyan Han, our chief executive officer. Chuanbang began to offer this service to our students in 2011. Chuanbang has ceased offering financing services to our students enrolled since January 1, 2014.

**Technology**

Building a reliable, scalable and secure technology infrastructure is crucial to our ability to support our live lecture broadcasts, online TTS and the various services that we provide to our students. We manage our lecture delivery system and TTS using a combination of commercially available software, hardware systems and proprietary technology. Since 2006, we have established a powerful online platform that enables thousands of students to simultaneously log onto our TTS and participate in activities online.

All of our servers and routers, including backup servers, are currently hosted at our learning centers or by third-party service providers in multiple cities in China. We regularly back up our databases. Our network administration department regularly monitors the performance of our websites and infrastructure to enable us to respond quickly to potential problems. We deliver live broadcast of audio and video of the lectures given in Beijing via the dedicated network of China Telecom or China Unicom to terminals located in selected learning centers with high student enrollment, and via public Internet infrastructure to our other learning centers.

We have recently developed our CRM software in-house to manage our student and corporate employer information, as well as to integrate our key administrative functions. We will rely on our internal IT resources to upgrade the CRM system as needed going forward.

**Seasonality**

Seasonal fluctuations have affected, and are likely to continue to affect, our business. Historically, we typically generate the highest net revenues in the third and fourth quarters because of the increased student enrollments during summer vacation. We generally generate less tuition fees in the first quarter of each year due to the Chinese New Year holiday. Our quarterly cost of revenue, selling and marketing expenses, general and administrative expenses and research and development expenses have generally been increasing in absolute amounts since 2012 as we expanded our network of learning centers, increased the number of our personnel and enhanced our marketing efforts.

**Intellectual Property**

Our trademarks, copyrights, domain names, trade secrets and other intellectual property rights distinguish our courses and services from those of our competitors and contribute to our ability to compete in our target markets. We rely on a combination of copyright and trademark law, trade secret protection and confidentiality agreements with senior executive officers and most other employees, to protect our intellectual property rights. In addition, we require certain of our senior executive officers and other employees to enter into agreements with us under which they acknowledge that all inventions, utility models, designs, know-how, copyrights and other forms of intellectual property made by them within the scope of their employment with us, pursuant to job assignments or using our materials and technology, or during the one year after their employment that relates to their employment with us, are our property and they should assign the same to us if we so require. We also regularly monitor any infringement or misappropriation of our intellectual property rights.

As of December 31, 2014, we had registered 202 domain names relating to our business, including our *www.tarena.com.cn*, *www.it211.com.cn* , *TMOOC.cn* and *jobshow.cn* websites, with the Internet Corporation for Assigned Names and Numbers and China Internet Network Information Center. Tarena Tech holds 20 registered software copyrights, two trademarks and 200 registered domain names including *www.tarena.com.cn*. Beijing Tarena holds two domain names, namely *www.it211.com.cn* and *TMOOC.cn.*

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**Competition**

The professional education services market in China is fragmented, rapidly evolving and highly competitive. We face competition in our offered courses and in many of the geographic markets in which we operate. For our IT training courses, we face competition from IT professional education providers that offer specialized training programs targeting certain niche job markets in the IT industry. In the future, we may also face competition from new entrants into the Chinese IT professional education market. For our non-IT training courses, we face competition for student enrollment from existing online and offline providers of professional education services, as well as smaller regional professional education services providers in China.

We believe that the principal competitive factors in our markets include the following:

- scope and quality of course offerings and services;
- student placement and employer satisfaction with our graduates;
- brand recognition;
- ability to effectively market course offerings and services to a broad base of prospective students;
- cost effectiveness of the education; and
- ability to align course offerings and services to specific needs of students and employers.

We believe that we are well-positioned to effectively compete in markets in which we operate on the basis of our innovative education platform, scalable and efficient business model, unparalleled access to corporate employers, training quality, strong content development capabilities and experienced management team. However, some of our current or future competitors may have longer operating histories, greater brand recognition, or greater financial, technical or marketing resources than we do. For a discussion of risks relating to competition, see Item 3. Key Information D. Risk Factors Risks Relating to Our Business We may lose market share and our profitability may be materially and adversely affected, if we fail to compete effectively with our present and future competitors or to adjust effectively to changing market conditions and trends.

**Insurance**

We do not maintain any liability insurance or property insurance policies covering students, equipment and facilities for injuries, death or losses due to fire, earthquake, flood or any other disaster. Consistent with customary industry practice in China, we do not maintain business interruption insurance, nor do we maintain key-man life insurance. We maintain accident injury insurance and accident injury medical insurance for our employees based in our headquarters in Beijing. Uninsured injury or death to our students or staff, or damage to any of our equipment or buildings could have a material adverse effect on our results of operations. See Item 3. Key Information D. Risk Factors Risks Relating to Our Business We have limited insurance coverage for our operations in China.

**Government Regulations**

**Regulations on Private Education**

The principal regulations governing private education in China consist of the *Education Law of the PRC*, the *Law for Promoting Private Education* and the *Implementation Rules for the Law for Promoting Private Education*, or the PE Implementation Rules and the Regulations on Chinese-Foreign Cooperation in Operating Schools.

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***Education Law of the PRC***

On March 18, 1995, the PRC National People s Congress promulgated the *Education Law of the PRC*, or the Education Law. Pursuant to the Education Law, enterprises, social organizations and individuals are generally encouraged to operate schools and other types of educational organizations in accordance with PRC laws and regulations, though private schools are prohibited from providing military, police, political and other kinds of education which are of a special nature. Although no organization or individual may establish or operate a school or any other institution of education for profit-making purposes, private schools may be operated for reasonable returns , as described in more detail below.

***The Law for Promoting Private Education and its Implementation Rules***

On December 28, 2002, the Standing Committee of the PRC National People s Congress promulgated the *Law for Promoting Private Education*, or the Private Education Law, which became effective on September 1, 2003 and was amended on June 29, 2013. On March 5, 2004, the PRC State Council promulgated the *Implementation Rules for the Law for Promoting Private Education*, which became effective on April 1, 2004, or the PE Implementation Rules. Under the Private Education Law and the Private Education Law Implementation Rules, private schools are defined as schools established by social organizations or individuals using non-government funds. Private schools providing certifications, pre-school education, education for self-study aid and other academic education shall be subject to approval by the education authorities, while private schools engaging in professional qualification training and professional education training shall be subject to approvals from the authorities in charge of labor and social welfare. A duly approved private school engaging in professional qualification training and professional education training shall (i) be granted a Permit for Operating a Private School by the authorities in charge of human resources and social security, (ii) be registered with the Ministry of Civil Affairs or its local counterparts as a privately run non-enterprise institution and (iii) pass the annual inspection with the Ministry of Civil Affairs or its local counterparts. As of December 31, 2014, we operated 15 schools, all of which are engaged in professional education training. Each has (i) obtained a Permit for Operating a Private School issued by the authorities in charge of human resources and social security or education, (ii) been registered with the relevant local counterpart of the Ministry of Civil Affairs and (iii) passed the annual inspection, as applicable, with the Ministry of Civil Affairs or its local counterparts.

The types and amounts of fees charged by a private school providing certifications shall be approved by the governmental pricing authority and be publicly disclosed. A private school that does not provide certifications shall file its pricing information with the governmental pricing authority and publicly disclose such information. A private school shall file its advertisement and school enrollment brochure with the relevant governmental authorities of human resources and social security or education. None of our schools provides a diploma or certification to students, and ten of our schools have filed their pricing information with the governmental pricing authority and publicly disclose such information. Seven of our schools have filed their advertisement and school enrollment brochure with the relevant governmental authorities of human resources and social security or education. See Item 3. Key Information D. Risk Factors Risks Relating to Our Business The operations of certain of our learning centers are, or may be deemed by relevant PRC government authorities to be, beyond their authorized business scope or without proper license or registration. If the relevant PRC government authorities take actions against such learning centers, our business and operations could be materially and adversely affected.

Private education is treated as a public welfare undertaking under relevant regulations, and entities and individuals who establish private schools are commonly referred to as sponsors instead of owners or shareholders under the regulations. Nonetheless, sponsors of a private school may choose to require reasonable returns from the annual net balance of the school after deduction of costs, donations received, government subsidies, if any, the reserved development fund and other expenses as required by the regulations. Private schools are divided into three categories:

private schools established with donated funds; private schools that require reasonable returns and private schools that do not require reasonable returns.

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The election to establish a private school requiring reasonable returns shall be provided in the articles of association of the school. The percentage of the school s annual net balance that can be distributed as a reasonable return shall be determined by the school s board of directors, taking into consideration the following factors: (i) school fee types and collection criteria, (ii) the ratio of the school s expenses used for educational activities and improving the educational conditions to the total fees collected, and (iii) the admission standards and educational quality. The relevant information relating to the above factors shall be publicly disclosed before the school s board determines the percentage of the school s annual net balance that can be distributed as reasonable returns. Such information and the decision to distribute reasonable returns shall also be filed with the approval authorities within 15 days from the decision made by the board. However, none of the current PRC laws and regulations provides a formula or guidelines for determining reasonable returns . In addition, none of the current PRC laws and regulations sets forth sponsors economic rights in schools that do not distribute reasonable returns, nor do they have different requirements or restrictions on a private school s ability to operate its education business based on such school s status as a school that requires reasonable returns or a school that does not require reasonable returns.

At the end of each fiscal year, every private school is required to allocate a certain amount to its development fund for the construction or maintenance of the school or procurement or upgrade of educational equipment. In the case of a private school that requires reasonable returns, this amount shall be no less than 25% of the annual net income of the school, while in the case of a private school that does not require reasonable returns, this amount shall be equal to no less than 25% of the annual increase in the net assets of the school, if any. Private schools that do not require reasonable returns shall be entitled to the same preferential tax treatment as public schools, while the preferential tax treatment policies applicable to private schools requiring reasonable returns shall be formulated by the finance authority, taxation authority and other authorities under the State Council. To date, however, no regulations have been promulgated by the relevant authorities in this regard.

Regardless of whether distributing reasonable return or not, the Private Education Law provides that properties that remain upon termination and liquidation of a school after payment of relevant fees and compensations shall be made in accordance with other relevant laws and regulations. However, there have been no other relevant national laws and regulations addressing the distribution of residual properties upon termination and liquidation of a private school.

Except for aforementioned differences, the sponsorship interest that a sponsor holds in a private school is, for all other practical purposes, substantially equivalent under PRC law and practice to the equity interest a shareholder holds in a company. A sponsor of a private school has the obligation to make capital contributions to the school in a timely manner. The contributed capital can be in the form of tangible or non-tangible assets such as materials in kind, land use rights or intellectual property rights. The capital contributed by the sponsor becomes assets of the school and the school has independent legal person status. In addition, the sponsor of a private school has the right to exercise ultimate control over the school by becoming the member of and controlling the composition of the school s decision making body. Specifically, the sponsor has control over the private school s constitutional documents and has the right to elect and replace the private school s decision making bodies, such as the school s board of directors, and therefore controls the private school s business and affairs.

As of December 31, 2014, we had nine schools registered as schools requiring reasonable returns, while all other schools are registered as schools not requiring reasonable returns.

**Regulations on Chinese-Foreign Cooperation in Operating Schools**

Chinese-foreign cooperation in operating schools or training programs is specifically governed by the Regulations on Operating Chinese-foreign Schools, promulgated by the State Council in 2003 in accordance with the Education Law, the Occupational Education Law and the Private Education Law. The Implementing Rules for the Regulations on

Operating Chinese-foreign Schools, or the Implementing Rules, were issued by the MOE in 2004. The Regulations on Chinese-Foreign Cooperation in Operating Schools and its Implementing Rules encourage substantive cooperation between overseas educational organizations with relevant qualifications and experience in providing high-quality education and Chinese educational organizations to jointly operate various types of schools in the PRC. Cooperation in the areas of higher education and occupational education is especially encouraged. Chinese-foreign cooperative schools are not permitted, however, to engage in compulsory education or military, police, political and other kinds of education that are of a special nature in China. The Regulations on Operating Chinese-foreign Schools prohibits foreign institutions or individuals from independently establishing schools in China, which provide educational services mainly for Chinese citizens.

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The Ministry of Human Resources and Social Security (formerly known as Ministry of Labor and Social Security) also promulgated the Regulations on Operation Chinese-foreign Cooperation School in Professional Education Training to implement the Regulations on Operating Chinese-foreign Schools on July 26, 2006, which took effect on October 1, 2006. The Regulations on Operation Chinese-foreign Cooperation School in Professional Education Training prohibits foreign institutions or individuals from independently establishing professional education training institutions in China, which provide educational services mainly for Chinese citizens.

We have not operated or applied for any Chinese-foreign schools. Prior to 2012, we operated a substantial portion of our learning centers through subsidiaries of our consolidated VIEs and schools to which our consolidated VIEs or their respective subsidiaries are sponsors. Starting from the second half of 2012, we began to transfer our operations to our wholly-owned subsidiary, Tarena Tech, and its subsidiaries. All of our learning center operations of VIEs had been transferred to Tarena Tech and its subsidiaries and schools. As of December 31, 2014, we operated 38 of our learning centers through private schools owned by subsidiaries of Tarena Tech. However, there are still uncertainties under the current PRC laws as to whether a wholly foreign owned enterprise (such as Tarena Tech) is allowed to indirectly invest in and own private schools through its PRC subsidiaries. See Item 3. Key Information D. Risk Factors Risks Relating to Our Business If the relevant PRC authorities determine that we can no longer own and operate certain of our learning centers through our PRC subsidiaries, we may need to restructure the ownership and operation of these learning centers (including possibly transferring these learning centers to our consolidated VIEs), our business may be disrupted and we may be exposed to increased risks associated with the contractual arrangements relating to our consolidated VIEs.

***Regulations on Professional Education***

On May 15, 1996, the Standing Committee of the PRC National People s Congress promulgated the Professional Education Law of the PRC, or the Professional Education Law which became effective on September 1, 1996. Pursuant to the Professional Education Law, professional training includes training pre-employment, training for military personnel transferring to civil positions, training for apprentices, on-the-job training, job-transfer training and other professional training. Professional training may be classified as junior, middle or senior level according to the actual situations. It shall be conducted by either professional training institutions or professional schools, which may develop various professional training to satisfy the needs of the society. The PRC government encourages institutional organizations, social organizations, other social groups and citizens to establish professional schools and professional training institutions, and the financial allocation for professional schools and professional training institutions from the governments at various levels shall be gradually increased. The PRC government also encourages financial institutions to support and develop professional education by means of credit facilities.

On August 3, 2007, the Standing Committee of the PRC National People s Congress promulgated the Employment Promotion Law of the PRC, or the *Employment Promotion Law* which became effective on January 1, 2008. Pursuant to the Employment Promotion Law, the PRC government at and above the county level shall encourage and support professional schools, professional training institutions and corporations to carry out pre-employment training, employment training, re-employment training and entrepreneurship training, and encourage workers to attend various types of training programs. Corporations in China are requested to set aside financial resources for the training and continued education of their employees.

**Foreign Investments in Professional Education Services**

The Catalogue for the Guidance of Foreign Investment Industries, or the Catalogue, as promulgated and amended from time to time by the MOFCOM and the National Development and Reform Commission, is the principal guide to foreign investors investment activities in the PRC. The most updated version of the Catalogue, which was

promulgated in March 2015 and became effective in April 2015, divides the industries into three categories: encouraged, restricted and prohibited. Industries not listed in the Catalogue are generally open to foreign investment unless specifically restricted by other PRC laws and regulations. A wholly foreign-owned enterprise is generally permitted for encouraged industries and industries not listed in the Catalogue, while there are some limitations to the ownership and/or corporate structure of the foreign-invested companies that operate in restricted industries. Industries in the prohibited category are not open to foreign investors. According to the latest Catalogue, foreign investment is encouraged in non accredited professional education services and there is no limitation with respect to maximum percentage of foreign ownership in a company conducting business in professional education services.

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**Regulations on For-profit Private Training Institutions**

The Private Education Law provides that the regulations applicable to private training institutions registered with the SAIC and its local counterparts shall be formulated by the State Council separately. On July 29, 2010, the PRC central government promulgated the Outline of China s National Plan for Medium- and Long-Term Education Reform and Development (2010-2020), which announced the policy that the government will implement a reform to divide private schools into two categories: (i) for-profit private schools and (ii) not-for-profit private schools. On October 24, 2010, the General Office of the State Council issued the Notices on the National Education System Innovation Pilot. Under this notice, the PRC government plans to implement a for-profit and non-profit classified management system for the private schools in Shanghai, Zhejiang, Shenzhen and Jilin Huaqiao Foreign Language School. However, the above outline and the pilot program is still new and no further national law or regulation has been promulgated to implement them and, except in Shanghai, no other local government of the pilot areas has promulgated relevant regulations on differentiated management of the private schools and for-profit training institutions.

On June 20, 2013, Shanghai promulgated the Interim Measures for Administration of Operational Private Training Institutions, or Measure No. 5, which requires for-profit private training institutions to register with local counterparts of the SAIC. The local counterparts of the SAIC shall consult with the local human resources and social securities authorities before completion of registration of for-profit private training institutions. Measure No. 5 came into effect on July 20, 2013 and will remain effective for two years.

As of December 31, 2014, 39 of our PRC subsidiaries, consolidated VIEs and subsidiaries of consolidated VIEs had computer technology training or training in its approved business scope.

**Regulations on Online and Distance Education**

Pursuant to the Administrative Regulations on Educational Websites and Online and Distance Education Schools issued by the Ministry of Education on July 5, 2000, educational websites and online education schools may provide educational services in relation to higher education, elementary education, pre-school education, teaching education, occupational education, adult education, other education and public educational information services. Educational websites refer to organizations providing education or education-related information services to website visitors by means of a database or online education platform connected via the Internet or an educational television station through an Internet Service Provider, or ISP. Online education schools refer to education websites providing academic education services or training services with the issuance of various certificates.

Setting up education websites and online education schools is subject to approval from relevant education authorities, depending on the specific types of education. Any education website and online education school shall, upon the receipt of approval, indicate on its website such approval information as well as the approval date and file number.

On June 29, 2004, the State Council promulgated the Decision on Setting Down Administrative Licenses for the Administrative Examination and Approval Items Really Necessary to be Retained, pursuant to which the administrative license for online education schools was retained, while the administrative license for educational websites was not retained. Accordingly, Beijing Tarena, our consolidated VIE engaging in online education-related services, is not required to obtain approval to operate educational websites from the Ministry of Education. On January 28, 2014, the State Council promulgated the Decision on Abolishing and Delegating Certain Administrative Examination and Approval Items, pursuant to which the administrative approval for online education schools of higher education was abolished. Beijing Tarena is not required to obtain a license to operate online education schools, as it does not directly offer government accredited degrees or certifications through its online education or training services.

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**Regulations on Online Publications**

On June 27, 2002, the State Administration of Press, Publication, Radio, Film and Television (formerly the General Administration of Press and Publication), or the SAPPRFT and the Ministry of Industry and Information Technology, or the MIIT jointly promulgated the Tentative Internet Publishing Administrative Measures, or the Internet Publishing Measures, which took effect on August 1, 2002. The Internet Publishing Measures require entities that engage in Internet publishing to obtain an Internet Publishing License for engaging in Internet publishing from the SAPPRFT. Pursuant to the Internet Publishing Measures, the definition of Internet publishing is broad and refers to the act of online spreading of articles, whereby the Internet information service providers select, edit and process works created by themselves or others and subsequently post such works on the Internet or transmit such works to the users end through Internet for the public to browse. These works include contents from books, newspapers, periodicals, audio-video products, electronic publications that have already been formally published or works that have been made public in other media.

Beijing Tarena has offered videos of lectures on its websites *www.it211.com.cn* and *TMOOC.cn* and has not obtained an Internet Publishing License from the SAPPRFT. Currently, Internet publishing is not officially defined in any publicly available regulations. However, governmental authorities could determine that Beijing Tarena s online content services fall within the scope of internet publishing, and therefore require Beijing Tarena to apply for an Internet Publishing License. Beijing Tarena may not be able to obtain such a license, and it may become subject to penalties, fines, legal sanctions or be ordered to suspend the video content on the website.

**Regulation on Broadcasting Audio-Video Programs through the Internet or Other Information Network**

The SAPPRFT promulgated the Rules for Administration of Broadcasting of Audio-Video Programs through the Internet and Other Information Networks, or the Broadcasting Rules, in 2004, which became effective on October 11, 2004. The Broadcasting Rules apply to the activities of broadcasting, integration, transmission, downloading of audio-video programs with computers, televisions or mobile phones as the main terminals and through various types of information networks. Pursuant to the Broadcasting Rules, a Permit for Broadcasting Audio-video Programs via Information Network is required to engage in these Internet broadcasting activities. On April 13, 2005, the State Council announced a policy on private investments in businesses in China that relate to cultural matters, which prohibits private investments in businesses relating to the dissemination of audio-video programs through information networks.

On December 20, 2007, the SAPPRFT and MIIT issued the Internet Audio-Video Program Measures, which became effective on January 31, 2008. Among other things, the Internet Audio-Video Program Measures stipulate that no entities or individuals may provide Internet audio-video program services without a Permit for Broadcasting Audio-video Programs via Information Network issued by the SAPPRFT or its local counterparts and only entities wholly owned or controlled by the PRC government may engage in the production, editing, integration or consolidation, and transfer to the public through the Internet, of audio-video programs, and the provision of audio-video program uploading and transmission services. On September 15, 2009, SAPPRFT promulgated the Notice on Several Issues regarding the Permit for Broadcasting Audio-video Programs via Information Network. The Notice restates the necessity of applying for such license and sets forth the legal liabilities for those providing Internet audio-video program services without the license.

On April 1, 2010, SAPPRFT promulgated the Test Implementation of the Tentative Categories of Internet Audio-Visual Program Services, or the Categories, which clarified the scope of Internet audio-video programs services. According to the Categories, there are four categories of Internet audio-visual program services which are further divided into seventeen sub-categories. The third sub-category to the second category covers the making and

editing of certain specialized audio-video programs concerning, among other things, educational content, and broadcasting such content to the general public online.

In the course of offering our lecture videos, we transmit our audio-video educational programs live through the Internet only to enrolled course participants, not to the general public. The limited scope of our audience distinguishes us from general online audio-video broadcasting companies. In addition, we do not provide audio-video program uploading and transmission services. As a result, we believe that we are not subject to the Internet Audio-Video Program Measures. However, there is no further official or publicly available interpretation of these definitions, especially the scope of Internet audio-video program service. If the governmental authorities determine that our provision of lecture videos falls within the Internet Audio-Video Program Measures, we may not be able to obtain the License for Disseminating Audio-Video Programs through Information Network. If this occurs, we may become subject to significant penalties, fines, legal sanctions or an order to suspend our use of audio-video content.

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**Regulations on Value-Added Telecommunications Services**

***Licenses for Value-Added Telecommunication Services***

On September 25, 2000, the Telecommunications Regulations of the People s Republic of China, or the Telecom Regulations, were issued by the PRC State Council as the primary governing law on telecommunication services. The Telecom Regulations set out the general framework for the provision of telecommunication services by PRC companies. Under the Telecom Regulations, it is a requirement that telecommunications service providers procure operating licenses prior to their commencement of operations. The Telecom Regulations draw a distinction between basic telecommunications services and value-added telecommunications services. A Catalog of Telecommunications Business was issued as an attachment to the Telecom Regulations to categorize telecommunications services as basic or value-added. In February 2003, the Catalog was updated and the information services such as content service, entertainment and online games services are classified as value-added telecommunications services.

On March 1, 2009, the MIIT issued the Administrative Measures for Telecommunications Business Operating Permit, or the Telecom Permit Measures, which took effect on April 10, 2009. The Telecom Permit Measures confirm that there are two types of telecom operating licenses for operators in China, namely, licenses for basic telecommunications services and licenses for value-added telecommunications services. The operation scope of the license will detail the permitted activities of the enterprise to which it was granted. An approved telecommunication services operator shall conduct its business in accordance with the specifications recorded on its value-added telecommunications services operating license, or VATS License. In addition, a VATS License s holder is required to obtain approval from the original permit-issuing authority prior to any change to its shareholders.

On September 25, 2000, the State Council promulgated the Administrative Measures on Internet Information Services, or the Internet Measures, which was amended in January 2011. Under the Internet Measures, commercial Internet information services operators shall obtain an ICP license from the relevant government authorities before engaging in any commercial Internet information services operations within the PRC. The ICP license has a term of five years and shall be renewed within 90 days before expiration. Our consolidated VIE, Beijing Tarena, obtained an ICP license for the website *www.it211.com.cn* issued by Beijing Communications Administration on March 1, 2012, which will expire on March 1, 2017. Beijing Tarena is in the process of applying to add our *TMOOC.cn* website under our ICP license.

***Foreign Investment in Value-Added Telecommunication Services***

Pursuant to the Provisions on Administration of Foreign Invested Telecommunications Enterprises promulgated by the State Council on December 11, 2001 and amended on September 10, 2008, the ultimate foreign equity ownership in a value-added telecommunications services provider may not exceed 50%. Moreover, for a foreign investor to acquire any equity interest in a value-added telecommunication business in China, it must satisfy a number of stringent performance and operational experience requirements, including demonstrating good track records and experience in operating value-added telecommunication business overseas. Foreign investors that meet these requirements must obtain approvals from the MIIT and the MOFCOM or their authorized local counterparts, which retain considerable discretion in granting approvals. Pursuant to publicly available information, the PRC government has issued telecommunications business operating licenses to only a limited number of foreign invested companies, all of which are Sino-foreign joint ventures engaging in the value-added telecommunication business.

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The MIIT Circular issued by the MIIT in July 2006 reiterated the regulations on foreign investment in telecommunications businesses, which require foreign investors to set up foreign-invested enterprises and obtain an ICP license to conduct any value-added telecommunications business in China. Under the MIIT Circular, a domestic company that holds an ICP license is prohibited from leasing, transferring or selling the license to foreign investors in any form, and from providing any assistance, including providing resources, sites or facilities, to foreign investors that conduct value-added telecommunications business illegally in China. Furthermore, the relevant trademarks and domain names that are used in the value-added telecommunications business must be owned by the local ICP license holder or its shareholder. The MIIT Circular further requires each ICP license holder to have the necessary facilities for its approved business operations and to maintain such facilities in the regions covered by its license. Currently, Beijing Tarena, our VIE, owns the domain names *www.it211.com.cn* and *TMOOC.cn* and holds the ICP license necessary to operate our *www.it211.com.cn* website in China, while the trademarks relating to our operations are held by Tarena Tech, our WFOE. If the relevant PRC government authorities determine in the future that the current ownership of our trademarks do not comply with the relevant regulations and the trademarks relating to our operations must be held by our VIE, we may need to transfer the trademarks to our VIE, which may severely disrupt our business. The Internet Electronic Messaging Service Administrative Measures promulgated by the MIIT in November 2000 require ICP operators to obtain specific approvals before providing BBS services. BBS services include electronic bulletin boards, electronic forums, message boards and chat rooms. On July 4, 2010, the approval requirement for operating BBS services was terminated by a decision issued by the PRC State Council. However, in practice, the competent authorities in Beijing still require the relevant operating companies to obtain such approval for the operation of BBS services which we have not obtained.

In light of the aforesaid restrictions, we rely on Beijing Tarena, our consolidated VIE in China, to hold and maintain the licenses necessary to provide online education and other value-added telecommunications services in China. We operate our *www.it211.com.cn* and *TMOOC.cn* websites and value-added telecommunications services through Beijing Tarena. Beijing Tarena, our consolidated VIE in China, holds an ICP license that is valid until March 1, 2017 for the operation of *www.it211.com.cn*. Beijing Tarena is in the process of applying to add our *TMOOC.cn* website under our ICP license.

***The Discussion Draft PRC Foreign Investment Law***

In January 2015, the MOFCOM published a discussion draft of the proposed Foreign Investment Law for public review and comments. The draft Foreign Investment Law purports to change the existing case-by-case approval regime to a filing or approval procedure for foreign investments in China. The MOFCOM, together with other relevant authorities, will determine a catalogue for special administrative measures, or the negative list, which will consist of a list of industry categories where foreign investments are strictly prohibited and a list of industry categories where foreign investments are subject to certain restrictions. Foreign investments in business sectors outside of the negative list will only be subject to filing procedures, in contrast to the existing prior approval requirements, whereas foreign investments in the restricted industries must apply for approval from the foreign investment administration authority.

The draft Foreign Investment Law for the first time defines foreign investor, foreign investment, Chinese investor and actual control. A foreign investor is not only determined based on the place of its incorporation, but also on the conditions of the actual control. The draft Foreign Investment Law specifically provides that entities established in China but controlled by foreign investors, such as via contracts or trust, will be treated as FIEs, whereas foreign investment in China in the foreign investment restricted industries by a foreign investor may nonetheless apply for being, when approving market entry clearance by the foreign investment administration authority, treated as a PRC domestic investment if the foreign investor is determined by the foreign investment administration authority as being controlled by PRC entities and/or citizens. In this connection, actual control is broadly defined in the draft Foreign

Investment Law to cover the following summarized categories: (i) holding 50% of more of the voting rights of the subject entity; (ii) holding less than 50% of the voting rights of the subject entity but having the power to secure at least 50% of the seats on the board or other equivalent decision making bodies, or having the voting power to material influence on the board, the shareholders meeting or other equivalent decision making bodies; or (iii) having the power to exert decisive influence, via contractual or trust arrangements, over the subject entity s operations, financial matters or other key aspects of business operations. According to the draft Foreign Investment Law, variable interest entities would also be deemed as FIEs, if they are ultimately controlled by foreign investors, and be subject to restrictions on foreign investments. However, the draft Foreign Investment Law has not taken a position on what actions will be taken with respect to the existing companies with the variable interest entity structure, whether or not these companies are controlled by Chinese parties.

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The draft Foreign Investment Law emphasizes on the security review requirements, whereby all foreign investments concerning national security must be reviewed and approved in accordance with the security review procedure. In addition, the draft Foreign Investment Law imposes stringent ad hoc and periodic information reporting requirements on foreign investors and the applicable FIEs. In addition to investment implementation report and investment amendment report that are required at each investment and alteration of investment specifics, an annual report is mandatory, and large foreign investors meeting certain criteria are required to report on a quarterly basis. Any company found to be non-compliant with these information reporting obligations may potentially be subject to fines and/or administrative or criminal liabilities, and the persons directly responsible may be subject to criminal liabilities.

The draft Foreign Investment Law is now open for public review and comments. It is still uncertain when the draft would be signed into law and whether the final version would have any substantial changes from this draft. When the Foreign Investment Law becomes effective, the trio of existing laws regulating foreign investment in China, namely, the Sino-foreign Equity Joint Venture Enterprise Law, the Sino-foreign Cooperative Joint Venture Enterprise Law and the Wholly Foreign-invested Enterprise Law, together with their implementation rules and ancillary regulations, will be abolished. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China Substantial uncertainties exist with respect to the enactment timetable, interpretation and implementation of draft PRC Foreign Investment Law and how it may impact the viability of our current corporate structure, corporate governance and business operations.

**Regulations on Intellectual Property Rights**

***Copyright and Software Products***

The National People s Congress adopted the Copyright Law in 1990 and amended it in 2001 and 2010, respectively. The amended Copyright Law extends copyright protection to Internet activities, products disseminated over the Internet and software products. In addition, there is a voluntary registration system administered by the China Copyright Protection Center. The amended Copyright Law also requires registration of a copyright pledge.

To address the problem of copyright infringement related to the content posted or transmitted over the Internet, the National Copyright Administration and the MIIT jointly promulgated the Measures for Administrative Protection of Copyright Related to Internet on April 29, 2005. This measure became effective on May 30, 2005.

The Administrative Measures on Software Products, issued by the MIIT in October 2000 and subsequently amended, provide a registration and filing system with respect to software products made in or imported into China. These software products may be registered with the relevant local authorities in charge of software industry administration. Registered software products may enjoy preferential treatment status granted by relevant software industry regulations. Software products can be registered for five years, and the registration is renewable upon expiration.

In order to further implement the Computer Software Protection Regulations promulgated by the State Council on December 20, 2001 and amended on January 30, 2013, the State Copyright Bureau issued the Computer Software Copyright Registration Procedures on February 20, 2002, which apply to software copyright registration, license contract registration and transfer contract registration. In compliance with, and in order to take advantage of the above rules, as of December 31, 2014, we had registered 20 software copyrights in China.

***Trademarks***

Trademarks are protected by the PRC Trademark Law which was adopted in 1982 and subsequently amended in 1993, 2001 and 2013 as well as the Implementation Regulation of the PRC Trademark Law adopted by the State Council in

2002. The Trademark Office under the SAIC handles trademark registrations and grants a term of ten years to registered trademarks which may be renewed for consecutive ten-year periods upon request by the trademark owner. Trademark license agreements must be filed with the Trademark Office for record. The PRC Trademark Law has adopted a first-to-file principle with respect to trademark registration. Where a trademark for which a registration has been made is identical or similar to another trademark which has already been registered or been subject to a preliminary examination and approval for use on the same kind of or similar commodities or services, the application for registration of such trademark may be rejected. Any person applying for the registration of a trademark may not prejudice the existing right first obtained by others, nor may any person register in advance a trademark that has already been used by another party and has already gained a sufficient degree of reputation through such party s use. We have registered two trademarks in China as of December 31, 2014.

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**Regulations on Foreign Currency Exchange**

The principal regulations governing foreign currency exchange in China are the Foreign Exchange Administration Regulations, or the Foreign Exchange Regulations, as amended on August 5, 2008. Under the Foreign Exchange Regulations, Renminbi is freely convertible for current account items, including the distribution of dividends, interest payments, trade and service-related foreign exchange transactions, but not for capital account items, such as direct investments, loans, repatriation of investments and investments in securities outside of China, unless the prior approval of the SAFE is obtained and prior registration with the SAFE is made. Though there are restrictions on the convertibility of Renminbi for capital account transactions, which principally include investments and loans, we generally follow the regulations and apply to obtain the approval of the SAFE and other relevant PRC governmental authorities.

On August 29, 2008, the SAFE promulgated SAFE Circular 142, regulating the conversion by a foreign invested company of foreign currency into Renminbi by restricting how the converted Renminbi may be used. SAFE Circular 142 requires that the registered capital of a foreign invested enterprise settled in Renminbi converted from foreign currencies may only be used for purposes within the business scope approved by the applicable governmental authority and may not be used for equity investments within China. In addition, the SAFE strengthened its oversight of the flow and use of the registered capital of a foreign invested enterprise settled in Renminbi converted from foreign currencies. The use of such Renminbi capital may not be changed without the SAFE s approval, and may not in any case be used to repay Renminbi loans if the proceeds of such loans have not been used. The SAFE also promulgated SAFE Circular 45 in November 2011, which, among other things, restricts a foreign-invested enterprise from using Renminbi funds converted from its registered capital to provide entrusted loans or repay loans between non-financial enterprises. On July 4, 2014, the SAFE promulgated Circular 36, which launched a pilot reform of the administration of the settlement of the foreign exchange capitals of foreign-invested enterprises in certain pilot areas from August 4, 2014. On March 30, 2015, the SAFE promulgated Circular 19, to expand the reform nationwide. Circular 19 will come into force and replace both Circular 142 and Circular 36 on June 1, 2015. Circular 36 allows enterprises established within the pilot areas to use their foreign exchange capitals to make equity investment and removes certain other restrictions provided under Circular 142 for these enterprises. Circular 19 will remove those restrictions for all foreign-invested enteprises established in the PRC. However, Circular 36 continues to, and Circular 19 will continue to, prohibit foreign-invested enterprises from, among other things, using the Renminbi fund converted from its foreign exchange capitals for expenditure beyond its business scope, providing entrusted loans or repaying loans between non-financial enterprises. These circulars may delay or limit us from using the proceeds of offshore offerings to make additional capital contributions or loans to our PRC subsidiaries and violations of these circulars could result in severe monetary or other penalties. See also Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China PRC regulation of direct investment and loans by offshore holding companies to PRC entities and governmental control of currency conversion may delay or limit us from using the proceeds of offshore offering to make additional capital contributions or loans to our PRC subsidiaries.

**Regulations on Dividend Distribution**

Under our current corporate structure, our Cayman Islands holding company primarily relies on dividend payments from Tarena Tech, which is a wholly foreign owned enterprise incorporated in the PRC, to fund any cash and financing requirements we may have. The principal regulations governing distribution of dividends of foreign invested enterprises include the Foreign Invested Enterprise Law, as amended on October 31, 2000, and the Implementation Rules of the Foreign Invested Enterprise Law, as amended on April 12, 2001.

Under these laws and regulations, wholly foreign owned enterprises in China may pay dividends only out of their accumulated after-tax profits, if any, determined in accordance with PRC accounting standards and regulations. In

addition, wholly foreign owned enterprises in China are required to allocate at least 10% of their respective accumulated profits each year, if any, to fund certain reserve funds until these reserves have reached 50% of the registered capital of the enterprises. Wholly foreign owned companies may, at their discretion, allocate a portion of their after-tax profits based on PRC accounting standards to staff welfare and bonus funds. These reserves are not distributable as cash dividends.

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**Regulations on Foreign Exchange Registration of Overseas Investment by PRC Residents**

Pursuant to SAFE s Notice on Relevant Issues Relating to Domestic Residents Investment and Financing and Round-Trip Investment through Special Purpose Vehicles, or SAFE Circular No. 37, issued and effective on July 4, 2014, and its appendixes, PRC residents, including PRC institutions and individuals, must register with local branches of SAFE in connection with their direct establishment or indirect control of an offshore entity, for the purpose of overseas investment and financing, with such PRC residents legally owned assets or equity interest in domestic enterprises or offshore assets or interests, referred to in SAFE Circular No. 37 as a special purpose vehicle. SAFE Circular No. 37 further requires amendment to the registration in the event of any significant changes with respect to the special purpose vehicle, such as increase or decrease of capital contributed by PRC individuals, share transfer or exchange, merger, division or other material event.

In the event that a PRC shareholder holding interests in a special purpose vehicle fails to fulfill the required SAFE registration, the PRC subsidiaries of that special purpose vehicle may be prohibited from making distributions of profit to the offshore parent and from carrying out subsequent cross-border foreign exchange activities and the special purpose vehicle may be restricted in their ability to contribute additional capital into its PRC subsidiary. Further, failure to comply with the various SAFE registration requirements described above could result in liability under PRC law for foreign exchange evasion. These regulations apply to our direct and indirect shareholders who are PRC residents and may apply to any offshore acquisitions and share transfer that we make in the future if our shares are issued to PRC residents. We have requested PRC residents currently holding direct or indirect interests in our company to our knowledge to make the necessary applications, filings and amendments as required under SAFE Circular No. 37 and other related rules. To our knowledge, all of our shareholders who are PRC citizens and hold interest in us, have registered with the local SAFE branch as required under SAFE Circular No. 37. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China PRC regulations relating to offshore investment activities by PRC residents may limit our PRC subsidiaries ability to increase their registered capital or distribute profits to us, limit our ability to inject capital into our PRC subsidiaries, or otherwise expose us to liability and penalties under PRC law.

**Regulations on Stock Incentive Plans**

In February 2012, SAFE promulgated the Stock Option Rules. Under the Stock Option Rules and other relevant rules and regulations, PRC residents who participate in stock incentive plan in an overseas publicly-listed company are required to register with SAFE or its local branches and complete certain other procedures. Participants of a stock incentive plan who are PRC residents must retain a qualified PRC agent, which could be a PRC subsidiary of the overseas publicly listed company or another qualified institution selected by the PRC subsidiary, to conduct the SAFE registration and other procedures with respect to the stock incentive plan on behalf of its participants. The participants must also retain an overseas entrusted institution to handle matters in connection with their exercise of stock options, the purchase and sale of corresponding stocks or interests and fund transfers. In addition, the PRC agent is required to amend the SAFE registration with respect to the stock incentive plan if there is any material change to the stock incentive plan, the PRC agent or the overseas entrusted institution or other material changes. The PRC agents must, on behalf of the PRC residents who have the right to exercise the employee share options, apply to SAFE or its local branches for an annual quota for the payment of foreign currencies in connection with the PRC residents exercise of the employee share options. The foreign exchange proceeds received by the PRC residents from the sale of shares under the stock incentive plans granted and dividends distributed by the overseas listed companies must be remitted into the bank accounts in the PRC opened by the PRC agents before distribution to such PRC residents.

We adopted two share incentive plans, namely the 2008 Plan and the 2014 Plan. Pursuant to the 2008 Plan, we may issue options, restricted shares (or share appreciation rights or other similar awards) and rights to purchase restricted

shares to our qualified employees and directors and consultants on a regular basis. Pursuant to the 2014 Plan, we may issue options, restricted shares and restricted share units to our qualified employees, directors and consultants on a regular basis. We have advised our employees and directors participating in the employee stock option plan to handle foreign exchange matters in accordance with the Stock Option Rules and we have completed the registrations of our stock incentive plan with the local SAFE as required by PRC law.

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In addition, the State Administration for Taxation has issued circulars concerning employee share options, under which our employees working in the PRC who exercise share options will be subject to PRC individual income tax. Our PRC subsidiaries have obligations to file documents related to employee share options with relevant tax authorities and to withhold individual income taxes of those employees who exercise their share options. If our employees fail to pay or if we fail to withhold their income taxes as required by relevant laws and regulations, we may face sanctions imposed by the PRC tax authorities or other PRC government authorities.

**Regulation on Tax**

***PRC Enterprise Income Tax Law***

On March 16, 2007, the National People s Congress, the PRC legislature, enacted the EIT Law. Both the EIT Law and its Implementing Rules, which was enacted on December 6, 2007 by the State Council, became effective on January 1, 2008. Under the EIT Law, enterprises are classified as PRC resident enterprises and non-PRC-resident enterprises. PRC resident enterprises typically pay an enterprise income tax at the rate of 25%. An enterprise established outside of the PRC with its de facto management bodies located within the PRC is considered a PRC resident enterprise, meaning that it shall be treated in a manner similar to a PRC resident enterprise for enterprise income tax purposes. The Implementing Rules to the EIT Law defines de facto management body as a managing body that in practice exercises substantial and overall management and control over the production and operations, personnel, accounting, and properties of an enterprise.

The SAT issued Circular 82 on April 22, 2009, as amended in January 2014. Circular 82 provides certain specific criteria for determining whether the de facto management body of a PRC-controlled and offshore-incorporated enterprise is located in China, which include all of the following conditions: (a) the location where senior management members responsible for an enterprise s daily operations discharge their duties; (b) the location where financial and human resource decisions are made or approved by organizations or persons; (c) the location where the major assets and corporate documents are kept; and (d) the location where more than half (inclusive) of all directors with voting rights or senior management have their habitual residence. In addition, the SAT issued a bulletin on July 27, 2011, effective September 1, 2011, or Bulletin 45, providing more guidance on the implementation of Circular 82. Bulletin 45 clarifies matters including PRC resident enterprise status determination, post-determination administration and competent tax authorities etc. Although both Circular 82 and Bulletin 45 only apply to offshore enterprises controlled by PRC enterprises or PRC enterprise groups, not those controlled by PRC individuals or foreign individuals like us, the determining criteria set forth in Circular 82 and Bulletin 45 may reflect the SAT s general position on how the de facto management body test should be applied in determining the PRC tax resident enterprise status of offshore enterprises, regardless of whether they are controlled by PRC enterprises, PRC enterprise groups or by PRC or foreign individuals.

We do not believe that Tarena International, Inc. meets all of the conditions above, and thus we do not believe that Tarena International, Inc. is a PRC resident enterprise despite the fact that all members of our management team as well as the management team of our offshore holding company are located in China. However, if the PRC tax authorities determine that Tarena International, Inc. is a PRC resident enterprise for PRC enterprise income tax purposes, a number of unfavorable PRC tax consequences could follow. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China Under the PRC Enterprise Income Tax Law, we may be classified as a PRC resident enterprise for PRC enterprise income tax purposes. Such classification would likely result in unfavorable tax consequences to us and our non-PRC shareholders and have a material adverse effect on our results of operations and the value of your investment.

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Pursuant to the Arrangement Between the Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Prevention of Fiscal Evasion with respect to Taxes on Income, or the Hong Kong Tax Treaty, and other applicable PRC regulations, if a Hong Kong resident enterprise is determined by the competent PRC tax authority to have satisfied the relevant conditions and requirements under such Hong Kong Tax Treaty and other applicable regulations, the 10% withholding tax on the dividends the Hong Kong resident enterprise receives from a PRC resident enterprise may be reduced to 5% upon receiving approval from in-charge tax authority. However, based on the Notice on Certain Issues with Respect to the Enforcement of Dividend Provisions in Tax Treaties issued on February 20, 2009 by the SAT, or Circular 81, if the relevant PRC tax authorities determine, in their discretion, that a company benefits from such reduced income tax rate due to a structure or arrangement that is primarily tax-driven, such PRC tax authorities may adjust the preferential tax treatment; and based on the Notice on the Interpretation and Recognition of Beneficial Owners in Tax Treaties, or Circular 601, issued on October 27, 2009 by the SAT, and the Announcement on the Recognition of Beneficial Owners in Tax Treaties issued on June 29, 2012 by the SAT, conduit companies, which are established for the purpose of evading or reducing tax, or transferring or accumulating profits, shall not be recognized as beneficial owners and thus are not entitled to the above-mentioned reduced income tax rate of 5% under the Hong Kong Tax Treaty. Tarena HK has not obtained the approval for a withholding tax rate of 5% from the local tax authority and does not currently plan to obtain such approval, as Tarena Hangzhou has not paid dividends in the past and does not currently have any concrete plan to pay dividends. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China We may not be able to obtain certain treaty benefits on dividends paid to us by our PRC subsidiary through our Hong Kong Subsidiary.

In January 2009, the SAT promulgated the Provisional Measures for the Administration of Withholding of Enterprise Income Tax for Non-resident Enterprises, or the Non-resident Enterprises Measures, pursuant to which, the entities which have the direct obligation to make certain payments to a non-resident enterprise shall be the relevant tax withholders for such non-resident enterprise. Further, the Non-resident Enterprises Measures provides that in case of an equity transfer between two non-resident enterprises which occurs outside China, the non-resident enterprise which receives the equity transfer payment shall, by itself or engage an agent to, file tax declaration with the PRC tax authority located at the place of the PRC company whose equity has been transferred, and the PRC company whose equity has been transferred shall assist the tax authorities to collect taxes from the relevant non-resident enterprise. On April 30, 2009, the MOF and the SAT jointly issued the Notice on Issues Concerning Process of Enterprise Income Tax in Enterprise Restructuring Business, or Circular 59. On December 10, 2009, the SAT issued the Notice on Strengthening the Administration of the Enterprise Income Tax concerning Proceeds from Equity Transfers by Non-resident Enterprises, or Circular 698. Both Circular 59 and Circular 698 became effective retroactively as of January 1, 2008. By promulgating and implementing these two circulars, the PRC tax authorities have enhanced their scrutiny over the direct or indirect transfer of equity interests in a PRC resident enterprise by a non-resident enterprise. Under Circular 698, where a non-resident enterprise transfers the equity interests of a PRC resident enterprise indirectly by disposition of the equity interests of an overseas holding company, or an Indirect Transfer, and such overseas holding company is located in certain low tax jurisdictions, the non-resident enterprise, being the transferor, shall report to the competent tax authority of the PRC resident enterprise this Indirect Transfer. The PRC tax authority may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established for the purpose of reducing, avoiding or deferring PRC tax. As a result, gains derived from such Indirect Transfer may be subject to PRC tax at a rate of up to 10%. On February 3, 2015, the SAT issued a Public Notice [2015] No.7, or Public Notice 7, to supersede the existing tax rules in relation to the Indirect Transfer as set forth in Circular 698, while the other provisions of Circular 698 remain in force. Public Notice 7 introduces a new tax regime that is significantly different from that under Circular 698. Public Notice extend its tax jurisdiction to to capture not only Indirect Transfer as set forth under Circular 698 but also transactions involving transfer of immovable property in China and assets held under the establishment and place, in China of a foreign company through the offshore transfer of a foreign intermediate holding company. Public Notice 7 also addresses the term transfer of the equity interest in a foreign intermediate holding company widely. In addition, Public Notice 7 provides clearer criteria than Circular 698

on how to assess reasonable commercial purposes and introduces safe harbor scenarios applicable to internal group restructurings on. However, it also brings challenges to both the foreign transferor and transferee of the Indirect Transfer as they have to make self-assessment on whether the transaction should be subject to PRC tax and to file or withhold the PRC tax accordingly. There is little guidance and practical experience as to the application of Circular 698 and Public Notice 7. Where non-resident investors were involved in our private equity financing, if such transactions were determined by the tax authorities to lack reasonable commercial purpose, we and our non-resident investors may become at risk of being taxed under Circular 698 and Public Notice 7 and may be required to expend valuable resources to comply with Circular 698 and Public Notice 7 or to establish that we should not be taxed under Circular 698 and Public Notice 7. The PRC tax authorities have the discretion under SAT Circular 59, Circular 698 and Public Notice 7 to make adjustments to the taxable capital gains based on the difference between the fair value of the equity interests transferred and the cost of investment.

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The State Administration of Taxation promulgated Administrative Measures on the General Anti-Avoidance Rule (Trial), or GAAR Measures, on December 12, 2014, which shows the authority s intention to fight against tax avoidance scheme that is adopted to obtain unwarranted tax benefit without reasonable commercial purpose. A press release, made by the State Administration of Taxation to clarify certain issues relating to the application of the GAAR Measures, stated that the GAAR Measures may be applicable if any general tax-avoidance scheme exists in the offshore indirect transfer of equity interests. Since GAAR Measures was recently promulgated and it is unclear how this set of measures, and any future implementation rules thereof, will be interpreted, amended and implemented by the relevant governmental authorities, we cannot predict how these regulations will affect our business operation, future acquisitions or strategy.

In addition, the EIT Law and its Implementation Rules permit certain high and new technology enterprises strongly supported by the state that hold independent ownership of core intellectual property and simultaneously meet a list of other criteria, financial or non-financial, as stipulated in the Implementation Rules and other regulations, to enjoy a reduced 15% enterprise income tax rate. The SAT, the Ministry of Science and Technology and the Ministry of Finance jointly issued the Administrative Measures on the Recognition Criteria and Procedures for Advance and New Technology Enterprise delineating the specific criteria and procedures for the high and new technology enterprises certification in April 2008. Enterprises recognized as high and new technology enterprises, or HNTEs, will enjoy a reduced 15% enterprise income tax rate after they go through tax reduction application formalities with relevant tax authorities. Tarena Tech, renewed its HNTE certificate in 2012, which was valid until the end of 2014. Tarena Tech is in the process of renewing its HNTE certificate. Tarena Hangzhou was established in 2013 and is qualified as a newly established software enterprise , which entitles it to two years of full tax exemption followed by three years of 50% tax exemption, commencing from the year in which its taxable income is greater than zero.

***PRC Value-added Tax ( VAT ) in lieu of Business Tax (the VAT Pilot Program )***

An enterprise or individual providing taxable service within the territory of China has been historically required to pay BT at the rate of 3% or 5% on the revenues generated from provision of such services in accordance with applicable PRC tax regulations. However, if the services provided are technical transfer or technical development, or technical consulting and technical service related to technology transfer or technical development, BT may be exempted subject to approval by the relevant tax authorities.

In November 2011, the Ministry of Finance and the SAT promulgated the Notice on the Pilot Program in Shanghai Replacing BT with VAT in Transportation and Some Modern Service Sectors. Pursuant to this circular and other relevant notices, VAT shall be imposed in lieu of BT in transportation and some modern service sectors firstly in Shanghai starting from January 1, 2012. Afterwards the VAT Pilot Program is expanded to Beijing from September 1, 2012, and then is rolled out to the whole country from August 1, 2013. Under the VAT Pilot Program, VAT at a rate of 6% applies to some modern service industries.

***Local Surcharges***

The city construction tax and education surcharge are local surcharges imposed as a certain percentage of PRC turnover taxes (i.e., business tax, value-added tax and consumption tax). The city construction tax is charged at rates of 1%, 5% or 7% (the applicable city construction tax rate depends on the location of the taxpayer) of the turnover tax paid while the education surcharge rate is currently at 3% of the turnover tax paid. Though in the past, foreign-invested enterprises, foreign enterprises and foreign individuals were exempted from such surcharges, these entities were required to make such payments from December 1, 2010 according to a notice issued by PRC State Council in October 2010.

In addition to the city construction tax and the education surcharge, the China Ministry of Finance issued Circular Caizong (2010) No. 98, or Circular 98, that requires all entities and individuals (including foreign-invested enterprises, foreign enterprises and foreign individuals) to pay a local education surcharge, or LES, at 2% on turnover tax paid. Local governments are required to report their implementation measures on LES to the Ministry of Finance. LES became applicable to all entities and individuals in Beijing on January 1, 2012.

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**Employment Laws and Social Insurance**

We are subject to laws and regulations governing our relationship with our employees, including wage and hour requirements, working and safety conditions, and social insurance, housing funds and other welfare. The compliance with these laws and regulations may require substantial resources.

China s National Labor Law, which became effective on January 1, 1995, and China s National Labor Contract Law, which became effective on January 1, 2008 and was amended on December 28, 2012, permit workers in both state-owned and private enterprises in China to bargain collectively. The National Labor Law and the National Labor Contract Law provide for collective contracts to be developed through collaboration between the labor union (or worker representatives in the absence of a union) and management that specify such matters as working conditions, wage scales, and hours of work. The laws also permit workers and employers in all types of enterprises to sign individual contracts, which are to be drawn up in accordance with the collective contract. The National Labor Contract Law has enhanced rights for the nation s workers, including permitting open-ended labor contracts and severance payments. The legislation requires employers to provide written contracts to their workers, restricts the use of temporary labor and makes it harder for employers to lay off employees. It also requires that employees with fixed-term contracts be entitled to an indefinite-term contract after a fixed-term contract is renewed twice or the employee has worked for the employer for a consecutive ten-year period.

On October 28, 2010, the National People s Congress of China promulgated the PRC Social Insurance Law, which became effective on July 1, 2011. In accordance with the PRC Social Insurance Law and other relevant laws and regulations, China establishes a social insurance system including basic pension insurance, basic medical insurance, work-related injury insurance, unemployment insurance and maternity insurance. An employer shall pay the social insurance for its employees in accordance with the rates provided under relevant regulations and shall withhold the social insurance that should be assumed by the employees. The authorities in charge of social insurance may request an employer s compliance and impose sanctions if such employer fails to pay and withhold social insurance in a timely manner. Under the Regulations on the Administration of Housing Fund effective in 1999, as amended in 2002, PRC companies must register with applicable housing fund management centers and establish a special housing fund account in an entrusted bank. Both PRC companies and their employees are required to contribute to the housing funds.

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**C. Organizational Structure**

The following diagram illustrates our corporate structure, including our subsidiaries and consolidated VIEs and their subsidiaries, as of the date of this annual report:

Equity control

Contractual arrangements consisted of exclusive business cooperation agreement, powers of attorney, equity interest pledge arrangements, exclusive option agreements, loan agreements and spousal consent letters

Sponsorship interest

Notes:

(1) Mr. Shaoyun Han, our founder, chairman and chief executive officer, owns 70% of the equity interest in Beijing Tarena. Mr. Jianguang Li, our director, owns 30% of the equity interest in Beijing Tarena.

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(2) Mr. Shaoyun Han and Mr. Jianguang Li own 49% and 51% of the equity interest in Shanghai Tarena, respectively.
(3) Shanghai Tarena is in the process of voluntary winding down.
(4) Tarena (Wuhan) Technology Co., Ltd., which is a wholly-owned subsidiary of Tarena Tech, wholly owns Wuhan Tarena Software Co., Ltd., which holds 100% of the sponsorship interest in Wuhan Tarena Professional Education School.
(5) Mr. Shaoyun Han is the principal of Shenyang Tarena Professional Education School, Jinan Tarena Professional Education School, Wuhan Tarena Professional Education School, Chongqing Jiulongpo Tarena Professional Education School, Kunming Tarena Professional Education School and Nanjing Tarena Professional Education School; De Xun Wang is the principal of Guangzhou Tarena Professional Education School and Shenzhen Bao an Tarena Professional Education School; Xuefeng Lu is the principal of Harbin Tarena Professional Education School; Qian Li is the principal of Qingdao Tarena Professional Education School; Yun Yang Gan is the principal of Zhengzhou Tarena Professional Education School; Chun Bo Shen is the principal of Dalian Gaoxin Tarena Professional Education School; Yue Qin Shen is the principal of Nanjing Weishang Tarena Professional Education School; Na Zhang is the principal of Shenyang Tarena Shidai Professional Education School; and Nini Tong is the principal of Zhuhai Tarena Professional Education School.

Because of foreign ownership restriction on Internet content and other value-added telecommunication services in China, we operate our *www.it211.com.cn* and *TMOOC.cn* websites through our consolidated VIE, Beijing Tarena. Beijing Tarena holds our ICP license for *www.it211.com.cn*. Beijing Tarena is 70% owned by Mr. Shaoyun Han, our founder, chairman and chief executive officer, and 30% owned by Mr. Jianguang Li, our director. Mr. Han and Mr. Li are both PRC citizens. We entered into a series of contractual arrangements with Beijing Tarena and its shareholders, which enable us to:

exercise effective financial control over Beijing Tarena;

receive substantially all of the economic benefits and bear the obligation to absorb substantially all of the losses of Beijing Tarena; and

have an exclusive option to purchase all or part of the equity interests in Beijing Tarena when and to the extent permitted by PRC law.

Because of these contractual arrangements, we are the primary beneficiary of Beijing Tarena and consolidate its financial results in our consolidated financial statements in accordance with U.S. GAAP.

The following is a summary of the currently effective contracts by and among Tarena International, our subsidiary Tarena Tech, our VIE, Beijing Tarena, and the shareholders of Beijing Tarena.

***Exclusive Business Cooperation Agreement***

Under the exclusive business cooperation agreement between Beijing Tarena and Tarena Tech, as amended and restated, Tarena Tech has the exclusive right to provide, among other things, technical support, business support and related consulting services to Beijing Tarena and Beijing Tarena agrees to accept all the consultation and services provided by Tarena Tech. Without Tarena Tech s prior written consent, Beijing Tarena is prohibited from engaging any third party to provide any of the services under this agreement. In addition, Tarena Tech exclusively owns all intellectual property rights arising out of or created during the performance of this agreement. Beijing Tarena agrees to

pay a monthly service fee to Tarena Tech at an amount determined solely by Tarena Tech after taking into account factors including the complexity and difficulty of the services provided, the time consumed, the seniority of the Tarena Tech employees providing services to Beijing Tarena, the value of services provided, the market price of comparable services and the operating conditions of Beijing Tarena. Furthermore, to the extent permitted under the PRC law, Tarena Tech agrees to provide financial support to Beijing Tarena if Beijing Tarena has any operating loss or suffered any critical operation adversity. The term of the agreement will remain effective unless Tarena Tech terminates the agreement in writing or a competent governmental authority rejects the renewal applications by either Beijing Tarena or Tarena Tech to renew its respective business license upon expiration. Without the consent of Tarena Tech, Beijing Tarena is not permitted to terminate this agreement in any event unless required by applicable laws.

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***Power of Attorney***

Pursuant to the power of attorney, as amended and restated, the shareholders of Beijing Tarena each irrevocably appointed Tarena Tech as the attorney-in-fact to act on their behalf on all matters pertaining to Beijing Tarena and to exercise all of their rights as a shareholder of Beijing Tarena, including but not limited to attend shareholders meetings, vote on their behalf on all matters of Beijing Tarena requiring shareholders approval under PRC laws and regulations and the articles of association of Beijing Tarena, and designate and appoint directors and senior management members. Tarena Tech may assign its rights under this power of attorney to any other person or entity at its sole discretion without prior notice to the shareholders of Beijing Tarena. Each power of attorney will remain in force until the shareholder ceases to hold any equity interest in Beijing Tarena.

***Equity Interest Pledge Agreements***

Under the equity interest pledge agreements between Tarena Tech, Beijing Tarena and the shareholders of Beijing Tarena, as amended and restated, the shareholders pledged all of their equity interests in Beijing Tarena to Tarena Tech to guarantee Beijing Tarena s and Beijing Tarena s shareholders performance of their obligations under the contractual arrangements including, but not limited to the service fees due to Tarena Tech. If Beijing Tarena or any of Beijing Tarena s shareholders breaches its contractual obligations under the contractual arrangements, Tarena Tech, as the pledgee, will be entitled to certain rights and entitlements, including receiving proceeds from the auction or sale of whole or part of the pledged equity interests of Beijing Tarena in accordance with legal procedures. Tarena Tech has the right to receive dividends generated by the pledged equity interests during the term of the pledge. If any event of default as provided in the contractual arrangements occurs, Tarena Tech, as the pledgee, will be entitled to dispose of the pledged equity interests in accordance with PRC laws and regulations. The equity interest pledge agreements became effective on the date when the agreements were duly executed. The pledge was registered with Changping Bureau of Beijing Administration for Industry and Commerce in December 2013, and will remain binding until Beijing Tarena and its shareholders discharge all their obligations under the contractual arrangements. The registration of the equity pledge enables Tarena Tech to enforce the equity pledge against third parties who acquire the equity interests of Beijing Tarena in good faith.

***Exclusive Option Agreements***

Under the exclusive option agreements between Tarena International, Inc., Tarena Tech, each of the shareholders of Beijing Tarena and Beijing Tarena, as amended and restated, each of the shareholders irrevocably granted Tarena International, Inc. or its designated representative(s) an exclusive option to purchase, to the extent permitted under PRC law, all or part of his equity interests in Beijing Tarena. In addition, Tarena International, Inc. has the option to acquire the equity interests of Beijing Tarena for a specified price equal to the loan provided by Tarena Tech to the individual shareholders. If the lowest price permitted under PRC law is higher than the above price, the lowest price permitted under PRC law shall apply. Tarena International, Inc. or its designated representative(s) has sole discretion as to when to exercise such options, either in part or in full. Without Tarena International, Inc. s prior written consent, Beijing Tarena s shareholders shall not sell, transfer, mortgage, or otherwise dispose any equity interests in Beijing Tarena. These agreements will remain effective until all equity interests in Beijing Tarena held by its shareholders are transferred or assigned to Tarena International, Inc. or Tarena International, Inc. s designated representatives.

***Loan Agreements***

Pursuant to the loan agreements between Tarena Tech and each individual shareholder of Beijing Tarena, as amended and restated, Tarena Tech provided loans with an aggregate amount of RMB2 million (US$0.3 million) to the individual shareholders of Beijing Tarena for the sole purpose of providing capital for Beijing Tarena. The loans can

only be repaid in a manner determined by Tarena Tech at its sole discretion, which repayment may take the form of transferring the individual shareholders equity interest in Beijing Tarena to Tarena or its designated person pursuant to the exclusive option agreements. The loan shall be interest-free, unless the transfer price exceeds the principal of the loan when each individual shareholder of Beijing Tarena transfers his equity interests in Beijing Tarena to Tarena or its designated person(s). Such excess over the principal of the loan shall be deemed the interest of the loan to the extent permitted under PRC law. The term of each loan agreement is ten years from the date of the agreement expiring in 2023 and can be extended with the written consent of both parties before expiration.

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***Spousal Consent Letters***

Ms. Ying Sun, the spouse of Mr. Shaoyun Han, and Ms. Nan Li, the spouse of Mr. Jianguang Li, executed spousal consent letters. Pursuant to the spousal consent letters, each of Ms. Ying Sun and Ms. Nan Li:

- undertook not to make any assertions in connection with the equity interests in Beijing Tarena held by her spouse;
- confirmed that her spouse can perform the amended and restated equity interest pledge agreements, the amended and restated exclusive option agreements, the power of attorney and the amended and restated loan agreements and to further amend or terminate such documents absent authorization or consent from her;
- undertook to execute all necessary documents and take all necessary actions to ensure appropriate performance of the amended and restated equity interest pledge agreements, the amended and restated exclusive option agreements, the power of attorney and the amended and restated loan agreements; and
- agreed and undertook to be bound by the amended and restated equity interest pledge agreements, the amended and restated exclusive option agreements, the power of attorney, the amended and restated loan agreements and the amended and restated exclusive business cooperation agreement and comply with the obligations thereunder as an equity holder of Beijing Tarena if she obtain any equity interests in Beijing Tarena held by her spouse for any reason.

The contractual arrangements by and among Tarena, our subsidiary Tarena Tech, Shanghai Tarena, and the shareholders of Shanghai Tarena are substantially the same as the contractual arrangements discussed above.

In the opinion of our PRC counsel, Han Kun Law Offices, these contractual arrangements are valid, binding and enforceable under current PRC laws. However, these contractual arrangements may not be as effective in providing control as direct ownership. There are substantial uncertainties regarding the interpretation and application of current or future PRC laws and regulations. For a description of the risks relating to our contractual arrangements, please see Item 3. Key Information D. Risk Factors Risks Relating to Our Corporate Structure.

## D. Property, Plants and Equipment

We have dual headquarters in China, located in Beijing and Hangzhou. Our principal executive offices in Beijing comprise of approximately 964 square meters and accommodate certain of our management and general and administrative activities, as well as our research and development activities. We also have approximately 13,062 square meters in leased classroom space in Beijing. Our principal executive offices and classrooms in Hangzhou comprise of approximately 9,399 square meters of leased space. Our principal executive offices in Hangzhou accommodate certain of our management and general and administrative activities.

In addition to our principal executive offices in Beijing and Hangzhou, we maintain a number of offices, classrooms and student dormitories with an aggregate of approximately 88,297 square meters in 35 cities in the PRC. We lease all of the facilities that we currently occupy from unrelated third parties. Our lease terms range from one to 10 years.

We believe that the facilities that we currently lease are adequate to meet our needs for the foreseeable future, and we believe that we will be able to obtain adequate facilities, principally through leasing of additional properties, to accommodate our future expansion plans.

**ITEM 4.A. UNRESOLVED STAFF COMMENTS**

Not Applicable.

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## ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

*The following discussion of our financial condition and results of operations is based upon and should be read in conjunction with our consolidated financial statements and their related notes included in this annual report on Form 20-F. This report contains forward-looking statements. See Forward-Looking Information. In evaluating our business, you should carefully consider the information provided under the caption Item 3. Key Information D. Risk Factors in this annual report on Form 20-F. We caution you that our businesses and financial performance are subject to substantial risks and uncertainties.*

### A. Operating Results

**Overview**

***Net Revenues***

We derive substantially all of our net revenues from tuition fees that we charge students. In 2012, 2013 and 2014, we generated net revenues of US$56.8 million, US$92.8 million and US$136.2 million, respectively. We record tuition fees that we collect in advance as deferred revenues. Our net revenues are presented net of business tax and surcharges.

*Number of Student Enrollments*

Our ability to generate and increase revenues is primarily driven by our ability to increase the number of student enrollments. The number of our student enrollments is primarily driven by the number and popularity of our course offerings. We evaluate the market demands for our course offerings and open new learning centers to cater to such demands. Our total student enrollments increased from 31,340 in 2012 to 46,458 in 2013 and further to 59,960 in 2014. The total number of our learning centers nationwide grew from 57 as of December 31, 2012 to 92 as of December 31, 2013 and to 118 as of December 31, 2014.

Our total student enrollment is affected by the continuing popularity of our existing courses and the number and popularity of new courses we offer. In 2014, our Java course remained the largest course in terms of revenues and number of student enrollments, with a total student enrollment of 21,610. Since 2012, we have developed and launched five new courses. Enrollment in our digital art course, launched in the first quarter of 2013, more than tripled from 5,003 in 2013 to 18,895 in 2014. Digital art has become our second largest course in terms of student enrollment for 2014. Our online sales and marketing course, launched in the fourth quarter of 2013, has become our third largest course in terms of student enrollment for 2014, enrolling 3,404 students. Enrollment in our iOS course, launched in the fourth quarter of 2012, nearly tripled from 627 in 2013 to 1,874 in 2014. We also launched our accounting course in October 2014, enrolling 247 students within first two months of launch. Expanding our course offerings and diversifying our sources of revenues help protect us from potential reduced student enrollments due to down-turns in certain industries or professions.

Our total student enrollment is also affected by our ability to maintain our cooperative relationships with financing service providers for student loans. A significant portion of our students enrolled in 2014 relied on loans provided or arranged by CreditEase, BOC CFC and BOB CFC to pay for our tuition fees. Historically, a significant portion of our students also relied on loans arranged by Chuanbang, a credit-sourcing company in China owned by Mr. Shaoyun Han, our chief executive officer. In 2014, 55% of our students took out loans provided or arranged by CreditEase, BOC CFC or BOB CFC to pay for our tuition fees. Our cooperative agreement with BOB CFC expired in February 2015, and we are in the process of renewing such agreement with BOB CFC. In Janurary 2015, we began to cooperate

with Renrendai, a third-party person-to-person lending service provider, in arranging loans for our students to pay for our tuition fees. Chuanbang ceased offering financing services to our students enrolled since January 1, 2014.

Starting from 2011, Chuanbang began to offer person-to-person lending services to our students to help them pay for our tuition fees. In connection with the person-to-person lending services provided by Chuanbang, we serve as a guarantor of the loans taken out by students. We recognized US$70,245, US$90,490 and US$18,188 as guarantee fee revenue in 2012, 2013 and 2014, respectively. We have stopped providing guarantees for any new student loan arranged by Chuanbang since April 2013. We have not generated any interest income in connection with the person-to-person lending services provided by Chuanbang.

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*Tuition fees*

Our net revenues are affected by the tuition fees for each of our courses. For our full-time and part-time classes, our standard tuition fees generally range from RMB16,800 (US$2,708) to RMB17,800 (US$2,869) per course. We increased our tuition fees for most of our full-time classes by approximately RMB1,000 (US$161) in 2012, further increased such tuition fees by RMB1,000 (US$161) in 2013 and again increased such tuition fees by RMB1,000 (US$161) in 2014. We also increased our tuition fees for part-time classes by RMB1,000 (US$161) to RMB3,000(US$483) per course in 2014. In March 2015, we increased tuition fees for selected courses by another RMB1,000 (US$161).

The actual tuition fees that we charge for our courses may vary according to the recruiting channel through which a student is enrolled. We recruit students either through our direct marketing efforts or from our network of cooperative universities and colleges. We generally offer a discount of approximately RMB4,000 (US$645) per person per full-time course for students enrolled through our network of cooperative universities and colleges. In 2014, we recruited approximately 18% of our students from these universities and colleges.

Our tuition fees are also affected by the payment option selected by our students. We primarily offer two payment options for our students, including one-time full payment upon enrollment and multiple payments within two months of enrollment. We also allow qualified students to pay our tuition fees within a period of time after graduation. We generally charge RMB1,000 (US$161) higher in tuition fees to students electing to pay in multiple payments within two months of enrollment and charge RMB3,000 (US$483) higher in tuition fees to students qualified and electing to pay in installments post graduation, as compared to students who elect to pay in full upfront.

***Cost of Revenues***

Our cost of revenues primarily consists of payroll and employee benefits for our instructors (as apportioned based on the amount of time that they devote to teaching), teaching assistants, career counselors and employer cooperation representatives, as well as rental payments for our learning centers, and to a lesser extent, depreciation relating to property and equipment used at our learning centers. The following table sets forth a breakdown of our cost of revenues in absolute amounts and as percentages of net revenues for the periods indicated:

| | For the Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2012 | | 2013 | | 2014 | |
| | US$ | % of net revenues | US$ | % of net revenues | US$ | % of net revenues |
| | (in thousands of US$, except percentages) | | | | | |
| Personnel cost and welfare | 6,560 | 11.5 | 11,109 | 12.0 | 14,409 | 10.6 |
| Rental cost | 5,112 | 9.0 | 8,668 | 9.3 | 11,263 | 8.3 |
| Others | 6,090 | 10.8 | 9,291 | 10.0 | 13,408 | 9.8 |
| Total cost of revenues | 17,762 | 31.3 | 29,068 | 31.3 | 39,080 | 28.7 |

Our cost of revenues is primarily affected by the number of our learning centers. We had a total of 57, 92 and 118 learning centers as of December 31, 2012, 2013 and 2014, respectively. Our cost of revenues as a percentage of net revenues was 31.3%, 31.3% and 28.7% in 2012, 2013 and 2014, respectively. We expect our cost of revenues to

continue to increase as we plan to open more learning centers.

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***Operating Expenses***

Our operating expenses consist primarily of selling and marketing expenses, general and administrative expenses and, to a lesser extent, research and development expenses. The following table sets forth our operating expenses in absolute amounts and as percentages of net revenues for the periods indicated:

| | For the Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2012 | | 2013 | | 2014 | |
| | US$ | % of net revenues | US$ | % of net revenues | US$ | % of net revenues |
| | (in thousands of US$, except percentages) | | | | | |
| Selling and marketing expenses | 16,875 | 29.7 | 30,252 | 32.6 | 42,562 | 31.2 |
| General and administrative expenses | 9,948 | 17.5 | 16,224 | 17.6 | 29,948 | 22.0 |
| Research and development expenses | 1,792 | 3.2 | 3,807 | 4.1 | 5,446 | 4.0 |
| Total operating expenses | 28,615 | 50.4 | 50,283 | 54.3 | 77,956 | 57.2 |

Our selling and marketing expenses primarily consist of compensation expenses relating to our personnel involved in selling and marketing, including our enrollment advisors and our university cooperation representatives based at our learning centers, advertising expenses relating to our marketing activities, and, to a lesser extent, rental expenses relating to our selling and marketing functions. We expect our selling and marketing expenses to increase as we further expand our business.

Our general and administrative expenses primarily consist of compensation expenses relating to our management and administrative personnel and bad debt allowance associated with our post-graduation tuition installment payment option for qualified students. To a lesser extent, our general and administrative expenses include share-based compensation and office expenses relating to administrative functions. We expect our general and administrative expenses to increase in the future on an absolute basis as our business grows and we incur costs related to complying with our reporting obligations as a public company under U.S. securities laws.

Our research and development expenses primarily consist of a portion of the personnel costs of our instructors as determined based on the amount of time that they devote to research and development-related activities, as well as the personnel costs of our software engineers.

**Seasonality**

Seasonal fluctuations have affected, and are likely to continue to affect, our business. Historically, we typically generate the highest net revenues in the third and fourth quarters because of the increased student enrollments during summer vacation. We generally generate less tuition fees in the first quarter of each year due to the Chinese New Year holiday. Our quarterly cost of revenue, selling and marketing expenses, general and administrative expenses and research and development expenses have generally been increasing in absolute amounts since 2012 as we expanded our network of learning centers, increased the number of our personnel and enhanced our marketing efforts.

**Taxation**

***Cayman Islands***

We are incorporated in the Cayman Islands. Under the current law of the Cayman Islands, we are not subject to income or capital gains tax. In addition, dividend payments are not subject to withholding tax in the Cayman Islands.

***Hong Kong***

Our wholly-owned subsidiary in Hong Kong, Tarena Hong Kong Limited, is subject to Hong Kong profits tax on its activities conducted in Hong Kong. No provision for Hong Kong profits tax has been made in the consolidated financial statements as Tarena Hong Kong Limited has no assessable income since its inception on October 22, 2012 to December 31, 2014.

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***China***

Pursuant to the EIT Law and its Implementation Rules, which became effective on January 1, 2008, foreign-invested enterprises and domestic companies are subject to enterprise income tax at a uniform rate of 25%. In addition, high and new technology enterprises, or HNTEs, will enjoy a preferential enterprise income tax rate of 15% under the EIT Law. Tarena Tech qualified as a HNTE under the EIT Law and is eligible for a preferential enterprise income tax rate of 15% for the period from 2009 to 2014. Tarena Tech is in the process of renewing its HNTE certificate. Tarena Hangzhou was established in 2013 and qualified as a newly established software enterprise , which entitles it to two years of full exemption followed by three years of 50% exemption, commencing from the year in which its taxable income is greater than zero. Certain of our subsidiaries qualified as Small Profit Enterprises in 2012, 2013 and 2014, and therefore are subject to the preferential income tax rate of 20%. Subject to the approvals from the tax authorities in certain locations in the PRC, our subsidiaries and consolidated VIEs that are based in these locations are required to use the deemed profit method to determine their income tax. Under the deemed profit method, these subsidiaries are subject to income tax at 25% on its deemed profit which is calculated based on revenues less deemed expenses equal to 85% to 90% of revenues.

**Internal Control over Financial Reporting**

In connection with the audit of our consolidated financial statements as of and for the year ended December 31, 2014, we and our independent registered public accounting firm identified a material weakness in our internal control over financial reporting as of December 31, 2014. As defined in standards established by the PCAOB, a material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weakness is related to the lack of GAAP expertise to perform sufficient review in areas subject to significant estimates and judgements.

Neither we nor our independent registered public accounting firm undertook a comprehensive assessment of our internal controls for purposes of identifying and reporting material weaknesses and other control deficiencies in our internal control over financial reporting, as we and they will be required to do under the Section 404 of the Sarbenes-Oxley Act of 2002. Had we performed a complete assessment of our internal control over financial reporting or had our independent registered public accounting firm performed an audit of our internal control over financial reporting, additional control deficiencies may have been identified.

To remedy our control deficiencies, we have adopted several measures to improve our internal control over financial reporting. We have engaged an external consulting firm to help us prepare for Section 404 compliance by documenting our processes and internal controls and benchmarking against industry best practices. In addition, we have (i) provided, and intend to continue to provide, on-going training to our accounting and operating personnel across different subsidiaries to improve their accounting knowledge; (ii) developed, and continue to update as needed, a more comprehensive manual on accounting policies and procedures; and (iii) reinforced the oversight and review procedure over high risk areas subject to significant estimates and judgements. We will continue to implement the necessary procedures and policies, including those outlined above, to improve our internal controls over financial reporting and remediate any potential material weaknesses and significant deficiencies as we prepare for our initial Section 404 reporting requirement under the Sarbanes-Oxley Act of 2002, which will take place in the fiscal year ending December 31, 2015 if certain conditions are met.

See Item 3. Key Information D. Risk Factors Risks Relating to Our Business If we fail to maintain an effective system of internal controls, we may be unable to accurately report our results of operations or prevent fraud or fail to meet our reporting obligations, and investor confidence and the market price of our ADSs may be materially and adversely

affected.

**Critical Accounting Policies**

We prepare our consolidated financial statements in accordance with U.S. GAAP, which requires us to make judgments, estimates and assumptions that affect (i) the reported amounts of our assets and liabilities; (ii) the disclosure of our contingent assets and liabilities at the end of each reporting period; and (iii) the reported amounts of revenues and expenses during each reporting period. We continually evaluate these judgments, estimates and assumptions based on our own historical experience, knowledge and assessment of current business and other conditions and our expectations regarding the future based on available information, which together form our basis for making judgments about matters that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, our actual results could differ from those estimates. Some of our accounting policies require a higher degree of judgment than others in their application.

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When reading our consolidated financial statements, you should consider our selection of critical accounting policies, the judgment and other uncertainties affecting the application of such policies and the sensitivity of reported results to changes in conditions and assumptions. We believe the following accounting policies involve the most significant judgments and estimates used in the preparation of our financial statements.

***Revenue recognition***

We derive substantially all of our net revenues from tuition fees, a portion of which we allow qualified students to pay on installment for a period of time exceeding one year. When tuition services are sold on repayment terms that exceed one year beyond the point in time that revenue is recognized, the receivable, and therefore the revenue is recorded at the present value of the total payments. The difference between the present value of the receivable and the nominal or principal value of the tuition fees is recognized as interest income over the contractual collection period using the effective interest rate method. The interest rate used to determine the present value of the total amount receivable is the rate at which students can obtain financing of a similar nature from other sources at the date of the transaction. Revenue is presented net of business tax and value added taxes at rates ranging between 3% and 6%, and surcharges.

***Allowance for doubtful accounts***

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our students to make payments according to their respective payment plans stipulated on the arrangement. We determine the allowance by analyzing students accounts that have known or potential collection issues and applying historical loss rates to the aging of the remaining balances of accounts receivable. In the event that we believe an account receivable will become uncollectible, we record an additional provision to increase the allowance for doubtful accounts.

***Long-lived assets***

Our long-lived assets include property and equipment. We depreciate our property and equipment using the straight-line method over the estimated useful lives of the assets. We make estimates of the useful lives of property and equipment, including the salvage values, in order to determine the amount of depreciation expense to be recorded during each reporting period. We amortize leasehold improvements of our learning center facilities and offices over the shorter of the lease term or the estimated useful life of the assets. We estimate the useful lives of our other property and equipment at the time the assets are acquired based on historical experience with similar assets, as well as anticipated technological or other changes. If technological changes were to occur more rapidly than anticipated or in a different form than anticipated, the useful lives assigned to these assets may be shortened, which would result in the recognition of increased depreciation expense in future periods. There has been no change to the estimated useful lives or salvage values of our property and equipment in 2012, 2013 and 2014.

We evaluate property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. We assess recoverability by comparing the carrying amount of a long-lived asset or asset group to the estimated undiscounted future cash flows expected to be generated by the asset or asset group. If the carrying amount of an asset or asset group exceeds its estimated undiscounted future cash flows, we recognize an impairment charge based on the amount by which the carrying amount exceeds the estimated fair value of the asset or asset group. We estimate the fair value of the asset or asset group based on the best information available, including prices for similar assets, and in the absence of an observable market price, the results of using a present value technique to estimate the fair value of the asset or asset group.

No impairment on our long-lived assets was recognized in 2012, 2013 and 2014.

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***Share-based Compensation***

We measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award and recognize the cost over the period the employee is required to provide service in exchange for the award, which is generally the vesting period. We have elected to recognize the compensation cost for an award with only service conditions that have a graded vesting schedule on a straight-line basis over the requisite service period for the entire award, net of estimated forfeitures, provided that the cumulative amount of compensation cost recognized at any date at least equals the portion of the grant-date value of such award that is vested at that date. Forfeiture rates are estimated based on historical and future expectations of employee turnover rates.

On September 22, 2008, we adopted the 2008 Plan, pursuant to which we can issue share options and other share-based awards to our key employees, directors and consultants to purchase up to 6,002,020 of our ordinary shares (being retroactively adjusted to reflect the effect of the share split). On November 28, 2012, we increased the number of our ordinary shares authorized for issuance under the 2008 Plan to 8,184,990. Share options issued before September 22, 2008 are also administered under the 2008 Plan.

In February 2014, we adopted the 2014 Plan, pursuant to which we were authorized to issue options, restricted shares and restricted share units to our qualified employees, directors and consultants. The maximum aggregate number of shares which may be issued pursuant to all awards under the 2014 Plan, or the Award Pool, is 1,833,696, provided that the shares reserved in the Award Pool shall be increased on the first day of each calendar year, commencing with January 1, 2015, if the unissued shares reserved in the Award Pool on such day account for less than 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year, as a result of which increase the shares unissued and reserved in the Award Pool immediately after each such increase shall equal 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year.

*Share Options*

Since January 1, 2004, our board of directors has granted the following options to our executive officers and employees:

| | Number of Options | Exercise Price (US$) | Fair Value of Ordinary Shares (US$) |
|---|---|---|---|
| **Grant date** | | | |
| Prior to January 1, 2012 | 7,117,020 | 0.058-1.00 | 0.04-0.83 |
| January 1, 2013 | 2,029,386 | 1.83 | 3.75 |
| September 16, 2013 | 488,424 | 1.83 | 5.69 |
| February 20, 2014 | 1,805,784 | 1.83-4.36 | 8.60 |

In determining the estimated fair value of share options granted to executive officers and certain employees, we have considered the guidance prescribed by the *AICPA Audit and Accounting Practice Aid, Valuation of Privately-Held-Company Equity Securities Issued as Compensation*, or the Practice Aid, which sets forth the preferred types of valuation that should be used. We have followed the *Level B* recommendation, and established the fair value of our ordinary shares at the dates of grant using a retrospective valuation for valuation dates prior to September 2013

with the assistance of an independent valuation firm. We obtained a retrospective valuation instead of contemporaneous valuation for valuation dates prior to September 2013, because at that time, our financial and managerial resources were limited. The valuation as of September 16, 2013 and February 20, 2014 was prepared on contemporaneous basis. We are ultimately responsible for all the fair value measurements in relation to the options and ordinary shares.

In determining the fair value of our ordinary shares for the purpose of determining the fair value of the share options, we followed a two-step process. In the first step, the equity value of our company was determined by taking into consideration the income approach, or the discounted cash flow on DCF, method. We considered the market approach and searched for public companies located in China with business nature and in a development stage similar to ours. However, no companies were similar to us in all aspects. We therefore did not apply any weight for the market approach to arrive at the equity value of our company and only used the market approach to corroborate the valuation results based on the income approach.

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In estimating the total equity value of our ordinary shares, we considered the DCF method, which incorporates the projected cash flow of our management s best estimation as of each measurement date. The projected cash flow estimation includes, among others, analysis of projected net revenue growth, gross margins and terminal value. The assumptions used in deriving the fair value of ordinary shares are consistent with our business plan.

The key assumptions used in developing the cash flow forecasts include: (i) compounded annualized growth rates of net revenue range from 19% to 52% for the forecasted period; (ii) gross margin forecast to improve with increasing economies of scale; and (iii) a terminal growth rate after the projection period.

The DCF method of the income approach involves applying appropriate weighted average cost of capital, or WACC, to discount the future cash flows forecast to present value. WACC comprises a required rate of return on equity plus the current tax effected rate of return on debt, weighted by the relative percentages of equity and debt in the capital structure of comparable public companies whose business operations are similar to that of ours. The required rates of return on equity were based on an estimation of the market required rate of return for investing in business similar to ours, which were derived by using the capital asset pricing model, or CAPM. Under CAPM, the discount rate was determined with consideration of the risk-free rate, industry-average correlated relative volatility coefficient beta, equity risk premium, size of our company, the scale of our business and our ability in achieving forecasted projections.

The risks associated with achieving the forecasts were assessed in selecting the appropriate WACC, which had been determined to range from 16.5% to 30%. The determined WACC decreased from 30% as of 2004 to 16.5% as of February 20, 2014 due to decrease in uncertainties associated with our financial forecast as we achieved millstones, progressed to later stage of development and developed solid track records.

In estimating the fair value of our ordinary shares by the DCF method, our management does not think there would be disproportionate returns of cash flows to different shareholders. Therefore, neither control premium nor a lack of control discount was considered in our valuations.

We also applied a discount for lack of marketability, or DLOM, ranging from 5% to 35%, to reflect the fact that there is no ready market for shares in a closely-held company like us. When determining the DLOM, the Black-Scholes option pricing model was used. Under this option-pricing method, the cost of the put option, which can hedge the price change before the privately held shares can be sold, was considered as a basis to determine the DLOM. This option pricing method was used because it takes into account certain company-specific factors, including the timing of the expected initial public offering and the volatility of the share price of the guideline companies engaged in the same industry.

The above assumptions used in determining the fair values were consistent with our business plan and major milestones we achieved. We also applied general assumptions, including the following:

- there will be no major changes in the existing political, legal, fiscal and economic conditions in countries in which we will carry on our business;

- there will be no major changes in the current tax laws in countries in which we operate and, that the rates of tax payable remain unchanged and that all applicable laws and regulations will be complied with;

exchange rates and interest rates will not differ materially from those presently prevailing;

the availability of financing will not be a constraint on the future growth of our operation;

we will retain and have competent management, key personnel, and technical staff to support our ongoing operations; and

industry trends and market conditions for related industries will not deviate significantly from economic forecasts.

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In the second step, since our capital structure comprised convertible redeemable preferred shares and ordinary shares at each grant date, we allocated our equity value among each class of equity securities using the option-pricing method. The option-pricing method treats ordinary shares and preferred shares as call options on our company s equity value and liquidation preference, redemption preference and conversion threshold of the preferred shares as exercise price of the call options.

The increase in the fair value of our ordinary shares from US$3.75 per share as of January 1, 2013 to US$5.69 per share as of September 16, 2013 was primarily attributable to the following factors:

We offered more courses at our learning centers in 2013. As a result of these offerings, we experienced rapid revenue and student growth in the nine-month period ended September 30, 2013. Our net revenues in the nine-month period ended September 30, 2013 were US$64.5 million, an increase of 64.5% from US$39.2 million in the nine-month period ended September 30, 2012. The number of learning centers increased from 57 as of December 31, 2012 to 86 as of September 30, 2013, and the number of student enrollments increased from 31,340 in 2012 to 33,289 in the nine months ended September 30, 2013, respectively. In view of the above, we adjusted our estimated earning upwards when we prepared financial forecast for valuation as of September 16, 2013, and lowered the discount rate used in valuation from 19.5% as of January 1, 2013 to 17.5% as of September 16, 2013.

As we progressed towards an initial public offering, or IPO, leading time to an expected liquidity event decreased, resulting in a decrease of DLOM from 20% as of January 1, 2013 to 15% as of September 16, 2013. We also increased our estimated probability of IPO from 50% to 60%. As preferred shares would be automatically converted into ordinary shares upon IPO, the increase in estimated probability of IPO results in allocation of a higher portion of our business enterprise value to ordinary shares.

The increase in the fair value of our ordinary shares from US$5.69 per share as of September 16, 2013 to US$8.60 per share as of February 20, 2014 was primarily attributable to the following factors:

We adjusted our projections upward when preparing our financial forecast to determine the fair value of our ordinary shares as of February 20, 2014 based on the following operational improvements:

(i) we expanded our new digital arts course offering nationally in the last quarter of 2013;

(ii) we launched a new online sales and marketing course in November 2013; and

(iii) in February 2014, we implemented a new pricing strategy resulting in an overall increase in tuition fees.

We made the first confidential submission of the draft registration statement on Form F-1 in respect of the proposed IPO in November 2013, increasing the probability of a successful IPO. This resulted in a decrease

of the DLOM from 15% as of September 16, 2013 to 5% as of February 20, 2014. Furthermore, we increased the estimated probability of a successful IPO from 60% as of September 16, 2013 to 90% as of February 20, 2014. Because our preferred shares will be automatically converted into ordinary shares upon the IPO, the increase in the estimated probability of the IPO resulted in the allocation of a higher portion of our business enterprise value to our ordinary shares.

The determined weighted average cost of capital decreased from 17.5% as of September 16, 2013 to 16.5% as of February 20, 2014 to reflect the decrease in uncertainties associated with our financial forecast, since we achieved our milestones, progressed to later stage of development and maintained a solid track record.

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In determining the fair value of share options granted to executive officers and certain employees, we have used the binomial option pricing model. Under this option pricing model, certain assumptions, including the risk-free interest rate, the expected dividends on the underlying ordinary shares and the expected volatility of the price of the underlying shares for the contract term of the options, are required in order to determine the fair value of the options. Changes in these assumptions could significantly affect the fair value of share options and hence the amount of compensation expense we recognize in our consolidated financial statements.

For the options granted, we used the following assumptions on the date of grant in determining the estimated fair value per option:

| | Options Granted In | | | |
|---|---|---|---|---|
| | **2011** | **2012** | **2013** | **2014** |
| Expected volatility | 45-46% | | 52% | 52% |
| Expected dividends yield | 0% | | 0% | 0% |
| Exercise multiple | 2.2 | | 2.2 | 2.2 |
| Risk-free interest rate per annum | 3.89%-3.93% | | 2.27%-3.38% | 3.81% |
| Estimated fair value of underlying ordinary shares (per share) | US$0.63-0.83 | | US$3.75-5.69 | US$8.60 |

For the purpose of determining the estimated fair value of our share options, we believe the expected volatility and the estimated fair value of our ordinary shares are the most critical assumptions since we are a privately held company when we granted these share options.

Since we did not have a trading history at the time the share options were granted and we did not have sufficient share price history to calculate our own historical volatility, expected volatility of our future ordinary share price was estimated based on the price volatility of the shares of comparable public traded companies engaged in the similar industry.

***Income taxes***

The realization of the future tax benefits of deferred income tax assets is dependent on future taxable income against which such tax benefits can be applied or utilized and any tax planning strategies. In assessing the realizability of deferred income tax assets, we consider whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. All available evidence must be considered in determining the realizability of the deferred income tax assets. Such evidence includes, but is not limited to, the financial performance of subsidiaries and consolidated VIEs, the market environment in which these entities operate, the utilization of past tax credits, and the length of relevant carryforward periods. Sufficient negative evidence, such as a cumulative net loss during a three-year period that includes the current year and the prior two years, may require that a valuation allowance be established with respect to existing and future deferred income tax assets. In view of cumulative losses sustained by our PRC subsidiaries and consolidated VIEs, valuation allowances of US$0.73 million, US$0.60 million and US$2.35 million were provided as of December 31, 2012, 2013 and 2014, respectively. If, in the future, taxable incomes are available for each tax-paying component, the valuation allowances against our deferred income tax assets may be adjusted.

In order to assess uncertain tax positions, we adopt a more likely than not threshold and a two-step approach for the tax position measurement and financial statement recognition. For the two-step approach, the first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained, including resolution of related appeals or litigation processes, if any. The

second step is to measure the tax benefit as the largest amount that is greater than 50% likely to be realized upon settlement. The unrecognized tax benefits were US$1.7 million, US$3.1 million and US$6.0 million as of December 31, 2012, 2013 and 2014, respectively. No interest and penalty expenses were recorded for the years ended December 31, 2012, 2013 and 2014.

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**Recently Issued Accounting Policies**

In April 2014, the FASB issued ASU No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. ASU 2014-08 change the requirements for reporting discontinued operations. This ASU limits discontinued operations reporting to disposals of components of an entity that represent strategic shifts that have a major effect on an entity s operations and financial results. As a result, the Company expects to report fewer discontinued operations under the new standard than would otherwise be reported under previous requirements. The new standard is effective for any disposals of components of the Company in annual reporting periods beginning after December 15, 2014. The Company will implement the provisions of ASU 2014-08 as of January 1, 2015.

The FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, in May 2014. ASU 2014-09 requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity should also disclose sufficient quantitative and qualitative information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new standard is effective for annual reporting periods beginning after December 15, 2017. The Company will implement the provisions of ASU 2014-09 as of January 1, 2018. The Company has not yet determined the impact of the new standard on its current policies for revenue recognition.

**Results of Operations**

The following table sets forth a summary of our consolidated results of operations for the periods indicated, both in absolute amounts and as percentages of our net revenues. This information should be read together with our consolidated financial statements and related notes included elsewhere in this annual report. The operating results in any period are not necessarily indicative of the results that may be expected for any future period.

| | For the Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2012 | | 2013 | | 2014 | |
| | US$ | % of Net Revenues | US$ | % of Net Revenues | US$ | % of Net Revenues |
| | (in thousands of US$, except percentages) | | | | | |
| Net revenues | 56,820 | 100.0 | 92,834 | 100.0 | 136,204 | 100.0 |
| Cost of revenues[(1)] | (17,762) | (31.3) | (29,068) | (31.3) | (39,080) | (28.7) |
| Gross profit | 39,058 | 68.7 | 63,766 | 68.7 | 97,124 | 71.3 |
| Operating expenses[(1)]: | | | | | | |
| Selling and marketing | (16,875) | (29.7) | (30,252) | (32.6) | (42,562) | (31.2) |
| General and administrative | (9,948) | (17.5) | (16,224) | (17.6) | (29,948) | (22.0) |
| Research and development | (1,792) | (3.2) | (3,807) | (4.1) | (5,446) | (4.0) |
| Operating income | 10,443 | 18.3 | 13,483 | 14.4 | 19,168 | 14.1 |
| Interest income | 1,165 | 2.1 | 1,541 | 1.7 | 4,360 | 3.2 |
| Interest expense | (6) | | | | | |
| Foreign exchange gain | | | | | 1,197 | 0.9 |
| Other income | 169 | 0.3 | 1,294 | 1.4 | 2,371 | 1.7 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Income before income taxes | 11,771 | 20.7 | 16,318 | 17.5 | 27,096 | 19.9 |
| Income tax expense | (2,219) | (3.9) | (2,271) | (2.4) | (2,405) | (1.8) |
| Net income | 9,552 | 16.8 | 14,047 | 15.1 | 24,691 | 18.1 |

Notes:

(1) Share-based compensation expenses were allocated in cost of revenues and operating expenses as follows:

| | For the Year Ended December 31 | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | (in thousands US$) | | |
| Cost of revenues | | 17 | 57 |
| Selling and marketing expenses | 1 | 45 | 169 |
| General and administrative expenses | 125 | 654 | 3,627 |
| Research and development expenses | 3 | 48 | 210 |

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***The Year Ended December 31, 2014 Compared to the Year Ended December 31, 2013***

*Net revenues*

Our net revenues increased by 46.7% from US$92.8 million in 2013 to US136.2 million in 2014. This increase was primarily due to increased student enrollments and higher average revenue per student. The number of total student enrollments grew by 29.1% from 46,458 in 2013 to 59,960 in 2014. The number of our student enrollments is primarily driven by the number and popularity of our course offerings. We experienced significant increase in student enrollment for our new courses in the past few years, such as digital art, online sales and marketing, and iOS. The number of our learning centers increased from 92 as of December 31, 2013 to 118 as of December 31, 2014 to cater to the increased demand for our courses. The increase in our average revenue per student was primarily a result of our tuition fees increase in 2014 and the decrease in the percentage of our students recruited through our network of cooperative universities and colleges. In 2014, we raised the standard tuition fees on most of our courses by RMB1,000 (US$161) per course. We generally offer a discount of approximately RMB4,000 (US$645) per person per full-time course for students enrolled through our network of cooperative universities and colleges. In 2014, the percentage of our students recruited from our network of cooperative universities and colleges was approximately 18%, as compared with 23% in 2013.

*Cost of Revenues*

Our cost of revenues increased by 34.4% from US$29.1 million in 2013 to US$39.1 million in 2014. This increase was mainly due to higher personnel cost and welfare expenses resulting from increased number of teaching and advisory staff at our learning centers, higher rental cost resulting from increased number of learning centers and expansion of existing learning centers, as well as higher depreciation expenses for our learning centers. Our instructors, teaching assistants, career counselors and employer cooperation representatives at our learning centers increased from 1,179 as of December 31, 2013 to 1,378 as of December 31, 2014. The number of our learning centers increased from 92 as of December 31, 2013 to 118 as of December 31, 2014.

*Gross Profit and Gross Margin*

As a result of the foregoing, our gross profit increased by 52.3% from US$63.8 million in 2013 to US$97.1 million in 2014. Our gross profit margin increased from 68.7% in 2013 to 71.3% in 2014. The improvement in gross margin was mainly due to increased operational scale and efficiency for our learning centers. Our overall center utilization rate in 2014 increased to 71% from 66% in 2013.

*Operating Expenses*

Our operating expenses increased by 55.0% from US$50.3 million in 2013 to US$78.0 million in 2014 as a result of increases in our selling and marketing, general and administrative and research and development expenses.

*Selling and Marketing Expenses*

Our selling and marketing expenses increased by 40.7% from US$30.3 million in 2013 to US$42.6 million in 2014. This increase was partially due to increased personnel cost and welfare expenses related to growth in our selling and marketing headcount from 1,321 as of December 31, 2013 to 1,773 as of December 31, 2014. The amount of personnel cost and welfare expenses for our selling and marketing staff increased from US$12.9 million in 2013 to US$19.1 million in 2014. The increase in selling and marketing expenses was also due to expanded marketing efforts, which increased advertising expenses from US$11.6 million in 2013 to US$16.7 million in 2014, primarily as a result

of increased spending on search engine advertising as we expanded our network of learning centers.

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*General and Administrative Expenses.*

Our general and administrative expenses increased by 84.6% from US$16.2 million in 2013 to US$29.9 million in 2014 primarily due to higher personnel costs and welfare expenses for our increased headcount of general and administrative personnel, from 591 as of December 31, 2013 to 742 as of December 31, 2014 to support our growing operations, higher bad debt allowance associated with our post-graduation tuition installment payment option for qualified students enrolled between 2010 and 2012 and higher share-based compensation expenses, which increased from US$0.7 million in 2013 to US$3.6 million in 2014.

*Research and Development Expenses.*

Our research and development expenses increased by 43.0% from US$3.8 million in 2013 to US$5.4 million in 2014 primarily due to increased personnel costs and welfare expenses of our instructors allocated to their content development activities for our new courses, as well as increased number of research and development staff as we expanded our course offerings and operations.

*Interest Income*

Our interest income increased from US$1.5 million in 2013 to US$4.4 million in 2014. Our interest income in both periods consisted of interest earned on our cash and time deposits deposited in commercial banks and interest income recognized in relation to our installment payment plan for students. The increase in interest income was primarily due to higher deposits resulting from our initial public offering and concurrent private placement in April 2014.

*Income Tax Expense*

Our income tax expense increased by 5.9% from US$2.3 million in 2013 to US$2.4 million in 2014. The increase was mainly due to higher taxable income, largely offset by a decrease in the effective income tax rate to 8.9% in 2014 from 13.9% in 2013. The decrease in our effective income tax rate is primarily due to the significant profits generated in one of our PRC subsidiaries, Tarena Hangzhou, which is entitled to the full income tax exemption during the year ended December 31, 2014.

The effective income tax rate of 13.9% in 2013 was lower than the statutory income tax rate of 25% primarily because of (i) the preferential income tax rate of 15% enjoyed by Tarena Tech, and (ii) the effect of research and development expenses bonus deduction allowed under PRC tax regulations, partially offset by recognition of valuation allowances for deferred income tax assets of certain subsidiaries, which were at cumulative loss position.

The effective income tax rate of 8.9% in 2014 was lower than the statutory income tax rate of 25% primarily because of (i) the preferential income tax rate of 15% enjoyed by Tarena Tech, (ii) the preferential income tax rate of 0% enjoyed by Tarena Hangzhou and (iii) the effect of research and development expenses bonus deduction allowed under PRC tax regulations, partially offset by recognition of valuation allowances for deferred income tax assets of certain subsidiaries, which were at cumulative loss position.

*Net Income*

As a result of the foregoing, our net income increased by 75.8% from US$14.0 million in 2013 to US$24.7 million in 2014.

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***The Year Ended December 31, 2013 Compared to the Year Ended December 31, 2012***

*Net revenues*

Our net revenues increased by 63.4% from US$56.8 million in 2012 to US$92.8 million in 2013. This increase was primarily due to new student enrollments. The number of total student enrollments grew by 48.2% from 31,340 in 2012 to 46,458 in 2013. The number of our student enrollments is primarily driven by the number and popularity of our course offerings. While our existing courses continued to attract increased student enrollments, we launched three new courses in 2013. For example, we launched our digital art course in February 2013, which enrolled 5,003 students in 2013. The number of our learning centers increased from 57 as of December 31, 2012 to 92 as of December 31, 2013 to cater to the increased demand for our courses. To a lesser degree, our net revenues increase was also attributable to the increase of our tuition fees. In 2013, we raised the standard tuition fees on most of our courses by RMB1,000 (US$165) per course.

*Cost of Revenues*

Our cost of revenues increased by 63.7% from US$17.8 million in 2012 to US$29.1 million in 2013. This increase was primarily due to higher compensation expenses resulting from increased number of teaching and advisory staff at our learning centers. Our instructors, teaching assistants, career counselors and employer cooperation representatives at our learning centers increased from 921 as of December 31, 2012 to 1,179 as of December 31, 2013. The increase in cost of revenues was also attributable to increased rental payments for our learning centers. The number of our learning centers increased from 57 as of December 31, 2012 to 92 as of December 31, 2013.

*Gross Profit and Gross Margin*

As a result of the foregoing, our gross profit increased by 63.3% from US$39.1 million in 2012 to US$63.8 million in 2013. Our gross profit margin was 68.7% in each of 2012 and 2013.

*Operating Expenses*

Our operating expenses increased by 75.7% from US$28.6 million in 2012 to US$50.3 million in 2013 as a result of increases in our selling and marketing, general and administrative and research and development expenses.

*Selling and Marketing Expenses*

Our selling and marketing expenses increased by 79.3% from US$16.9 million in 2012 to US$30.3 million in 2013. This increase was partially due to increased personnel cost and welfare expenses related to growth in our selling and marketing headcount from 959 as of December 31, 2012 to 1,321 as of December 31, 2013. The amount of personnel cost and welfare expenses for our selling and marketing staff increased from US$6.2 million in 2012 to US$12.9 million in 2013. The increase in selling and marketing expenses was also due to expanded marketing efforts, which increased advertising expenses from US$5.9 million in 2012 to US$11.6 million in 2013, primarily as a result of increased spending on search engine advertising as we expand our network of learning centers.

*General and Administrative Expenses.*

Our general and administrative expenses increased by 63.1% from US$9.9 million in 2012 to US$16.2 million in 2013 primarily due to increased headcount to support our growing operations from 456 as of December 31, 2012 to 591 as of December 31, 2013 and higher office expenses and office rental payments.

*Research and Development Expenses.*

Our research and development expenses increased by 112.5% from US$1.8 million in 2012 to US$3.8 million in 2013 primarily due to increased compensation expenses of our instructors allocated to their content development activities for our new courses.

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*Interest Income*

Our interest income increased from US$1.2 million in 2012 to US$1.5 million in 2013. Our interest income in both periods consisted of interest earned on our cash and time deposits deposited in commercial banks and interest income recognized in relation to our installment payment plan for students.

*Income Tax Expense*

Our income tax expense increased from US$2.2 million in 2012 to US$2.3 million in 2013 due to the increase in our taxable income, partially offset by a decrease in our effective income tax rate. The decrease in our effective income tax rate is primarily due to the effect of the higher proportion of taxable income generated by Tarena Tech which enjoys preferential income tax rate of 15%.

The effective income tax rate of 19% in 2012 was lower than the statutory income tax rate of 25% primarily because of (i) the preferential income tax rate of 15% enjoyed by Tarena Tech, (ii) the deemed profit method in determining income tax used by certain of our subsidiaries and consolidated VIEs, and (iii) the effect of research and development expenses bonus deduction allowed under PRC tax regulations, partially offset by recognition of valuation allowances for deferred income tax assets of certain subsidiaries, which were at cumulative loss position.

The effective income tax rate of 13.9% in 2013 was lower than the statutory income tax rate of 25% primarily because of the effect of the abovementioned Tarena Tech s preferential income tax rate and the effect of research and development expenses bonus deduction allowed under PRC tax regulations.

*Net Income*

As a result of the foregoing, our net income increased from US$9.6 million in 2012 to US$14.0 million in 2013.

**Inflation**

Since our inception, inflation in China has not materially impacted our results of operations. According to the National Bureau of Statistics of China, the year-over-year percent changes in the consumer price index for December 2012, 2013 and 2014 were increases of 2.5%, 2.5% and 1.5%, respectively.

**Impact of Foreign Currency Fluctuation**

See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China Fluctuations in exchange rates could have a material adverse effect on our results of operations and the value of your investment. and Item 11. Quantitative and Qualitative Disclosures About Market Risk Foreign Exchange Risk.

**Impact of Governmental Policies**

See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China and Item 4. Information on the Company B. Business Overview Government Regulations.

**B. Liquidity and Capital Resources**

***Cash Flows and Working Capital***

Our principal sources of liquidity have been cash generated from operating activities and proceeds from the issuance and sale of our shares. As of December 31, 2014, we had US$166.8 million in cash, cash equivalents and time deposits and we had no bank borrowings. Our cash consists of cash on hand and cash in bank, which are unrestricted as to withdrawal. Cash of our consolidated VIEs, in the amount of US$0.2 million as of December 31, 2014, can be used only to settle obligations of our consolidated VIEs. Cash equivalents consist of interest-bearing certificates of deposit with initial term of no more than three months when purchased. Time deposits, which mature within one year as of the balance sheet date, represent interest-bearing certificates of deposit with an initial term of greater than three months when purchased, while the time deposits that mature over one year as of the balance sheet date are included in non-current assets.

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We believe that our current cash, cash equivalents and time deposits and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs, including our cash needs for working capital and capital expenditures, for at least the next 12 months.

See *Cash, cash equivalents and time deposits* under Note 2(d) to our audited consolidated financial statements included in this annual report for information regarding the the currencies in which cash, cash equivalents and time deposits were held as of December 31, 2014.

The following table sets forth a summary of our cash flows for the periods indicated:

| | For the Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | (US$ in thousands) | | |
| Net cash provided by operating activities | 7,444 | 29,706 | 28,460 |
| Net cash used in investing activities | (7,915) | (19,537) | (119,459) |
| Net cash provided by (used in) financing activities | (227) | (591) | 106,472 |
| Net increase (decrease) in cash and cash equivalents | (653) | 9,942 | 16,521 |
| Cash and cash equivalents at the beginning of the year | 16,850 | 16,197 | 26,139 |
| Cash and cash equivalents at end of the year | 16,197 | 26,139 | 42,660 |

***Operating Activities***

Net cash provided by operating activities decreased to US$28.5 million in 2014 from US$29.7 million in 2013, primarily due to an increase of approximately US$26 million in cash operating expenditures in 2014, which were partially offset by an increase of approximately US$24 million in cash collected from our students and a decrease of approximately US$1 million in income tax payment in 2014.

Net cash provided by operating activities increased to US$29.7 million in 2013 from US$7.4 million in 2012, primarily due to an increase of approximately US$48 million in cash collected from our students in 2013, which were partially offset by an increase of approximately US$25 million in cash operating expenditures and an increase of approximately US$1 million in income tax payment in 2013.

Net cash provided by operating activities was US$7.4 million in 2012 compared with net cash used in operating activities of US$1.0 million in 2011, primarily due to an increase of approximately US$28 million in cash collected from our students in 2012, which were partially offset by an increase of approximately US$20 million in cash operating expenditures and an increase of approximately US$1 million in income tax payment in 2012.

***Investing Activities***

We lease all of our facilities. Our cash used in investing activities is primarily related to leasehold improvements, purchase of property and equipment, and investments in time deposits and short-term financial products.

Net cash used in investing activities was US$119.5 million in 2014, consisting of purchases of property and equipment, including computers and servers, of approximately US$8 million in connection with the expansion of our network of learning centers; purchase of time deposits of approximately US$115 million; purchase of short-term investment in the amount of approximately US$101 million; and partially offset by the maturity of short-term

investment of approximately US$101 million, and maturity of time deposits of approximately US$4 million.

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Net cash used in investing activities was US$19.5 million in 2013, consisting of purchases of property and equipment, including computers and servers, of approximately US$9 million in connection with the expansion of our network of learning centers; purchase of time deposits of approximately US$17 million; purchase of short-term investment in the amount of approximately US$11 million; and partially offset by the maturity of short-term investment of approximately US$11 million, maturity of time deposits of approximately US$6 million, and proceeds from repayment of housing loans from employees in the amount of approximately US$1 million.

Net cash used in investing activities was US$7.9 million in 2012, consisting of purchases of property and equipment, including computers and servers, of approximately US$7 million in connection with the expansion of our network of learning centers, purchase of time deposits of approximately US$1 million and issuance of housing loans to employees in the amount of approximately US$1 million, partially offset by the maturity of time deposits in the amount of approximately US$1 million. Our loans to employees were aimed at helping them finance their purchase of apartments. Our loans issued to our employees in 2012 have been collected as of December 31, 2013.

***Financing Activities***

Net cash provided by financing activities in 2014 was US$106.5 million, which was primarily attributable to the gross proceeds from our initial public offering of approximately US$96.2 million, payment of costs related to our initial public offering in the amount of US$3.5 million and net proceeds from our concurrent private placement of US$13.5 million in April.

Net cash used in financing activities in 2013 was US$0.6 million, which was primarily attributable to the payment of costs related to our initial public offering in the amount of US$0.5 million.

Net cash used in financing activities in 2012 was US$0.2 million.

***Capital Expenditures***

Our capital expenditures are primarily related to leasehold improvements and investments in computers, network equipment and software. Our capital expenditures were US$7.2 million, US$9.1 million and US$8.0 million in 2012, 2013 and 2014, respectively. We intend to continue to lease facilities for our learning centers in order to allocate our capital resources cost-efficiently. We may make acquisitions of businesses and properties that complement our operations when suitable opportunities arise. We expect our capital expenditures will continue to be significant for the near future as we continue to expand our network of learning centers. We expect to fund our future capital expenditures with our current cash, cash equivalents and time deposits and anticipated cash flow from operations.

**Holding Company Structure**

We are a holding company with no material operations of our own. We conduct our operations primarily through our wholly-owned subsidiaries in China. As a result, our ability to pay dividends depends upon dividends paid by our wholly-owned subsidiaries. If our wholly-owned subsidiaries or any newly formed subsidiaries incur any debt in the future, the instruments governing their debt may restrict their ability to pay dividends to us. In addition, our wholly-owned subsidiaries are permitted to pay dividends to us only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. Under PRC law, each of our subsidiaries is required to set aside at least 10% of its after-tax profits each year, if any, to fund a statutory surplus reserve until such reserve reaches 50% of its registered capital. Although the statutory surplus reserves can be used to increase the registered capital and eliminate future losses in excess of retained earnings of the respective companies, the reserve funds are not distributable as cash dividends except in the event of liquidation. As a result of these PRC laws and

regulations, as of December 31, 2014, we had US$5.1 million in statutory surplus reserves that are not distributable as cash dividends. Our PRC subsidiaries have not historically paid any dividends to our offshore entities from their accumulated profits. However, we do not expect that the statutory surplus reserve requirement will materially limit our ability to pay dividends to our shareholders or our plan to expand our business because we are only required to set aside an additional US$15.6 million to satisfy the maximum requirement of statutory surplus reserves for all of our PRC subsidiaries. In addition, our private schools requiring reasonable returns are required to appropriate no less than 25% of their net income to a statutory development fund, whereas in the case of private schools requiring no reasonable return, this amount shall be no less than 25% of the annual increase of their net assets. As of December 31, 2014, we had US$1.1 million in statutory development fund that are not distributable as cash dividends.

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## C. Research and Development, Patents and Licenses, etc.

### Research and Development

Building a reliable, scalable and secure technology infrastructure is crucial to our ability to support our live lecture broadcasts, online TTS and the various services that we provide to our students. We manage our lecture delivery system and TTS using a combination of commercially available software, hardware systems and proprietary technology. Since 2006, we have established a powerful online platform that enables thousands of students to simultaneously log onto our TTS and participate in activities online.

We have developed our CRM software in-house to manage our student and corporate employer information, as well as to integrate our key administrative functions. We rely on our internal IT resources to upgrade the CRM system as needed.

Our research and development expenses primarily consist of a portion of the personnel costs of our instructors as determined based on the amount of time that they devote to research and development-related activities, as well as the personnel costs of our software engineers. Our research and development expenses were US$1.8 million, US$3.8 million and US$5.4 million in 2012, 2013 and 2014, respectively.

### Intellectual Property

Our trademarks, copyrights, domain names, trade secrets and other intellectual property rights distinguish our courses and services from those of our competitors and contribute to our ability to compete in our target markets. We rely on a combination of copyright and trademark law, trade secret protection and confidentiality agreements with senior executive officers and most other employees, to protect our intellectual property rights. In addition, we require certain of our senior executive officers and other employees to enter into agreements with us under which they acknowledge that all inventions, utility models, designs, know-how, copyrights and other forms of intellectual property made by them within the scope of their employment with us, pursuant to job assignments or using our materials and technology, or during the one year after their employment that relates to their employment with us, are our property and they should assign the same to us if we so require. We also regularly monitor any infringement or misappropriation of our intellectual property rights.

As of December 31, 2014, we had registered 202 domain names relating to our business, including our *www.tarena.com.cn*, *www.it211.com.cn*, *TMOOC.cn* and *jobshow.cn* websites, with the Internet Corporation for Assigned Names and Numbers and China Internet Network Information Center. Tarena Tech holds 20 registered software copyrights, two trademarks and 200 registered domain names including *www.tarena.com.cn*. Beijing Tarena holds two domain names, namely *www.it211.com.cn* and *TMOOC.cn.*

## D. Trend Information

Other than as disclosed elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events for the period from January 1, 2014 to December 31, 2014 that are reasonably likely to have a material effect on our net revenues, income, profitability, liquidity or capital resources, or that would cause the disclosed financial information to be not necessarily indicative of future operating results or financial conditions.

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**E. Off-Balance Sheet Arrangements**

Starting from 2011, Chuanbang, a credit-sourcing company in China owned by Mr. Shaoyun Han, our chief executive officer, began to offer person-to-person lending services to our students to help them pay for our tuition fees. Under the person-to-person lending service, we serve as the guarantor of the loans taken out by students. Starting from April 2013, we had stopped providing guarantees for any new student loans arranged by Chuanbang. See Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Transactions with Shareholders and Affiliates Transactions with Chuanbang. As of December 31, 2012, 2013 and 2014, our maximum exposure to guarantees of student loans obtained through Chuanbang was US$7.4 million, US$4.4 million and US$0.2 million, respectively.

Other than the above, we have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as shareholders equity, or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

**F. Tabular Disclosure of Contractual Obligations**

The following table sets forth our contractual obligations as of December 31, 2014:

| | | Payment due by December 31, | | | | | |
|---|---|---|---|---|---|---|---|
| | **Total** | **2015** | **2016** | **2017** | **2018** | **2019** | **2020 and thereafter** |
| | | | **(in thousands of US$)** | | | | |
| Operating lease commitments[(1)] | 38,185 | 12,398 | 8,770 | 6,259 | 3,623 | 2,332 | 4,803 |

Note:

(1) Represents our non-cancelable leases for our offices and learning centers.

**G. Safe Harbor**

This annual report on Form 20-F contains forward-looking statements that involve risks and uncertainties. All statements other than statements of historical facts are forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements.

You can identify these forward-looking statements by words or phrases such as may, will, expect, anticipate, aim, estimate, intend, plan, believe, likely to or other similar expressions. We have based these forward-looking state

largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. These forward-looking statements include, but are not limited to, statements about:

our goals and growth strategies;

our expectations regarding demand for and market acceptance of our courses;

our ability to retain and increase our student enrollments;

our ability to maintain and increase the utilization rate of our learning centers;

our ability to offer new courses in existing and new subject areas;

our ability to maintain and increase the tuition fees of our courses;

our ability to deepen and expand our corporate employer relationships;

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our ability to maintain our relationships with universities and colleges;

our future business development, results of operations and financial condition;

the expected growth of, and trends in, the markets for our services in China;

relevant government policies and regulations relating to our corporate structure, business and industry; and

assumptions underlying or related to any of the foregoing.

You should read thoroughly this annual report and the documents that we refer to in this annual report with the understanding that our actual future results may be materially different from and worse than what we expect. Other sections of this annual report include additional factors which could adversely impact our business and financial performance. Moreover, we operate in an evolving environment. New risk factors and uncertainties emerge from time to time and it is not possible for our management to predict all risk factors and uncertainties, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. We qualify all of our forward-looking statements by these cautionary statements.

You should not rely upon forward-looking statements as predictions of future events. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### A. Directors and Executive Officers

The following table sets forth information regarding our executive officers and directors as of the date of this annual report.

| Directors and Executive Officers | Age | Position/Title |
|---|---|---|
| Shaoyun Han | 44 | Founder, chairman and chief executive officer |
| Jianguang Li | 50 | Director |
| Yongji Sun | 50 | Independent director |
| Xiaosong Zhang | 51 | Independent director |
| Ya-Qin Zhang | 49 | Independent director |
| Suhai Ji | 38 | Chief financial officer |
| Ying Sun | 38 | Vice president |
| Yi Li | 39 | Vice president |
| Yinan Qi | 36 | Vice president |
| Jiangyou Wang | 37 | Vice president |
| Xiaolan Tang | 35 | General manager |

*Shaoyun Han* is our founder and has served as chairman of our board of directors and chief executive officer since our inception. Before founding Tarena in September 2002, Mr. Han was deputy chief engineer and director of the software division of AsiaInfo-Linkage between 1995 and 2002, responsible for software research and development and corporate management. Mr. Han received a bachelor s degree in computer application from Jilin University in China.

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*Jianguang Li* is our director. Mr. Li has served as our director since January 2004. Mr. Li has been a partner of IDG Capital Partners since March 2006, responsible for providing venture capital and private equity investment-related advice. Between 1999 and 2006, Mr. Li served as a vice-president of IDG Technology Venture Investment Inc. Prior to joining IDG in 1999, Mr. Li worked in Crosby Assets Management Limited as an investment manager. Mr. Li received a bachelor s degree in management from Peking University and a master s of science degree from the University of Guelph.

*Yongji Sun* has served as our independent director since April 2014. Mr. Sun currently serves as the chairman of Dilato Infotech Inc. Between 2011 and 2014, Mr. Sun served as the chief executive officer of Shangxue Education Technology Inc. Between 2005 and 2011, Mr. Sun served as executive vice president of special projects and strategic relationships at HiSoft Technology International Ltd., or HiSoft . Prior to joining HiSoft in November 2005, Mr. Sun founded Beijing Tianhai Hongye International Software Co., Ltd. (Ensemble) in 2002 and served as its chief executive officer from 2003 to 2005. He founded and served as chief executive officer of Newland Network Co. from 2000 to 2002. He founded Lotus China in 1993 and served as the head of the research and development center until 1998. Mr. Sun received a bachelor s degree from North Eastern Machinery Institute in 1985, a master s degree in Computer Science from Nanjing Aerospace & Aeronautic University in 1988, and received a master of business administration from Babson College in 2000.

*Xiaosong Zhang* has served as our independent director since April 2014. Mr. Zhang currently serves as the chief financial officer of Momo Inc., a NASDAQ-listed company. Mr. Zhang served as an independent director and chairman of the audit committee of Sungy Mobile Limited, a NASDAQ-listed mobile internet company, between November 2013 and July 2014. Mr. Zhang served as the chief financial officer of iSoftStone Holdings Limited, a NYSE-listed company, between July 2010 and April 2014, and was an independent director of iSoftStone between February 2010 and July 2010. Prior to joining iSoftStone, Mr. Zhang served as chief financial officer of BJB Career Education Company Limited from 2009 to June 2010, as chief financial officer of Emarket Holding Group, Ltd. from 2008 to 2009, as chief financial officer of Chinacars, Inc. from 2007 to 2008 and as chief financial officer of Vimicro International Corporation, a NASDAQ-listed company, from 2004 to 2007. From 2000 to 2004, Mr. Zhang was a manager and then a senior manager at the Beijing office of PricewaterhouseCoopers. From 1995 to 1999, Mr. Zhang was an auditor and then a senior auditor at the Los Angeles office of KPMG LLP. Mr. Zhang received his master degree in accountancy from University of Illinois, his master degree in professional meteorology from Saint Louis University, and his bachelor degree in meteorology from Peking University. Mr. Zhang is a Certified Public Accountant in the State of California.

*Mr. Ya-Qin Zhang* has served as our independent director since April 2014. Mr. Zhang has served as president of Baidu, Inc., a NASDAQ-listed company, since September 2014. Mr. Zhang has served as a director of ChinaCache International Holdings Ltd., a NASDAQ-listed company, since September 2010. Mr. Zhang served as an independent director and member of the audit committee of Autohome Inc., a NYSE-listed company, between December 2013 and January 2015. Mr. Zhang served as the chairman of Microsoft Asia-Pacific R&D Group between 2005 and September 2014 and was in charge of the research and development of Microsoft Corporation in the Asia-Pacific region. Mr. Zhang is one of the founding members of the Microsoft Research Asia lab, where he served as managing director and chief scientist, and he also founded the Advanced Technology Center in 2003. Before joining Microsoft in 1999, Mr. Zhang was a director for the Multimedia Technology Laboratory at Sarnoff Corp. and worked as a senior technical staff member for GTE Laboratories Inc. and Contel Corp. From 2009 to 2012, Mr. Zhang served as an independent director of China Real Estate Information Corporation, a provider of real estate information, consulting and online services in China. Mr. Zhang received his bachelor s and master s degrees in electrical engineering from the University of Science and Technology of China and a Ph.D. in electrical engineering from George Washington University.

*Suhai Ji* is our chief financial officer. Mr. Ji has served as our chief financial officer since September 2013. From November 2010 to September 2013, Mr. Ji served as the chief financial officer of NQ Mobile Inc., a NYSE-listed company. From June 2009 to November 2010, Mr. Ji was a director in the NYSE Beijing Representative Office where he was responsible for NYSE s business development in China. From 2005 to 2009, Mr. Ji worked as an associate and vice president in investment banking at Deutsche Bank AG, Hong Kong Branch. Prior to that, Mr. Ji was a management consultant at A.T. Kearney Beijing Office from 2003 to 2005. Mr. Ji received a bachelor s degree in economics and a master s degree in international economics and finance from Brandeis University, as well as an MBA degree in finance from Columbia Business School.

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*Ying Sun* is our vice president. Ms. Sun has served as our vice president since December 2009, responsible for our nation-wide operations. Ms. Sun joined us in June 2005 as the general manager of our Beijing learning centers. Between 2007 and 2009, she was the general manager of our northern region. From 1999 to 2005, Ms. Sun worked in Gloria Hotels and Resorts, serving in various sales and human resources-related roles. Ms. Sun received a bachelor s degree in tourism economics management from Dongbei University of Finance and Economics in China. Ms. Sun is the spouse of Mr. Shaoyun Han.

*Yi Li* is our vice president. Mr. Li has served as our vice president since January 2012, responsible for our teaching and research efforts. Mr. Li joined us in November 2008, serving as our director of teaching between 2008 and 2012. Prior to joining us, Mr. Li was a senior teacher and later a general supervisor of the Java training course at Oriental Standard between 2005 and 2008. From 2004 to 2005, Mr. Li was a senior development engineer at IBM China R&D center. Mr. Li received a bachelor s degree in Automation from the Institute of Technology of Taiyuan and a master s degree in software engineering from Beihang University.

*Yinan Qi* is our vice president. Mr. Qi has served as our vice president since September 2013, responsible for student recruitment through retail channels. Mr. Qi served as our general manager of northern region between 2010 and 2015, responsible for our operations in Northern China. Mr. Qi joined us in March 2007, previously serving in roles including the deputy general manager of northern region, deputy general manager of our Beijing learning centers and director of our Hangzhou learning center. Prior to joining us, Mr. Qi served as the general manager of the Beihang campus of GAMFE between 2005 and 2006 and as director of technology at Zhonghe Wangxun (Beijing) Information Technology Co., Ltd. between 2002 and 2005. Mr. Qi received a bachelor s degree in optoelectronic technology from China Jiliang University and a master s degree in multimedia technologies from the University of Science and Technology Beijing.

*Jiangyou Wang* is our vice president. Mr. Wang has served as our vice president since February 2015, responsible for our cooperation with universities and colleges. Mr. Wang served as our general manager of southern region between January 2010 and February 2015, responsible for our operations in Southern China. Mr. Wang joined us in March 2008 as the director of our Hangzhou learning center before being promoted to his current position. Between 2007 and 2008, Mr. Wang founded Hangzhou Daowei Information Technology Co., Ltd., an IT operating services provider. Between 2006 and 2007, Mr. Wang co-founded Hangzhou Beiteng Technology Co., Ltd., a business simulation and course content provider. Between 2005 and 2006, Mr. Wang served as general manager of Talking Street English School in Ningbo. Between 2001 and 2004, Mr. Wang worked in Hangzhou New Grand Software Co., Ltd. as a regional sales director and general manager of the Ningbo branch. Mr. Wang received an associate s degree in sales and marketing management from Zhejiang Industrial & Commercial University.

*Xiaolan Tang* is our general manager of operations, and he has served in such role since 2015. Mr. Tang served as our general manager of central and western region between 2011 and 2015, responsible for our operations in central and western China. Mr. Tang joined us in October 2007, serving as marketing director of our Beijing branch, marketing director of the northern region and vice-general manager of northern region before being promoted to his current position. From 2006 to 2007, Mr. Tang worked as the director of marketing at Beijing Blue Point Technology Co., Ltd. From 2002 to 2006, Mr. Tang served as executive assistant to the general manager and training school headmaster of Jilin Education Technology Co., Ltd. Mr. Li received a bachelor s degree in management from Jilin University.

**B. Compensation of Directors and Executive Officers**

For the fiscal year ended December 31, 2014, we paid an aggregate of approximately US$776 thousand in cash to our executive officers, and we paid an aggregate of US$29 thousand in cash to our non-executive directors. For share incentive grants to our directors and executive officers, see Share Incentive Plan.

Our PRC subsidiaries and consolidated affiliated entities are required by law to make contributions equal to certain percentages of each employee s salary for his or her pension insurance, medical insurance, housing fund, unemployment and other statutory benefits. Other than the above-mentioned statutory contributions mandated by applicable PRC law, we have not set aside or accrued any amount to provide pension, retirement or other similar benefits to our executive officers and directors.

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**Employment Agreements and Indemnification Agreements**

We have entered into employment agreements with each of our executive officers. Under these agreements, each of our executive officers is employed for a specified time period. We may terminate employment for cause, at any time, without advance notice or remuneration, for certain acts of the executive officer, such as conviction or plea of guilty to a felony or any crime involving moral turpitude, negligent or dishonest acts to our detriment, or misconduct or a failure to perform agreed duties. We may also terminate an executive officer s employment without cause upon three-month advance written notice. In such case of termination by us, we will provide severance payments to the executive officer as expressly required by applicable law of the jurisdiction where the executive officer is based. The executive officer may resign at any time with a three-month advance written notice.

Each executive officer has agreed to hold, both during and after the termination or expiry of his or her employment agreement, in strict confidence and not to use, except as required in the performance of his or her duties in connection with the employment or pursuant to applicable law, any of our confidential information or trade secrets, any confidential information or trade secrets of our clients or prospective clients, or the confidential or proprietary information of any third party received by us and for which we have confidential obligations. The executive officers have also agreed to disclose in confidence to us all inventions, designs and trade secrets which they conceive, develop or reduce to practice during the executive officer s employment with us and to assign all right, title and interest in them to us, and assist us in obtaining and enforcing patents, copyrights and other legal rights for these inventions, designs and trade secrets.

In addition, each executive officer has agreed to be bound by non-competition and non-solicitation restrictions during the term of his or her employment and typically for two years following the last date of employment. Specifically, each executive officer has agreed not to (i) approach our suppliers, clients, customers or contacts or other persons or entities introduced to the executive officer in his or her capacity as a representative of us for the purpose of doing business with such persons or entities that will harm our business relationships with these persons or entities; (ii) assume employment with or provide services to any of our competitors, or engage, whether as a principal, partner, licensor or otherwise, any of our competitors, without our express consent; or (iii) seek directly or indirectly, to solicit the services of any of our employees who is employed by us on or after the date of the executive officer s termination, or in the year preceding such termination, without our express consent.

We have also entered into indemnification agreements with each of our directors and executive officers. Under these agreements, we agree to indemnify our directors and executive officers against certain liabilities and expenses incurred by such persons in connection with claims made by reason of their being a director or officer of our company.

**Share Incentive Plan**

***The 2008 Plan***

We have adopted the 2008 Plan in September 2008. The purpose of the 2008 Plan is to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentives to selected directors, officers, employees and consultants and to promote the success of Tarena s business by offering these individuals an opportunity to acquire a proprietary interest in Tarena.

Under the 2008 Plan, the maximum aggregate number of shares which may be issued is 8,184,990. As of February 28, 2015, options to purchase 6,267,635 Class A ordinary shares are issued and outstanding, and there are 130,906 Class A ordinary shares available for future issuance upon the exercise of future grants under the 2008 Plan.

Options to purchase a total of 3,815,000 Class A ordinary shares were granted prior to our adoption of the 2008 Plan. Such options were ratified by our board and included in the 2008 Plan.

The following paragraphs summarize the terms of the 2008 Plan.

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***Types of Awards.*** The 2008 Plan permits the awards of options, restricted shares (or share appreciation rights or other similar awards) and rights to purchase restricted shares.

***Plan Administration.*** Our board of directors or a committee appointed by our board will administer the 2008 Plan. The committee or the full board of directors, as applicable, will determine the participants to receive awards, the type and number of awards to be granted to each participant, and the terms and conditions of each award grant, among other things.

***Award Agreement.*** Awards granted under the 2008 Plan are evidenced by an award agreement that sets forth terms, conditions and limitations for each award, which may include the term of the award and the provisions applicable in the event of the grantee s employment or service terminates.

***Eligibility.*** We may grant awards to our employees, directors and consultants of our company, as well as trusts or companies established in connection with any of our employee benefit plan for the benefit of our employees, directors or consultants.

***Acceleration.*** The plan administrator may accelerate the vesting or exercisability of an option or lapsing of a repurchase or redemption right to which restricted shares may be subject.

***Vesting Schedule.*** In general, the plan administrator determines the vesting schedule, which is specified in the relevant award agreement.

***Exercise of Options.*** The plan administrator determines the exercise price for each award, which is stated in the award agreement. The vested portion of option will expire if not exercised prior to the time as the plan administrator determines at the time of its grant. However, the maximum exercisable term is the tenth anniversary after the date of a grant.

***Transfer Restrictions.*** Awards may not be transferred in any manner by the recipient other than by will or applicable laws of descent and distribution or pursuant to a qualified domestic relations order and by trusts or companies established in connection with any of our employee benefit plan for the benefit of an employee, director or consultant, except as otherwise provided by the plan administrator.

***Termination of Employment or Service.*** In the event that a grantee ceases employment with us or ceases to provide services to us, any vested options will generally terminate after a period of time following the termination of employment if the grantee does not exercise the options during this period.

***Restrictions on Issue of Shares.*** Options granted under the 2008 Plan can only be exercised and ordinary shares can only be issued upon the occurrence of (i) the consummation of a qualified initial public offering, (ii) the consummation of a liquidation event or (iii) the expiry of the five year period commencing from the grant date.

***Termination of the 2008 Plan.*** Unless terminated earlier, the 2008 Plan will terminate automatically in 2018. Our board of directors has the authority to amend or terminate the plan subject to shareholder approval if required by applicable law.

***The 2014 Plan***

We adopted the 2014 Plan in February 2014. The maximum aggregate number of shares which may be issued pursuant to all awards under the 2014 Plan, or the Award Pool, is 1,833,696, provided that the shares reserved in the

Award Pool shall be increased on the first day of each calendar year, commencing with January 1, 2015, if the unissued shares reserved in the Award Pool on such day account for less than 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year, as a result of which increase the shares unissued and reserved in the Award Pool immediately after each such increase shall equal 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year. The maximum aggregate number of Class A ordinary shares which may be issued pursuant to our 2014 Plan was 1,210,250 as of January 1, 2015 As of February 28, 2015, options to purchase 1,754,784 Class A ordinary shares are issued and outstanding under the 2014 Plan, and 29,724 restricted shares were granted under the 2014 Plan. The following paragraphs summarize the terms of the 2014 Plan.

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***Types of Awards.*** The 2014 Plan permits the awards of options, restricted shares and restricted share units.

***Plan Administration.*** Our board or a committee of one or more members of our board duly authorized for the purpose of the 2014 Plan can act as the plan administrator.

***Award Agreement.*** Options, restricted shares or restricted share units granted under the 2014 Plan are evidenced by an award agreement that sets forth the terms, conditions and limitations for each grant.

***Eligibility.*** We may grant awards to our employees, consultants or directors. However, we may grant options that are intended to qualify as incentive share options only to our employees and employees of our parent companies and subsidiaries.

***Acceleration of Awards upon Change in Control.*** If a change in control, liquidation or dissolution of our company occurs, the plan administrator may, in its sole discretion, provide for (i) all awards outstanding to terminate at a specific time in the future and give each participant the right to exercise the vested portion of such awards during a specific period of time, or (ii) the purchase of any award for an amount of cash equal to the amount that could have been attained upon the exercise of such award, or (iii) the replacement of such award with other rights or property selected by the plan administrator in its sole discretion, or (iv) payment of award in cash based on the value of ordinary shares on the date of the change-in-control transaction plus reasonable interest.

***Exercise of Options.*** The plan administrator determines the exercise price for each award, which is stated in the award agreement. The vested portion of option will expire if not exercised prior to the time as the plan administrator determines at the time of its grant. However, the maximum exercisable term is the tenth anniversary after the date of a grant.

***Exercise Price of Options.*** The exercise price in respect of any option shall be determined by the plan administrator and set forth in the award agreement which may be a fixed or variable price related to the fair market value of the shares. The exercise price per share subject to an option may be amended or adjusted in the absolute discretion of the plan administrator, the determination of which shall be final, binding and conclusive.

***Vesting Schedule.*** In general, the plan administrator determines the vesting schedule, which is set forth in the award agreement.

***Transfer Restrictions.*** Awards may not be transferred in any manner by the recipient other than by will or the laws of descent and distribution, except as otherwise provided by the plan administrator.

***Termination.*** Unless terminated earlier, the 2014 Plan will terminate automatically in 2024.

The following table summarizes, as of February 28, 2015, the outstanding options granted to our directors and executive officers under our share plan.

| Name | Ordinary Shares Underlying Options Awarded | Exercise Price (US$/Share) | Date of Grant | Date of Expiration |
|---|---|---|---|---|
| Shaoyun Han | 600,000 | 0.158 | January 1, 2008 | December 31, 2017 |
| | 1,523,020 | 1.000 | August 26, 2011 | August 25, 2021 |

| | | | | |
|---|---|---|---|---|
| | 1,326,980 | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | December 31, 2022 |
| | 916,848 | 1.830 | February 20, 2014 | February 19, 2024 |
| Jianguang Li | * | 0.058 | January 1, 2004 | December 31, 2013 |
| Yongji Sun | | | | |

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| Name | Ordinary Shares Underlying Options Awarded | Exercise Price (US$/Share) | Date of Grant | Date of Expiration |
|---|---|---|---|---|
| Xiaosong Zhang | | | | |
| Ya-Qin Zhang | | | | |
| Suhai Ji | * | 1.830 | September 16, 2013 | September 15, 2023 |
| | * | 1.830 | February 20, 2014 | December 31, 2022 |
| Ying Sun | * | 0.058 | September 1, 2005 | August 31, 2015 |
| | * | 0.058 | February 20, 2007 | January 31, 2017 |
| | * | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | February 1, 2017 |
| Yi Li | * | 0.890 | March 1, 2009 | February 28, 2019 |
| | * | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | December 31, 2022 |
| Yinan Qi | * | 0.890 | June 1, 2009 | May 31, 2019 |
| | * | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | December 31, 2022 |
| Jiangyou Wang | * | 0.890 | June 1, 2009 | May 31, 2019 |
| | * | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | December 31, 2022 |
| Xiaolan Tang | * | 0.890 | June 1, 2009 | May 31, 2019 |
| | * | 1.830 | January 1, 2013 | December 31, 2022 |
| | * | 4.360 | February 20, 2014 | January 1, 2017 |
| Total | 5,970,028 | | | |

* The aggregate number of ordinary shares underlying the outstanding options held by this individual is less than 1% of our total outstanding shares as of February 28, 2015.

The following table summarizes, as of February 28, 2015, the outstanding restricted shares we granted to our directors and executive officers under the 2014 Plan.

| Name | Number of Class A Ordinary Shares Underlying Restricted Shares | Date of Grant |
|---|---|---|
| Shaoyun Han | | |
| Jianguang Li | | |
| Yongji Sun | * | April 3, 2014 |
| Xiaosong Zhang | * | April 3, 2014 |
| Ya-Qin Zhang | * | April 3, 2014 |
| Suhai Ji | | |
| Ying Sun | | |
| Yi Li | | |
| Yinan Qi | | |
| Jiangyou Wang | | |

| | |
|---|---|
| Xiaolan Tang | |
| | |
| Total | 27,780 |

* Less than 1% of our total outstanding shares as of February 28, 2015.
As of February 28, 2015, other individuals as a group hold outstanding options to purchase a total of 2,052,391 Class A ordinary shares of our company, with exercise prices ranging from US$0.058 to US$4.360 per share, as well as 1,944 restricted shares of our company.

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## C. Board Practices

### Board of Directors

Our board of directors currently consists of five directors. A director is not required to hold any shares in our company. Subject to the rules of the NASDAQ Global Select Market and disqualificiation by the chairman of the relevant board meeting, a director may vote with respect to any contract, proposed contract, or arrangement in which he or she is materially interested. The board may exercise all the powers of the company to borrow money, mortgage its business, property and uncalled capital, and issue debentures or other securities whenever money is borrowed or as security for any obligation of the company or of any third party. There is no age limit requirement for directors. The service agreements between us and the directors do not provide benefits upon termination of their services.

### Committees of the Board of Directors

We have an audit committee, a compensation committee and a nominating and corporate governance committee under the board of directors. We have adopted a charter for each of the three committees. Each committee s members and functions are described below.

***Audit Committee.*** Our audit committee consists of Messrs. Xiaosong Zhang, Yongji Sun and Ya-Qin Zhang and is chaired by Mr. Xiaosong Zhang. Each member of our audit committee satisfies the independence requirements of Rule5605(c)(2) of the NASDAQ Stock Market Rules and meets the independence standards under Rule 10A-3 under the Securities Exchange Act of 1934, as amended, or the Exchange Act. We have determined that Mr. Xiaosong Zhang qualifies as an audit committee financial expert. The audit committee oversees our accounting and financial reporting processes and the audits of the financial statements of our company. The audit committee is responsible for, among other things:

- selecting the independent registered public accounting firm and pre-approving all auditing and non-auditing services permitted to be performed by the independent registered public accounting firm;
- reviewing with the independent registered public accounting firm any audit problems or difficulties and management s response;
- reviewing and approving all proposed related party transactions, as defined in Item 404 of Regulation S-K under the Securities Act;
- discussing the annual audited financial statements with management and the independent registered public accounting firm;
- reviewing major issues as to the adequacy of our internal controls and any special audit steps adopted in light of material control deficiencies;
- reviewing and reassessing annually the adequacy of our audit committee charter;

meeting separately and periodically with management and the independent registered public accounting firm;

monitoring compliance with our code of business conduct and ethics, including reviewing the adequacy and effectiveness of our procedures to ensure proper compliance; and

reporting regularly to the board.

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***Compensation Committee.*** Our compensation committee consists of Messrs. Ya-Qin Zhang, Yongji Sun and Xiaosong Zhang, and is chaired by Ya-Qin Zhang. Each member of our compensation committee satisfies the independence requirements of Rule5605(c)(2) of the NASDAQ Stock Market Rules. The compensation committee assists the board in reviewing and approving the compensation structure, including all forms of compensation, relating to our directors and executive officers. Our chief executive officer may not be present at any committee meeting during which their compensation is deliberated upon. The compensation committee is responsible for, among other things:

- reviewing and approving, or recommending to the board for its approval, the compensation for our chief executive officer and other executive officers;
- reviewing and recommending to the board for determination with respect to the compensation of our non-employee directors;
- reviewing and recommending to the board for determination with respect to the compensation of our non-employee directors
- selecting compensation consultant, legal counsel or other adviser only after taking into consideration all factors relevant to that person s independence from management.

***Nominating and Corporate Governance Committee.*** Our nominating and corporate governance committee consists of Messrs. Yongji Sun, Xiaosong Zhang and Ya-Qin Zhang, and is chaired by Mr. Yongji Sun. Each member of our nominating and corporate governance committee satisfies the independence requirements of Rule5605(c)(2) of the NASDAQ Stock Market Rules. The nominating and corporate governance committee assists the board in selecting individuals qualified to become our directors and in determining the composition of the board and its committees. The nominating and corporate governance committee is responsible for, among other things:

- recommending nominees to the board for election or re-election to the board, or for appointment to fill any vacancy on the board;
- reviewing annually with the board the current composition of the board with regards to characteristics such as independence, age, skills, experience and availability of service to us;
- selecting and recommending to the board the names of directors to serve as members of the audit committee and the compensation committee, as well as of the nominating and corporate governance committee itself;
- developing and reviewing the corporate governance principles adopted by the board and advising the board with respect to significant developments in the law and practice of corporate governance and our compliance with such laws and practices; and

evaluating the performance and effectiveness of the board as a whole.

**Duties of Directors**

Under Cayman Islands law, our directors have a duty of loyalty to act honestly in good faith with a view to our best interests. Our directors also have a duty to exercise the skill they actually possess and such care and diligence that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association. A shareholder may have the right to seek damages in our name if a duty owed by our directors is breached.

**Terms of Directors and Officers**

Our officers are elected by and serve at the discretion of the board. Our directors are not subject to a term of office and hold office until such time as they resign or are removed from office by ordinary resolution of our shareholders. A director will be removed from office automatically if, among other things, the director (i) becomes bankrupt or makes any arrangement or composition with his creditors; or (ii) dies or is found by our company to be of unsound mind.

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**D. Employees**

We have dual headquartered in Beijing and Hangzhou, where our instructors, software engineers and certain general and administrative staff are based. We have divided our national network of learning centers into three regions, namely northern region, southern region, and central and western region, and we have regional offices that are responsible for managing the daily operations of learning centers located within each territory.

We had a total of 2,352, 3,104 and 3,904 employees as of December 31, 2012, 2013 and 2014, respectively. As of December 31, 2014, we had 366 employees in Beijing, 235 employees in Hangzhou and 3,303 employees in other areas within China. The following table sets forth the number of our employees, categorized by function, as of December 31, 2014:

| Functions | Number of Employees |
|---|---|
| Teaching and content development | 994 |
| Selling and marketing | 1,773 |
| Career development | 231 |
| Employer cooperation | 164 |
| General and administration | 742 |
| Total | 3,904 |

As required by regulations in China, we participate in various employee social security plans that are organized by municipal and provincial governments, including pension, unemployment insurance, childbirth insurance, work-related injury insurance, medical insurance and housing insurance. We are required under PRC law to make contributions from time to time to employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the local government.

Our employees are not covered by any collective bargaining agreement. We believe that we maintain a good working relationship with our employees, and we have not experienced any significant labor disputes.

**E. Share Ownership**

Except as specifically noted, the following table sets forth information with respect to the beneficial ownership of our ordinary shares as of February 28, 2015 by:

each of our directors and executive officers; and

each person known to us to own beneficially more than 5% of our ordinary shares.

The calculations in the table below are based on 52,445,782 ordinary shares outstanding as of February 28, 2015, comprising of 23,712,758 Class A ordinary shares and 28,733,024 Class B ordinary shares.

Beneficial ownership is determined in accordance with the rules and regulations of the SEC. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, we have included shares that

the person has the right to acquire within 60 days, including through the exercise of any option, warrant or other right or the conversion of any other security. These shares, however, are not included in the computation of the percentage ownership of any other person.

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| | Ordinary Shares Beneficially Owned | | | | |
|---|---|---|---|---|---|
| | Class A ordinary Shares | Class B ordinary Shares | Total ordinary shares on an as-converted basis | % of total ordinary shares on an as-converted basis | % of aggregate voting power |
| **Directors and Executive Officers:**** | | | | | |
| Shaoyun Han(1) | 4,419,264 | 9,800,498 | 14,219,762 | 25.7 | 32.6 |
| Jianguang Li(2) | * | | * | * | * |
| Yongji Sun(3) | * | | * | * | * |
| Xiaosong Zhang(4) | * | | * | * | * |
| Ya-Qin Zhang(5) | * | | * | * | * |
| Suhai Ji | * | | * | * | * |
| Ying Sun(6) | 4,419,264 | 9,800,498 | 14,219,762 | 25.7 | 32.6 |
| Yinan Qi | * | | * | * | * |
| Yi Li | * | | * | * | * |
| Jiangyou Wang | | | | * | * |
| Xiaolan Tang | * | | * | * | * |
| All directors and executive officers as a group | 5,106,639 | 9,800,498 | 14,907,137 | 26.6 | 32.8 |
| **Principal and Selling Shareholders:** | | | | | |
| Goldman Sachs funds(7) | | 10,914,852 | 10,914,852 | 20.8 | 35.1 |
| IDG funds(8) | | 6,737,674 | 6,737,674 | 12.8 | 21.7 |
| Learningon Limited(9) | 1,500,000 | 6,060,000 | 7,560,000 | 14.4 | 20.0 |
| Connion Capital Limited(10) | 2,439,014 | 2,594,439 | 5,033,453 | 9.2 | 9.1 |

Notes:

* Less than 1%.

** Except for Mr. Jianguang Li, Mr. Yongji Sun, Mr. Xiaosong Zhang and Mr. Ya-Qin Zhang, the business address of our directors and executive officers is Suite 10017, Building E, Zhongkun Plaza, A18 Bei San Huan West Road, Haidian District, Beijing, 100098, PRC.

For each person and group included in this column, percentage of voting power is calculated by dividing the voting power beneficially owned by such person or group by the voting power of all of our Class A and Class B ordinary shares as a single class. Each holder of Class A ordinary shares is entitled to one vote per share and each holder of our Class B ordinary shares is entitled to ten votes per share on all matters submitted to them for a vote. Our Class A ordinary shares and Class B ordinary shares vote together as a single class on all matters submitted to a vote of our shareholders, except as may otherwise be required by law. Our Class B ordinary shares are convertible at any time by the holder thereof into Class A ordinary shares on a one-for-one basis.

(1) Represents (i) 6,060,000 Class B ordinary shares held by Learningon Limited, (ii) 2,594,439 Class B ordinary shares held by Connion Capital Limited, (iii) 1,146,059 Class B ordinary shares held by Techedu Limited, a British Virgin Islands company wholly owned by Mr. Han, (iv) 2,439,014 Class A ordinary shares that Connion Capital Limited may purchase upon exercise of options within 60 days of February 28, 2015 and (v) 480,250

Class A ordinary shares that Beeson Services Limited may purchase upon exercise of options within 60 days of February 28, 2015. Each of Connion Capital Limited and Learningon Limited is ultimately wholly owned by HANQQ Trust. TMF (Cayman) Ltd. is the trustee of HANQQ Trust, with Mr. Shaoyun Han as settlor and Mr. Shaoyun Han and his family as beneficiaries. Beeson Services Limited is a British Virgin Islands company wholly owned by Ms. Ying Sun. Mr. Han and Ms. Sun are husband and wife. Mr. Han is the sole director of Techedu Limited.

(2) Mr. Li is a director of our company jointly appointed by IDG Technology Venture Investments, L.P. and IDG Technology Venture Investment III, L.P. The business address of Mr. Li is 6/F., COFCO Plaza, No.8 Jianguomennei Ave, Jiannei St, Dongcheng District, Beijing, 100020, PRC.

(3) The business address of Mr. Sun is Grand Palace B12, 5 Hui-zhong Road, Chaoyang District, Beijing, 100101, PRC.

(4) The business address of Mr. Zhang is 20th Floor, Block B, Tower 2, Wangjing SOHO, No.1 Futongdong Street, Chaoyang District, Beijing, PRC.

(5) The business address of Mr. Zhang is Baidu Campus, No. 10 Shangdi 10th Street, Haidian District, Beijing 100085 PRC.

(6) See footnote (1).

(7) The number of ordinary shares beneficially owned is as of December 31, 2014, as reported in a Schedule 13G filed by Goldman Sachs Asset Management, L.P. on February 17, 2015, and consists of (i) 5,457,426 Class B ordinary shares held by Goldman Sachs Investment Partners Master Fund, L.P. and (ii) 5,457,426 Class B ordinary shares held by Goldman Sachs Investment Partners Private Opportunities Holdings, L.P. The general partner of Goldman Sachs Investment Partners Master Fund, L.P. is Goldman Sachs Investment Partners GP, L.L.C., and the investment manager of Goldman Sachs Investment Partners Master Fund, L.P. is GS Investment Strategies, LLC. Goldman Sachs Investment Partners GP, L.L.C. and GS Investment Strategies, LLC are wholly owned by The Goldman Sachs Group, Inc. The business address of Goldman Sachs Investment Partners Master Fund, L.P. is 200 West Street, NY NY 10282. The general partner of Goldman Sachs Investment Partners Private Opportunities Holdings, L.P. is Goldman Sachs Investment Partners Private Opportunities Holdings Advisors, Inc., and the investment manager of Goldman Sachs Investment Partners Private Opportunities Holdings, L.P. is GS Investment Strategies, LLC. Goldman Sachs Investment Partners Private Opportunities Holdings Advisors, Inc. and GS Investment Strategies, LLC are wholly owned by The Goldman Sachs Group, Inc. The business address of Goldman Sachs Investment Partners Private Opportunities Holdings, L.P. is 200 West Street, NY NY 10282. The percentage of beneficial ownership and voting power was calculated based on the total number of our ordinary shares outstanding as of February 28, 2015.

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(8) The number of ordinary shares beneficially owned is as of December 31, 2014, as reported in a Schedule 13G filed by Ho Chi Sing on February 10, 2015, and consists of (i) 5,048,484 Class B ordinary shares held by IDG Technology Venture Investments, L.P. and (ii) 1,689,190 Class B ordinary shares held by IDG Technology Venture Investment III, L.P. IDG Technology Venture Investments, L.P. is a Delaware limited partnership which is controlled by IDG Technology Venture Investments, LLC, its general partner. IDG Technology Venture Investments, LLC is controlled by its two managing members: Mr. Quan Zhou and Mr. Chi Sing Ho. The business address of IDG Technology Venture Investments, L.P. is c/o IDG Capital Management (KH) Limited, Unit 5505, The Center, 99 Queen s Road Central, Hong Kong. IDG Technology Venture Investment III, L.P. is a Delaware limited partnership which is controlled by IDG Technology Venture Investment III, LLC, its general partner. IDG Technology Venture Investment III, LLC is controlled by its two managing members: Mr. Quan Zhou and Mr. Chi Sing Ho. The business address of IDG Technology Venture Investment III, L.P. is c/o IDG Capital Management (KH) Limited, Unit 5505, The Center, 99 Queen s Road Central, Hong Kong. The percentage of beneficial ownership and voting power was calculated based on the total number of our ordinary shares outstanding as of February 28, 2015. The percentage ownership in terms of total ordinary shares on an as-converted basis held by IDG funds decreased from 17.5% as of April 8, 2014 to 12.8% as of December 31, 2014.

(9) The registered office address of Learingon Limited is the offices of Trident Trust Company (B.V.I.) Limited, Trident Chambers, P.O. Box 146, Road Town, Tortola, the British Virgin Islands. Learingon Limited is ultimately owned by Mr. Shaoyun Han through a trust.

(10) The registered office address of Connion Capital Limited is the offices of Trident Trust Company (B.V.I.) Limited, Trident Chambers, P.O. Box 146, Road Town, Tortola, the British Virgin Islands. Connion Capital Limited is ultimately owned by Mr. Shaoyun Han through a trust.

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares are entitled to one vote per share, while holders of Class B ordinary shares are entitled to ten votes per share. We issued Class A ordinary shares represented by our ADSs in our initial public offering inApril 2014. Holders of our Class B ordinary shares may choose to convert their Class B ordinary shares into the same number of Class A ordinary shares at any time. Class A ordinary shares are not convertible into Class B ordinary shares under any circumstance.

To our knowledge, we are not owned or controlled, directly or indirectly, by another corporation, by any foreign government or by any other natural or legal persons, severally or jointly. We are not aware of any arrangement that may, at a subsequent date, result in a change of control of our company.

To our knowledge, as of February 28, 2015, 22,212,758 of our Class A ordinary shares are held by one record holder in the United States, which is the depositary of our ADS program, representing 93.7% of our total issued and outstanding Class A ordinary shares as of such date. The number of beneficial owners of our ADSs in the United States is likely to be much larger than the number of record holders of our ordinary shares in the United States. As of February 28, 2015, 17,652,526 of our Class B ordinary shares are held by four record holders in the United States, representing 61.4% of our total issued and outstanding Class B ordinary shares as of such date.

For options and restricted shares granted to our officers, directors and employees, see B. Compensation of Directors and Executive Officers Share Incentive Plan.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

**A. Major Shareholders**

See Item 6. Directors, Senior Management and Employees E. Share Ownership.

**B. Related Party Transactions**

**Contractual Arrangements with our VIEs**

See Item 4. Information on the Company C. Organizational Structure.

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**Transactions with Shareholders and Affiliates**

***Transactions with Chuanbang***. Starting from the second half of 2011, Chuanbang, a company owned by our chief executive officer, Mr. Shaoyun Han, began to offer person-to-person lending to enable qualified students to borrow unsecured loans from unrelated individuals to pay for our tuition fees. Under the person-to-person lending service offered by Chuanbang, a student enters into a loan agreement with Mr. Han, as the designated representative of Chuanbang, to borrow an amount equal to our tuition fees. Mr. Han then assigns the existing loan agreement to an unrelated individual lender identified by Chuanbang, or the person-to-person lender, with us serving as the guarantor of the loan to the student. Upon the receipt of cash from the person-to-person lenders, Mr. Han remits the cash to us directly on behalf of the student for the payment of such student s tuition fees. Chuanbang services the student loans by collecting repayments on behalf of the person-to-person lenders from students, made to an account opened in the name of Mr. Han. The interest spread between (i) the interest rate under the loan agreement between the student and Mr. Han and (ii) the anticipated annual yield under the assignment agreement between Mr. Han and the person-to-person lender represents compensation for Chuanbang s estimated costs incurred in originating and servicing the student loans, plus the amount payable to us for guaranteeing the student loans.

As of December 31, 2014, our maximum exposure to guarantees of student loans was US$0.2 million. US$18 thousand were recognized as guarantee fee revenue and included in other revenues in 2014. Starting from April 2013, we had stopped providing guarantees for any new student loans arranged by Chuanbang. The estimated amount of the loss contingency related to the guarantee was immaterial as of December 31, 2014. Chuanbang ceased offering financing services to our students enrolled since January 1, 2014. We did not receive any tuition fees under Chuanbang s person-to-person financing arrangements in 2014.

Pursuant to our agreement with Chuanbang, Chuanbang provided cash collection service on our accounts receivable to better manage our cash collection since August 2013. The fee is calculated based on 6%~8% of the amount collected. The staff of Chuanbang includes our former employees who joined Chuanbang in July 2013. Chuanbang also provides similar cash collection service to other financial institutions. The cash collection service fee was US$0.1 million for 2014.

**Registration Rights**

In connection with our issuance of Series C preferred shares, we and all our then shareholders entered into an amended and restated shareholders agreement on September 6, 2011. Pursuant to our amended and restated shareholders agreement dated September 6, 2011, we have granted certain registration rights to certain of our shareholders. Set forth below is a description of the registration rights granted under the agreement.

***Demand Registration Rights***. At any time after the completion of our initial public offering in April 2014, upon a written request from the holders of at least 10% of the registrable securities held by our preferred shareholders, we must file a registration statement covering the offer and sale of the registrable securities held by the requesting shareholders and other holders of registrable securities who choose to participate in the offering. Registrable securities include, among others, our ordinary shares issued or to be issued upon conversion of the preferred shares.

However, we are not obligated to proceed with a demand registration if we have, within the six-month period preceding the date of such request, already effected a registration under the Securities Act pursuant to the exercise of the holders registration rights, unless the registrable securities of the holders were excluded from such registration. We have the right to defer filing of a registration statement for up to 90 days if our board of directors determines in good faith that the filing of a registration statement would be materially detrimental to us and our shareholders, but we cannot exercise the deferral right more than once in any 12-month period.

***Form F-3 Registration Rights***. When we are eligible for registration on Form F-3, upon a written request from the holders of a majority of the registrable securities held by our preferred shareholders, we must file a registration statement on Form F-3 covering the offer and sale of the registrable securities.

We are not obligated to effect a Form F-3 registration, among other things, if we already effected a registration under the Securities Act pursuant to the exercise of the holders demand or piggyback registration rights, unless the registrable securities of the holders were excluded from such registration. We have the right to defer filing of a registration statement for up to 60 days if our board of directors determines in good faith that the filing of a registration statement would be materially detrimental to us and our shareholders, but we cannot exercise the deferral right more than once in any 12-month period.

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***Piggyback Registration Rights***. If we propose to file a registration statement for a public offering of our ordinary shares on a form that would be suitable for registrable securities, we must offer holders of registrable securities an opportunity to include in that registration all or any part of their registrable securities. The underwriters of any underwritten offering have the right to limit the number of shares with registration rights to be included in the registration statement, subject to certain limitations.

***Expenses of Registration***. We will pay all expenses relating to any demand, Form F-3, or piggyback registration, with certain limited exceptions.

***Termination of Obligations***. We shall have no obligation to effect any demand, Form F-3, or piggyback registration on the earlier of (a) the date that is five years after the completion of our initial public offering, or (b) as to any holder of registrable securities, the time when all registrable securities held by such holder may be sold in any 90-day period without registration pursuant to Rule 144 under the Securities Act.

**Employment Agreements and Indemnification Agreements**

See Item 6. Directors, Senior Management and Employees B. Compensation of Directors and Executive Officers Employment Agreements and Indemnification Agreements.

**Share Option Grants**

See Item 6. Directors, Senior Management and Employees B. Compensation of Directors and Executive Officers Share Incentive Plan.

**C. Interests of Experts and Counsel**

Not applicable.

**ITEM 8. FINANCIAL INFORMATION**

**A. Consolidated Statements and Other Financial Information**

We have appended consolidated financial statements filed as part of this annual report.

**Legal Proceedings**

We are currently not a party to, and are not aware of any threat of, any legal, arbitration or administrative proceedings that, in the opinion of our management, are likely to have a material and adverse effect on our business, financial condition or results of operations. From time to time, we have become, and may in the future become, a party to various legal or administrative proceedings or claims arising in the ordinary course of our business. Regardless of the outcome, legal or administrative proceedings or claims may have an adverse impact on us because of defense and settlement costs, diversion of management attention and other factors.

**Dividend Policy**

We have not previously declared or paid cash dividends, and we currently have no concrete plan to declare or pay any dividends on our shares or ADSs. We currently intend to retain most, if not all, of our available funds and any future earnings to operate and expand our business.

We are a holding company incorporated in the Cayman Islands. PRC regulations may restrict the ability of our PRC subsidiaries to pay dividends to us. See Item 4. Information on the Company B. Business Overview Government Regulations Regulations on Dividend Distribution.

Our board of directors has discretion as to whether to distribute dividends, subject to applicable laws. Even if our board of directors decides to pay dividends, the form, frequency and amount will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that the board of directors may deem relevant. If we pay any dividends, we will pay our ADS holders to the same extent as holders of our ordinary shares, subject to the terms of the deposit agreement, including the fees and expenses payable thereunder. Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

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**B. Significant Changes**

Except as disclosed elsewhere in this annual report, we have not experienced any significant changes since the date of our audited consolidated financial statements included in this annual report.

## ITEM 9. THE OFFER AND LISTING

**A. Offering and Listing Details.**

Our ADSs, each representing one Class A ordinary share, have been listed on the NASDAQ Global Select Market since April 3, 2014 under the symbol TEDU. Update until April 14, 2015 (starting from April 3, 2014), the trading price of our ADSs on the NASDAQ Global Select Market ranged from US$6.54 to US$15.85 per ADS.

The following table provides the high and low trading prices for our ADSs on the NASDAQ Global Select Market for the periods indicated below.

| | Trading Price | |
|---|---|---|
| | **High** | **Low** |
| **Quarterly Highs and Lows** | | |
| Second Quarter 2014 (since April 3, 2014) | 14.23 | 6.54 |
| Third Quarter 2014 | 15.85 | 11.12 |
| Fourth Quarter 2014 | 14.40 | 10.17 |
| First Quarter 2015 | 12.50 | 9.26 |
| **Monthly Highs and Lows** | | |
| October 2014 | 13.83 | 10.68 |
| November 2014 | 14.40 | 12.30 |
| December 2014 | 12.46 | 10.17 |
| January 2015 | 12.49 | 10.77 |
| February 2015 | 12.50 | 11.09 |
| March 2015 | 11.52 | 9.26 |
| April 2015 (through April 14, 2015) | 13.12 | 9.28 |

**B. Plan of Distribution**

Not applicable.

**C. Markets**

Our ADSs, each representing one Class A ordinary share, have been listed on the NASDAQ Global Select Market under the symbol TEDU since April 3, 2014.

**D. Selling Shareholders**

Not applicable.

**E. Dilution**

Not applicable.

**F. Expenses of the Issue**

Not applicable.

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## ITEM 10. ADDITIONAL INFORMATION

### A. Share Capital

Not applicable.

### B. Memorandum and Articles of Association

The following are summaries of material provisions of our currently effective fifth amended and restated memorandum and articles of association, as well as the Companies Law (2013 Revision) insofar as they relate to the material terms of our ordinary shares.

**Registered Office and Objects**

Our registered office in the Cayman Islands is located at the offices of Codan Trust Company (Cayman) Limited, Cricket Square, Hutchins Drive, PO Box 2681, Grand Cayman KY1-1111, Cayman Islands. As set forth in article 3 of our fifth amended and restated memorandum of association, the objects for which our company is established are unrestricted.

**Board of Directors**

See Item 6. Directors, Senior Management and Employees C. Board Practices.

**Ordinary Shares**

***General***. Holders of Class A ordinary shares and Class B ordinary shares have the same rights except for voting and conversion rights. All of our outstanding ordinary shares are fully paid and non-assessable. Certificates representing the ordinary shares are issued in registered form. Our shareholders who are non-residents of the Cayman Islands may freely hold and transfer their ordinary shares.

***Dividends***. The holders of our ordinary shares are entitled to such dividends as may be declared by our board of directors, provided that dividends may be declared and paid out of funds legally available therefor, namely out of either profit, our share premium account or any other fund or account which can be authorized for this purpose in accordance with the Companies Law. Holders of Class A ordinary shares and Class B ordinary shares will be entitled to the same amount of dividends, if declared.

***Voting Rights***. Holders of our ordinary shares are entitled to ten calendar days notice of meetings of our shareholders. In respect of all matters subject to a shareholders vote, each Class A ordinary share is entitled to one vote, and each Class B ordinary share is entitled to ten votes, voting together as one class. Voting at any meeting of shareholders is by show of hands unless a poll is demanded. A poll may be demanded by the chairman of such meeting or any shareholder present in person or by proxy.

A quorum required for a meeting of shareholders consists of two shareholders who hold at least 50% of all voting power of our share capital in issue at the meeting present in person or by proxy or, if a corporation or other non-natural person, by its duly authorized representative. Shareholders meetings may be held annually. Each general meeting, other than an annual general meeting, shall be an extraordinary general meeting. Extraordinary general meetings may be called by a majority of our board of directors or our chairman or upon a requisition of shareholders

holding at the date of deposit of the requisition not less than 1/3 of the aggregate voting power of our company. Advance notice of at least ten calendar days is required for the convening of our annual general meeting and other general meetings.

An ordinary resolution to be passed at a meeting by the shareholders requires the affirmative vote of a simple majority of the votes attaching to the ordinary shares cast at a meeting, while a special resolution requires the affirmative vote of no less than 2/3 of the votes cast attaching to the outstanding ordinary shares at a meeting. A special resolution will be required for important matters such as a change of name or making changes to our fifth amended and restated memorandum and articles of association.

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***Conversion.*** Each Class B ordinary share is convertible into one Class A ordinary share at any time by the holder thereof. Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances. Upon any transfer of Class B ordinary shares by a holder to any person or entity which is not an affiliate of such holder, such Class B ordinary shares shall be automatically and immediately converted into the equivalent number of Class A ordinary shares.

***Transfer of Ordinary Shares.*** Subject to the restrictions set out below and the provisions above in respect of Class B ordinary shares, any of our shareholders may transfer all or any of his or her ordinary shares by an instrument of transfer in the usual or common form or any other form approved by our board of directors.

Our board of directors may, in its absolute discretion, decline to register any transfer of any ordinary share which is not fully paid up or on which we have a lien. Our board of directors may also decline to register any transfer of any ordinary share unless:

- the instrument of transfer is lodged with us, accompanied by the certificate for the ordinary shares to which it relates and such other evidence as our board of directors may reasonably require to show the right of the transferor to make the transfer;
- the instrument of transfer is in respect of only one class of ordinary shares;
- the instrument of transfer is properly stamped, if required;
- in the case of a transfer to joint holders, the number of joint holders to whom the ordinary share is to be transferred does not exceed four; and
- a fee of such maximum sum as the NASDAQ Global Market may determine to be payable or such lesser sum as our directors may from time to time require is paid to us in respect thereof.

If our directors refuse to register a transfer they shall, within three months after the date on which the instrument of transfer was lodged, send to each of the transferor and the transferee notice of such refusal.

The registration of transfers may, after compliance with any notice required of the NASDAQ Global Market, be suspended and the register closed at such times and for such periods as our board of directors may from time to time determine, provided, however, that the registration of transfers shall not be suspended nor the register closed for more than thirty days in any year as our board may determine.

***Liquidation.*** On a return of capital on winding up or otherwise (other than on conversion, redemption or purchase of ordinary shares), assets available for distribution among the holders of ordinary shares shall be distributed among the holders of the ordinary shares on a pro rata basis. If our assets available for distribution are insufficient to repay all of the paid-up capital, the assets will be distributed so that the losses are borne by our shareholders proportionately. Any distribution of assets or capital to a holder of a Class A ordinary share and a holder of a Class B ordinary share will be the same in any liquidation event.

***Calls on Ordinary Shares and Forfeiture of Ordinary Shares.*** Our board of directors may from time to time make calls upon shareholders for any amounts unpaid on their ordinary shares in a notice served to such shareholders at least fourteen calendar days prior to the specified time of payment. The ordinary shares that have been called upon and remain unpaid are subject to forfeiture.

***Repurchase and Redemption of Ordinary Shares.*** The Companies Law and our fifth amended and restated articles of association permit us to purchase our own shares. In accordance with our fifth amended and restated articles of association and provided the necessary shareholders or board approval have been obtained, we may issue shares on terms that are subject to redemption, at our option or at the option of the holders of these shares, on such terms and in such manner, including out of capital, as may be determined by our board of directors.

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***Variations of Rights of Shares.*** All or any of the special rights attached to any class of shares may, subject to the provisions of the Companies Law, be varied with the written consent of the holders of three-fourths of the issued shares of that class or with the sanction of a special resolution passed at a general meeting of the holders of the shares of that class. The rights conferred upon the holders of the shares of any class issued shall not, unless otherwise expressly provided by the terms of issue of the shares of that class, be deemed to be varied by the creation or issue of further shares ranking *pari passu* with such existing class of shares.

***Inspection of Books and Records.*** Holders of our ordinary shares have no general right under Cayman Islands law to inspect or obtain copies of our list of shareholders or our corporate records. However, we will provide our shareholders with annual audited financial statements. See Item 10. Additional Information H. Documents on Display.

***Issuance of Additional Shares.*** Our fifth amended and restated memorandum of association authorizes our board of directors to issue additional ordinary shares from time to time as our board of directors shall determine, to the extent of available authorized but unissued shares.

Our fifth amended and restated memorandum of association also authorizes our board of directors to establish from time to time one or more series of preferred shares and to determine, with respect to any series of preferred shares, the terms and rights of that series, including:

the designation of the series;

the number of shares of the series;

the dividend rights, dividend rates, voting rights; and

the rights and terms of redemption and liquidation preferences.

Our board of directors may issue preferred shares without action by our shareholders to the extent authorized but unissued. Issuance of these shares may dilute the voting power of holders of ordinary shares.

***Anti-Takeover Provisions.*** Some provisions of our fifth amended and restated memorandum and articles of association may discourage, delay or prevent a change of control of our company or management that shareholders may consider favorable, including provisions that authorize our board of directors to issue preferred shares in one or more series and to designate the price, rights, preferences, privileges and restrictions of such preferred shares without any further vote or action by our shareholders.

***Exempted Company.*** We are an exempted company with limited liability under the Companies Law. Limited liability means that the liability of each shareholder is limited to the amount unpaid by the shareholder on the shares of the company. The Companies Law distinguishes between ordinary resident companies and exempted companies. Any company that is registered in the Cayman Islands but conducts business mainly outside of the Cayman Islands may apply to be registered as an exempted company. The requirements for an exempted company are essentially the same as for an ordinary company except that an exempted company:

does not have to file an annual return of its shareholders with the Registrar of Companies;

is not required to open its register of members for inspection;

does not have to hold an annual general meeting;

may issue negotiable or bearer shares or shares with no par value;

may obtain an undertaking against the imposition of any future taxation (such undertakings are usually given for 20 years in the first instance);

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may register by way of continuation in another jurisdiction and be deregistered in the Cayman Islands;

may register as a limited duration company; and

may register as a segregated portfolio company.

Our fifth amended and restated memorandum and articles of association do not provide provisions that are different from those that are applicable to an exempted company as set forth above, except that they do not permit us to issue bearer shares or shares with no par value.

**C. Material Contracts**

We have not entered into any material contracts other than in the ordinary course of business and other than those described in Item 4. Information on the Company or elsewhere in this annual report on Form 20-F.

**D. Exchange Controls**

See Item 4. Information on the Company B. Business Overview Government Regulations Regulations on Foreign Exchange Registration of Overseas Investment by PRC Residents, Item 4.Information on the Company B. Business Overview Government Regulations Regulations on Foreign Currency Exchange and Item 4. Information on the Company B. Business Overview Government Regulations Regulations on Dividend Distribution.

**E. Taxation**

The following summary of certain Cayman Islands, PRC and United States federal income tax consequences of an investment in our ADSs or ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change or differing interpretation, possibly with retroactive effect. This summary does not deal with all possible tax consequences relating to an investment in our ADSs or ordinary shares, such as the tax consequences under other federal, state, local and other tax laws not addressed herein. To the extent the at the discussion relates to matters of Cayman Islands tax law, it represents the opinion of Conyers Dill & Pearman, our Cayman Islands counsel. To the extent that the discussion relates to matters of PRC tax law, it represents the opinion of Han Kun Law Offices, our PRC counsel.

**Cayman Islands Taxation**

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes levied by the Government of the Cayman Islands that are likely to be material to holders of ADSs or ordinary shares. The Cayman Islands is not party to any double tax treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.

Pursuant to Section 6 of the Tax Concessions Law (2011 Revision) of the Cayman Islands, we have obtained an undertaking from the Governor-in-Council:

(i) that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits or income or gains or appreciation shall apply to us or our operations; and

(ii) that the aforesaid tax or any tax in the nature of estate duty or inheritance tax shall not be payable on our shares, debentures or other obligations.

The undertaking for us is for a period of twenty years from March 25, 2014.

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**People s Republic of China Taxation**

Under the EIT Law, an enterprise established outside the PRC with de facto management bodies within the PRC is considered a resident enterprise for PRC enterprise income tax purposes and is generally subject to a uniform 25% enterprise income tax rate on its worldwide income as well as tax reporting obligations. Under the Implementation Rules to the EIT Law, a de facto management body is defined as a body that has material and overall management and control over the manufacturing and business operations, personnel and human resources, finances and properties of an enterprise. In addition, Circular 82 issued by the SAT in April 2009, as amended in January 2014, specifies that certain offshore-incorporated enterprises controlled by PRC enterprises or PRC enterprise groups will be classified as PRC resident enterprises if the following are located or resident in the PRC: senior management personnel and departments that are responsible for daily production, operation and management; financial and personnel decision making bodies; key properties, accounting books, company seal, minutes of board meetings and shareholders meetings; and half or more of the senior management or directors having voting rights. Further to Circular 82, the SAT issued the Bulletin 45, which took effect in September 2011, to provide more guidance on the implementation of Circular 82. Bulletin 45 provides for procedures and administration details of determination on PRC resident enterprise status and administration on post-determination matters. We do not believe that Tarena International, Inc. is a PRC resident enterprise. If the PRC tax authorities determine that Tarena International, Inc. is a PRC resident enterprise for PRC enterprise income tax purposes, a number of unfavorable PRC tax consequences could follow. One example is that a 10% withholding tax would be imposed on dividends we pay to our non-PRC enterprise shareholders and with respect to gains derived by our non-PRC enterprise shareholders from transferring our shares or ADSs and potentially a 20% of withholding tax would be imposed on dividends we pay to our non-PRC individual shareholders and with respect to gains derived by our non-PRC individual shareholders from transferring our shares or ADSs.

Under the EIT Law, dividends generated from retained earnings after January 1, 2008 from a PRC company and distributed to a foreign parent company are subject to a withholding tax rate of 10% unless the foreign parent s jurisdiction of incorporation has a tax treaty with China that provides for a preferential withholding arrangement. Pursuant to the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Prevention of Fiscal Evasion with respect to Taxes on Income, or the Hong Kong Tax Treaty, which became effective on December 8, 2006, a company incorporated in Hong Kong, such as Tarena HK, will be subject to withholding income tax at a rate of 5% on dividends it receives from its PRC subsidiary if it holds a 25% or more interest in that particular PRC subsidiary, or 10% if it holds less than a 25% interest in that subsidiary. However, the SAT promulgated a tax notice on October 27, 2009, or Circular 601, which provides that tax treaty benefits will be denied to conduit or shell companies without business substance, and a beneficial ownership analysis will be used based on a substance-over-the-form principle to determine whether or not to grant tax treaty benefits. On June 29, 2012, the SAT further issued the Announcement of the SAT regarding Recognition of Beneficial Owner under Tax Treaties, or Announcement 30, which provides that a comprehensive analysis should be made when determining the beneficial owner status based on various factors supported by various types of documents including the articles of association, financial statements, records of cash movements, board meeting minutes, board resolutions, staffing and materials, relevant expenditures, functions and risk assumption as well as relevant contracts and other information. Our Hong Kong subsidiary has not obtained the approval for a withholding tax rate of 5% from the relevant tax authority and currently does not plan to obtain such approval because our PRC subsidiaries have not paid any dividends and currently do not plan to pay dividends.

It is unclear whether, if we are considered a PRC resident enterprise, holders of our shares or ADSs would be able to claim the benefit of income tax treaties or agreements entered into between China and other countries or areas. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China Under the PRC Enterprise Income Tax Law, we may be classified as a PRC resident enterprise for PRC enterprise income tax purposes. Such

classification would likely result in unfavorable tax consequences to us and our non-PRC shareholders and have a material adverse effect on our results of operations and the value of your investment.

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The SAT issued a Circular 59 together with the Ministry of Finance in April 2009 and a Circular 698 in December 2009. Both Circular 59 and Circular 698 became effective retroactively as of January 1, 2008. By promulgating and implementing these two circulars, the PRC tax authorities have enhanced their scrutiny over the direct or indirect transfer of equity interests in a PRC resident enterprise by a non-resident enterprise. Under Circular 698, where a non-resident enterprise transfers the equity interests of a PRC resident enterprise indirectly by disposition of the equity interests of an overseas holding company, and such overseas holding company is located in certain low tax jurisdictions, the non-resident enterprise, being the transferor, must report to the relevant tax authority of the PRC resident enterprise this Indirect Transfer. The PRC tax authority may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established for the purpose of reducing, avoiding or deferring PRC tax. As a result, gains derived from such Indirect Transfer may be subject to PRC tax at a rate of up to 10%. On February 3, 2015, the SAT issued a Public Notice [2015] No.7, or Public Notice 7, to supersede the existing tax rules in relation to the Indirect Transfer as set forth in Circular 698, while the other provisions of Circular 698 remain in force. Public Notice 7 introduces a new tax regime that is significantly different from that under Circular 698. Public Notice extend its tax jurisdiction to capture not only Indirect Transfer as set forth under Circular 698 but also transactions involving transfer of immovable property in China and assets held under the establishment and place, in China of a foreign company through the offshore transfer of a foreign intermediate holding company. Public Notice 7 also addresses the term transfer of the equity interest in a foreign intermediate holding company widely. In addition, Public Notice 7 provides clearer criteria than Circular 698 on how to assess reasonable commercial purposes and introduces safe harbor scenarios applicable to internal group restructurings. Where non-resident investors were involved in our private equity financing, if such transactions were determined by the tax authorities to lack reasonable commercial purpose, we and our non-resident investors may become at risk of being taxed under Circular 698 and Public Notice 7 and may be required to expend valuable resources to comply with Circular 698 and Public Notice 7 or to establish that we should not be taxed under Circular 698 and Public Notice 7. The PRC tax authorities have the discretion under SAT Circular 59, Circular 698 and Public Notice 7 to make adjustments to the taxable capital gains based on the difference between the fair value of the equity interests transferred and the cost of investment. See Item 3. Key Information D. Risk Factors Risks Relating to Doing Business in China We face uncertainty regarding the PRC tax reporting obligations and consequences for certain indirect transfers of our operating company s equity interests. Enhanced scrutiny over acquisition transactions by the PRC tax authorities may have a negative impact on potential acquisitions we may pursue in the future.

**United States Federal Income Tax Considerations**

The following discussion is a summary of United States federal income tax considerations relating to the ownership and disposition of our ADSs or ordinary shares by a U.S. Holder, as defined below, that holds our ADSs or ordinary shares as capital assets (generally, property held for investment) under the United States Internal Revenue Code of 1986, as amended (the Code ). This discussion is based upon existing United States federal income tax law, which is subject to differing interpretations or change, possibly with retroactive effect. No ruling has been sought from the Internal Revenue Service (the IRS ) with respect to any United States federal income tax consequences described below, and there can be no assurance that the IRS or a court will not take a contrary position. This discussion does not address all aspects of United States federal income taxation that may be important to particular investors in light of their individual circumstances, including investors subject to special tax rules (such as, for example, certain financial institutions, insurance companies, regulated investment companies, real estate investment trusts, broker-dealers, traders in securities that elect mark-to-market treatment, partnerships and their partners, tax-exempt organizations (including private foundations), investors who are not U.S. Holders, investors that own (directly, indirectly, or constructively) 10% or more of our voting stock, investors that hold their ADSs or ordinary shares as part of a straddle, hedge, conversion, constructive sale or other integrated transaction, or investors that have a functional currency other than the United States dollar, all of whom may be subject to tax rules that differ significantly from those summarized below). In addition, this discussion does not address any state, local, alternative minimum tax, or

non-United States tax considerations. Each potential investor is urged to consult its tax advisor regarding the United States federal, state, local and non-United States income and other tax considerations of an investment in our ADSs or ordinary shares.

***General***

For purposes of this discussion, a U.S. Holder is a beneficial owner of our ADSs or ordinary shares that is, for United States federal income tax purposes, (i) an individual who is a citizen or resident of the United States, (ii) a corporation (or other entity treated as a corporation for United States federal income tax purposes) created in, or organized under the laws of, the United States or any state thereof or the District of Columbia, (iii) an estate the income of which is includible in gross income for United States federal income tax purposes regardless of its source, or (iv) a trust (A) the administration of which is subject to the primary supervision of a United States court and which has one or more United States persons who have the authority to control all substantial decisions of the trust or (B) that has otherwise elected to be treated as a United States person under the Code.

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If a partnership (or other entity treated as a partnership for United States federal income tax purposes) is a beneficial owner of our ADSs or ordinary shares, the tax treatment of a partner in the partnership will generally depend upon the status of the partner and the activities of the partnership. Partnerships and partners of a partnership holding our ADSs or ordinary shares are urged to consult their tax advisors regarding an investment in our ADSs or ordinary shares.

Based in part on certain representations from the depositary bank, a U.S. Holder of ADSs will be treated as the beneficial owner for United States federal income tax purposes of the underlying shares represented by the ADSs.

***Passive Foreign Investment Company Considerations***

A non-United States corporation, such as our company, will be classified as a passive foreign investment company, or PFIC, for United States federal income tax purposes, if, in the case of any particular taxable year, either (i) 75% or more of its gross income for such year consists of certain types of passive income or (ii) 50% or more of its average quarterly assets (as determined on the basis of fair market value) during such year produce or are held for the production of passive income. For this purpose, cash is categorized as a passive asset and the company s unbooked intangibles associated with active business activities may generally be classified as active assets. Passive income generally includes, among other things, dividends, interest, rents, royalties, and gains from the disposition of passive assets. We will be treated as owning our proportionate share of the assets and earning our proportionate share of the income of any other corporation in which we own, directly or indirectly, more than 25% (by value) of the stock.

Although the law in this regard is unclear, we treat our consolidated VIEs as being owned by us for United States federal income tax purposes, not only because we exercise effective financial control over the operation of such entities but also because we are entitled to substantially all of their economic benefits, and, as a result, we consolidate their operating results in our consolidated financial statements. If it were determined, however, that we are not the owner of our consolidated VIEs for United States federal income tax purposes, we may be treated as a PFIC for our current taxable year and in future taxable years.

Based on our current income and assets and the value of our ADSs and ordinary shares , we do not believe that we were a PFIC for our taxable year ended December 31, 2014 and we do not expect to be classified as a PFIC for our taxable year ending December 31, 2015 or in the foreseeable future.

While we do not expect to become a PFIC in the current or future taxable years, the determination of whether we will be or become a PFIC will depend upon the composition of our income and assets and the value of our assets from time to time, including, in particular the value of our goodwill and other unbooked intangibles (which may depend upon the market value of our ADSs or ordinary shares from time to time, which may be volatile). Among other factors, if market capitalization is less than anticipated or subsequently declines, we may be classified as a PFIC for the current or future taxable years. It is also possible that the IRS, may challenge our classification or valuation of our goodwill and other unbooked intangibles, or determine that such assets should not be included in the determination of whether we are classified as a PFIC, which may result in our company being, or becoming classified as, a PFIC for the current or one or more future taxable years.

The determination of whether we will be or become a PFIC may also depend, in part, on how, and how quickly, we use our liquid assets. Under circumstances where we determine not to deploy significant amounts of cash for active purposes or our consolidated VIEs were not treated as owned by us for United States federal income tax purposes, our risk of being classified as a PFIC may substantially increase. Because there are uncertainties in the application of the relevant rules and PFIC status is a factual determination made annually after the close of each taxable year, there can be no assurance that we will not be a PFIC for the current taxable year or any future taxable year. If we were classified as a PFIC for any year during which a U.S. holder held our ADSs or ordinary shares, we generally would continue to

be treated as a PFIC for all succeeding years during which such U.S. holder held our ADSs or ordinary shares.

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The discussion below under Dividends and Sale or Other Disposition of ADSs or Ordinary Shares is written on the basis that we will not be classified as a PFIC for United States federal income tax purposes. The United States federal income tax rules that apply if we are classified as a PFIC for the current taxable year or any subsequent taxable year are generally discussed below under Passive Foreign Investment Company Rules.

***Dividends***

Any cash distributions (including the amount of any PRC tax withheld) paid on our ADSs or ordinary shares out of our current or accumulated earnings and profits, as determined under United States federal income tax principles, will generally be includible in the gross income of a U.S. Holder as dividend income on the day actually or constructively received by the U.S. Holder, in the case of ordinary shares, or by the depositary bank, in the case of ADSs. Because we do not intend to determine our earnings and profits on the basis of United States federal income tax principles, any distribution paid will generally be treated as a dividend for United States federal income tax purposes. A non-corporate recipient of dividend income will generally be subject to tax on dividend income from a qualified foreign corporation at a lower applicable capital gains rate rather than the marginal tax rates generally applicable to ordinary income provided that certain holding period and other requirements are met.

A non-United States corporation (other than a corporation that is classified as a PFIC for the taxable year in which the dividend is paid or the preceding taxable year) will generally be considered to be a qualified foreign corporation (a) if it is eligible for the benefits of a comprehensive tax treaty with the United States which the Secretary of Treasury of the United States determines is satisfactory for purposes of this provision and which includes an exchange of information program, or (b) with respect to any dividend it pays on stock (or ADSs in respect of such stock) which is readily tradable on an established securities market in the United States. United States Treasury guidance indicates that common or ordinary shares, or ADSs representing such shares, are considered for the purpose of clause (b) above to be readily tradable on an established securities market in the United States if they are listed on the NASDAQ Global Select Market, as are our ADSs. Since we do not expect that our ordinary shares will be listed on established securities markets, it is unclear whether dividends that we pay on our ordinary shares that are not backed by ADSs currently meet the conditions required for the reduced tax rate. There can be no assurance that our ADSs will continue to be considered readily tradable on an established securities market in later years. In the event we are deemed to be a resident enterprise under the EIT Law, we may be eligible for the benefits of the United States-PRC income tax treaty (which the U.S. Treasury Department has determined is satisfactory for this purpose) and we would be treated as a qualified foreign corporation with respect to dividends paid on our ordinary shares or ADSs. U.S. Holders are urged to consult their tax advisors regarding the availability of the reduced tax rate on dividends in their particular circumstances. Dividends received on our ADSs or ordinary shares will not be eligible for the dividends received deduction allowed to corporations.

For United States foreign tax credit purposes, dividends paid on our ADSs or ordinary shares will generally be treated as income from foreign sources and will generally constitute passive category income. In the event that we are deemed to be a PRC resident enterprise under the EIT Law, a U.S. Holder may be subject to PRC withholding taxes on dividends paid, if any, on our ADSs or ordinary shares. A U.S. Holder may be eligible, subject to a number of complex limitations, to claim a foreign tax credit in respect of any foreign withholding taxes imposed on dividends received on our ADSs or ordinary shares. A U.S. Holder who does not elect to claim a foreign tax credit for foreign tax withheld may instead claim a deduction for United States federal income tax purposes in respect of such withholding, but only for a year in which such holder elects to do so for all creditable foreign income taxes. The rules governing the foreign tax credit are complex. U.S. Holders are urged to consult their tax advisors regarding the availability of the foreign tax credit under their particular circumstances.

***Sale or Other Disposition of ADSs or Ordinary Shares***

A U.S. Holder will generally recognize capital gain or loss, if any, upon the sale or other disposition of ADSs or ordinary shares in an amount equal to the difference between the amount realized upon the disposition and the holder s adjusted tax basis in such ADSs or ordinary shares. Any capital gain or loss will be long-term gain or loss if the ADSs or ordinary shares have been held for more than one year and will generally be United States source gain or loss for United States foreign tax credit purposes. In the event that we are treated as a PRC resident enterprise under the PRC Enterprise Income Tax Law, and gain from the disposition of the ADSs or ordinary shares is subject to tax in the PRC, such gain may be treated as PRC source gain for foreign tax credit purposes under the United States-PRC income tax treaty. The deductibility of a capital loss may be subject to limitations. U.S. Holders are urged to consult their tax advisors regarding the tax consequences if a foreign tax is imposed on a disposition of our ADSs or ordinary shares, including the availability of the foreign tax credit under their particular circumstances.

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***Passive Foreign Investment Company Rules***

If we are classified as a PFIC for any taxable year during which a U.S. Holder holds our ADSs or ordinary shares, unless the U.S. Holder makes a mark-to-market election (as described below), the U.S. Holder will generally be subject to special tax rules that have a penalizing effect, regardless of whether we remain a PFIC, on (i) any excess distribution that we make to the U.S. Holder (which generally means any distribution paid during a taxable year to a U.S. Holder that is greater than 125% of the average annual distributions paid in the three preceding taxable years or, if shorter, the U.S. Holder s holding period for the ADSs or ordinary shares), and (ii) any gain realized on the sale or other disposition, including, under certain circumstances, a pledge, of ADSs or ordinary shares. Under the PFIC rules:

- the excess distribution and/or gain will be allocated ratably over the U.S. Holder s holding period for the ADSs or ordinary shares;
- the amount allocated to the current taxable year and any taxable years in the U.S. Holder s holding period prior to the first taxable year in which we are classified as a PFIC, or pre-PFIC year, will be taxable as ordinary income; and
- the amount allocated to each prior taxable year, other than the current taxable year or a pre-PFIC year, will be subject to tax at the highest tax rate in effect applicable to the individuals or corporations, as appropriate, for that year, and
- will be increased by an additional tax equal to interest on the resulting tax deemed deferred with respect to each such other taxable year.

If we are a PFIC for any taxable year during which a U.S. Holder holds our ADSs or ordinary shares and any of our non-United States subsidiaries is also a PFIC, such U.S. Holder would be treated as owning a proportionate amount (by value) of the shares of the lower-tier PFIC for purposes of the application of these rules. Each U.S. Holder is advised to consult its tax advisors regarding the application of the PFIC rules to any of our subsidiaries.

As an alternative to the foregoing rules, a U.S. Holder of marketable stock in a PFIC may make a mark-to-market election with respect to our ADSs, provided that the ADSs are regularly traded on the NASDAQ Global Market. In addition, we do not expect that holders of ordinary shares that are not represented by ADSs will be eligible to make a mark-to-market election. We believe that our ADSs qualify as being regularly traded, but no assurances can be given in this regard. If a mark-to-market election is made, the U.S. Holder will generally (i) include as ordinary income for each taxable year that we are a PFIC the excess, if any, of the fair market value of ADSs held at the end of the taxable year over the adjusted tax basis of such ADSs and (ii) deduct as an ordinary loss the excess, if any, of the adjusted tax basis of the ADSs over the fair market value of such ADSs held at the end of the taxable year, but only to the extent of the net amount previously included in income as a result of the mark-to-market election. The U.S. Holder s adjusted tax basis in the ADSs would be adjusted to reflect any income or loss resulting from the mark-to-market election. If a U.S. Holder makes an effective mark-to-market election, in each year that we are a PFIC any gain recognized upon the sale or other disposition of the ADSs will be treated as ordinary income and loss will be treated as ordinary loss, but only to the extent of the net amount previously included in income as a result of the mark-to-market election.

If a U.S. Holder makes a mark-to-market election in respect of a corporation classified as a PFIC and such corporation ceases to be classified as a PFIC, the U.S. Holder will not be required to take into account the mark-to-market gain or loss described above during any period that such corporation is not classified as a PFIC.

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Because, as a technical matter, a mark-to-market election cannot be made for any lower-tier PFICs that a PFIC may own, a U.S. Holder who makes a mark-to-market election with respect to our ADSs may continue to be subject to the general PFIC rules with respect to such U.S. Holder s indirect interest in any of our non-United States subsidiaries that is classified as a PFIC.

We do not intend to provide information necessary for U.S. Holders to make qualified electing fund elections, which, if available, would result in tax treatment different from the general tax treatment for PFICs described above.

As discussed above under Dividends , dividends that we pay on our ADSs or ordinary shares will not be eligible for the reduced tax rate that applies to qualified dividend income if we are classified as a PFIC for the taxable year in which the dividend is paid or the preceding taxable year. In addition, if a U.S. Holder owns our ADSs or ordinary shares during any taxable year that we are a PFIC, the holder must file an annual report with the IRS. Each U.S. Holder is urged to consult its tax advisor concerning the United States federal income tax consequences of purchasing, holding, and disposing ADSs or ordinary shares if we are or become a PFIC, including the possibility of making a mark-to-market election and the unavailability of the qualified electing fund election.

***Medicare Tax***

An additional 3.8% tax is imposed on a portion or all of the net investment income of certain individuals with a modified adjusted gross income of over $200,000 (or $250,000 in the case of joint filers or $125,000 in the case of married individuals filing separately) and on the undistributed net investment income of certain estates and trusts. For these purposes, net investment income generally includes interest, dividends (including dividends paid with respect to our ADSs or ordinary shares), annuities, royalties, rents, net gain attributable to the disposition of property not held in a trade or business (including net gain from the sale, exchange or other taxable disposition of an ADS or ordinary share) and certain other income, reduced by any deductions properly allocable to such income or net gain. You are urged to consult a tax advisor regarding the applicability of this tax to their income and gains in respect of an investment in our ADSs or ordinary shares.

***Information Reporting and Backup Withholding***

Pursuant to the Hiring Incentives to Restore Employment Act enacted on March 18, 2010, in tax years beginning after the date of enactment, an individual U.S. Holder and certain entities may be required to submit to the IRS certain information with respect to his or her beneficial ownership of the ADSs or ordinary shares, if such ADSs or ordinary shares are not held on his or her behalf by a U.S. financial institution. This new law also imposes penalties if an individual U.S. Holder is required to submit such information to the IRS and fails to do so.

In addition, U.S. Holders may be subject to information reporting to the IRS and United States backup withholding with respect to dividends on and proceeds from the sale or other disposition of our ADSs or ordinary shares. Backup withholding will not apply to you, however, if you furnish a correct taxpayer identification number and make any other required certification or that are otherwise exempt from backup withholding. U.S. Holder that are required to establish their exempt satus generally must provide such certification on IRS Form W-9. You should consult your tax advisor regarding the application of the United States information reporting and backup withholding rules to your particular circumstances.

Backup withholding is not an additional tax. Amounts withheld as backup withholding can be credited against your United States federal income tax liability, and you may obtain a refund of any excess amounts withheld under the backup withholding rules by timely filing the appropriate claim for refund with the IRS and furnishing any required information in a timely manner

**F. Dividends and Paying Agents**

Not Applicable.

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**G. Statement by Experts**

Not Applicable.

**H. Documents on Display**

We previously filed with the SEC our registration statement on Form F-1 (Registration No. 333-194191), as amended, including the prospectus contained therein, to register our Class A ordinary shares in relation to our initial public offering . We have also filed with the SEC a related registration statement on F-6 (Registration No. 333-194662) to register the ADSs.

We are subject to the periodic reporting and other informational requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Under the Exchange Act, we are required to file reports and other information with the SEC. Specifically, we are required to file annually a Form 20-F within four months after the end of each fiscal year, which is December 31. Copies of reports and other information, when so filed, may be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. The public may obtain information regarding the Washington, D.C. Public Reference Room by calling the Commission at 1-800-SEC-0330. The SEC also maintains a website at www.sec.gov that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

We will furnish Citibank, N.A., the depositary of our ADSs, with our annual reports, which will include a review of operations and annual audited consolidated financial statements prepared in conformity with U.S. GAAP, and all notices of shareholders meetings and other reports and communications that are made generally available to our shareholders. The depositary will make such notices, reports and communications available to holders of ADSs and, upon our request, will mail to all record holders of ADSs the information contained in any notice of a shareholders meeting received by the depositary from us.

In accordance with NASDAQ Stock Market Rules 5250(d), we will post this annual report on Form 20-F on our website at http://*ir.tarena.com.cn*.

**I. Subsidiary Information**

Not applicable.

**ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

***Foreign Exchange Risk***

Substantially all of our net revenues, costs and expenses are denominated in Renminbi. The Renminbi is not freely convertible into foreign currencies for capital account transactions. Our exposure to foreign exchange risk primarily relates to the U.S. dollar proceeds of the offerings of our equity securities. We had a net foreign exchange gain of US$1.2 million in 2014. To date, we have not entered into any hedging transactions in an effort to reduce our

exposure to foreign currency exchange risk.

The value of the Renminbi against the U.S. dollar and other currencies is affected by, among other things, changes in China s political and economic conditions and China s foreign exchange policies. In 2005, the PRC government changed its decade-old policy of pegging the value of the RMB to the U.S. dollar, and the Renminbi appreciated more than 20% against the U.S. dollar over the following three years. Between July 2008 and June 2010, this appreciation halted and the exchange rate between the Renminbi and the U.S. dollar remained within a narrow band. Since June 2010, the PRC government has allowed the Renminbi to appreciate slowly against the U.S. dollar again, though there also have been periods when it depreciated against the U.S. dollar. It is difficult to predict how market forces or PRC or U.S. government policy may impact the exchange rate between the Renminbi and the U.S. dollar in the future.

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To the extent that we need to convert the U.S. dollars we received from our equity offerings into Renminbi to fund our operations, acquisitions, or for other uses within the PRC, appreciation of the Renminbi against the U.S. dollar would have an adverse effect on the Renminbi amount we receive from the conversion. To the extent that we seek to convert Renminbi into U.S. dollars, depreciation of the Renminbi against the U.S. dollar would have an adverse effect on the U.S. dollar amount we receive from the conversion. On the other hand, a decline in the value of the Renminbi against the U.S. dollar could reduce the U.S. dollar equivalent of our financial results, the value of your investment in the company and the dividends that we may pay in the future, if any, all of which may have a material adverse effect on the prices of our ADS.

A hypothetical 10% decrease in the exchange rate of the U.S. dollar against the RMB would have resulted in a decrease of RMB92.8 million (US$17.3 million) in the value of our U.S. dollar-denominated financial assets at December 31, 2014.

***Interest Rate Risk***

Our exposure to interest rate risk primarily relates to interest income generated by excess cash invested in demand deposits with original maturities of three months to 5 years. Interest-earning instruments carry a degree of interest rate risk. We have not used any significant derivative financial instruments to manage our interest rate risk exposure. We have not been exposed, nor do we anticipate being exposed to, material risks due to changes in interest rates. However, our future interest income may be different from expectations due to changes in market interest rates.

## ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

### A. Debt Securities

Not applicable.

### B. Warrants and Rights

Not applicable.

### C. Other Securities

Not applicable.

### D. American Depositary Shares

**Fees and Charges Our ADS holders May Have to Pay**

Holders of our ADSs will be required to pay the following service fees to the depositary bank:

| Service | Fees |
|---|---|
| Issuance of ADSs | Up to U.S. 5¢ per ADS issued |
| Cancellation of ADSs | Up to U.S. 5¢ per ADS canceled |
| Distribution of cash dividends or other cash distributions | Up to U.S. 5¢ per ADS held |
| Distribution of ADSs pursuant to stock dividends, free stock distributions or exercise of rights | Up to U.S. 5¢ per ADS held |
| Distribution of securities other than ADSs or rights to purchase additional ADSs | Up to U.S. 5¢ per ADS held |
| Depositary Services | Up to U.S. 5¢ per ADS held on the applicable record date(s) established by the depositary bank |

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Holders of our ADSs will also be responsible to pay certain fees and expenses incurred by the depositary bank and certain taxes and governmental charges such as:

- fees for the transfer and registration of ordinary shares charged by the registrar and transfer agent for the ordinary shares in the Cayman Islands (i.e., upon deposit and withdrawal of ordinary shares);
- expenses incurred for converting foreign currency into U.S. dollars;
- expenses for cable, telex and fax transmissions and for delivery of securities;
- taxes and duties upon the transfer of securities (i.e., when ordinary shares are deposited or withdrawn from deposit); and
- fees and expenses incurred in connection with the delivery or servicing of ordinary shares on deposit.

Depositary fees payable upon the issuance and cancellation of ADSs are typically paid to the depositary bank by the brokers (on behalf of their clients) receiving the newly issued ADSs from the depositary bank and by the brokers (on behalf of their clients) delivering the ADSs to the depositary bank for cancellation. The brokers in turn charge these fees to their clients. Depositary fees payable in connection with distributions of cash or securities to ADS holders and the depositary services fee are charged by the depositary bank to the holders of record of ADSs as of the applicable ADS record date.

The depositary fees payable for cash distributions are generally deducted from the cash being distributed. In the case of distributions other than cash (i.e., stock dividend, rights), the depositary bank charges the applicable fee to the ADS record date holders concurrent with the distribution. In the case of ADSs registered in the name of the investor (whether certificated or uncertificated in direct registration), the depositary bank sends invoices to the applicable record date ADS holders. In the case of ADSs held in brokerage and custodian accounts (via DTC), the depositary bank generally collects its fees through the systems provided by DTC (whose nominee is the registered holder of the ADSs held in DTC) from the brokers and custodians holding ADSs in their DTC accounts. The brokers and custodians who hold their clients ADSs in DTC accounts in turn charge their clients accounts the amount of the fees paid to the depositary banks.

In the event of refusal to pay the depositary fees, the depositary bank may, under the terms of the deposit agreement, refuse the requested service until payment is received or may set off the amount of the depositary fees from any distribution to be made to the ADS holder.

The fees and charges holders of our ADSs may be required to pay may vary over time and may be changed by us and by the depositary bank.

**Fees and Other Payments Made by the Depositary to Us**

The depositary has agreed to reimburse us for certain expenses we incur that are related to establishment and maintenance of the ADS program upon such terms and conditions as we and the depositary may agree from time to

time. In 2014, we received US$1.9 million from the depository for expenses incurred in connection with the establishment and maintenance of the ADS program.

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## PART II.

### ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

### ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

**Material Modifications to the Rights of Security Holders**

See Item 10. Additional Information B. Memorandum and Articles of Association Ordinary Shares for a description of the rights of securities holders, which remain unchanged.

**Use of Proceeds**

The following Use of Proceeds information relates to the Registration Statement on Form F-1, as amended (File number: 333-19419) in relation to the initial public offering of 15,300,000 ADSs representing 15,300,000 of our Class A ordinary shares, at an initial offering price of US$9.00 per ADS. We offered and sold 11,500,000 ADSs and the selling shareholders offered and sold 3,800,000 ADSs in our initial public offering. Our initial public offering closed in April 2014. Goldman Sachs (Asia) L.L.C. and Credit Suisee Security (USA) LLC were the representatives of the underwriters for our initial public offering. The aggregate price of the offering amount registered and sold were US$137.7 million.

We received net proceeds of approximately US$92.2 million from our initial public offering. Our expenses incurred and paid to others in connection with the issuance and distribution of the ADSs in our initial public offering totaled US$13.6 million, which included US$9.6 million for underwriting discounts and commissions and US$4.0 million for other expenses. Among the US$13.6 million in expenses, US$4.8 million were paid to Goldman Sachs (Asia) L.L.C., an affiliate of ours and one of the underwriters for our initial public offering.

For the period from April 2, 2014, the date that the F-1 Registration Statement was declared effective by the SEC, to December 31, 2014, we invested the net proceeds from our initial public offering in term deposits and still intend to use the proceeds from our initial public offering for general corporate purposes, which may include investing in course development, expanding our learning center network, sales and marketing activities, technology infrastructure and capital expenditures, upgrading facilities and other general and administrative matters. We may also use a portion of the net proceeds for investing in, or acquiring, complementary businesses, although we have not identified any near-term investment or acquisition targets.

### ITEM 15. CONTROLS AND PROCEDURES

**Evaluation of Disclosure Controls and Procedures**

Our chief executive officer and chief financial officer have performed an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this annual report. Based upon that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were ineffective as of

December 31, 2014 and as of the date that the evaluation of the effectiveness of our disclosure controls and procedures was completed, because of the material weakness in our internal control over financial reporting described below. Our disclosure controls and procedures were not effective to satisfy the objectives for which they are intended.

Notwithstanding management s assessment that our internal control over financial reporting was ineffective as of December 31, 2014 due to the material weakness descrbibed below, we believe that the consolidated financial statements included in this annual report on Form 20-F correctly present our financial position, results of operations and cash flows for the fiscal years covered thereby in all material respects.

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**Management s Annual Report on Internal Control over Financial Reporting and Attestation Report of the Registered Public Accounting Firm**

This annual report does not include a report of management s assessment regarding internal control over financial reporting or an attestation report by our independent registered public accounting firm due to a transition period established by rules of the SEC for newly public companies.

**Changes in Internal Control over Financial Reporting**

In connection with the audit of our consolidated financial statements as of and for the year ended December 31, 2014, we and our independent registered public accounting firm identified a material weakness in our internal control over financial reporting as of December 31, 2014. As defined in standards established by the PCAOB, a material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

The material weakness is related to the lack of GAAP expertise to perform sufficient review in areas subject to significant estimates. To remedy our control deficiencies, we have adopted several measures to improve our internal control over financial reporting. We have engaged an external consulting firm to help us prepare for Section 404 compliance by documenting our processes and internal controls and benchmarking against industry best practices. In addition, we have (i) provided, and intend to continue to provide, on-going training to our accounting and operating personnel across different subsidiaries to improve their accounting knowledge; (ii) developed, and continue to update as needed, a more comprehensive manual on accounting policies and procedures; and (iii) reinforced the oversight and review procedure over high risk areas subject to significant estimates and judgements.

Neither we nor our independent registered public accounting firm undertook a comprehensive assessment of our internal controls for purposes of identifying and reporting material weaknesses and other control deficiencies in our internal control over financial reporting, as we and they will be required to do under the Section 404 of the Sarbenes-Oxley Act of 2002. Had we performed a complete assessment of our internal control over financial reporting or had our independent registered public accounting firm performed an audit of our internal control over financial reporting, additional control deficiencies may have been identified. We will continue to implement the necessary procedures and policies, including those outlined above, to improve our internal controls over financial reporting and remediate any potential material weaknesses and significant deficiencies as we prepare for our initial Section 404 reporting requirement under the Sarbanes-Oxley Act which will take place in the fiscal year ending December 31, 2015 if certain conditions are met.

See Item 3. Key Information D. Risk Factors Risks Relating to Our Business If we fail to maintain an effective system of internal controls, we may be unable to accurately report our results of operations or prevent fraud or fail to meet our reporting obligations, and investor confidence and the market price of our ADSs may be materially and adversely affected.

**ITEM 16.A. AUDIT COMMITTEE FINANCIAL EXPERT**

Our board of directors has determined that Mr. Xiaosong Zhang, an independent director and member of our audit committee, is an audit committee financial expert.

**ITEM 16.B. CODE OF ETHICS**

Our board of directors has adopted a code of ethics that applies to all of the directors, officers and employees of us and our subsidiaries, whether they work for us on a full-time, part-time, consultative, or temporary basis. Certain provisions of the code apply specifically to our chief executive officer, chief financial officer, senior finance officer, controller, senior vice presidents, vice presidents and any other persons who perform similar functions for us. We have posted a copy of our code of business conduct and ethics on our website at http://ir.tarena.com.cn/phoenix.zhtml?c=253008&p=irol-govhighlights.

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**ITEM 16.C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The following table sets forth the aggregate fees by the categories specified below in connection with certain professional services rendered by KPMG Huazhen (SGP), our independent registered public accounting firm, for the periods indicated. We did not pay any other fees to our auditors during the periods indicated below.

| | 2013 | 2014 |
|---|---|---|
| Audit Fees[1] | 977,940 | 975,530 |
| Audit-Related Fees | | |
| Tax Fees[2] | 53,079 | |
| All Other Fees[3] | | 130,362 |

(1) Audit fees means the aggregate fees in each of the fiscal years listed for professional services rendered by our independent registered public accounting firm for the audit of our annual financial statements or services that are normally provided by the auditors in connection with and regulatory filling or engagements.

(2) Tax fees consist of fees billed for the aggregate fees for professional services rendered by our independent registered public accounting firm for tax compliance work and other tax related services.

(3) All Other Fees represent the aggregate fees for services rendered by our independent registered public accounting firm for risk management advisory services.

The policy of our audit committee is to pre-approve all audit and non-audit services provided by KPMG Huazhen (SGP), including audit services, audit-related services, tax services and other services as described above, other than those for *de minimis* services which are approved by the Audit Committee prior to the completion of the audit.

**ITEM 16.D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not Applicable.

**ITEM 16.E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

Not Applicable.

**ITEM 16.F. CHANGE IN REGISTRANT S CERTIFYING ACCOUNTANT**

Not applicable.

**ITEM 16.G. CORPORATE GOVERNANCE**

As a Cayman Islands company listed on the NASDAQ Global Select Market, we are subject to the NASDAQ corporate governance listing standards. However, NASDAQ rules permit a foreign private issuer like us to follow the corporate governance practices of its home country. Certain corporate governance practices in the Cayman Islands, which is our home country, may differ significantly from the NASDAQ corporate governance listing standards. Currently, we do not plan to rely on home country exemption for corporate governance matters. However, if we choose to follow home country practice in the future, our shareholders may be afforded less protection than they

otherwise would under the NASDAQ corporate governance listing standards applicable to U.S. domestic issuers. See Item 3. Key Information D. Risk Factors Risks Relating to Our ADSs We are a foreign private issuer within the meaning of the rules under the Exchange Act, and as such we are exempt from certain provisions applicable to United States domestic public companies.

**ITEM 16.H. MINE SAFETY DISCLOSURE**

Not applicable.

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## PART III.

### ITEM 17. FINANCIAL STATEMENTS

We have elected to provide financial statements pursuant to Item 18.

### ITEM 18. FINANCIAL STATEMENTS

The consolidated financial statements of Tarena International, Inc. and its subsidiaries are included at the end of this annual report.

### ITEM 19. EXHIBITS

| Exhibit Number | Description of Document |
|---|---|
| 1.1 | Fifth Amended and Restated Memorandum and Articles of Association of the Registrant (incorporated herein by reference to Exhibit 3.2 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 2.1 | Registrant s Specimen American Depositary Receipt (included in Exhibit 3.3) |
| 2.2 | Registrant s Specimen Certificate for Class A ordinary shares (incorporated herein by reference to Exhibit 4.2 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 2.3 | Deposit Agreement, among the Registrant, the depositary and holder of the American Depositary Receipts (incorporated herein by reference to Exhibit 4.3 to the registration statement on Form S-8 (File No. 333-197226) filed with the SEC on July 3, 2014) |
| 2.4 | Second Amended and Restated Shareholders Agreement dated as of September 6, 2011 among the Registrant and certain shareholders of the Registrant. (incorporated herein by reference to Exhibit 4.4 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 2.5* | Registration Rights Agreement dated as of April 8, 2014 among the Registrant and New Oriental Education & Technology Group Inc. |
| 4.1 | 2008 Share Incentive Plan, as amended on November 28, 2012 (incorporated herein by reference to Exhibit 10.1 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.2 | 2014 Share Incentive Plan (incorporated herein by reference to Exhibit 10.2 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.3 | Form of Indemnification Agreement with the Registrant s directors (incorporated herein by reference to Exhibit 10.3 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed |

with the SEC on February 27, 2014)

4.4 Form of Employment Agreement between the Registrant and an Executive Officer of the Registrant (incorporated herein by reference to Exhibit 10.5 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

4.5 Amended and Restated Exclusive Business Cooperation Agreement dated November 25, 2013 between Tarena Tech and Beijing Tarena (incorporated herein by reference to Exhibit 10.6 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

4.6 Power of Attorney dated November 25, 2013 granted to Tarena Tech by Mr. Shaoyun Han and acknowledged by Beijing Tarena (incorporated herein by reference to Exhibit 10.7 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

4.7 Power of Attorney dated November 25, 2013 granted to Tarena Tech by Mr. Jianguang Li and acknowledged by Beijing Tarena (incorporated herein by reference to Exhibit 10.8 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

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| | |
|---|---|
| 4.8 | Amended and Restated Exclusive Option Agreement dated November 25, 2013 among Tarena, Tarena Tech, Mr. Shaoyun Han and Beijing Tarena (incorporated herein by reference to Exhibit 10.9 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.9 | Amended and Restated Exclusive Option Agreement dated November 25, 2013 among Tarena, Tarena Tech, Mr. Jianguang Li and Beijing Tarena (incorporated herein by reference to Exhibit 10.10 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.10 | Amended and Restated Loan Agreement dated November 25, 2013 between Tarena Tech and Mr. Shaoyun Han in connection with Beijing Tarena (incorporated herein by reference to Exhibit 10.11 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.11 | Amended and Restated Loan Agreement dated November 25, 2013 between Tarena Tech and Mr. Jianguang Li in connection with Beijing Tarena (incorporated herein by reference to Exhibit 10.12 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.12 | Amended and Restated Share Pledge Agreement dated November 25, 2013 among Tarena Tech, Mr. Shaoyun Han and Beijing Tarena (incorporated herein by reference to Exhibit 10.13 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.13 | Amended and Restated Share Pledge Agreement dated November 25, 2013 among Tarena Tech, Mr. Jianguang Li and Beijing Tarena (incorporated herein by reference to Exhibit 10.14 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.14 | Spousal consent letter dated November 25, 2013 signed by Ying Sun in connection with Beijing Tarena (incorporated herein by reference to Exhibit 10.15 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.15 | Spousal consent letter dated November 25, 2013 signed by Nan Li in connection with Beijing Tarena (incorporated herein by reference to Exhibit 10.16 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.16 | Amended and Restated Exclusive Business Cooperation Agreement dated November 25, 2013 between Tarena Tech and Shanghai Tarena (incorporated herein by reference to Exhibit 10.17 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.17 | Power of Attorney dated November 25, 2013 granted to Tarena Tech by Mr. Shaoyun Han and acknowledged by Shanghai Tarena (incorporated herein by reference to Exhibit 10.18 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.18 | Power of Attorney dated November 25, 2013 granted to Tarena Tech by Mr. Jianguang Li and acknowledged by Shanghai Tarena (incorporated herein by reference to Exhibit 10.19 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |

4.19 Amended and Restated Exclusive Option Agreement dated November 25, 2013 among Tarena, Tarena Tech, Mr. Shaoyun Han and Shanghai Tarena (incorporated herein by reference to Exhibit 10.20 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

4.20 Amended and Restated Exclusive Option Agreement dated November 25, 2013 among Tarena, Tarena Tech, Mr. Jianguang Li and Shanghai Tarena (incorporated herein by reference to Exhibit 10.21 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

4.21 Amended and Restated Loan Agreement dated November 25, 2013 between Tarena Tech and Mr. Shaoyun Han in connection with Shanghai Tarena (incorporated herein by reference to Exhibit 10.22 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014)

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| | |
|---|---|
| 4.22 | Amended and Restated Loan Agreement dated November 25, 2013 between Tarena Tech and Mr. Jianguang Li in connection with Shanghai Tarena (incorporated herein by reference to Exhibit 10.23 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.23 | Amended and Restated Share Pledge Agreement dated November 25, 2013 among Tarena Tech, Mr. Shaoyun Han and Shanghai Tarena (incorporated herein by reference to Exhibit 10.24 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.24 | Amended and Restated Share Pledge Agreement dated November 25, 2013 among Tarena Tech, Mr. Jianguang Li and Shanghai Tarena (incorporated herein by reference to Exhibit 10.25 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.25 | Spousal consent letter dated November 25, 2013 signed by Ying Sun in connection with Shanghai Tarena (incorporated herein by reference to Exhibit 10.26 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 4.26 | Spousal consent letter dated November 25, 2013 signed by Nan Li in connection with Shanghai Tarena (incorporated herein by reference to Exhibit 10.27 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 8.1* | List of Subsidiaries of the Registrant |
| 11.1 | Code of Business Conduct and Ethics of the Registrant (incorporated herein by reference to Exhibit 99.1 to the registration statement on Form F-1 (File No. 333-194191), as amended, initially filed with the SEC on February 27, 2014) |
| 12.1* | CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 12.2* | CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 13.1** | CEO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 13.2** | CFO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 15.1* | Consent of Conyers Dill & Pearman |
| 15.2* | Consent of Han Kun Law Offices |
| 15.3* | Consent of KPMG Huazhen (SGP) |
| 101.INS* | XBRL Instance Document |
| 101.SCH* | XBRL Taxonomy Extension Schema Document |
| 101.CAL* | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF* | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB* | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE* | XBRL Taxonomy Extension Presentation Linkbase Document |

* Filed herewith.

** Furnished herewith.

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**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing its annual report on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

Tarena International, Inc.

By: /s/ Shaoyun Han
Name: Shaoyun Han
Title: Chairman and Chief Executive Officer

Date: April 15, 2015

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## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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**Report of Independent Registered Public Accounting Firm**

**The Board of Directors and Shareholders**

**Tarena International, Inc.:**

We have audited the accompanying consolidated balance sheets of Tarena International, Inc. and subsidiaries (the Company ) as of December 31, 2013 and 2014, and the related consolidated statements of comprehensive income, changes in equity (deficit) and cash flows for each of the years in the three-year period ended December 31, 2014. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as 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 Tarena International, Inc. and subsidiaries as of December 31, 2013 and 2014, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG Huazhen (SGP)

Beijing, China

April 15, 2015

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**TARENA INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

| | Note | December 31, 2013 US$ | December 31, 2014 US$ |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets:** | | | |
| Cash and cash equivalents (including cash of VIEs of US$186,698 and US$243,292 as of December 31, 2013 and 2014, respectively) | | 26,139,255 | 42,659,791 |
| Time deposits | | | 106,834,876 |
| Accounts receivable, net of allowance for doubtful accounts (including accounts receivable, net of allowance for doubtful accounts of VIEs of US$530,826 and nil as of December 31, 2013 and 2014, respectively) | 3 | 15,001,222 | 23,184,239 |
| Prepaid expenses and other current assets (including prepaid expenses and other current assets of VIEs of US$96,980 and US$25,166 as of December 31, 2013 and 2014, respectively) | 4 | 3,497,332 | 8,730,124 |
| Deferred income tax assets (including deferred income tax assets of VIEs of US$484,699 and nil as of December 31, 2013 and 2014, respectively) | 8 | 1,546,213 | 2,055,596 |
| **Total current assets** | | **46,184,022** | **183,464,626** |
| Time deposits | | 12,161,617 | 17,313,054 |
| Accounts receivable, net of allowance for doubtful accounts (including accounts receivable, net of allowance for doubtful accounts of VIEs of US$64,325 and nil as of December 31, 2013 and 2014, respectively) | 3 | 415,881 | 1,488,251 |
| Property and equipment, net (including property and equipment, net of VIEs of US$974,295 and US$19,582 as of December 31, 2013 and 2014, respectively) | 5 | 12,805,567 | 13,373,950 |
| Other non-current assets (including other non-current assets of VIEs of US$3,850 and nil as of December 31, 2013 and 2014, respectively) | | 2,105,832 | 2,314,293 |
| **Total assets** | | **73,672,919** | **217,954,174** |
| **LIABILITIES, MEZZANINE EQUITY AND SHAREHOLDERS EQUITY (DEFICIT)** | | | |
| **Current liabilities:** | | | |
| Accounts payable (including accounts payable of VIEs of US$16,287 and nil as of December 31, 2013 and 2014, respectively) | | 217,451 | 319,138 |
| Income taxes payable (including income taxes payable of VIEs of US$590,281 and US$616,515 as of December 31, 2013 and 2014, respectively) | 8 | 3,012,165 | 5,394,036 |
| Deferred revenue | | 15,487,494 | 19,276,602 |
| Accrued expenses and other current liabilities (including accrued expenses and other current liabilities of VIEs of US$421,531 and US$103,231 as of December 31, 2013 and 2014, respectively) | 6 | 6,617,558 | 8,439,410 |
| **Total current liabilities** | | **25,334,668** | **33,429,186** |

| | | | |
|---|---|---|---|
| Other non-current liabilities (including other non-current liabilities of VIEs of US$20,541 and US$43,664 as of December 31, 2013 and 2014, respectively) | | 243,555 | 1,637,756 |
| **Total liabilities** | | **25,578,223** | **35,066,942** |
| **Commitments and contingencies** | 14 | | |
| **Mezzanine equity:** | | | |
| Series A convertible redeemable preferred shares | 11 | 419,776 | |
| Series B convertible redeemable preferred shares | 11 | 15,747,869 | |
| Series C convertible redeemable preferred shares | 11 | 95,211,135 | |
| **Total mezzanine equity** | | **111,378,780** | |
| **Shareholders equity (deficit)**: | | | |
| Class A ordinary shares (US$0.001 par value, 860,000,000 shares authorized, nil and 23,712,758 shares issued and outstanding as of December 31, 2013 and 2014, respectively) | 10 | | 23,712 |
| Class B ordinary shares (US$0.001 par value, 40,000,000 shares authorized, 12,226,558 shares and 28,733,024 shares issued and outstanding as of December 31, 2013 and 2014, respectively) | 10 | 12,226 | 28,733 |
| Additional paid-in capital | | | 135,886,427 |
| Accumulated other comprehensive income | | 1,634,920 | 1,701,598 |
| Retained earnings (accumulated deficit) | | (64,931,230) | 45,246,762 |
| **Total shareholders equity (deficit)** | | **(63,284,084)** | **182,887,232** |
| **Total liabilities, mezzanine equity and shareholders equity (deficit)** | | **73,672,919** | **217,954,174** |

The accompanying notes are an integral part of these consolidated financial statements.

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**TARENA INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

| | Note | Year Ended December 31, 2012 US$ | 2013 US$ | 2014 US$ |
|---|---|---|---|---|
| Net revenues | 7 | 56,820,281 | 92,833,660 | 136,204,017 |
| Cost of revenues[(a)] | | (17,762,096) | (29,068,058) | (39,079,756) |
| **Gross profit** | | **39,058,185** | **63,765,602** | **97,124,261** |
| Selling and marketing expenses[(a)] | | (16,875,338) | (30,251,656) | (42,562,280) |
| General and administrative expenses[(a)] | | (9,948,830) | (16,223,871) | (29,947,822) |
| Research and development expenses[(a)] | | (1,791,515) | (3,807,155) | (5,445,668) |
| **Operating income** | | **10,442,502** | **13,482,920** | **19,168,491** |
| Interest income | | 1,165,155 | 1,541,175 | 4,360,315 |
| Interest expense | | (5,967) | | |
| Foreign currency exchange gains | | | | 1,196,530 |
| Other income | | 169,891 | 1,294,262 | 2,370,736 |
| **Income before income taxes** | | **11,771,581** | **16,318,357** | **27,096,072** |
| Income tax expense | 8 | (2,219,110) | (2,271,326) | (2,404,824) |
| **Net income** | | **9,552,471** | **14,047,031** | **24,691,248** |
| Accretion of convertible redeemable preferred shares | 11 | (26,545,560) | (44,360,060) | (576,431) |
| **Net income (loss) attributable to Class A and Class B ordinary shareholders** | | **(16,993,089)** | **(30,313,029)** | **24,114,817** |
| **Basic earnings (loss) per Class A and Class B ordinary share** | 13 | **(1.57)** | **(2.77)** | **0.51** |
| **Diluted earnings (loss) per Class A and Class B ordinary share** | 13 | **(1.57)** | **(2.77)** | **0.44** |
| **Net income** | | **9,552,471** | **14,047,031** | **24,691,248** |
| **Other comprehensive income** | | | | |
| Foreign currency translation adjustment, net of nil income taxes | | 68,415 | 1,150,824 | 66,678 |
| **Comprehensive income** | | **9,620,886** | **15,197,855** | **24,757,926** |
| (a) Includes share-based compensation expense as follows (note 12): | | | | |
| Cost of revenues | | (14) | (17,179) | (56,743) |

| | | | |
|---|---|---|---|
| Selling and marketing expenses | (1,296) | (45,233) | (168,601) |
| General and administrative expenses | (124,811) | (654,323) | (3,627,078) |
| Research and development expenses | (3,310) | (48,011) | (209,737) |

The accompanying notes are an integral part of these consolidated financial statements.

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**TARENA INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (DEFICIT)**

| | Ordinary Shares | | | | | | |
|---|---|---|---|---|---|---|---|
| | Number of Class A Ordinary Shares | Amount US$ | Number of Class B Ordinary Shares | Amount US$ | Additional Paid-in Capital US$ | Accumulated Other Comprehensive Income US$ | Retained Earnings (Accumulated Deficit) US$ | Total Shareholders Equity (Deficit) US$ |
| **Balance as of January 1, 2012** | | | **10,851,287** | **10,851** | | **415,681** | **(18,598,138)** | **(18,171,606)** |
| Net income | | | | | | | 9,552,471 | **9,552,471** |
| Foreign currency translation adjustment, net of nil income taxes | | | | | | 68,415 | | **68,415** |
| Share-based compensation | | | | | 129,431 | | | **129,431** |
| Accretion of convertible redeemable preferred shares | | | | | (129,431) | | (26,416,129) | **(26,545,560)** |
| **Balance as of December 31, 2012** | | | **10,851,287** | **10,851** | | **484,096** | **(35,461,796)** | **(34,966,849)** |
| Net income | | | | | | | 14,047,031 | **14,047,031** |
| Conversion of Series A convertible redeemable preferred shares to Class B ordinary shares (note 10 (a)) | | | 1,375,271 | 1,375 | 78,849 | | | **80,224** |
| Foreign currency translation adjustment, net of nil income | | | | | | 1,150,824 | | **1,150,824** |

| | | | | | | |
|---|---|---|---|---|---|---|
| taxes | | | | | | |
| Share-based compensation | | | 764,746 | | | **764,746** |
| Accretion of convertible redeemable preferred shares | | | (843,595) | | (43,516,465) | **(44,360,060)** |
| **Balance as of December 31, 2013** | | **12,226,558** | **12,226** | **1,634,920** | **(64,931,230)** | **(63,284,084)** |
| Net income | | | | | 24,691,248 | **24,691,248** |
| Foreign currency translation adjustment, net of nil income taxes | | | | 66,678 | | **66,678** |
| Share-based compensation | | | 4,062,159 | | | **4,062,159** |
| Accretion of convertible redeemable preferred shares | | | (495,159) | | (81,272) | **(576,431)** |
| Issuance of Class A ordinary shares, upon initial public offering ( IPO ), net of issuance cost of US$4,031,356 | 11,500,000 | 11,500 | 92,212,139 | | | **92,223,639** |
| Issuance of Class A ordinary shares in private placement concurrent with the IPO | 1,500,000 | 1,500 | 13,498,500 | | | **13,500,000** |
| Conversion of Series A convertible redeemable preferred shares to Class B ordinary shares | | 7,196,159 | 7,196 | 412,580 | | **419,776** |
| Conversion of Series B | | 7,319,820 | 7,320 | 16,316,980 | | **16,324,300** |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| convertible redeemable preferred shares to Class B ordinary shares | | | | | | | | |
| Conversion of Series C convertible redeemable preferred shares to Class B ordinary shares | | | 10,914,852 | 10,915 | 95,200,220 | | | **95,211,135** |
| Issuance of Class A ordinary shares upon exercise of share options and vesting of non-vested shares | 1,788,393 | 1,788 | | | 247,024 | | | **248,812** |
| Conversion of Class B ordinary shares to Class A ordinary shares | 8,924,365 | 8,924 | (8,924,365) | (8,924) | | | | |
| Reclassification of APIC and retained earnings (note 10(c)) | | | | | (85,568,016) | | 85,568,016 | |
| **Balance as of December 31, 2014** | **23,712,758** | **23,712** | **28,733,024** | **28,733** | **135,886,427** | **1,701,598** | **45,246,762** | **182,887,232** |

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**TARENA INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| | **US$** | **US$** | **US$** |
| **Operating activities:** | | | |
| Net income | 9,552,471 | 14,047,031 | 24,691,248 |
| *Adjustments to reconcile net income to net cash provided by operating activities:* | | | |
| Depreciation | 2,426,188 | 4,653,914 | 7,078,108 |
| Bad debt expense | 419,383 | 941,065 | 7,487,174 |
| Loss (gain) on disposal of property and equipment | (6,634) | 66,470 | 179,479 |
| Deferred income tax benefit | (21,191) | (1,052,265) | (683,078) |
| Share based compensation expense | 129,431 | 764,746 | 4,062,159 |
| Foreign currency exchange losses (gains), net | | 197,040 | (1,075,257) |
| *Changes in operating assets and liabilities* | | | |
| Accounts receivable | (11,004,712) | 1,117,160 | (16,762,469) |
| Prepaid expenses and other current assets | (993,676) | (534,531) | (2,495,692) |
| Accrued interest income on time deposits | | (330,579) | (2,863,061) |
| Other non-current assets | (421,512) | (472,702) | (651,774) |
| Accounts payable | (133,390) | (7,038) | (45,050) |
| Income taxes payable | 1,113,516 | 1,422,375 | 2,383,557 |
| Deferred revenue | 5,239,498 | 5,444,456 | 3,830,271 |
| Accrued expenses and other current liabilities | 1,055,429 | 3,393,767 | 1,929,718 |
| Other non-current liabilities | 88,744 | 54,642 | 1,394,535 |
| **Net cash provided by operating activities** | **7,443,545** | **29,705,551** | **28,459,868** |
| **Investing activities:** | | | |
| Purchase of property and equipment | (7,188,777) | (9,108,968) | (7,878,945) |
| Proceeds from disposal of property and equipment | 26,209 | 50,060 | 156,216 |
| Purchase of short term investments | | (11,298,158) | (101,390,291) |
| Proceeds from maturity of short term investments | | 11,298,158 | 101,390,291 |
| Purchase of time deposits | (792,104) | (17,286,182) | (115,280,749) |
| Proceeds from maturity of time deposits | 697,052 | 6,456,091 | 3,634,521 |
| Issuance of housing loans to employees | (656,954) | (339,623) | (496,172) |
| Proceeds from repayment of housing loans from employees | | 691,492 | 406,589 |
| **Net cash used in investing activities** | **(7,914,574)** | **(19,537,130)** | **(119,458,540)** |
| **Financing activities:** | | | |
| Proceeds from bank borrowings | 301,000 | | |
| Repayment of bank borrowings | (301,000) | | |
| Amounts received on behalf of a related party | 668,652 | 141,329 | |

| | | | |
|---|---|---|---|
| Repayment of amounts received on behalf of a related party | (745,918) | (232,879) | |
| Advances from a related party | 308,658 | 153,386 | |
| Repayment of advances from a related party | (308,658) | (153,386) | |
| Issuance of Class A ordinary shares upon the IPO | | | 96,254,995 |
| Issuance of Class A ordinary shares in private placement concurrent with the IPO | | | 13,500,000 |
| Issuance of Class A ordinary shares in connection with exercise of share options | | | 248,812 |
| Payment of issuance cost of Series C convertible redeemable preferred shares | (150,000) | | |
| Payment of IPO costs | | (499,331) | (3,532,025) |
| **Net cash provided by (used in) financing activities** | **(227,266)** | **(590,881)** | **106,471,782** |
| Effect of foreign currency exchange rate changes on cash and cash equivalents | 45,756 | 364,495 | 1,047,426 |
| Net increase (decrease) in cash equivalents | (652,539) | 9,942,035 | 16,520,536 |
| Cash and cash equivalents at beginning of year | 16,849,759 | 16,197,220 | 26,139,255 |
| Cash and cash equivalents at end of year | **16,197,220** | **26,139,255** | **42,659,791** |
| **Supplemental disclosure of cash flow information:** | | | |
| Income taxes paid | 1,038,042 | 1,846,576 | 567,401 |
| Interest paid | 5,967 | | |
| **Non-cash investing and financing activities:** | | | |
| Accrual for purchase of equipment | 86,244 | | 286,144 |
| Conversion of Series A convertible redeemable preferred shares to Class B ordinary shares | | 80,224 | 419,776 |
| Conversion of Series B convertible redeemable preferred shares to Class B ordinary shares | | | 16,324,300 |
| Conversion of Series C convertible redeemable preferred shares to Class B ordinary shares | | | 95,211,135 |
| Accrual of IPO costs | | 107,866 | |

The accompanying notes are an integral part of these consolidated financial statements.

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**TARENA INTERNATIONAL, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## 1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS

### *(a) Description of business*

Tarena International, Inc. ( Tarena International ), through its wholly-owned subsidiaries and consolidated variable interest entities or VIEs (collectively referred to hereinafter as the Company ), is principally engaged in providing professional education services including professional information technology ( IT ) training courses and non-IT training courses across the People s Republic of China ( PRC ). All of the Company s operations and customers are located in the PRC.

### *(b) Organization*

Tarena International is a holding company that was incorporated in the Cayman Islands on October 8, 2003 by Mr. Han Shaoyun ( Mr. Han ), the founder and chief executive officer of the Company, and five other individuals. Tarena International is the parent company of a number of wholly-owned subsidiaries that are engaged in professional education services. The Company s education services in certain locations of the PRC were previously conducted through Beijing Tarena Jinqiao Technology Co., Ltd. ( Beijing Tarena ) and Shanghai Tarena Software Technology Co., Ltd. ( Shanghai Tarena ), and their subsidiaries (collectively, the Tarena Entities ), in order to comply with the PRC laws and regulations which restricted foreign investments in companies that were engaged in education services. Tarena Entities were principally engaged in providing professional education services including professional IT training courses in those locations and operated 23 learning centers as of December 31, 2011. Pursuant to the VIE Agreements as described below, Tarena International has effective financial control over Tarena Entities and their initial capital funding was provided by Tarena Technologies Inc., (a wholly-owned subsidiary of Tarena International or the WOFE , formerly known as Beijing Tarena Technology Co., Ltd.). The recognized and unrecognized revenue-producing assets that were held by Tarena Entities primarily consisted of property and equipment, operating leases for the learning premises, ICP license, www.it211.com.cn website and assembled workforce in those learning centers. Because of change in PRC laws and regulations in 2012 which encourages foreign investments in education services, the Company began to transfer most of the operations, including related assets and liabilities of Tarena Entities to the wholly-owned subsidiaries of Tarena International.

The registered capital of Beijing Tarena and Shanghai Tarena is RMB2 million and RMB1 million, respectively. All of the equity interests of Tarena Entities are legally held by Mr. Han and Mr. Li Jianguang ( Mr. Li ), a director of Tarena International. Both individuals are nominee equity holders of Tarena Entities and holding their equity interests on behalf of Tarena International. Through a series of contractual agreements and arrangements (the VIE Agreements ), among Tarena International, WOFE, Tarena Entities and their nominee equity holders, the nominee equity holders of Tarena Entities have granted all their legal rights including voting rights and disposition rights of their equity interests in Tarena Entities to Tarena International. The nominee equity holders of Tarena Entities do not participate significantly in income and loss and do not have the power to direct the activities of the Tarena Entities that most significantly impact their economic performance. Accordingly, the Tarena Entities are considered variable interest entities.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(b) Organization (continued)***

In accordance with Accounting Standards Codification ( ASC ) 810-10-25-38A, Tarena International has a controlling financial interest in Tarena Entities because Tarena International has (i) the power to direct activities of Tarena Entities that most significantly impact the economic performance of Tarena Entities; and (ii) the obligation to absorb the expected losses and the right to receive expected residual return of Tarena Entities that could potentially be significant to Tarena Entities. Thus, Tarena International is the primary beneficiary of the Tarena Entities.

Under the terms of the VIE Agreements, Tarena International has (i) the right to receive economic benefits that could potentially be significant to Tarena Entities in the form of service fees under the exclusive business cooperation agreements; (ii) the right to receive all dividends declared by Tarena Entities and the right to all undistributed earnings of Tarena Entities; (iii) the right to receive the residual benefits of Tarena Entities through its exclusive option to acquire 100% of the equity interests in Tarena Entities, to the extent permitted under PRC law. Accordingly, the financial statements of Tarena Entities are consolidated in Tarena International s consolidated financial statements.

Under the terms of the VIE Agreements, Tarena Entities nominee equity holders have no rights to the net assets nor have the obligations to fund the deficit, and such rights and obligations have been vested to Tarena International. All of the equity (net assets) and net income of Tarena Entities are attributed to Tarena International.

The key terms of the VIE Agreements are as follows:

**Loan Agreements:** The WOFE provided RMB3 million loans in aggregate to Tarena Entities nominee equity holders for the sole purpose of their contribution of Tarena Entities registered capital. The nominee equity holders of Tarena Entities can only repay the loans by transferring all of their legal equity interest in Tarena Entities to the WOFE or its designated representatives pursuant to the exclusive option agreements. The loans shall be interest-free, unless the transfer price exceeds the principal of the loans when each nominee equityholder of Tarena Entities transfers his equity interests in Tarena Entities to Tarena International or its designated representatives. Such excess over the principal of the loan shall be deemed as the interest of the loans to the extent permitted under the PRC law. The initial terms of the loans expire in 2023, which can be extended with the written notice of both the WOFE and Tarena Entities before expiration.

**Exclusive Option Agreements:** Each of the nominee equity holders irrevocably granted Tarena International, Inc. or its designated representatives an exclusive option to purchase, to the extent permitted under PRC law, all or part of his equity interests in Tarena Entities. In addition, Tarena International has the option to acquire the equity interests of Tarena Entities for a specified price equal to the loan provided by the WOFE to the nominee equity holders. If the lowest price permitted under PRC law is higher than the above price, the lowest price permitted under PRC law shall apply. Without Tarena International s prior written consent, the nominee equity holders shall not sell, transfer, mortgage, or otherwise dispose any equity interests in Tarena Entities. These agreements will remain effective until all equity interests held in Tarena Entities by the nominee equity holders are transferred or assigned to Tarena International or its designated representatives.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(b) Organization (continued)***

**Exclusive Business Cooperation Agreements:** The WOFE has the exclusive right to provide, among other things, technical support, business support and related consulting services to Tarena Entities and Tarena Entities agree to accept all the consultation and services provided by the WOFE. Without the WOFE s prior written consent, Tarena Entities are prohibited from engaging any third party to provide any of the services under this agreement. In addition, the WOFE exclusively owns all intellectual property rights arising out of or created during the performance of this agreement. Tarena Entities agree to pay a monthly service fee to the WOFE at an amount determined solely by the WOFE after taking into account factors including the complexity and difficulty of the services provided, the time consumed, the seniority of the WOFE employees providing services to Tarena Entities, the value of services provided, the market price of comparable services and the operating conditions of Tarena Entities. Furthermore, to the extent permitted under the PRC law, the WOFE agrees to provide financial support to Tarena Entities. The term of the agreement will remain effective unless the WOFE terminates the agreement in writing or a competent governmental authority rejects the renewal applications by either Tarena Entities or the WOFE to renew its respective business license upon expiration. Tarena Entities are not permitted to terminate this agreement in any event unless required by applicable laws.

**Power of Attorney:** Each nominee equity holder of Tarena Entities appointed the WOFE as the attorney-in-fact to act on all matters pertaining to Tarena Entities and to exercise all of their rights as an equity holder of Tarena Entities, including but not limited to attend shareholders meetings, vote on their behalf on all matters of Tarena Entities requiring shareholders approval under PRC laws and regulations and the articles of association of Tarena Entities, designate and appoint directors and senior management members. The WOFE may authorize or assign its rights under this appointment to any other person or entity at its sole discretion without prior notice to the nominee equity holders of Tarena Entities. Each power of attorney will remain effective until the nominee equity holder ceases to hold any equity interest in Tarena Entities.

**Spousal Consent Letters:** The spouses of the nominee equity holders of Tarena Entities executed spousal consent letters to acknowledge that the equity interests in Tarena Entities held by their spouses will be disposed of pursuant to the equity disposal agreement and equity interest pledge agreement and they will not make any assertions in connection with the equity interests in Tarena Entities held by their spouses. They shall be bound by the related VIE agreements and comply with the obligations thereunder as an equity holder of Tarena Entities if they obtain any equity interests in Tarena Entities which are held by their spouses for any reasons.

**Equity Interest Pledge Agreements:** Pursuant to the equity interest pledge agreement, Tarena Entities nominee equity holders pledged all of their equity interests in Tarena Entities to the WOFE to guarantee their performance of the obligations under the contractual arrangements including but not limited to, the service fees due to the WOFE. If Tarena Entities or any of Tarena Entities nominee equity holders breaches its contractual obligations under the contractual arrangements, the WOFE, as the pledgee, will be entitled to certain rights and entitlements, including receiving proceeds from the auction or sale of whole or part of the pledged equity interests of Tarena Entities in accordance with legal procedures. The WOFE has the right to receive dividends generated by the pledged equity interests during the term of the pledge. If any event of default as provided in the contractual arrangements occurs, the WOFE, as the pledgee, will be entitled to dispose of the pledged equity interests in accordance with PRC laws and regulations. The equity interest pledge agreements became effective on the date when the agreements were duly

executed. The pledge was registered with the relevant local administration for industry and commerce in 2013 and will remain binding until Tarena Entities and their nominee equity holders discharge all their obligations under the contractual arrangements. The registration of the equity pledge enables the WOFE to enforce the equity pledge against third parties who acquire the equity interests of Tarena Entities in good faith.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(b) Organization (continued)***

Tarena International relies on the VIE Agreements to operate and control the Tarena Entities. However, these contractual arrangements may not be as effective as direct equity ownership in providing Tarena International with control over Tarena Entities. Any failure by Tarena Entities or the nominee equity holders to perform their obligations under the VIE Agreements would have a material adverse effect on the consolidated financial position and consolidated financial performance of the Company. All the VIE Agreements are governed by PRC law and provide for the resolution of disputes through arbitration in the PRC. Accordingly, these contracts would be interpreted in accordance with PRC law and any disputes would be resolved in accordance with PRC legal procedures. The legal system in the PRC is not as developed as some other jurisdictions, such as the United States. As a result, uncertainties in the PRC legal system could limit Tarena International s ability to enforce these contractual arrangements. In addition, if the legal structure and the VIE Agreements were found to be in violation of any existing or future PRC laws and regulations, Tarena International may be subject to fines or other legal or administrative sanctions.

In the opinion of management, based on the legal opinion obtained from the Company s PRC legal counsel, the above contractual arrangements are legally binding and enforceable and do not violate current PRC laws and regulations. However, there are uncertainties regarding the interpretation and application of existing and future PRC laws and regulations. Accordingly, Tarena International cannot be assured that PRC regulatory authorities will not ultimately take a contrary view to its opinion. If the current ownership structure of the Company and the VIE Arrangements are found to be in violation of any existing or future PRC laws and regulations, the PRC government could:

- revoke the business and operating licenses of the WOFE, its subsidiaries and Tarena Entities;
- discontinue or restrict the conduct of any transactions between the WOFE, its subsidiaries and Tarena Entities;
- impose fines, confiscate the income from Tarena Entities, or impose other requirements with which the Company may not be able to comply;
- require Tarena International to restructure its ownership structure or operations, including terminating the contractual arrangements with Tarena Entities and deregistering the equity pledges of Tarena Entities; and
- restrict or prohibit the use of the proceeds of future offering to finance the Company s business and operations in the PRC.

If the imposition of any of these government actions causes Tarena International to lose its right to direct the activities of Tarena Entities or its right to receive substantially all the economic benefits and residual returns from Tarena

Entities and Tarena International is not able to restructure its ownership structure and operations in a satisfactory manner, Tarena International would no longer be able to consolidate the financial results of Tarena Entities. In the opinion of management, the likelihood of deconsolidation of the Tarena Entities is remote based on current facts and circumstances.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(b) Organization (continued)***

The equity interests of Tarena Entities are legally held by Mr. Han and Mr. Li as nominee equity holders on behalf of the Company. Mr. Han and Mr. Li are also directors of Tarena International. Mr. Han and Mr. Li each holds 32.7% and 21.2% of the total voting rights as of December 31, 2014, respectively, assuming the exercise of all outstanding options held by Mr. Han (and his spouse) and Mr. Li as of such date. The Company cannot assure that when conflicts of interest arise, either of the nominee equity holders will act in the best interests of the Company or such conflicts will be resolved in the Company s favor. Currently, the Company does not have any arrangements to address potential conflicts of interest between the nominee equity holders and the Company, except that Tarena International could exercise the purchase option under the exclusive option agreement with the nominee equity holders to request them to transfer all of their equity ownership in Tarena Entities to a PRC entity or individual designated by Tarena International. The Company relies on the nominee equity holders, who are both Tarena International s directors and who owe a fiduciary duty to Tarena International, to comply with the terms and conditions of the contractual arrangements. Such fiduciary duty requires directors to act in good faith and in the best interests of Tarena International and not to use their positions for personal gains. If the Company cannot resolve any conflict of interest or dispute between the Company and the nominee equity holders of Tarena Entities, the Company would have to rely on legal proceedings, which could result in disruption of the Company s business and subject the Company to substantial uncertainty as to the outcome of any such legal proceedings.

The Company s involvement with Tarena Entities under the VIE Agreements affected the Company s consolidated financial position, results of operations and cash flows as indicated below.

The assets and liabilities of Tarena Entities that were included in the accompanying consolidated financial statements as of December 31, 2013 and 2014 are as follows:

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| Cash | 186,698 | 243,292 |
| Accounts receivable, net of allowance for doubtful accounts | 530,826 | |
| Prepaid expenses and other current assets | 96,980 | 25,166 |
| Amounts due from related parties | 5,783,142 | 4,394,839 |
| Deferred income tax assets | 484,699 | |
| **Total current assets** | **7,082,345** | **4,663,297** |
| Accounts receivable, net of allowance for doubtful accounts | 64,325 | |
| Property and equipment, net | 974,295 | 19,582 |
| Other non-current assets | 3,850 | |
| **Total assets** | **8,124,815** | **4,682,879** |

| | | |
|---|---|---|
| Accounts payable | 16,287 | |
| Income taxes payable | 590,281 | 616,515 |
| Accrued expenses and other current liabilities | 421,531 | 103,231 |
| Amounts due to related parties, including amounts due to WOFE for accrued service fees | 4,445,366 | 3,486,740 |
| **Total current liabilities** | **5,473,465** | **4,206,486** |
| Other non-current liabilities | 20,541 | 43,664 |
| **Total liabilities** | **5,494,006** | **4,250,150** |

Amounts due from/to related parties represents the amounts due from/to Tarena International and its wholly-owned subsidiaries, which are eliminated upon consolidation.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(b) Organization (continued)***

The financial performance and cash flows of Tarena Entities that were included in the accompanying consolidated financial statements for the years ended December 31, 2012, 2013 and 2014 are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Net revenues | 18,343,915 | 8,191,886 | 472,512 |
| Net income (loss) | 3,607,731 | (1,917,256) | (2,285,932) |
| Net cash provided by (used in) operating activities | 4,172,858 | (1,538,619) | (610,826) |
| Net cash provided by (used in) investing activities | (933,382) | (470,805) | 66,824 |
| Net cash provided by (used in) financing activities | (3,253,753) | 1,436,631 | 671,417 |

All of the assets of Tarena Entities can be used only to settle obligations of Tarena Entities. None of the assets of Tarena Entities have been pledged or collateralized. The creditors of Tarena Entities do not have recourse to the general credit of Tarena International and its wholly-owned subsidiaries. Assets of Tarena Entities that can be used only to settle obligations of Tarena Entities and liabilities of Tarena Entities for which creditors (or beneficial interest holders) do not have recourse to the general credit of Tarena International and its wholly owned subsidiaries have been presented parenthetically alongside each balance sheet caption on the face of the consolidated balance sheets.

During the periods presented, Tarena International and its wholly-owned subsidiaries provided financial support to Tarena Entities that they were not previously contractually required to provide in the form of advances. To the extent Tarena Entities require financial support, pursuant to the exclusive business cooperation agreements, the WOFE may, at its option and to the extent permitted under the PRC law, provide such support to Tarena Entities through loans to Tarena Entities nominee equity holders or entrustment loans to Tarena Entities.

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(c) Basis of presentation***

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ( U.S. GAAP ).

***(d) Significant concentrations and risks***

*Revenue concentration*

A substantial portion of the Company s total net revenues are generated from Java and Digital Arts courses. The percentages of the Company s total net revenues from Java and Digital Arts training courses are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| Java | 71.3% | 59.3% | 36.7% |
| Digital Arts | 0.4% | 6.7% | 29.1% |
| **Total** | **71.7%** | **66.0%** | **65.8%** |

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**1 DESCRIPTION OF BUSINESS, ORGANIZATION, BASIS OF PRESENTATION AND SIGNIFICANT CONCENTRATIONS AND RISKS (CONTINUED)**

***(d) Significant concentrations and risks (continued)***

The Company expects net revenues from these two training courses to continue to represent a substantial portion of its total net revenues in the future. Negative factors that adversely affect net revenues generated by these two training courses will have a material adverse effect on the Company s business, financial condition and results of operations.

*Geographic concentration*

A substantial portion of the Company s total net revenues are derived from learning centers that operate in Beijing and Hangzhou. The percentages of the Company s total net revenues generated from learning centers that operate in Beijing and Hangzhou are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| Beijing | 30.6% | 36.1% | 15.5% |
| Hangzhou | 7.4% | 5.3% | 25.5% |
| **Total** | **38.0%** | **41.4%** | **41.0%** |

The Company expects revenues derived from the learning centers that operate in Beijing and Hangzhou to continue to represent a significant portion of its total net revenues. Negative factors that adversely affect professional education services in Beijing or Hangzhou will have a material adverse effect on the Company s business, financial condition and results of operations.

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***(a) Principles of consolidation***

The consolidated financial statements include the financial statements of Tarena International, its wholly-owned subsidiaries, VIEs in which Tarena International is the primary beneficiary and their wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated on consolidation.

***(b) Use of estimates***

The preparation of consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such

estimates and assumptions include the collectability of accounts receivable, the fair values of financial instruments and share-based compensation awards, the realizability of deferred income tax assets, the accruals for tax uncertainties and other contingencies, the recoverability of the carrying amounts of property and equipment and the useful lives of property and equipment. The current economic environment has increased the degree of uncertainty inherent in those estimates and assumptions.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(c) Foreign currency***

The accompanying consolidated financial statements have been expressed in U.S. dollar ( USD ), the Company s reporting currency. The functional currency of Tarena International and Tarena Hong Kong Limited ( Tarena HK ) is the USD. The functional currency of Tarena International s PRC subsidiaries and consolidated VIEs is Renminbi ( RMB ). Transactions denominated in currencies other than the functional currency are translated into the functional currency at the exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using the applicable exchange rate at the balance sheet date. The resulting exchange differences are recorded in foreign currency exchange gains in the consolidated statements of comprehensive income.

Assets and liabilities of entities with functional currencies other than USD are translated into USD using the exchange rate on the balance sheet date. Revenues and expenses are translated into USD at average rates prevailing during the reporting period. The resulting foreign currency translation adjustment are recorded in accumulated other comprehensive income within shareholders equity (deficit).

Since the RMB is not a fully convertible currency, all foreign exchange transactions involving RMB must take place either through the People s Bank of China (the PBOC ) or other institutions authorized to buy and sell foreign exchange. The exchange rates adopted for the foreign exchange transactions are the rates of exchange quoted by the PBOC.

***(d) Cash, cash equivalents and time deposits***

Cash consist of cash on hand and cash in bank, which are unrestricted as to withdrawal. Cash equivalents consist of interest-bearing certificates of deposit with initial term of no more than three months when purchased.

Time deposits, which mature within one year as of the balance sheet date, represent interest-bearing certificates of deposit with an initial term of greater than three months when purchased. Time deposits which mature over one year as of the balance sheet date are included in non-current assets.

Cash, cash equivalents and time deposits maintained at banks consist of the following:

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| RMB denominated bank deposits with financial institutions in the PRC | 35,234,336 | 58,639,210 |
| US dollar denominated bank deposits with a financial institutions in the PRC | 1,669,384 | 36,216,381 |
| US dollar denominated bank deposits with financial institutions in Hong Kong Special Administrative Region ( HK SAR ) | 1,378,195 | 771,786 |
| | 5,017 | 7 |

| | | |
|---|---|---|
| HK dollar denominated bank deposits with a financial institution in HK SAR | | |
| RMB denominated bank deposits with a financial institution in HK SAR | 414 | 412 |
| RMB denominated bank deposits in the Singapore | | 71,178,287 |

To limit exposure to credit risk relating to bank deposits, the Company primarily places bank deposits only with large financial institutions in the PRC, HK SAR and Singapore with acceptable credit rating.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(e) Short-term investment***

During the years ended December 31, 2013 and 2014, the Company invested US$11,298,158 and US$101,390,291, respectively, in financial products managed by two banks in the PRC. The terms of the financial products range between 17 days and 91 days. The financial products matured before December 31, 2013 and 2014, respectively. The Company earned investment income of US$39,930 and US$757,300, respectively on the financial products, which was included in other income in the consolidated statements of comprehensive income for the years ended December 31, 2013 and 2014.

***(f) Accounts receivable***

Accounts receivable primarily represent tuition fees due from students. Accounts receivable which are due over one year as of the balance sheet date are presented as non-current assets. The unearned interest on accounts receivable which are due over one year is reported in the consolidated balance sheets as a direct deduction from the principal amount of accounts receivable. See note 2 (h). The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Accounts receivable is considered past due based on its contractual terms. In establishing the allowance, management considers historical losses, the students financial condition, the amount of accounts receivables in dispute, the accounts receivables aging and the students payment patterns. Accounts receivable which are deemed to be uncollectible are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. There is a time lag between when the Company estimates a portion of or the entire account balances to be uncollectible and when a write off of the account balances is taken. The Company takes a write off of the account balances when the Company can demonstrate all means of collection on the outstanding balances have been exhausted or the balances have been overdue for more than three years.

***(g) Property and equipment***

Property and equipment are recorded at cost. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets. The estimated useful life of property and equipment is as follows:

| | |
|---|---|
| Furniture | 5 years |
| Office equipment | 3 to 4 years |
| Leasehold improvements | Shorter of the lease term or the estimated useful life of the assets |

Ordinary maintenance and repairs are charged to expenses as incurred, while replacements and betterments are capitalized. When items are retired or otherwise disposed of, income is charged or credited for the difference between net book value of the item disposed and proceeds realized thereon.

Property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Recoverability of a long-lived asset or asset group to be held and used is measured by a comparison of the carrying amount of an asset or asset group to the estimated undiscounted future cash flows expected to be generated by the asset or asset group. If the carrying value of an asset or asset group exceeds its estimated undiscounted future cash flows, an impairment loss is recognized by the amount that the

carrying value exceeds the estimated fair value of the asset or asset group. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values and third party independent appraisals, as considered necessary. Assets to be disposed are reported at the lower of carrying amount or fair value less costs to sell, and are no longer depreciated. No impairment of long-lived assets was recognized for any of the years presented.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(h) Revenue recognition***

Revenue is recognized when all of the following conditions are met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. These criteria as they relate to each of the following major revenue generating activities are described below. Revenue is presented net of business tax and value added taxes ( VAT ) at rates ranging between 3% and 6%, and surcharges. VAT and business tax collected from customers, net of VAT paid for purchases, is recorded as a liability in the consolidated balance sheets until it is paid to the tax authorities.

*Tuition fees*

Educational and professional tuition fees are recognized as revenue ratably over the period of the training course, which primarily range from four to five months. The unearned portion of tuition fees is recorded as deferred revenue.

The Company offers certain qualified students to pay their tuition fees on installment for a period of time exceeding one year. When tuition services are sold on repayment terms that exceeds one year beyond the point in time that revenue is recognized, the receivable, and therefore the revenue is recorded at the present value of the payments. The difference between the present value of the receivable and the nominal or principal value of the tuition fees is recognized as interest income over the contractual repayment period using the effective interest rate method. The interest rate used to determine the present value of total amount receivable is the rate at which the students can obtain financing of a similar nature from other sources at the date of the transaction.

*Certification service revenue*

The Company provides certification service to students who complete the training course and enroll for the exams. The Company is responsible for the certification service, including organization, proctoring and grading of exams. All certificates are issued by third parties to the students who pass the exam. The Company acts as the principal in providing this service and recognizes revenue on gross basis because the Company is the primary obligor in the arrangement and is responsible for fulfilling the ordered services by the students. Cash received before the students taking the exam, is recorded as deferred revenue, and subsequently recognized as certification service revenue upon completion of the certification service.

***(i) Cost of revenues***

Cost of revenues consists of payroll and employee benefits, rent expenses of learning centers, depreciation relating to property and equipment used for operating the learning centers, and other operating costs that are directly attributed to the provision of training services.

***(j) Advertising costs***

Advertising costs are expensed as incurred and included in selling and marketing expenses. Advertising costs were US$5,928,454, US$11,570,458 and US$16,738,921 for the years ended December 31, 2012, 2013 and 2014, respectively.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(k) Operating lease***

The Company leases premises for learning centers and offices under non-cancellable operating leases. Leases with escalated rent provisions are recognized on a straight-line basis commencing with the beginning of the lease term. There are no capital improvement funding, other lease concessions or contingent rent in the lease agreements. The lease terms of the Company s learning centers range between 1 and 10 years. The Company has historically been able to renew all learning centers leases. The Company has no legal or contractual asset retirement obligations at the end of the lease term.

Certain learning centers of the Company sublease a portion of the areas to certain students for their living accommodation. Income from subleases is recognized on a straight-line basis over the term of the lease and recognized as reduction of costs of revenues.

***(l) Government grant***

Government grant is recognized when there is reasonable assurance that the Company will comply with the conditions attach to it and the grant will be received. Government grant for the purpose of giving immediate financial support to the Company with no future related costs is recognized in the Company s consolidated statements of comprehensive income when the grant becomes receivable. Government grant of US$169,891, US$1,254,332 and US$1,613,436 was recognized and included in other income for the years ended December 31, 2012, 2013 and 2014, respectively.

***(m) Research and development costs***

Research and development costs primarily consist of software developed for internal use. The Company expenses all costs that are incurred in connection with the planning and implementation phases of the development of software. Costs incurred in the development phase are capitalized and amortized over the estimated life of the software. No costs were capitalized for any of the periods presented.

***(n) Employee benefits***

Pursuant to relevant PRC regulations, the Company is required to make contributions to various defined contribution plans organized by municipal and provincial PRC governments. The contributions are made for each PRC employee at rates ranging from 22.0% to 52.5% on a standard salary base as determined by local social security bureau. Contributions to the defined contribution plans are charged to the consolidated statements of comprehensive income when the related service is provided. For the years ended December 31, 2012, 2013 and 2014, the costs of the Company s obligations to the defined contribution plans amounted to US$3,518,397, US$5,850,415 and US$8,385,747, respectively. The Company has no other obligation for the payment of employee benefits associated with these plans beyond the contributions described above.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(o) Income taxes***

Income taxes are accounted for under the asset and liability method. Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and tax loss and tax credit carry forwards. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the periods in which those temporary differences are expected to be recovered or settled. The effect on deferred income tax assets and liabilities of a change in tax rates or tax laws is recognized in the consolidated statements of comprehensive income in the period the change in tax rates or tax laws is enacted. A valuation allowance is provided to reduce the carrying amount of deferred income tax assets if it is considered more likely than not that some portion or all of the deferred income tax assets will not be realized.

The Company recognizes in the consolidated financial statements the impact of a tax position, if that position is more likely than not of being sustained upon examination, based on the technical merits of the position. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company has elected to classify interest and penalties related to an unrecognized tax benefits, if and when required, as part of income tax expense in the consolidated statements of comprehensive income.

***(p) Deferred offering costs***

Deferred offering costs consist principally of legal, printing and registration costs in connection with the IPO. Deferred offering costs as of December 31, 2013 amounted to US$615,793 and were included in other non-current assets. Upon completion of the IPO on April 3, 2014, the deferred offering costs were recognized as a reduction the offering proceeds.

***(q) Share based compensation***

The Company measures the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award and recognizes the cost over the period the employee is required to provide service in exchange for the award, which generally is the vesting period. The Company recognizes compensation cost for an award with only service conditions that has a graded vesting schedule on a straight-line basis over the requisite service period for the entire award, net of estimated forfeitures, provided that the cumulative amount of compensation cost recognized at any date at least equals the portion of the grant-date value of such award that is vested at that date. Forfeiture rates are estimated based on historical and future expectations of employee turnover rates.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(r) Commitments and contingencies***

In the normal course of business, the Company is subject to loss contingencies, such as legal proceedings and claims arising out of its business, that cover a wide range of matters, including, among others, government investigations, shareholder lawsuits, and non-income tax matters. An accrual for a loss contingency is recognized when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. If a potential material loss contingency is not probable but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, is disclosed.

The allowance for off-balance-sheet credit exposures is maintained at a level believed by management to be sufficient to absorb estimated probable losses related to the guarantee under the Student Loan Program. See note 9. The Company evaluates the current status of the payment and performance risk of the guarantee based on periodic evaluations of the actual defaults, estimated future defaults, current understanding of the students status and existing economic conditions.

***(s) Earnings (loss) per share***

Basic earnings (loss) per Class A and Class B ordinary share is computed by dividing net income (loss) attributable to Tarena International s Class A and Class B ordinary shareholders by the weighted average number of Class A and Class B ordinary shares outstanding during the year using the two-class method. Under the two-class method, net income (loss) attributable to Tarena International s Class A and Class B ordinary shareholders is allocated between Class A and Class B ordinary shares and other participating securities based on participating rights in undistributed earnings. Tarena International s Series A convertible redeemable preferred shares, Series B convertible redeemable preferred shares and Series C convertible redeemable preferred shares are participating securities since the holders of these securities participate in dividends on the same basis as Class A and Class B ordinary shareholders. These participating securities are not included in the computation of basic loss per Class A and Class B ordinary share in periods when the Company reports net loss, because these participating security holders have no obligation to share in the losses of Tarena International based on the contractual rights and obligations of these participating securities.

Diluted earnings (loss) per share is calculated by dividing net income (loss) attributable to Tarena International s Class A and Class B ordinary shareholders as adjusted for the effect of dilutive Class A and Class B ordinary share equivalents, if any, by the weighted average number of Class A and Class B ordinary and dilutive Class A and Class B ordinary share equivalents outstanding during the year. Class A and Class B ordinary share equivalents include the Class A and Class B ordinary shares issuable upon the exercise of the outstanding share options (using the treasury stock method) and conversion of convertible redeemable preferred shares (using the as-if-converted method). Potential dilutive securities are not included in the calculation of diluted earnings (loss) per Class A and Class B ordinary share if the impact is anti-dilutive.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(t) Segment reporting***

The Company uses the management approach in determining its operating segments. The management approach considers the internal reporting used by the Company s chief operating decision maker for making decisions about the allocation of resources to and the assessment of the performance of the segments of the Company. Management has determined that the Company has one operating segment, which is the training segment. All of the Company s operations and customers are located in the PRC. Consequently, no geographic information is presented.

***(u) Fair value measurements***

The Company applies the provisions of ASC Topic 820, *Fair Value Measurements and Disclosures,* for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring and nonrecurring basis. ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when pricing the asset or liability. ASC Topic 820 also establishes a framework for measuring fair value and expands disclosures about fair value measurements.

ASC Topic 820 establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. ASC Topic 820 establishes three levels of inputs that may be used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety. In situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects management s own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by management based on the best information available in the circumstances.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***(u) Fair value measurements (continued)***

The carrying amounts of accounts receivable, housing loans to employees, accounts payable, accrued expenses and other current liabilities as of December 31, 2013 and 2014 approximate their fair value.

The carrying amounts of non-current time deposits as of December 31, 2013 and 2014 approximates their fair value since the interest rates of the time deposits did not differ significantly from the market interest rates for similar types of time deposits.

The fair values of time deposits as of December 31, 2013 and 2014 are categorized as Level 2 measurement.

***(v) Recently issued accounting standards***

In April 2014, the Financial Reporting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. ASU 2014-08 changes the requirements for reporting discontinued operations. This ASU limits discontinued operations reporting to disposals of components of an entity that represent strategic shifts that have a major effect on an entity s operations and financial results. As a result, the Company expects to report fewer discontinued operations under the new standard than would otherwise be reported under previous requirements. The new standard is effective for any disposals of components of the Company in annual reporting periods beginning after December 15, 2014. The Company will implement the provisions of ASU 2014-08 as of January 1, 2015.

The FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, in May 2014. ASU 2014-09 requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity should also disclose sufficient quantitative and qualitative information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new standard is effective for annual reporting periods beginning after December 15, 2017. The Company will implement the provisions of ASU 2014-09 as of January 1, 2018. The Company has not yet determined the impact of the new standard on its current policies for revenue recognition.

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**3 ACCOUNTS RECEIVABLE**

Accounts receivable consists of the following:

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| **Accounts receivable:** | | |
| Gross | 18,859,182 | 32,420,858 |
| Unearned interest | (1,139,050) | (1,971,843) |
| **Total accounts receivable** | **17,720,132** | **30,449,015** |
| Less: allowance for doubtful accounts | (2,303,029) | (5,776,525) |
| **Accounts receivable, net** | **15,417,103** | **24,672,490** |

The classification of accounts receivable is as follows:

| | | December 31, | |
|---|---|---|---|
| | | 2013 | 2014 |
| | | US$ | US$ |
| Accounts receivable, net | current portion | 15,001,222 | 23,184,239 |
| Accounts receivable, net | non-current portion | 415,881 | 1,488,251 |
| **Total accounts receivable, net** | | **15,417,103** | **24,672,490** |

The movements of the allowance for doubtful accounts are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Balance at the beginning of the year | 882,972 | 1,306,306 | 2,303,029 |
| Additions charged to bad debt expense | 419,383 | 941,065 | 7,487,174 |
| Write-off of bad debt allowance | | | (4,035,620) |
| Foreign currency translation adjustment | 3,951 | 55,658 | 21,942 |
| Balance at the end of the year | 1,306,306 | 2,303,029 | 5,776,525 |

The aging analysis of our accounts receivable based on due date is as follows:

| | As of December 31, |
|---|---|

| | 2013<br>US$ | 2014<br>US$ |
|---|---|---|
| **Aging:** | | |
| current | 11,032,162 | 11,940,237 |
| 1-3 months past due | 2,583,817 | 5,058,887 |
| 4-6 months past due | 1,428,159 | 4,139,377 |
| 7-12 months past due | 1,454,967 | 6,119,995 |
| greater than one year past due | 1,221,027 | 3,190,519 |
| **Total accounts receivable** | **17,720,132** | **30,449,015** |

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**4 PREPAID EXPENSES AND OTHER CURRENT ASSETS**

Prepaid expenses and other current assets consist of the following:

| | | December 31, | |
|---|---|---|---|
| | | 2013 | 2014 |
| | | US$ | US$ |
| **Prepaid expenses and other current assets:** | | | |
| Interest receivable from time deposits | | | 2,556,518 |
| Prepaid rental expenses | | 1,451,388 | 2,260,000 |
| Prepaid advertising expenses | | 638,143 | 1,751,146 |
| Prepaid value-added tax | | | 715,157 |
| Housing loans made to employees | (a) | 345,126 | 436,467 |
| Staff advances | (b) | 164,896 | 81,903 |
| Others | (c) | 897,779 | 928,933 |
| **Total prepaid expenses and other current assets** | | **3,497,332** | **8,730,124** |

(a) The Company provided one-year housing loans to the employees to help them finance their purchase of apartments.
(b) Staff advances are provided to staff for traveling and related expenses and are expensed when incurred.
(c) Others mainly represent textbooks and other miscellaneous prepaid expenses.

**5 PROPERTY AND EQUIPMENT, NET**

Property and equipment consists of the following:

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| Furniture | 760,434 | 934,033 |
| Office equipment | 19,249,724 | 23,583,820 |
| Leasehold improvements | 4,300,909 | 5,525,229 |
| **Total property and equipment** | **24,311,067** | **30,043,082** |
| Less: accumulated depreciation | (11,505,500) | (16,669,132) |
| **Property and equipment, net** | **12,805,567** | **13,373,950** |

Depreciation expense for property and equipment was allocated to the following:

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| | **US$** | **US$** | **US$** |
| Cost of revenues | 2,033,006 | 4,001,726 | 6,200,645 |
| Selling and marketing expenses | 128,527 | 278,094 | 366,819 |
| General and administrative expenses | 196,233 | 347,904 | 431,246 |
| Research and development expenses | 68,422 | 26,190 | 79,398 |
| **Total** | **2,426,188** | **4,653,914** | **7,078,108** |

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**6 ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| VAT and other tax payables | 1,250,544 | 1,913,361 |
| Accrued payroll and employee benefits | 3,280,317 | 4,389,540 |
| Others | 2,086,697 | 2,136,509 |
| **Total** | **6,617,558** | **8,439,410** |

Others mainly represent deferred income under American Depositary Receipt program, accrual for communication expenses, postal expenses and other miscellaneous expenses.

**7 NET REVENUES**

Net revenues consist of the following:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Tuition fee | 57,559,681 | 92,927,773 | 135,932,251 |
| Certification service fee | 1,177,284 | 2,001,705 | 2,936,647 |
| Others | 420,273 | 897,862 | 467,433 |
| Business taxes and surcharges | (2,336,957) | (2,993,680) | (3,132,314) |
| **Total** | **56,820,281** | **92,833,660** | **136,204,017** |

Others mainly represent miscellaneous fees, including franchise fee and guarantee fee (see note 9(b)).

**8 INCOME TAXES**

Under the current laws of the Cayman Islands, Tarena International is not subject to tax on its income or capital gains. For the period from its inception on October 22, 2012 to December 31, 2014, Tarena HK did not have any assessable profits arising in or derived from HK SAR. Tarena International s PRC subsidiaries and consolidated VIEs file separate tax returns in the PRC. Effective from January 1, 2008, the PRC statutory income tax rate is 25% according to the Corporate Income Tax ( CIT ) Law which was passed by the National People s Congress on March 16, 2007.

Under the CIT Law, entities that qualify as Advanced and New Technology Enterprise ( ANTE ) are entitled to a preferential income tax rate of 15%. In 2009, the WOFE qualified as an ANTE, which entitled it to the preferential income tax rate of 15% from January 1, 2009 to December 31, 2011. In 2012, the WOFE renewed its ANTE qualification, which entitled it to the preferential income tax rate of 15% from January 1, 2012 to December 31, 2014. Subject to renewal, WOFE s ANTE status will enable it to continue to enjoy the preferential income tax rate.

Management believes that WOFE meets all the criteria for the renewal of ANTE status.

Tarena Software Technology (Hangzhou) Co., Ltd. was established in 2013 and qualified as an eligible software enterprise. As a result of this qualification, it is entitled to a tax holiday of a two-year full exemption followed by a three-year 50% exemption, commencing from the year in which its taxable income is greater than zero.

Certain Tarena International s subsidiaries and branches qualified as Small Profit Enterprises in 2012, 2013 and 2014, and therefore are subject to the preferential income tax rate of 20%.

According to the approvals from the tax authorities in certain locations in the PRC, Tarena International s subsidiaries and consolidated VIEs that are based in these locations are required to use the deemed profit method to determine their income tax. Under the deemed profit method, these subsidiaries are subject to income tax at 25% on its deemed profit which is calculated based on revenues less deemed expenses equal to 85% to 90% of revenues.

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**8 INCOME TAXES (CONTINUED)**

The components of income before income taxes are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| PRC | 11,773,448 | 16,533,265 | 23,827,863 |
| Hong Kong | (280) | (182,447) | (319,685) |
| Cayman Islands | (1,587) | (32,461) | 3,587,894 |
| **Total income before income taxes** | **11,771,581** | **16,318,357** | **27,096,072** |

Income tax expense consists of the following:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Current income tax expense | 2,240,301 | 3,323,591 | 3,087,902 |
| Deferred income tax benefit | (21,191) | (1,052,265) | (683,078) |
| **Total** | **2,219,110** | **2,271,326** | **2,404,824** |

The actual income tax expense reported in the consolidated statements of comprehensive income for each of the years ended December 31, 2012 , 2013 and 2014 differs from the amount computed by applying the PRC statutory income tax rate to income before income taxes due to the following:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| PRC statutory income tax rate | 25.0% | 25.0% | 25.0% |
| Increase (decrease) in effective income tax rate resulting from: | | | |
| Non-PRC entity not subject to income taxes | 0.0% | 0.3% | (3.0%) |
| Research and development bonus deduction | (2.1%) | (3.3%) | (2.7%) |
| Non-deductible selling, general and administrative expenses | | | |
| Share based compensation | 0.3% | 1.2% | 3.8% |
| Other non-deductible selling, general and administrative expenses | 1.5% | 0.4% | 0.5% |
| Preferential tax rates | (5.6%) | (9.6%) | (1.4%) |
| Change in valuation allowance | 2.6% | (0.9%) | 6.4% |
| Tax holiday | | | (20.0%) |
| Deemed profit method differential | (2.9%) | (0.2%) | (0.1%) |

| | | | |
|---|---|---|---|
| Tax rate differential | | 0.8% | 0.3% |
| Others | 0.1% | 0.2% | 0.1% |
| **Actual income tax expense** | 18.9% | 13.9% | 8.9% |

Basic and diluted per Class A ordinary share and Class B ordinary share effect of the Company s tax holiday for the year ended December 31, 2014 was US$0.10 per share.

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**8 INCOME TAXES (CONTINUED)**

The principal components of deferred income tax assets are as follows:

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| Deferred income tax assets: | | |
| Accounts receivable | 966,148 | 2,729,700 |
| Tax loss carry forwards | 548,571 | 691,350 |
| Advertising expense | 529,063 | 1,151,432 |
| Accrued expenses and other current liabilities | 100,548 | |
| **Total deferred income tax assets** | **2,144,330** | **4,572,482** |
| Valuation allowance | (598,117) | (2,347,093) |
| **Deferred income tax assets, net** | **1,546,213** | **2,225,389** |
| Net deferred income tax assets-current | 1,546,213 | 2,055,596 |
| Net deferred income tax assets-non-current (included in other non-current assets) | | 169,793 |

The movements of the valuation allowance are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Balance at the beginning of the year | 424,967 | 731,828 | 598,117 |
| Additions of valuation allowance | 427,438 | 525,061 | 1,823,101 |
| Reduction of valuation allowance | (122,920) | (678,916) | (78,687) |
| Foreign currency translation adjustment | 2,343 | 20,144 | 4,562 |
| Balance at the end of the year | 731,828 | 598,117 | 2,347,093 |

The valuation allowance as of December 31, 2013 and 2014 was primarily provided for the deferred income tax assets of certain Tarena International s PRC subsidiaries and consolidated VIEs, which were at cumulative loss positions. In assessing the realization of deferred income tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible or utilizable. Management considers projected future taxable income and tax planning strategies in making this assessment. As of December 31, 2014, the Company had tax losses carryforwards of US$2,765,401. Tax losses of US$12,319, US$477,647 and US$2,275,435 will expire, if unused, by 2017, 2018 and 2019, respectively.

The CIT Law and its implementation rules impose a withholding income tax at 10%, unless reduced by a tax treaty or arrangement, on the amount of dividends distributed by a PRC-resident enterprise to its immediate holding company outside the PRC that are related to earnings accumulated beginning on January 1, 2008. Dividends relating to undistributed earnings generated prior to January 1, 2008 are exempt from such withholding income tax.

Due to the plan to indefinitely reinvest its earnings in the PRC, the Company has not provided for deferred income tax liabilities on undistributed earnings of US$36,072,588 and US$77,848,789 as of December 31, 2013 and 2014, respectively. It is not practicable to estimate the unrecognized deferred income tax liabilities thereof.

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**8 INCOME TAXES (CONTINUED)**

A reconciliation of the beginning and ending amount of total unrecognized tax benefits for the years ended December 31, 2012, 2013 and 2014 is as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Balance at beginning of year | 518,024 | 1,700,106 | 3,077,693 |
| Increase related to current year tax positions | 1,600,020 | 2,843,585 | 5,768,868 |
| Settlement | (424,220) | (1,539,717) | (2,813,061) |
| Foreign currency translation adjustment | 6,282 | 73,719 | 274 |
| Balance at end of year | 1,700,106 | 3,077,693 | 6,033,774 |

US$2,965,958 and US$5,822,319 of unrecognized tax benefits as of December 31, 2013 and 2014, if recognized, would affect the effective tax rate. No interest and penalty expenses were recorded for the years ended December 31, 2012, 2013 or 2014. US$1,613,832 and US$4,849,529 of unrecognized tax benefits as of December 31, 2013 and 2014 were included in income taxes payable. US$243,555 and US$384,686 of unrecognized tax benefits as of December 31, 2013 and 2014 were included in other non-current liabilities. The remaining US$1,220,306 and US$799,559 unrecognized tax benefit as of December 31, 2013 and 2014, respectively were presented as a reduction of the deferred income tax assets for tax loss carry forwards since the uncertain tax position would reduce the tax loss carry forwards under the tax law. The unrecognized tax benefits represent the estimated income tax expenses the Company would be required to pay should its revenue for tax purposes be recognized in accordance with current PRC tax laws and regulations. Management believes that it is reasonably possible that US$5,649,088 unrecognized tax benefits as of December 31, 2014 will be recognized in the next twelve months as a result of such revenue being reported in the income tax filing during the next twelve months.

According to the PRC Tax Administration and Collection Law, the statute of limitation is three years if the underpayment of taxes is due to computational errors made by the taxpayer or the withholding agent. The statute of limitation is extended to five years under special circumstances where the underpayment of taxes is more than RMB100,000. In the case of transfer pricing issues, the statute of limitation is 10 years. There is no statute of limitation in the case of tax evasion. The income tax returns of Tarena International s PRC subsidiaries and consolidated VIEs for the years from 2010 to 2014 are open to examination by the PRC tax authorities.

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**9 RELATED PARTY TRANSACTIONS**

During the years ended December 31, 2012, 2013 and 2014, the Company entered into related party transactions with Mr. Han and Chuanbang Business Consulting (Beijing) Co., Ltd. ( Chuanbang ), which is wholly owned by Mr. Han. The significant related party transactions are summarized as follows:

| | | Year Ended December 31, | | |
|---|---|---|---|---|
| | | 2012 | 2013 | 2014 |
| | | US$ | US$ | US$ |
| Tuition fees paid under the Student Loan Program | (a) | 7,924,903 | 8,672,904 | |
| Guarantee fee | (b) | 70,245 | 90,490 | 18,188 |
| Amounts received under the Student Loan Program | (c) | (668,652) | (141,329) | |
| Repayment of amounts received under the Student Loan Program | (c) | 745,918 | 232,879 | |
| Advances from Chuanbang | (d) | (308,658) | (153,386) | |
| Repayment of advances from Chuanbang | (d) | 308,658 | 153,386 | |
| Cash collection service fee | (e) | | 64,586 | 108,068 |

Notes:

(a) Starting from the second half of 2011, the Company began to refer its students who need financial assistance for the payment of their tuition fees to Chuanbang. Chuanbang is a person-to-person or a peer-to-peer (P2P) lending intermediary that assists students in obtaining loans to pay for their tuition fees by identifying potential third-party individual lenders (the Student Loan Program ). The third-party lenders remit cash to Mr. Han, who is a representative of Chuanbang, rather than directly to the Company, because the P2P arrangement is between Chuanbang (rather than the Company) and the third party individual lenders. As a P2P lending intermediary and pursuant to the relevant agreements between the two parties, Chuanbang is responsible for processing payments from student borrowers and forwarding those payments to individual lenders. The Company has no direct involvement in or is a party to the P2P arrangement, other than serving as the guarantor of the student loans. The role of the third-party individual lenders is to provide the students with funding of the student loans that are arranged or identified by Chuanbang.

Under the Student Loan Program, before the training courses commence, the students entered into loan agreements with Mr. Han, a designated representative of Chuanbang, to borrow an amount equal to the total amount of the tuition fees. The repayment term of the loan agreements ranges between 12 and 20 months. Shortly thereafter, Mr. Han assigned such loan agreements to third party individual lenders (including certain employees and a director of the Company), with the Company serving as the guarantor of the loan amount. The terms of the assignment agreements between Mr. Han and the third party individual lenders are identical to the terms of the loan agreements between the students and Mr. Han, except that the interest rate charged to the students by Mr. Han is higher than the interest rate charged to Mr. Han by the third party individual lenders. The interest rate differential represents the compensation to Mr. Han for the estimated costs he incurred to originate and will incur to service the student loans as well as the amount payable to the Company for guaranteeing the student loans. Upon the receipt of the cash from the third party individual lenders, Mr. Han remits the cash to the Company on behalf of students for the payment of the students tuition fees. In substance, the Company has agreed to guarantee amounts borrowed by the students (indirectly from third-party individual lenders through Mr. Han) to purchase the training services of the Company.

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**9 RELATED PARTY TRANSACTIONS** (CONTINUED)

The terms of the guarantee coincide with the terms of loan agreements, which range between 12 and 20 months. If the students default on a payment, the Company would have to perform under the guarantee. However, the Company would have recourse against the students. The maximum amount of undiscounted payments the Company would have to make in the event of default is US$4,448,162 and US217,356 as of December 31, 2013 and 2014, respectively. Upon the inception of the guarantee, the Company recognized a liability based on the estimated fair value of the guarantee. The liability is amortized over the term of the guarantee. The balance of the liability, which is included in accrued expenses and other current liabilities, was US$18,313 and nil as of December 31, 2013 and 2014, respectively. The estimated amount of the loss contingency related to the guarantee was immaterial as of December 31, 2013 and 2014. The Company paid US$78,931 in 2013 to discharge its guarantee obligations, which represented cumulative default of repayments by students as of December 31, 2013. All the third-part lenders were repaid and the Company s guarantee was released by March 15, 2015.

Under the Student Loan Program, upon the receipt of cash from third party individual lenders, Mr. Han remitted US$7,924,903 and US$8,672,904 to the Company on behalf of students for the payment of the students tuition fees during the years ended December 31, 2012 and 2013, respectively. The Company has stopped providing guarantees for any new student loans arranged by Chuanbang since April 2013.

(b) Under the Student Loan Program, the Company allocates the total consideration between the fair value of the tuition service and the loan guarantee. Subsequent to the initial recognition, the loan guarantee liability is recognized as guarantee fee revenue over the term of the guarantee on a straight-line basis. US$70,245, US$90,490 and US$18,188 was recognized as guarantee fee revenue and included in other revenues for the years ended December 31, 2012, 2013 and 2014, respectively.

(c) Under the Student Loan Program, the Company is not required to service the loans indirectly obtained by the students from the third party individual lenders. However, certain students remitted payments to the Company directly instead to Mr. Han. During the years ended December 31, 2012 and 2013, the Company received cash repayments from students in the amount of US$668,652 and US$141,329, respectively. The amount received by the Company on behalf of Mr. Han is recorded in amounts due to Mr. Han. The Company repaid US$745,918 and US$232,879 to Mr. Han during the years ended December 31, 2012 and 2013 respectively.

(d) Represents advance for prepayment of services received from Chuanbang. During the years ended December 31, 2012 and 2013, the Company received advances in the amount of US$308,658 and US$153,386, respectively from Chuanbang. The Company repaid advances of US$308,658 and US$153,386 during the years ended December 31, 2012 and 2013, respectively, as the services were no longer required.

(e) Pursuant to an agreement between Chuanbang and the Company, beginning August 2013, Chuanbang provides cash collection service on the Company s accounts receivable. The fee for the service is calculated based on 6%~8% of the amount collected. Employees of Chuanbang include former

employees of the Company who worked in the credit evaluation department. Chuanbang also provides similar cash collection service to financial institutions in the PRC. The cash collection service fee was US$64,586 and US$108,068 for the years ended December 31, 2013 and 2014, respectively.

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## 10 ORDINARY SHARES AND STATUTORY RESERVE

### (a) Ordinary shares

On October 8, 2003, Tarena International was established with authorized share capital of US$150,000, or 90,000,000 ordinary shares with a par value of US$0.001 (being retroactively adjusted to reflect the effect of the share split) and 60,000,000 preferred shares with a par value of US$0.001 (being retroactively adjusted to reflect the effect of the share split).

On December 16, 2008, the Board of Directors of Tarena International approved a 10:1 share split, which increased (i) the total number of authorized ordinary shares of 9,000,000, and issued and outstanding ordinary shares of 1,358,000, to 90,000,000 and 13,580,000, respectively; and (ii) the total number of authorized preferred shares of 6,000,000, and issued and outstanding preferred shares of 1,589,125, to 60,000,000 and 15,891,250, respectively. All applicable share and per share amounts in the accompanying consolidated financial statements have been retroactively adjusted to reflect the effect of the share split.

On April 9, 2013, IDG Technology Venture Investments, LP ( IDG ), the Series A convertible redeemable preferred shareholder, entered into a series of agreements with Mr. Han, Connion Capital Ltd. ( Connion ), a company incorporated in the Cayman Islands with limited liability and wholly owned by Mr. Han, Techedu Limited, a company incorporated in the British Virgin Islands ( BVI ) with limited liability and wholly owned by Mr. Han, and GF Tarena Limited, a third party company incorporated with limited liability under the law of the BVI, pursuant to which IDG sold 1,146,059 and 229,212 of its Series A convertible redeemable preferred shares to Techedu Limited and GF Tarena Limited for a consideration of US$5 million and US$1 million, respectively, or US$4.3628 per share. At the same time, Connion sold 916,848 of its ordinary shares to GF Tarena Limited for a consideration of US$4 million, or US$4.3628 per share. The 1,146,059 Series A convertible redeemable preferred shares purchased by Techedu Limited and 229,212 Series A convertible redeemable preferred shares purchased by GF Tarena Limited were converted to ordinary shares on December 10, 2013. To facilitate the purchase of the Series A convertible redeemable preferred shares, Techedu Limited borrowed a loan in the amount of US$5 million from GF Tarena Limited on April 9, 2013, with an annual interest rate of 19% for a period of 30 months.

On February 27, 2014, the Board of Directors of Tarena International approved the fifth amendment of the Memorandum and Articles of Association (the Amended M&A ), pursuant to which the authorized share capital was amended to 1,000,000,000 ordinary shares at a par value of US$0.001 per share, of which 860,000,000 shares were designated as Class A ordinary shares, 40,000,000 as Class B ordinary shares and 100,000,000 shares were designated as Reserved Shares, each with such rights, preferences and privileges set forth in the Amended M&A. The rights of the holders of Class A and Class B ordinary shares are identical, except with respect to voting and conversion rights. Each share of Class A ordinary shares is entitled to one vote per share and is not convertible into Class B ordinary shares under any circumstances. Each share of Class B ordinary shares is entitled to ten votes per share and is convertible into one Class A ordinary share at any time by the holder thereof.

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**10 ORDINARY SHARES AND STATUTORY RESERVE (CONTINUED)**

**(a) Ordinary shares (continued)**

In the Amended M&A, the Board of Directors of Tarena International approved that the Company to adopt a dual class ordinary share structure immediately upon the completion of the IPO. Upon the completion of the IPO, the Group s ordinary shares were divided into Class A ordinary shares and Class B ordinary shares. All of its issued and outstanding ordinary share prior to this offering were re-designated as Class B ordinary shares, all of its issued and outstanding preferred shares were automatically re-designated or converted into Class B ordinary shares on a one-for-one basis immediately upon the completion of the IPO and all of the issued and outstanding options, non-vested shares and non-vested share units granted by the Company pursuant to the 2008 Share Plan and the 2014 Share Incentive Plan were re-designated as options in Class A shares, non-vested Class A ordinary shares, non-vested Class A ordinary share units.

In connection with its IPO, Tarena International issued 11,500,000 Class A ordinary shares with par value of US$0.001, at a price of US$9.00 per share to investors. Net proceeds from the issuance of 11,500,000 Class A ordinary shares amounted to US$92,223,639 (net of issuance costs of US$4,031,356), of which US$11,500 and US$92,212,139 were recorded in the Class A ordinary shares and additional paid-in capital, respectively.

Concurrently upon the completion of the Company s IPO, the Company issued 1,500,000 Class A ordinary shares with par value of US$0.001 to New Oriental Education & Technology Group Inc., in a private placement at a price of US$9.00 per share. Proceeds from the issuance of Class A ordinary shares were US$13,500,000, of which US$1,500 and US$13,498,500 were recorded in the Class A ordinary shares and additional paid-in capital, respectively.

Upon completion of the IPO on April 3, 2014, the Company had 50,657,389 ordinary shares outstanding comprised of 16,800,000 Class A ordinary shares and 33,857,389 Class B ordinary shares. As of December 31, 2014, 860,000,000 Class A ordinary shares and 40,000,000 Class B ordinary shares had been authorized, 52,445,782 ordinary shares had been issued and outstanding, of which 23,712,758 were Class A ordinary shares and 28,733,024 were Class B ordinary shares.

**(b) Statutory reserves**

Under PRC rules and regulations, Tarena International s PRC subsidiaries and consolidated VIEs (the PRC Entities ) are required to appropriate 10% of their net profit, as determined in accordance with PRC accounting rules and regulations, to a statutory surplus reserve until the reserve balance reaches 50% of their registered capital. In addition, private schools (held by the PRC Entities) which require reasonable returns are required to appropriate 25% of their net profit, as determined in accordance with PRC accounting rules and regulations, to a statutory development fund, whereas in the case of private schools which do not require reasonable return, 25% of the annual increase of their net assets. The appropriation to these statutory reserves must be made before distribution of dividends to Tarena International can be made.

For the years ended December 31, 2012, 2013 and 2014, the PRC Entities made appropriations to the statutory reserves of US$1,236,843, US$1,972,313 and US$2,572,599, respectively. As of December 31, 2013 and 2014, the accumulated balance of the statutory reserves was US$3,674,841 and US$6,247,440 respectively.

**(c) Reclassification between additional paid-in capital and retained earnings**

On August 19, 2014, the Board of Directors approved the Company to undertake a reclassification of the balances between additional paid-in capital and retained earnings of US$85,568,016. The reclassification was primarily due to the accretion of convertible redeemable preferred shares, of which US$85,568,016 were charged against the balance in accumulated deficit in the absence of additional paid-in capital.

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**11 PREFERRED SHARES**

***Series A convertible redeemable preferred shares***

On January 16, 2004, pursuant to the Series A convertible redeemable preferred shares purchase agreements ( Series A Purchase Agreement ), Tarena International issued 8,571,430 Series A convertible redeemable preferred shares to a third party investor for a total consideration of US$500,000 or US$0.05833 per share ( Series A Original Issuance Price ) (being retroactively adjusted to reflect the effect of the share split).

The Company determined that there was no embedded beneficial conversion feature attributable to the Series A convertible redeemable preferred shares at the commitment date since the initial conversion price of the Series A convertible redeemable preferred shares was greater than the estimated fair value of the Company s ordinary shares as of January 16, 2004. The estimated fair value of the underlying ordinary shares on January 16, 2004 was determined by management based on a retrospective valuation with the assistance of American Appraisal China Limited ( American Appraisal ), an independent valuation firm, using an income approach which requires the estimation of future cash flows and the application of an appropriate discount rate with reference to comparable listed companies engaged in a similar industry to convert such future cash flows to a single present value.

The significant terms of Series A convertible redeemable preferred shares are as follows:

(i) Conversion

The holders of Series A convertible redeemable preferred shares have the right to convert all or any portion of their holdings into ordinary shares at a rate of one-for-one at any time, subject to a contingent conversion price adjustment if there are additional ordinary shares issued or deemed to be issued, as defined in Tarena International s Memorandum and Articles of Association, at a price lower than the Series A Original Issuance Price. In addition, each Series A Preferred Share is automatically converted into ordinary shares upon the consummation of a Qualified Public Offering, as defined in the Series A Purchase Agreement.

The contingent conversion price adjustment may provide the holders of the Series A convertible redeemable preferred shares with a beneficial conversion feature. However, any such beneficial conversion feature relating to the conversion price adjustment, if any, is recognized when the contingency is resolved.

(ii) Voting

The holders of Series A convertible redeemable preferred shares have voting rights equivalent to the ordinary shareholders on an if-converted basis.

(iii) Dividends

Any dividend declared and paid on ordinary shares shall be also declared and paid in respect of the Series A convertible redeemable preferred shares as if all such Series A convertible redeemable preferred shares has been converted to ordinary shares.

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**11 PREFERRED SHARES (CONTINUED)**

***Series A convertible redeemable preferred shares (continued)***

(iv) Liquidation preference

The liquidation preference of the holders of Series A convertible redeemable preferred shares as of December 31, 2013 is as follows:

In the event of any liquidation, dissolution, or winding up of the Company, the proceeds shall be distributed according to the following sequence: (i) first to the holders of the Series C convertible redeemable preferred shares at 150% of the Series C Original Issuance Price, plus declared but unpaid dividends on each share of Series C convertible redeemable preferred shares; (ii) second to the holders of Series B convertible redeemable preferred shares at 150% of the Series B Original Issuance Price, plus declared but unpaid dividends on each share of Series B convertible redeemable preferred shares, (iii) third to the holders of Series A convertible redeemable preferred shares at 100% of the Series A Original Issuance Price, plus declared but unpaid dividends on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of Series C convertible redeemable preferred shares, Series B convertible redeemable preferred shares, Series A convertible redeemable preferred shares and ordinary shares on an if-converted basis.

From the date of September 25, 2008 to August 11, 2011 (the date of the issuance of Series C convertible redeemable preferred shares), the liquidation preference of the holders of Series A convertible redeemable preferred shares was as follows:

In the event of any liquidation, dissolution, or winding up of the Company, the proceeds shall be distributed according to the following sequence: (i) first to the holders of the Series B convertible redeemable preferred shares at 150% of the Series B Original Issuance Price, plus declared but unpaid dividends on each share of Series B convertible redeemable preferred shares; (ii) second to the holders of Series A convertible redeemable preferred shares at 100% of the Series A Original Issuance Price, plus declared but unpaid dividends on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of Series B convertible redeemable preferred shares, Series A convertible redeemable preferred shares and ordinary shares on an if-converted basis.

From the date of its issuance (January 16, 2004) to September 25, 2008 (the date of the issuance of Series B convertible redeemable preferred shares), the liquidation preference of the holders of Series A convertible redeemable preferred shares was as follows:

In the event of any liquidation, dissolution, or winding up of the Company, the holders of the outstanding Series A convertible redeemable preferred shares shall be entitled to receive, prior and in preference to any distribution of any of the assets of Tarena International to the holders of the ordinary shares by reason of their ownership of such shares, an amount equal to the Series A Original Issuance Price plus dividends declared but unpaid on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of ordinary shares and Series A convertible redeemable preferred shares then outstanding, based on the number of ordinary shares then held by each shareholder on an if-converted basis

(v) Drag-along rights

Holders of a majority of the Series A convertible redeemable preferred shares have a drag-along right whereby they can require the ordinary shareholders to approve a third-party offer to directly or indirectly purchase all, or substantial all, of the equity interests or assets of the Company, provided that the transaction shall occur on or after the fifth anniversary of the closing of the issuance of the Series A convertible redeemable preferred shares or the transaction shall be at a price per share of not less than US$0.5833 per share (being retroactively adjusted to reflect the effect of the share split). Triggering of this drag-along right results in a deemed liquidation of the Company at the option of a majority of the holders of Series A convertible redeemable preferred shares with a required distribution of the transaction proceeds in accordance with the Company s Memorandum and Articles of Association.

Consequently, the Series A convertible redeemable preferred shares are classified outside of permanent equity.

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**11 PREFERRED SHARES (CONTINUED)**

***Series B convertible redeemable preferred shares***

On September 25, 2008, pursuant to Series B convertible redeemable preferred shares purchase agreement, Tarena International issued 5,630,630 Series B convertible redeemable preferred shares to a third party investor for a total consideration of US$5 million or US$0.888 per share ( Series B Original Issuance Price ) (being retroactively adjusted to reflect the effect of the share split). On the same date, an outstanding US$1.5 million short term borrowing was exchanged for 1,689,190 shares of Series B convertible redeemable preferred shares (being retroactively adjusted to reflect the effect of the share split).

The Company determined that there was no embedded beneficial conversion feature attributable to the Series B convertible redeemable preferred shares at the commitment date since the initial conversion price of the Series B convertible redeemable preferred shares was greater than the estimated fair value of the Company s ordinary shares as of September 25, 2008. The estimated fair value of the underlying ordinary shares on September 25, 2008 was determined by management based on a retrospective valuation with the assistance of American Appraisal, using an income approach which requires the estimation of future cash flows and the application of an appropriate discount rate with reference to comparable listed companies engaged in a similar industry to convert such future cash flows to a single present value.

The significant terms of Series B convertible redeemable preferred shares are as follows:

(i) Conversion

The holders of Series B convertible redeemable preferred shares have the right to convert all or any portion of their holdings into ordinary shares at a rate of one-for-one at any time, subject to a contingent conversion price adjustment if there are additional ordinary shares issued or deemed to be issued, as defined in Tarena International s Memorandum and Articles of Association, at a price lower than the Series B Original Issuance Price. In addition, each Series B convertible redeemable preferred share is automatically converted into ordinary shares upon the written consent of the holders of more than 45% of the then outstanding Series B convertible redeemable preferred shares and the holders of more than 45% of the then outstanding Series A convertible redeemable preferred shares or the consummation of a Qualified Public Offering, as defined in the Series B convertible redeemable preferred shares purchase agreement.

The contingent conversion price adjustment may provide the holders of the Series B convertible redeemable preferred shares with a beneficial conversion feature. However, any such beneficial conversion feature relating to the conversion price adjustment, if any, is recognized when the contingency is resolved.

(ii) Voting

The holders of Series B convertible redeemable preferred shares have voting rights equivalent to the ordinary shareholders on an if-converted basis.

(iii) Dividends

Any dividend declared and paid on ordinary shares shall be also declared and paid in respect of the Series B convertible redeemable preferred shares as if all such Series B convertible redeemable preferred shares have been converted to ordinary shares.

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**11 PREFERRED SHARES (CONTINUED)**

***Series B convertible redeemable preferred shares (continued)***

(iv) Liquidation preference

The liquidation preference of the holders of Series B convertible redeemable preferred shares as of December 31, 2013 is as follows:

In the event of any liquidation, dissolution, or winding up of the Company, the proceeds shall be distributed according to the following sequence: (i) first to the holders of the Series C convertible redeemable preferred shares at 150% of the Series C Original Issuance Price, plus declared but unpaid dividends on each share of Series C convertible redeemable preferred shares; (ii) second to the holders of Series B convertible redeemable preferred shares at 150% of the Series B Original Issuance Price, plus declared but unpaid dividends on each share of Series B convertible redeemable preferred shares, (iii) third to the holders of Series A convertible redeemable preferred shares at 100% of the Series A Original Issuance Price, plus declared but unpaid dividends on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of Series C convertible redeemable preferred shares, Series B convertible redeemable preferred shares, Series A convertible redeemable preferred shares and ordinary shares on an if-converted basis.

From the date of September 25, 2008 to August 11, 2011 (the date of the issuance of Series C convertible redeemable preferred shares), the liquidation preference of the holders of Series B convertible redeemable preferred shares was as follows:

In the event of any liquidation, dissolution, or winding up of the Company, the proceeds shall be distributed according to the following sequence: (i) first to the holders of the Series B convertible redeemable preferred shares at 150% of the Series B Original Issuance Price, plus declared but unpaid dividends on each share of Series B convertible redeemable preferred shares; (ii) second to the holders of Series A convertible redeemable preferred shares at 100% of the Series A Original Issuance Price, plus declared but unpaid dividends on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of Series B convertible redeemable preferred shares, Series A convertible redeemable preferred shares and ordinary shares on an if-converted basis.

(v) Redemption

If a Qualified Initial Public Offering or a Trade Sale, as defined in the Series B convertible redeemable preferred shares purchase agreement, did not occur by December 31, 2012 (the Redemption Date ), the holders of Series B convertible redeemable preferred shares had the right to request for redemption any portion of the Series B convertible redeemable preferred shares they held at a price equal to the sum of:

an amount equal to 150% of Series B Original Issuance Price; plus,

an amount equal to all declared but unpaid dividends on each share of Series B convertible redeemable preferred shares; plus,

10% compound interest per annum on 150% of Series B Original Issuance Price for each Series B convertible redeemable preferred share from the date of issuance to the earliest redemption date of the security.

On August 11, 2011, in connection with the issuance of Series C convertible redeemable preferred shares, the Company and holders of Series B convertible redeemable preferred shares agreed to defer the Redemption Date until June 30, 2014.

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**11 PREFERRED SHARES (CONTINUED)**

***Series C convertible redeemable preferred shares***

On August 11, 2011, pursuant to the Series C convertible redeemable preferred shares purchase agreement ( Series C Purchase Agreement ), Tarena International issued 10,914,852 Series C convertible redeemable preferred shares to a third party investor for a total consideration of US$19,974,179 or US$1.83 per share ( Series C Original Issuance Price ). Total issuance cost of Series C convertible redeemable preferred shares was US$218,376.

The Company determined that there was no embedded beneficial conversion feature attributable to the Series C convertible redeemable preferred shares at the commitment date since the initial conversion price of the Series C convertible redeemable preferred shares was greater than the estimated fair value of the Company s ordinary shares as of August 11, 2011. The estimated fair value of the underlying ordinary shares on August 11, 2011 was determined by management based on a retrospective valuation with the assistance of American Appraisal, a third party valuation firm, using an income approach which requires the estimation of future cash flows and the application of an appropriate discount rate with reference to comparable listed companies engaged in a similar industry to convert such future cash flows to a single present value.

The significant terms of Series C convertible redeemable preferred shares are as follows:

(i) Conversion

The holders of Series C convertible redeemable preferred shares have the right to convert all or any portion of their holdings into ordinary shares at a rate of one-for-one at any time, subject to a contingent conversion price adjustment if there are additional ordinary shares issued or deemed to be issued, as defined in Tarena International s Memorandum and Articles of Association, at a price lower than the Series C Original Issuance Price. In addition, each Series C Preferred Share is automatically converted into ordinary shares upon the closing of a Qualified Public Offering, as defined in the Memorandum and Articles of Association or the written consent of 67% of the holders of the Series C convertible redeemable preferred shares as well as the written consent of the holders of more than 45% of the then outstanding Series B convertible redeemable preferred shares and the written consent of the holders of more than 45% of the then outstanding Series A convertible redeemable preferred shares for conversion.

The contingent conversion price adjustments may provide the holders of the Series C convertible redeemable preferred shares with a beneficial conversion feature. However, any such beneficial conversion feature relating to the conversion price adjustment, is recognized when the contingency is resolved.

(ii) Voting

The holders of Series C convertible redeemable preferred shares have voting rights equivalent to the ordinary shareholders on an if-converted basis.

(iii) Dividends

The board of directors of Tarena International may approve the payment of dividends at their discretion to the holders of Series C convertible redeemable preferred shares. Any dividend declared and paid on ordinary shares shall be also declared and paid in respect of the Series C convertible redeemable preferred shares as if all such Series C convertible redeemable preferred shares have been converted to ordinary shares.

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**11 PREFERRED SHARES (CONTINUED)**

***Series C convertible redeemable preferred shares (continued)***

(iv) Liquidation preference

The liquidation preference of the holders of Series C convertible redeemable preferred shares is as follows:

In the event of liquidation, dissolution, or winding up of the Company, the proceeds shall be distributed according to the following sequence: (i) first to the holders of the Series C convertible redeemable preferred shares at 150% of the Series C Original Issuance Price, plus declared but unpaid dividends on each share of Series C convertible redeemable preferred shares; (ii) second to the holders of Series B convertible redeemable preferred shares at 150% of the Series B Original Issuance Price, plus declared but unpaid dividends on each share of Series B convertible redeemable preferred shares, (iii) third to the holders of Series A convertible redeemable preferred shares at 100% of the Series A Original Issuance Price, plus declared but unpaid dividends on each share of Series A convertible redeemable preferred shares. The remaining assets of the Company, if any, shall be distributed pro rata to the holders of Series C convertible redeemable preferred shares, Series B convertible redeemable preferred shares, Series A convertible redeemable preferred shares and ordinary shares on an if-converted basis.

(v) Redemption

If a Qualified Initial Public Offering or a Trade Sale, as defined in the Series C convertible redeemable preferred shares purchase agreement, does not occur by June 30, 2014 (the Redemption Date ), the holders of the Series C convertible redeemable preferred shares have the right to request for redemption for all or a portion of the Series C convertible redeemable preferred shares they hold at a price equal to the greater of (i) an amount equal to 137.50% of the Series C Original Issuance Price, plus declared but unpaid dividends on each share of Series C convertible redeemable preferred shares; or (ii) the fair market value of the Series C convertible redeemable preferred shares as of the most recent year end, as determined by an independent appraiser mutually agreeable to the Company and the holder of the Series C convertible redeemable preferred shares.

As of December 31, 2013, the Company concluded that it was probable that the Series B and Series C convertible redeemable preferred shares will become redeemable. The Company has elected to accrete changes in the redemption value over the period from the date of issuance to the earliest redemption date using the interest method. The total accretion of Series B convertible redeemable preferred shares of US$1,804,179, US$2,072,284 and US$576,431 and total accretion of Series C convertible redeemable preferred shares of US$24,741,381, US$42,287,776 and nil were recorded as a reduction to additional paid-in capital first and then charged against accumulated deficit in the absence of additional paid-in capital for the years ended December 31, 2012, 2013 and 2014, respectively.

All the Series A, Series B and Series C convertible redeemable preferred shares were automatically converted into Class B ordinary shares upon completion of the Company s IPO on April 3, 2014. As a result, 25,430,831 Class B ordinary shares were issued upon the conversion of Series A, Series B and Series C convertible preferred shares. Upon the conversion, the carrying amounts of the Series A, Series B and Series C convertible preferred shares were recorded in additional paid-in capital of US$111,929,780 and Class B ordinary shares of US$25,431.

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**12 SHARE BASED COMPENSATION**

***Share options***

On September 22, 2008, Tarena International adopted the 2008 Share Plan (the 2008 Plan ), pursuant to which Tarena International is authorized to issue share options and other share-based awards to key employees, directors and consultants of the Company to purchase up to 6,002,020 of its Class A ordinary shares (being retroactively adjusted to reflect the effect of the share split) under the 2008 Plan. On November 28, 2012, the Company increased the number of Class A ordinary shares authorized for issuance under the 2008 Plan to 8,184,990 Class A ordinary shares. Share options issued before September 22, 2008 are also administered under the 2008 Plan.

On February 1, 2014, Tarena International adopted the 2014 Share Plan (the 2014 Plan ), pursuant to which Tarena International was authorized to issue options, non-vested shares and non-vested share units to qualified employees, directors and consultants of the Company. The maximum aggregate number of shares which may be issued pursuant to all awards under the 2014 Plan, or the Award Pool, is 1,833,696, provided that the shares reserved in the Award Pool shall be increased on the first day of each calendar year, commencing with January 1, 2015, if the unissued shares reserved in the Award Pool on such day account for less than 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year, as a result of which increase the shares unissued and reserved in the Award Pool immediately after each such increase shall equal 2% of the total number of shares issued and outstanding on a fully-diluted basis on December 31 of the immediately preceding calendar year.

On January 1, 2011 and September 26, 2011, the board of directors of Tarena International approved the grant of options to purchase 124,000 and 1,533,020 ordinary shares of Tarena International to certain employees and directors. These options vest over a five-year period. The option holders can only exercise their vested options upon the occurrence of the earliest of (i) a qualified IPO as defined in the Plan, (ii) a liquidation event as defined in the Company s Memorandum and Articles of Association, or (iii) the five-year anniversary of the option grant date. The options have a contractual term of ten years. The fair value of Tarena International s ordinary shares on January 1, 2011 and September 26, 2011 was determined to be US$0.63 and US$0.83 per share, respectively.

On January 1, 2013, the board of directors of Tarena International approved the grant of options to certain employees to purchase 2,029,386 ordinary shares of Tarena International. These options vest over a four year period. The option holders can only exercise their vested options upon the occurrence of the earliest of (i) a qualified IPO as defined in the Plan, (ii) a liquidation event as defined in the Company s Memorandum and Articles of Association, or (iii) the five-year anniversary of the option grant date. The options have a contractual term of ten years.

On September 16, 2013, the board of directors of Tarena International approved the grant of options to an employee to purchase 30,000 ordinary shares of Tarena International. 25% of the options will be vested at the closing of the Company s IPO while the remaining 75% will vest over a four-year period, that can only be exercised upon the occurrence of the earliest of (i) a qualified IPO, (ii) a liquidation event, or (iii) the five-year anniversary of the option grant date. The options have a contractual term of ten years.

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On September 16, 2013, the board of directors of Tarena International approved the grant of options to an officer to purchase 458,424 ordinary shares of Tarena International. If the Company undertakes any additional round of financing or any other activities to effect an increase of the total shares outstanding on a fully diluted basis before the IPO, the officer will be granted additional share options at the same exercise price. The total number of share options the officer will be granted will be equal to not less than 1% of the Company s total shares outstanding on a fully diluted basis on the date immediately preceding the closing of the Company s IPO. 25% of the options will be immediately and fully vested at the closing of the Company s IPO while the remaining 75% will vest over a four-year period, that can only be exercised upon the occurrence of the earliest of (i) a qualified IPO, (ii) a liquidation event, or (iii) the five-year anniversary of the option grant date. The options have a contractual term of ten years. The fair value of Tarena International s ordinary shares on January 1, 2013 and September 16, 2013 was determined to be US$3.75 and US$5.69 per share, respectively.

On February 20, 2014, the board of the directors of Tarena International approved the grant of options to certain officers and employees to purchase 1,805,784 ordinary shares of Tarena International. The options vest over a four year period. The option holders can only exercise their vested options upon the occurrence of the earliest of (i) a qualified IPO, (ii) a liquidation event, or (iii) the five-year anniversary of the option grant date. The options have a contractual term of ten years. The fair value of Tarena International s ordinary shares on February 20, 2014 was determined to be US$8.60 per share.

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**12 SHARE BASED COMPENSATION (CONTINUED)**

***Share options (continued)***

A summary of share options activity for the years ended December 31, 2012, 2013 and 2014 is as follows:

| | Number of Share Options | Weighted Average Exercise Price US$ | Weighted Average Remaining Contractual Years | Aggregate Intrinsic Value US$ |
|---|---|---|---|---|
| **Outstanding at December 31, 2011** | **5,844,020** | **0.36** | | |
| Granted | | | | |
| Exercised | | | | |
| Forfeited | (205,000) | 0.06 | | |
| Expired | | | | |
| **Outstanding at December 31, 2012** | **5,639,020** | **0.37** | | |
| Granted | 2,517,810 | 1.83 | | |
| Exercised | | | | |
| Forfeited | (22,000) | 1.83 | | |
| Expired | | | | |
| **Outstanding at December 31, 2013** | **8,134,830** | **0.82** | | |
| Granted | 1,805,784 | 3.05 | | |
| Exercised | (1,786,449) | 0.14 | | 25,047,974 |
| Forfeited | (115,215) | 2.91 | | |
| Expired | | | | |
| **Outstanding at December 31, 2014** | **8,038,950** | **1.44** | **6.19** | **77,657,938** |
| **Vested and expected to vest as of December 31, 2014** | **7,383,591** | **1.33** | **5.99** | **72,163,881** |
| **Exercisable as of December 31, 2014** | **4,420,502** | **0.77** | **4.42** | **45,664,778** |

The Company calculated the fair value of the share options on the grant date using the Binomial option-pricing valuation model. The assumptions used in the valuation model are summarized in the following table.

**Year Ended December 31,**

| | 2012<br>US$ | 2013<br>US$ | 2014<br>US$ |
|---|---|---|---|
| Expected volatility | | 52% | 51.7% |
| Expected dividends yield | | 0% | 0% |
| Exercise multiple | | 2.2 | 2.2 |
| Risk-free interest rate per annum | | 2.27%-3.38% | 3.81% |
| Estimated fair value of underlying ordinary shares (per share) | | US$ 3.75-US$5.69 | US$ 8.60 |

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**12 SHARE BASED COMPENSATION (CONTINUED)**

***Share options (continued)***

Because the Company s ordinary shares did not have a trading history at the time the options were issued, the expected volatility was based on the historical volatilities of comparable publicly traded companies engaged in the similar industry.

The estimated fair value of the underlying ordinary shares on each date of grant prior to September 2013, was determined by management based on a retrospective valuation conducted by American Appraisal. The estimated fair values of the underlying ordinary shares on September 16, 2013 and February 20, 2014 were determined by management based on a contemporaneous valuation conducted by American Appraisal. The Company first determined its enterprise value by using income approach, which required the estimation of future cash flows, and the application of an appropriate discount rate with reference to comparable listed companies engaged in the similar industry to convert such future cash flows to a single present value, and then allocated the enterprise value between the ordinary shares and preferred shares.

No income tax benefit was recognized in the consolidated statements of comprehensive income as the share-based compensation expense was not tax deductible.

The fair values of the options granted for the years ended December 31, 2012, 2013 and 2014 are as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 | 2013 | 2014 |
| | US$ | US$ | US$ |
| Weighted average grant date fair value of option per share | | 2.13 | 6.35 |
| Aggregate grant date fair value of options | | 5,372,463 | 11,467,907 |

As of December 31, 2014, there was approximately US$10,197,608 of total unrecognized compensation cost related to unvested share options. The unrecognized compensation costs are expected to be recognized over a weighted average period of approximately 2.55 years.

***Non-vested shares***

On April 3, 2014, the board of directors of Tarena International approved the grant of two batches of non-vested shares to three independent directors. The number of the first batch of non-vested shares is equal to 27,780 shares, which was calculated as US$250,000 divided by US$9, i.e. the IPO price of ordinary share of Tarena International. Conditioned on the Grantee s continuous services as a director of the Company, a second batch of non-vested shares should be granted with the number equal to US$250,000 divided by the closing price of ordinary share of Tarena International on April 3, 2015. One hundred percent of the first batch of non-vested shares shall vest on the April 3, 2015. One hundred percent of the second batch of non-vested shares shall vest on April 3, 2016. Grantees of non-vested shares have no voting rights or dividend rights with respect to shares that have not been vested.

On November 11, 2014, the board of directors of Tarena International approved the grant of 1,944 non-vested shares to 8 employees. One hundred percent of the non-vested shares shall vest immediately on the grant date.

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**12 SHARE BASED COMPENSATION (CONTINUED)**

***Non-vested shares (continued)***

A summary of the non-vested shares activity under the 2014 Share Plan is summarized as follows:

| | Number of Non-vested Shares | Weighted Average Grant Date Fair Value US$ |
|---|---|---|
| **Outstanding as of December 31, 2013** | | |
| Granted | 29,724 | 9.38 |
| Vested | (1,944) | 13.95 |
| Forfeited | | |
| **Outstanding as of December 31, 2014** | 27,780 | 9.06 |

As of December 31, 2014, there was approximately US$41,493 of total unrecognized compensation cost related to non-vested shares, which is expected to be recognized over a weighted average period of approximately 0.25 years. The total fair value of shares vested during the year ended December 31, 2014 was US$27,120.

**13 EARNINGS (LOSS) PER SHARE**

Basic and diluted earnings (loss) per share is calculated as follows:

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 US$ | 2013 US$ | 2014 US$ |
| Numerator: | | | |
| Net income (loss) attributable to Class A and Class B ordinary shareholders | (16,993,089) | (30,313,029) | 24,114,817 |
| Less: | | | |
| Earnings allocated to participating Series A convertible redeemable preferred shares | | | (918,266) |
| Earnings allocated to participating Series B convertible redeemable preferred shares | | | (934,046) |
| Earnings allocated to participating Series C convertible redeemable preferred shares | | | (1,392,790) |

| | | | |
|---|---|---|---|
| Net income (loss) for basic and diluted earnings (loss) per share | (16,993,089) | (30,313,029) | 20,869,715 |
| | | | |
| Denominator: | | | |
| Denominator for basic earnings per share: | | | |
| Weighted average number of Class A and Class B ordinary shares outstanding | 10,851,287 | 10,930,412 | 41,223,389 |
| Dilutive effect of outstanding share options | | | 6,546,743 |
| | | | |
| Denominator for diluted earnings (loss) per share | 10,851,287 | 10,930,412 | 47,770,132 |
| | | | |
| **Basic earnings (loss) per Class A and Class B ordinary share** | **(1.57)** | **(2.77)** | **0.51** |
| | | | |
| **Diluted earnings (loss) per Class A and Class B ordinary share** | **(1.57)** | **(2.77)** | **0.44** |

The following table summarizes potential ordinary shares outstanding excluded from the calculation of diluted earnings per Class A and Class B ordinary share for the years ended December 31, 2012, 2013 and 2014, because their effect is anti-dilutive:

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| Shares issuable upon exercise of share options | 5,639,020 | 8,134,830 | |
| Shares issuable upon conversion of preferred shares | 26,806,102 | 25,430,831 | |

The Company uses the two-class method to calculate basic and diluted earnings per Class A and Class B ordinary share. Under the two-class method, when calculating the basic and dilutive earnings per Class A and Class B ordinary share, net income attributable to Class A and Class B ordinary shareholders is adjusted to reflect the net income which is allocated to preferred shares.

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## 14 COMMITMENTS AND CONTINGENCIES

***(a) Operating lease commitments***

Future minimum lease payments under non-cancelable operating lease agreements as of December 31, 2014 were as follows. The Company s leases do not contain any contingent rent payment terms.

| | **US$** |
|---|---|
| Year ending December 31, | |
| 2015 | 12,398,271 |
| 2016 | 8,770,230 |
| 2017 | 6,259,451 |
| 2018 | 3,622,792 |
| 2019 | 2,332,153 |
| 2020 and thereafter | 4,802,841 |
| **Total** | **38,185,738** |

Gross rent expenses incurred under operating leases were US$5,494,341, US$9,684,871 and US$12,615,613 for the years ended December 31, 2012, 2013 and 2014, respectively. Sublease rental income of US$67,274, US$114,361 and US$230,503 for the years ended December 31, 2012, 2013 and 2014, respectively, were recognized as reductions of gross rental expenses.

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**15 PARENT ONLY FINANCIAL INFORMATION**

The following presents condensed parent company financial information of Tarena International.

**Condensed Balance Sheets**

| | December 31, | |
|---|---|---|
| | 2013 | 2014 |
| | US$ | US$ |
| **ASSETS** | | |
| **Current assets:** | | |
| Cash | 52,878 | 1,296,102 |
| Time deposits | | 92,182,582 |
| Prepaid expenses and other current assets | 1,537 | 2,256,709 |
| **Total current assets** | **54,415** | **95,735,393** |
| Investments and loans to subsidiaries | 47,963,562 | 88,854,260 |
| Other non-current assets | 76,719 | |
| **Total assets** | **48,094,696** | **184,589,653** |
| **LIABILITIES, MEZZANINE EQUITY AND SHAREHOLDERS EQUITY (DEFICIT)** | | |
| **Current liabilities:** | | |
| Accrued expenses and other current liabilities | | 449,351 |
| Other non-current liabilities | | 1,253,070 |
| **Total liabilities** | | 1,702,421 |
| Commitments and contingencies | | |
| **Mezzanine equity:** | | |
| Series A convertible redeemable preferred shares | 419,776 | |
| Series B convertible redeemable preferred shares | 15,747,869 | |
| Series C convertible redeemable preferred shares | 95,211,135 | |
| **Total mezzanine equity** | **111,378,780** | |
| **Shareholders equity (deficit):** | | |
| Class A ordinary shares (US$0.001 par value, 860,000,000 shares authorized, nil and 23,712,758 shares issued and outstanding as of December 31, 2013 and 2014, respectively) | | 23,712 |
| Class B ordinary shares (US$0.001 par value, 40,000,000 shares authorized, 12,226,558 shares and 28,733,024 shares issued and outstanding as of December 31, 2013 and 2014, respectively) | 12,226 | 28,733 |
| Additional paid-in capital | | 135,886,427 |
| Accumulated other comprehensive income | 1,634,920 | 1,701,598 |
| Retained earnings (Accumulated deficit) | (64,931,230) | 45,246,762 |
| **Total shareholders equity (deficit)** | **(63,284,084)** | **182,887,232** |

| | | | |
|---|---|---|---|
| **Total liabilities, mezzanine equity and shareholders equity (deficit)** | | **48,094,696** | **184,589,653** |

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**15 PARENT ONLY FINANCIAL INFORMATION (CONTINUED)**

**Condensed Statements of Comprehensive Income**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | **2013** | **2014** |
| | **US$** | **US$** | **US$** |
| General and administrative expenses | (83,001) | (57,172) | (170,440) |
| **Operating loss** | **(83,001)** | **(57,172)** | **(170,440)** |
| Equity in income of subsidiaries | 9,554,058 | 14,079,492 | 21,103,354 |
| Foreign currency exchange gains | | | 1,180,466 |
| Interest income | 81,414 | 24,711 | 2,288,698 |
| Other income | | | 289,170 |
| **Income before income taxes** | **9,552,471** | **14,047,031** | **24,691,248** |
| Income tax expense | | | |
| **Net income** | **9,552,471** | **14,047,031** | **24,691,248** |
| **Other comprehensive income** | | | |
| Foreign currency translation adjustment, net of nil income tax | 68,415 | 1,150,824 | 66,678 |
| **Comprehensive Income** | **9,620,886** | **15,197,855** | **24,757,926** |

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**15 PARENT ONLY FINANCIAL INFORMATION (CONTINUED)**

**Condensed Statements of Cash Flows**

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2012 US$ | 2013 US$ | 2014 US$ |
| **Operating activities:** | | | |
| **Net cash provided by (used in) operating activities** | **(42,825)** | **(3,570)** | **3,226,599** |
| **Investing activities:** | | | |
| Purchase of time deposits | | | (92,682,582) |
| Proceeds from maturity of time deposits | | | 500,000 |
| Investments made to subsidiaries | (14,671,162) | | (17,000,000) |
| Issuance of loans made to a subsidiary | (3,000,000) | | |
| Repayment of loans from a subsidiary | 3,000,000 | | |
| **Net cash used in investing activities** | **(14,671,162)** | | **(109,182,582)** |
| **Financing activities:** | | | |
| Payment of issuance cost of Series C convertible redeemable preferred shares | (150,000) | | |
| Payment of IPO costs | | (76,719) | (2,804,600) |
| Issuance of Class A ordinary shares upon the IPO | | | 96,254,995 |
| Issuance of Class A ordinary shares in private placement concurrent with the IPO | | | 13,500,000 |
| Issuance of Class A ordinary shares in connection with exercise of share options | | | 248,812 |
| **Net cash provided by (used in) financing activities** | **(150,000)** | **(76,719)** | **107,199,207** |
| Net increase (decrease) in cash | (14,863,987) | (80,289) | 1,243,224 |
| Cash at beginning of year | 14,997,154 | 133,167 | 52,878 |
| Cash at end of year | 133,167 | 52,878 | 1,296,102 |
| **Non-cash investing and financing activities:** | | | |
| Conversion of Series A convertible redeemable preferred shares to Class B ordinary shares | | 80,224 | 419,776 |
| Conversion of Series B convertible redeemable preferred shares to Class B ordinary shares | | | 16,324,300 |
| Conversion of Series C convertible redeemable preferred shares to Class B ordinary shares | | | 95,211,135 |
| Accrual of IPO costs | | 107,866 | |