

Performant Financial Corp  
Form 10-K  
March 13, 2017  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-35628

PERFORMANT FINANCIAL CORPORATION  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

20-0484934  
(I.R.S. Employer  
Identification No.)

333 North Canyons Parkway, Livermore, CA 94551  
(Address of principal executive offices) (Zip Code)  
Registrant's telephone number, including area code: (925) 960-4800

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

Title of each class: \_\_\_\_\_ Name of each exchange on which registered:  
Common Stock, par value \$.0001 per share NASDAQ Global Select Market

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

Common Stock, par value \$.0001 per share  
(Title of class)

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

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

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

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

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

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

Large accelerated filer

Accelerated filer

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

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

As of June 30, 2016 (the last business day of the registrant's most recently completed second quarter), the aggregate market value of the common stock held by non-affiliates of the registrant was \$40,708,614. Shares of common stock beneficially held by each officer and director and by each person who owns 10% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 10, 2017, 50,317,704 shares of the registrant's common stock were outstanding.

### Documents Incorporated By Reference

All or a portion of Items 10 through 14 in Part III of this Form 10-K are incorporated by reference to the Registrant's definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if the Registrant's Schedule 14A is not filed within such period, will be included in an amendment to this Report on Form 10-K which will be filed within such 120 day period.

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PART I

Cautionary Statement Regarding Forward-Looking Information

This Annual Report on Form 10-K contains, in addition to historical information, certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact contained in this Annual Report on Form 10-K, including statements regarding our future results of operations and financial position, strategy and plans, and our expectations for future operations, are forward-looking statements. The words “believe,” “may,” “estimate,” “continue,” “anticipate,” “design,” “intend,” “expect” and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, strategy, short-term and long-term business operations and objectives, and financial needs. Forward-looking statements include, but are not limited to, statements about:

- our opportunities and expectations for growth in the student lending, healthcare and other markets;
- anticipated trends and challenges in our business and competition in the markets in which we operate;
- our client relationships and future growth opportunities;
- the adaptability of our technology platform to new markets and processes;
- our ability to invest in and utilize our data and analytics capabilities to expand our capabilities;
- sufficiency of our appeals reserve;
- our growth strategy of expanding in our existing markets and considering strategic alliances or acquisitions;
- our ability to meet our liquidity and working capital needs;
- maintaining, protecting and enhancing our intellectual property;
- our expectations regarding future expenses;
- expected future financial performance; and
- our ability to comply with and adapt to industry regulations and compliance demands.

These statements reflect current views with respect to future events and are based on assumptions and subject to risks and uncertainties. There are a variety of factors could cause actual results to differ materially from the anticipated results or expectations expressed in our forward-looking statements. These risks and uncertainties include, but are not limited to, those risks discussed in Item 1A of this report. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Forward-looking statements contained in this report present management’s views only as of the date of this report. We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our quarterly reports on Form 10-Q and current reports on Form 8-K filed with the Securities and Exchange Commission.

ITEM 1. Business

Overview

We provide technology-enabled recovery and related analytics services in the United States. Our services help identify and recover delinquent or defaulted assets and improper payments for both government and private clients in a broad range of markets. Our clients typically operate in complex and regulated environments and outsource their recovery needs in order to reduce losses on billions of dollars of defaulted student loans, improper healthcare payments and delinquent state tax and federal treasury and other receivables. We generally provide our services on an outsourced basis, where we handle many or all aspects of our clients’ recovery processes.

We believe we have a leading position in our markets based on our technology-enabled services platform, long-standing client relationships and the large volume of funds we have recovered for our clients. In 2016, we provided recovery services on approximately \$6.6 billion of combined student loans and other delinquent federal and state receivables and recovered approximately \$22.7 million in improper Medicare payments in the first half year of 2016. Our clients in the student loan recovery market include 9 of the 27 active guaranty agencies, which are state or non-profit agencies that administer and rehabilitate student loans issued under the former federally-governed student loan program and these relationships average more than 10 years in length. As of September 30, 2016, guaranty agencies, or GAs, held approximately \$30.0 billion of



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defaulted government-supported student loans. In the healthcare market, we have been a Medicare Recovery Audit Contractor, or RAC, in the United States for the Centers for Medicare and Medicaid Services, or CMS since 2009, with responsibility for identifying improper Parts A and B Medicare payments in the Northeastern United States. In December 2016, as part of a contract procurement process, we were awarded a new RAC contract for 11 states located in the Northeast and Midwest, as well as a national contract for the post-payment review of Durable Medical Equipment, Prosthetics, Orthotics, and Supplies (or DMEPOS) and home health/hospice claims.

We utilize our technology platform to efficiently provide recovery and analytics services in the markets we serve. We have continuously developed and refined our technology platform for almost two decades by using our extensive domain and data processing expertise. Our technology platform allows us to disaggregate otherwise complex recovery processes into a series of simple, efficient and consistent component steps, which we refer to as workflows, for our recovery and healthcare claims review specialists. This approach enables us to continuously refine our recovery processes to achieve higher rates of recovery with greater efficiency. By optimizing what traditionally have been manually-intensive processes, we believe we achieve higher workforce productivity versus more traditional labor-intensive outsourcing business models. For example, we generated in excess of \$123,000 of revenues per employee during 2016, based on the average number of employees during the year.

We believe that our platform is easily adaptable to new markets and processes. Over the past several years, we have successfully extended our platform into additional markets with significant recovery opportunities. For example, we utilized the same basic platform previously used primarily for student loan recovery activities to enter the state tax, federal treasury receivables and healthcare recovery markets. We have enhanced our platform through investment in new data and analytics capabilities, which we believe will enable us to provide additional services such as services relating to the detection of fraud, waste and abuse.

Our revenue model is generally success-based as we earn fees based on a percentage of the aggregate amount of funds that we enable our clients to recover. Our services do not require any significant upfront investments by our clients and we offer our clients the opportunity to recover significant funds otherwise lost. Because our model is based upon the success of our efforts and the dollars we enable our clients to recover, our business objectives are aligned with those of our clients and we are generally not reliant on their spending budgets. Furthermore, our business model does not require significant capital expenditures and we do not purchase loans or obligations.

For the year ended December 31, 2016, we generated approximately \$141.4 million in revenues, \$11.5 million in net loss, \$25.9 million in adjusted EBITDA and \$4.1 million in adjusted net income. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Adjusted EBITDA and Adjusted Net Income" in Item 7 below for a definition of adjusted EBITDA and adjusted net income and reconciliations of adjusted EBITDA and adjusted net income to net income determined in accordance with generally accepted accounting principles.

We commenced our operations in 1976 under the corporate name Diversified Collection Services, Inc., or DCS. We were incorporated in Delaware on October 8, 2003 under the name DCS Holdings, Inc. and subsequently changed our name to Performant Financial Corporation. Our website address is [www.performantcorp.com](http://www.performantcorp.com).

### Our Markets

We operate in markets characterized by strong growth, a complex regulatory environment and a significant amount of delinquent, defaulted or improperly paid assets.

### Student Lending

Government-supported student loans are authorized under Title IV of the Higher Education Act of 1965. Historically, there have been two distribution channels for student loans: (i) the Federal Direct Student Loan Program, or FDSLSP, which represents loans made and managed directly by the Department of Education; and (ii) the Federal Family Education Loan Program, or FFELP, which represents loans made by private institutions and currently backed by any of the 27 Guaranty Agencies, or "GAs".

In July 2010, the government-supported student loan sector underwent a structural change with the passage of the Student Aid and Fiscal Responsibility Act, or SAFRA. This legislation transitioned all new government-supported student loan originations to the FDSLSP, and away from originations made by private institutions within the FFELP that had previously utilized the GAs to guarantee, manage and service loans. The GAs are non-profit 501(c)(3) public benefit corporations operating under contract with the U.S. Secretary of Education, pursuant to the Higher Education

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Act of 1965, as amended, solely for the purpose of guaranteeing and managing student loans originated by lenders participating in the FFELP.

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Consequently, while the original distribution channels for student loans have been consolidated into one channel, the Department of Education, this does not impact the volume of government-supported student loan origination, which is a key driver of the volume of defaulted student loan inventory. In addition, despite this transition of all new loan originations to the FDSLPL, GAs will continue to manage a significant amount of defaulted student loans for some period of time, due to their large outstanding portfolios of loans originated prior to July 2010. The outstanding portfolios of defaulted FFELP loans will, therefore, require recovery for the foreseeable future.

The Department of Education estimates that the balance of defaulted loans was approximately \$66.0 billion in the FDSLPL and approximately \$34.5 billion in the FFELP as of March 31, 2015. These programs collectively guaranteed approximately \$1,136 billion of federal government-supported student loans according to the Congressional Budget Office as of September 30, 2015. Given the operational and logistical complexity involved in managing the recovery of defaulted student loans, the GAs and the Department of Education generally choose to outsource these services to third parties.

### Healthcare

The healthcare industry represents a significant portion of the U.S. GDP. According to CMS, U.S. healthcare spending reached \$2.9 trillion in 2013 and is forecast to grow at a 5.7% compound annual growth rate through 2023. In particular, CMS indicates that federal government-related healthcare spending for 2013 totaled approximately \$1.0 trillion. This federal government-related spending included approximately \$591.2 billion for Medicare, which provides a range of healthcare coverage primarily to elderly and disabled Americans, and \$431.1 billion for Medicaid, which provides federal matching funds for states to finance healthcare for individuals at or below the public assistance level.

Medicare was initially established as part of the Social Security Act of 1965 and consists of four parts: Part A covers hospital and other inpatient stays; Part B covers hospital outpatient, physician and other services; Part C is known as Medicare Advantage, under which beneficiaries receive benefits through private health plans; and Part D is the Medicare outpatient prescription drug benefit.

Of the \$358 billion of Medicare spending in 2013, the Department of Health and Human Services estimated that approximately \$43 billion, or approximately 12.1%, was improper, and that Medicare is the federal program with the largest amount of improper payments. Medicare improper payments generally involve incorrect coding, procedures performed which were not medically necessary, and incomplete documentation or claims submitted based on outdated fee schedules, among other issues.

In accordance with the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, a demonstration program was conducted from March 2005 to March 2008 in six states to determine if recovery audit contractors could be effectively used to identify improper payments for claims paid under Medicare Part A and Part B. Due to the success of this demonstration, under The Tax Relief and Health Care Act of 2006, the U.S. Congress authorized the expansion of the recovery audit program nationwide. CMS relies on third-party contractors to execute the recovery audit program to analyze millions of Medicare claims annually for improper payments to healthcare providers. The program was implemented by designating one prime contractor in each of the four major regions in the United States: West, Midwest, South, and Northeast. Contracts with recovery audit contractors, or RACs, were initially awarded in 2009. These contracts effectively expired in 2016 and new contracts were awarded in October 2016.

In addition to government-related healthcare spending, significant growth in spending is expected in the private healthcare market. According to CMS' National Health Expenditures Projections, the private healthcare market accounted for approximately \$961 billion in spending in 2013 and private expenditures are projected to grow more than 5.7% annually through 2023.

### Other Markets

#### State Tax Market

As state governments struggle with revenue generation and face significant budget deficits, many states have focused on recovery of delinquent state taxes. According to the Center on Budget and Policy Priorities, an independent think tank, 31 U.S. states faced projected budget shortfalls totaling \$55 billion in the year ended September 30, 2013. The economic recession beginning in 2008 led to lower income and sales taxes from both individuals and corporations, reducing overall tax revenues and leading to large budget deficits at the state government level. While many states



have received federal aid, most have cut services and increased taxes to help close the budget shortfall and have evaluated outsourcing at least some aspect of delinquent tax recovery.

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### Federal Agency Market

The federal agency market consists of government debt subrogated to the Department of the Treasury by numerous different federal agencies, comprising a mix of commercial and individual obligations and a diverse range of receivables. These debts are managed by the Bureau of the Fiscal Service (formerly the Department of Financial Management Service), or FS, a bureau of the Department of the Treasury. Since 1996, the FS has recovered more than \$63 billion in delinquent federal and state debt. For the fiscal year ended September 30, 2013, federal agency recoveries in this market totaled more than \$7 billion, an increase of more than \$13 million over 2012. A significant portion of these collections are processed by private collection firms on behalf of the FS.

### Our Competitive Strengths

We believe that our business is difficult to replicate, as it incorporates a combination of several important and differentiated elements, including:

**Scalable and flexible technology-enabled services platform.** We have a technology platform that is highly flexible, intuitive and easy to use for our recovery and claims specialists. Our platform is easily configurable and deployable across multiple markets and processes. For example, we have successfully extended our platform from the student loan market to the state and federal tax, federal treasury receivables and the healthcare recovery markets, each having its own industry complexities and specific regulations.

**Advanced, technology-enabled workflow processes.** Our technology-enabled workflow processes, developed over many years of operational experience in recovery services, disaggregate otherwise complex recovery processes into a series of simple, efficient and consistent steps that are easily configurable and applicable to different types of recovery-related applications. We believe our workflow software is highly intuitive and helps our recovery and claims specialists manage each step of the recovery process, while automating a series of otherwise manually-intensive and document-intensive steps in the recovery process. We believe our streamlined workflow technology drives higher efficiencies in our operations, as illustrated by our ability to generate in excess of \$123,000 of revenues per employee during 2016, based on the average number of employees during the year. We believe our streamlined workflow technology also improves recovery results relative to more labor-intensive outsourcing models.

**Strong data and analytics capabilities.** Our data and analytics capabilities allow us to achieve strong recovery rates for our clients. We have collected recovery-related data for over two decades, which we combine with large volumes of client and third-party data to effectively analyze our clients' delinquent or defaulted assets and improper payments. We have also developed a number of analytics tools that we use to score our clients' recovery inventory, determine the optimal recovery process and allocation of resources, and achieve higher levels of recovery results for our clients. In addition, we utilize analytics tools to continuously measure and test our recovery workflow processes to drive refinements and further enhance the quality and effectiveness of our capabilities.

**Long-standing client relationships.** We believe our long-standing focus on achieving superior recovery performance for our clients and the significant value our clients derive from this focus have helped us achieve long-tenured client relationships, strong contract retention and better access to new clients and future growth opportunities. We have business relationships with numerous GAs in the student loan market and these relationships average more than 10 years in length. In the healthcare market, we have a ten-year relationship with CMS and in October 2016 we were awarded two contracts out of the second recovery audit program procurement process, including for a region consisting of 11 states in the Northeast and Midwest and the national DMEPOS and home health contract.

**Extensive domain expertise in complex and regulated markets.** We have extensive experience and domain expertise in providing recovery services for government and private institutions that generally operate in complex and regulated markets. We have demonstrated our ability to develop domain expertise in new markets such as healthcare and state tax and federal Treasury receivables. We believe we have the necessary organizational experience to understand and adapt to evolving public policy and how it shapes the regulatory environment and objectives of our clients. We

believe this helps us identify and anticipate growth opportunities. For example, we successfully identified government healthcare as a potential growth opportunity that has thus far led to the award of five contracts to us by CMS. Together with our flexible technology platform, we have the ability to adapt our

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business strategy, to allocate resources and to respond to changes in our regulatory environment to capitalize on new growth opportunities.

Proven and experienced management team. Our management team has significant industry experience and has demonstrated strong execution capabilities. Our senior management team, led by Lisa Im, has been with us for an average of approximately 15 years. This team has successfully grown our revenue base and service offerings beyond the original student loan market into healthcare and delinquent state tax and private financial institutions receivables. Our management team's industry experience, combined with deep and specialized understanding of complex and highly regulated industries, has enabled us to maintain long-standing client relationships and strong financial results.

### Our Growth Strategy

Key elements of our growth strategy include the following:

Expand our student loan recovery volume. The balance of defaulted government-supported student loans was approximately \$100.5 billion as of March 31, 2015. While we have long-standing relationships with some of the largest participants in the government-supported student loan market, we believe there are significant opportunities within this growing market to increase the volume of student loans placed with us by existing and new clients. For example, as a result of our relationships with four of the five largest GAs, we believe we are well-positioned to benefit as a result of any consolidation of smaller GAs over the coming years. In December 2016, it was announced that we were not selected as one of the recovery contractors for the Department of Education after more than 25 years in that role. We have filed a protest of this contract award and that protest remains pending, with a decision expected in April 2017.

Expand our recovery services in the healthcare market. According to CMS, Medicare spending totaled approximately \$591.2 billion in 2013 and is expected to increase to \$1.1 trillion in 2022, representing a compound annual growth rate of 7.4%. In the private healthcare market, spending totaled \$961 billion in 2013 and is expected to grow more than 5.7% annually through 2023, according to CMS' National Health Expenditures Projections. As these large markets continue to grow, we expect the need for recovery services to increase in the public and private healthcare markets. We were awarded new RAC contracts for Region 1 which consists of 11 states in the Northeast and Midwest, and Region 5, which covers claims for durable medical equipment, prosthetics and orthotics and home health and hospice payment claims across the U.S. We have also entered into contracts and are pursuing additional opportunities to provide audit, recovery and analytics services in the private healthcare market. In addition, we intend to pursue opportunities to find and eliminate losses prior to payment for healthcare services, including the detection of fraud, waste and abuse in the public and private healthcare markets.

Expand recovery services in other markets. We intend to expand our recovery services in other markets, including the private healthcare recovery market, state and federal tax and federal treasury receivables. We intend to capitalize on our extensive experience and domain expertise and our highly-flexible technology platform to seek opportunities in these additional markets.

Pursue strategic alliances and acquisitions. We intend to selectively consider opportunities to grow through strategic alliances or acquisitions that are complementary to our business. These opportunities may enhance our existing capabilities, enable us to enter new markets, expand our product offerings and allow us to diversify our revenues.

### Our Platform

Our technology-enabled services platform is based on over two decades of experience in recovering large amounts of funds on behalf of our clients across several markets. The components of our platform include our data management expertise, analytics capabilities and technology-based workflow processes. Our platform integrates these components to allow us to achieve optimized outcomes for our clients in the form of increased efficiency and productivity and high recovery rates. Our platform and workflow processes are also intuitive and easy to use for our recovery and claims specialists and allow us to increase our employee retention and productivity.



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The components of our platform include the following:

Data Management Expertise

Our platform manages and stores large amounts of data throughout the workflow process. This includes both proprietary data we have compiled over two decades, as well as third-party data which we can integrate efficiently and in real-time to reduce errors, reduce cycle time processing and, ultimately, improve recovery rates. The strength of our data management expertise augments our analytics capabilities and provides our recovery and claims specialists with powerful workflow processes.

Data Analytics Capabilities

Our data analytics capabilities efficiently screen and allocate massive volumes of recovery inventory. For example, upon receipt of each placement of student loans, we utilize our proprietary algorithms to assist us in determining the most efficient recovery process and the optimal allocation of recovery specialist resources for each loan. In the healthcare market, we analyze millions of Medicare claims to find potential correlations between claims data and improper payments, which enhance our future recovery rates. Across all of our current markets, we utilize our proprietary analytics tools to continuously and rigorously test our workflow processes in real-time to drive greater process efficiency and improvement in recovery rates.

Furthermore, we believe our analytics capabilities will extend our potential markets, permitting us to pursue significant new business opportunities. For example, we have expanded the use of our data analytics capabilities in the healthcare sector to offer a variety of services from post and pre-payment audit of healthcare claims in both the public and private healthcare sector, to detection of fraud, waste and abuse of healthcare claims, to coordination of benefits and pharmacy fraud detection.

Workflow Processes

Over many years, we have developed and refined our recovery workflow processes, which we believe drive higher efficiency and productivity and reduce our reliance on labor-intensive methods relative to more traditional recovery outsourcing models. We refer to the patented technology that supports our proprietary workflows as “Smart Bins.” Smart Bins disaggregate otherwise complex recovery processes into a series of simple, efficient and consistent steps that are easily configurable and applicable to different types of recovery-related applications. Our workflow processes integrate a broad range of functions that encompass each stage of a recovery process.

Smart Bins have been designed to be highly intuitive and help our recovery and claims specialists manage each step in the recovery process and enhance their productivity to high levels, regardless of skill differences among specialists. Smart Bins direct specialists toward the most efficient and effective action or step with respect to the management and recovery of a defaulted student loan, with some input by specialists. Our technology places expert system rules into the workflow engine, allowing employees at different skill levels to manage the more complex work steps that highly experienced workers would perform, while automating document management and compliance functionality as industry regulations and compliance demands change.

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The following recovery diagram illustrates how the various components of our platform work together to solve a typical client workflow:

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Our Services

We use our technology-enabled services platform to provide recovery and analytics services in a broad range of markets for the identification and recovery of student loans, improper healthcare payments and delinquent state tax and federal treasury receivables. The table below summarizes our recovery services and related analytics capabilities and the markets we serve.

Recovery Services			Analytics Capabilities
<p>Student Loans</p> <ul style="list-style-type: none"> <li>• Provide recovery services to GAs and private institutions</li> <li>• Identify and track defaulted borrowers across our clients' portfolios of student loans</li> <li>• Utilize our proprietary technology, our history of borrower data and our analytics capabilities to rehabilitate and recover past due student loans</li> <li>• Earn contingent, success-based fees calculated as a percentage of funds that we enable our clients to recover</li> </ul>	<p>Healthcare</p> <ul style="list-style-type: none"> <li>• Provide audit and recovery services to identify improper healthcare payments for public and private healthcare clients</li> <li>• Identify improper payments typically resulting from incorrect coding, procedures that were not medically necessary, incomplete documentation or claims submitted based on outdated fee schedules</li> <li>• Earn contingent, success-based fees based on a percentage of claim amounts recovered</li> </ul>	<p>Other Markets</p> <ul style="list-style-type: none"> <li>• Provide tax recovery services to state and municipal agencies</li> <li>• Recover government debt for numerous different federal agencies under a contract with the Treasury</li> <li>• Enable financial institutions to proactively manage loan portfolios and reduce the incidence of defaulted loan assets</li> <li>• Earn contingent, success-based fees calculated as a percentage of the amounts recovered, fees based on dedicated headcount and hosted technology licensing fees</li> </ul>	<ul style="list-style-type: none"> <li>• We use our enhanced data analytics capabilities, which we refer to as Performant Insight, to offer a variety of services from post- and pre-payment audit of healthcare claims to detection of fraud, waste and abuse of healthcare claims, to coordination of benefits and pharmacy fraud detection</li> </ul>

Recovery Services  
Student Loans

We provide recovery services primarily to the government-supported student loan industry, and our current clients include several of the largest GAs, as well as private financial institutions. We use our proprietary technology to identify, track and communicate with defaulted borrowers on behalf of our clients to implement suitable recovery programs for the repayment of outstanding student loan balances.

Our clients contract with us to provide recovery services for large pools of student loans generally representing a portion of the total outstanding defaulted balances they manage, which they provide to us as “placements” on a periodic basis. Generally, the volume of placements that we receive from our clients is influenced by our performance under our contracts and our ability to recover funds from defaulted student loans, as measured against the performance of competitors who may service a similar pool of defaulted loans for the same client. To the extent we perform well under our existing contracts and differentiate our services from those of our competitors, we may receive a relatively greater number of student loan placements under these contracts and may improve our ability to obtain future contracts from these clients and other potential clients.

We use algorithms derived from over two decades of experience with defaulted student loans to make reasonably accurate estimates of the recovery outcomes likely to be derived from a placement of defaulted student loans. In December 2016, the Department of Education awarded contracts for student loan recovery services to seven contractors. We were not selected to receive one of these contract awards. We, along with 19 other contractors, have



filed protests with the Government Accountability Office, or GAO, regarding the award of these contracts. We expect to receive a ruling on our protest in April 2017. The Department of Education has historically been our largest or one of our largest clients, accounting for 15.5%, 23.8%, and 27.2% of our revenues in 2016, 2015 and 2014, respectively. We also restructure and recover student loans issued directly by banks to students outside of federal lending programs. These types of loans typically supplement government-supported student loans to meet any shortfall in supply of student loan needs that cannot be met by grants or federal loans. Unlike government-supported student loans, private student loans do not have capped interest rates and, accordingly, involve higher instances of default relative to federally-backed student loans.

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### Healthcare

We provide recovery services related to improper payments in the healthcare market. In 2009 we were awarded the role as one of four prime RAC contractors in the United States, with exclusive responsibility to identify and facilitate the recovery of improper Parts A and B Medicare payments in the Northeastern United States. This contract expired in 2016 and, following a lengthy procurement process, in October 2016 we were awarded two new RAC contracts by CMS. One new award covers Parts A and B Medicare payments in a region consisting of 11 states in the Northeast and Midwest. The second award involves post-payment review of DMEPOS and home health and hospice claims across the U.S.

Under our RAC contracts with CMS, we utilize our technology-enabled services platform to screen Medicare claims against several criteria, including coding procedures and medical necessity standards, to determine whether a claim should be further investigated for recoupment or adjustment by CMS. We conduct automated and, where appropriate, detailed medical necessity reviews. If we determine that the likelihood of finding a potential improper payment warrants further investigation, we request and review healthcare provider medical records related to the claim, utilizing experts in Medicare coding and registered nurses. We interact and communicate with healthcare providers and other administrative entities, and ultimately submit the claim to CMS for correction.

In anticipation of the award of the latest round of RAC contracts, beginning in 2013 CMS adopted a series of contract transition procedures that restricted our ability to request medical records for audit, and has otherwise suspended our ability to perform any audit services for certain periods of time or limited the scope of our audit activities, thus adversely affecting our revenues under this contract. For example, collections by CMS for corrections under the RAC program decreased by 82.8% in fiscal 2015 as compared to fiscal 2014, due to CMS and Congress prohibiting RACs from performing inpatient hospital patient status reviews, as well as additional limitations on audit activity imposed in connection with the prolonged contract transition process. As a result, our revenues from the RAC program have steadily decreased over the last several years, from \$66.8 million in 2013, to \$29.2 million in 2014, to \$12.5 million in 2015 and \$5.7 million in 2016.

In the private healthcare market, we utilize our technology-enabled services platform to provide audit, recovery and analytical services for private healthcare payors. Our experience from our existing RAC contract has helped establish our presence in the private healthcare market by providing us the opportunity to provide audit and recovery services for several national commercial health plans. Our audit and analytic capabilities have allowed us not only to expand our services with these initial private healthcare clients, but also gain entry into other related private healthcare opportunities.

### Other Markets

We also provide recovery services to several federal, state and municipal tax authorities, the Department of the Treasury and a number of financial institutions.

In September 2016 the Internal Revenue Service, or IRS, announced its plans to begin private collection of certain federal tax debts starting in the spring of 2017 and named us as one of four companies to perform these recovery services. The new program, authorized under a federal law, calls for the use of private companies to recover, on the government's behalf, outstanding inactive tax receivables. While we expect that work under this contract will begin in April 2017, we do not anticipate that this contract will generate significant revenues in 2017 due to the expected relatively slow ramp up process under this new program.

For state and municipal tax authorities, we analyze a portfolio of delinquent tax and other receivables placed with us, develop a recovery plan and execute a recovery process designed to maximize the recovery of funds. In some instances, we have also run state tax amnesty programs, which provide one-time relief for delinquent tax obligations, and other debtor management services for our clients. We currently have relationships with numerous state and municipal governments. Delinquent obligations are placed with us by our clients and we utilize a process that is similar to the student loan recovery process for recovering these obligations.

For the Department of the Treasury, we recover government debt subrogated to it by numerous different federal agencies. The placements we are provided represent a mix of commercial and individual obligations. We are one of four contractors for the most recent Treasury contract.

We also provide risk management advisory services that enable these clients to proactively manage loan portfolios and reduce the incidence of defaulted loan assets over time. Our experience suggests that proactive default prevention practices produce significant net yield and earnings gains for our clients. We deliver these services in two forms. First, we contact and consult with borrowers to implement a repayment program, including payment through automatic debit arrangements, prior to the beginning of the repayment period in order to increase the likelihood that payments begin on time. Second, we offer a service that involves contacting delinquent borrowers in an effort to cure the delinquency prior to the loan entering default.

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### Analytics Capabilities

For several years, we have leveraged our data analytics tools to help filter, identify and recover delinquent and defaulted assets and improper payments as part of our core recovery services platform. Through our data analytics capabilities, which we refer to as Performant Insight, we are able to review, aggregate, and synthesize very large volumes of structured and unstructured data, at high speeds, from the initial intake of disparate data sources, to the warehousing of the data, to the analysis and reporting of the data. We believe we have built a differentiated, next-generation “end-to-end” data processing solution that will maximize value for current and future customers. Performant Insight provides numerous benefits for our recovery services platform. Performant Insight has not only enhanced our existing recovery services under our RAC contract by analyzing significantly higher volumes of healthcare claims at faster rates and reducing our cycle time to review and assess healthcare claims, but has also enabled us to develop improved and more sophisticated business intelligence rules that can be applied to our audit processes. We believe our analytics capabilities will extend our potential markets, permitting us to pursue significant new business opportunities. We have expanded the use of our data analytics capabilities in the healthcare sector to offer a variety of services from post and pre-payment audit of healthcare claims in both the public and private healthcare sector, to detection of fraud, waste and abuse of healthcare claims, to coordination of benefits and pharmacy fraud detection.

### Our Clients

We provide our services across a broad range of government and private clients in several markets.

### Guaranty Agencies

We restructure and recover defaulted student loans issued by private lenders and backed by GAs under the FFELP. Despite the transition from FFELP to FDSLPL, we believe GA default volumes will continue to rise for a few years as there generally is a lag between originations and defaults of at least three to four years. When a borrower stops making regular payments on a FFELP loan, the GA is obligated to reimburse the lender approximately 97% of the loan’s principal and accrued interest. GAs then seek to recover and restructure these obligations. The GAs with which we contract generally structure one to three-year initial term contracts with multiple renewal periods, and historically the fees that we receive are generally similar to the fees we receive from the Department of Education contract. For some GA clients, we provide services through MSAs, under which we manage a GA’s entire portfolio of defaulted student loans and, for certain clients, engage subcontractors to provide a portion of the recovery services associated with a GA’s student loan portfolio.

We have a relationship with numerous active GAs in the U.S., including Great Lakes Higher Education Guaranty Corporation and Pennsylvania Higher Education Assistance Authority, which were responsible for 23.5% and 16.4%, respectively, of our revenues for the year ended December 31, 2016. We have had relationships with numerous GA clients and these relationships average more than 10 years in length.

### CMS

We have a ten-year relationship with CMS. Under our first RAC contract with CMS, which was awarded in 2009 and expired in 2016, we were responsible for identifying and facilitating the recovery of improper Part A and Part B Medicare payments in the Northeast region of the United States. This RAC contract accounted for approximately 4.1% of our revenues for the year ended December 31, 2016. In October 2016, we were awarded two new RAC contracts. We received the contract to audit improper payments for claims made under Medicare Parts A and B in Region 1, which consists of Connecticut, Michigan, Indiana, Maine, Massachusetts, New Hampshire, New York, Ohio, Kentucky, Rhode Island and Vermont, and the contract for Region 5, which involves post-payment review of claims related to DMEPOS and home health and hospice across the U.S. The fees that we receive for identifying improper payments from CMS under these contracts are entirely contingency-based, and the contingency-fee percentage depends on the methods of recovery, and, in some cases, the type of improper payment that we identify. Our level of activity and the revenues that we derive as a RAC contractor have varied significantly depending on changes in the permitted scope of review and limitations imposed in connection with the transition from the first to the second round of RAC contracts. For example, collections by CMS for corrections under the RAC program decreased by 82.8% in fiscal 2015 as compared to fiscal 2014, due to CMS and Congress prohibiting RACs from performing inpatient hospital patient status reviews, as well as additional limitations on audit activity imposed in connection with

the prolonged contract transition process. As a result, our revenues from the RAC program have steadily decreased over the last several years, from \$66.8 million in 2013, to \$29.2 million in 2014, to \$12.5 million in 2015 and \$5.7 million in 2016. It is expected that audit activity

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under our newly awarded RAC contracts will commence in April 2017, although it appears that permitted audit activity will continue to be constrained, at least initially.

Department of Education

We have provided student loan recovery services to the Department of Education for approximately 25 years until our most recent contract expired in April 2015. Traditionally, we have restructured and recovered defaulted student loans distributed directly by the Department of Education as part of the FDSLPL. Due to its limited resources and recovery capabilities, the Department of Education outsources much of its defaulted student loan portfolio to third-party vendors for recovery. Recovery fees are entirely contingency-based, and our fee for a particular recovery have traditionally depended on the type of recovery facilitated.

In December 2016, the Department of Education awarded contracts for student loan recovery services to seven contractors. We were not a recipient of one of those awards. We, along with 19 other contractors have protested the Department of Education's awards to the GAO. We do not anticipate receiving any new loan placements from the Department of Education, if at all, until the protests are resolved. Because all federally-supported student loans are being originated by the Department of Education as a result of SAFRA, the Department of Education will become an increasingly important player in the Guaranteed Student Loan arena. The Department of Education was responsible for approximately 16% of our revenues for the year ended December 31, 2016.

U.S. Department of the Treasury

We have assisted the Department of the Treasury for 19 years in the recovery of delinquent receivables owed to a number of different federal agencies. The debt obligations we help to recover on behalf of the Department of the Treasury include commercial and individual debt obligations. We are one of the four firms servicing the current Department of the Treasury contract. Similar to our other recovery contracts, our fees under this contract are contingency-based. We view this as an important strategic relationship, as it provides us valuable insight into other business opportunities within the federal government.

State Tax and Municipal Agencies

We provide outsourced recovery services for individuals' delinquent state tax and other municipal obligations on a hosted model and under MSAs. We currently have relationships with ten state and municipal governments.

Private Lenders

We provide recovery services for private student loans, which supplement federally guaranteed loans, and home mortgages to private lenders.

Internal Revenue Service

In September 2016 the Internal Revenue Service, or IRS, announced it plans to begin private collection of certain federal tax debts starting in 2017 and awarded us a contract to perform these recovery services. The new program, authorized under a federal law enacted by Congress, enables us, along with three other contractors to collect, on the government's behalf, outstanding inactive tax receivables. Our ability to recover these receivables will be limited to accounts where taxpayers owe money, but the IRS is no longer actively working their accounts. While we expect that work under this contract will begin in April 2017, we do not expect that this contract will generate significant revenues in 2017. Additionally, we do not expect to receive any significant commercial placements under this contract until 2018.

Sales and Marketing

Our new business opportunities have historically been driven largely by referrals and natural extensions of our existing client relationships, as well as a targeted outreach by senior management. Our sales cycles are often lengthy, and demand high levels of attention from our senior management. At any point in time, we are typically focused on a limited number of potentially significant new business opportunities. As a result, to date, we have operated with a small staff of experienced individuals with responsibility for developing new sales, relying heavily upon our executive staff, including an appropriate sales and marketing team covering various markets.

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### Technology Operations

Our technology center is based in Livermore, California, with a redundant capacity in our Grants Pass, Oregon office. Additionally, Performant Insight, our data analytics business, is supported by staff in Miami Lakes, Florida. We have designed our infrastructure for scalability and redundancy, which allows us to continue to operate in the event of an outage at either datacenter. We maintain an information systems environment with advanced network security intrusion detection and prevention with 24x7 monitoring and security incident response capabilities. We utilize encryption technologies to protect sensitive data on our systems, all data during transmission and all data on redundancy or backup media. We also maintain a comprehensive enterprise-wide information security system based upon recognized standards, including the NIST800 53 and ISO 27002 Code of Practice for Information Security Program Management, to uphold high security standards needed for the protection of sensitive information.

### Competition

We face significant competition in all aspects of our business.

In recovery services for delinquent and defaulted assets, we face competition from a number of companies. Holders of these delinquent and defaulted assets typically engage several firms simultaneously to provide recovery services on different portions of their portfolios. The number of recovery firms engaged varies by client. Initially, we compete to be one of the retained firms in a competitive bidding process and, if we are successful, we then face continuing competition from the client's other retained firms based on the client's benchmarking of the recovery performance of its several vendors. Some clients will allocate additional placements to those recovery vendors producing the highest recovery rates. We believe that we primarily compete on the basis of recovery rate performance, as well as maintenance of high standards of recovery practices and data security capabilities. We believe that we compete favorably with respect to most of these factors as evidenced by our long-standing relationships with our clients in these markets. Pricing is not usually a major competitive factor as all recovery services vendors in these markets typically receive the same contingency-based fee rate.

In the recovery of improper healthcare payments, we face competition in the bidding process for the RAC contracts and for obtaining audit work from commercial healthcare providers. In the most recent RAC bidding process, the identified competitive factors were demonstrated experience in effective recovery services in the healthcare market, sufficient capacity to address claims volumes, maintenance of high standards of recovery practices, financial capability to perform under the RAC contract and recovery fee rates. In the commercial healthcare space, those same factors are generally applicable. Our competition in the private healthcare arena includes the other RAC service providers, Health Management Systems, Inc. and Cotivity, LLC, and a variety of healthcare consulting and healthcare information services companies. Many of these companies have greater financial, technological and other resources than we do.

### Government Regulation

The nature of our business requires that we adhere to a complex array of federal and state laws and regulations. These include the Health Insurance Portability and Accountability Act, or HIPAA, the Fair Debt Collection Practices Act, or FDCPA, the Fair Credit Reporting Act, or FCRA, the rules and regulations established by the Consumer Financial Protection Bureau, or CFPB, and related state laws. We are also governed by a variety of state laws that regulate the collection, use, disclosure and protection of personal information. We have implemented and maintain physical, technical and administrative safeguards intended to protect all personal data and we have processes in place to assist us in complying with applicable laws and regulations regarding the protection of this data. Our compliance efforts include training of personnel and monitoring our systems and personnel.

### HIPAA and Related State Laws

Our Medicare recovery business subjects us to compliance with HIPAA and various related state laws that contain substantial restrictions and requirements with respect to the use and disclosure of an individual's protected health information. HIPAA prohibits us from using or disclosing an individual's protected health information unless the use or disclosure is authorized by the individual or is specifically required or permitted under HIPAA. Under HIPAA, we must establish administrative, physical and technical safeguards to protect the confidentiality, integrity and availability of electronic protected health information maintained or transmitted by us or by others on our behalf. We are required to notify affected individuals and government authorities of data security breaches involving unsecured protected

health information. The Department of Health and Human Services Office of Civil Rights enforces HIPAA privacy violations; CMS enforces HIPAA security violations and the Department of Justice enforces criminal violations of HIPAA. We are subject to statutory penalties for violations of HIPAA.



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Most states have enacted patient confidentiality laws that protect against the unauthorized disclosure of confidential medical information, and many states have adopted or are considering further legislation in this area, including privacy safeguards, security standards and data security breach notification requirements. These state laws, if more stringent than HIPAA requirements, are not preempted by the federal requirements, and we must comply with them even though they may be subject to different interpretations by various courts and other governmental authorities. In addition, numerous other state laws govern the collection, dissemination, use, access to and confidentiality of individually identifiable health and healthcare provider information.

Our compliance efforts include the encryption of protected health information that we hold and the development of procedures to detect, investigate and provide appropriate notification if protected health information is compromised. Our employees and contractors receive initial and periodic supplemental training and are tested to ensure compliance. As part of our certification and accreditation process, we must undergo audits by federal agencies as noted below. CMS regularly audits us for, among other items, compliance with their security standards.

### Privacy Act of 1974

The Privacy Act of 1974 governs the collection, use, storage, destruction and disclosure of personal information about individuals by a government agency and extends to government contractors who have access to agency records performing services for government agencies. The Privacy Act requires maintenance of a code of conduct for employees with access to the agency records addressing the obligations under the Privacy Act, training of employees and discipline procedures for noncompliance. The Privacy Act also requires adopting and maintaining appropriate administrative, technical and physical safeguards to insure the security and confidentiality of records and to protect against any anticipated threats or hazards to their security or integrity.

As a contractor to federal government agencies we are required to comply with the Privacy Act of 1974. Our compliance effort includes initial and ongoing training of employees and contractors in their obligations under the Privacy Act. In addition we have implemented and maintain physical, technical and administrative safeguards and processes intended to protect all personal data consistent with or exceeding our obligations under the Privacy Act.

### Certification, Accreditation and Security

Business services that collect, store, transmit or process information for United States government agencies and organizations are required to undergo a rigorous certification and accreditation process to ensure that they operate at an acceptable level of security risk. As a government contractor, we currently have Authority to Operate, or ATO, licenses from both the Department of Education and CMS.

We maintain a comprehensive enterprise-wide information security system based upon recognized standards, including the NIST800 53 and ISO 27002 Code of Practice for Information Security Program Management, to uphold high security standards needed for the protection of sensitive information. In addition, we hold SSAE – SOC 1 Type II certification, which provides assurance to auditors of third parties that we maintain the necessary controls and procedures to effectively manage third party data. We undergo an independent audit by our government agency clients on the award of the contract and periodically thereafter. We also conduct periodic self-assessments.

Our regulatory compliance group is charged with the responsibility of ensuring our regulatory compliance and security. All our facilities have security perimeter controls with segregated access by security clearance level. The information systems environment maintains advanced network security intrusion detection and prevention with 24x7 monitoring and security incident response capabilities. We utilize encryption technologies to protect sensitive data on our systems, all data during transmission and all data on redundancy or backup media. Employees undergo background and security checks appropriate to their position. This can include security clearances by the Federal Bureau of Investigation. We also maintain compliant disaster recovery and business continuity plans, annually conduct two table top disaster exercises, conduct routine security risk assessments and maintain a continuous improvement process as part of our security risk mitigation and management activity.

### FDCPA and Related State Laws

The FDCPA regulates persons who regularly collect or attempt to collect, directly or indirectly, consumer debts owed or asserted to be owed to another person. Certain of our debt recovery and loan restructuring activities may be subject to the FDCPA. The FDCPA establishes specific guidelines and procedures that debt recovery firms must follow in communicating with consumer debtors, including the time, place and manner of such communications. Further, it

prohibits harassment or abuse by debt recovery firms, including the threat of violence or criminal prosecution, obscene language or repeated telephone calls

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made with the intent to abuse or harass. The FDCPA also places restrictions on communications with individuals other than consumer debtors in connection with the collection of any consumer debt and sets forth specific procedures to be followed when communicating with such third parties for purposes of obtaining location information about the consumer. In addition, the FDCPA contains various notice and disclosure requirements and prohibits unfair or misleading representations by debt recovery firms. Finally, the FDCPA imposes certain limitations on lawsuits to collect debts against consumers.

Prior to the adoption of amendments to the FDCPA as part of the Dodd-Frank Act, no federal agency had the authority to issue interpretative regulations for the FDCPA. As a result, judicial determinations and non-binding interpretative positions issued by the Federal Trade Commission under the FDCPA created compliance difficulties for the consumer debt collections industry. With the adoption of the amendments to the FDCPA as part of the Dodd-Frank Act in 2011, however, as well as specific statutory authority to issue implementing regulations for the FDCPA, primary jurisdiction for the FDCPA was transferred to the Consumer Financial Protection Bureau, or CFPB. Subsequently, the CFPB has indicated that it may issue proposed regulations under the FDCPA.

Debt recovery activities are also regulated at the state level. Most states have laws regulating debt recovery activities in ways that are similar to, and in some cases more stringent than, the FDCPA. In addition, some states require debt recovery firms to be licensed.

Our compliance efforts include written procedures for compliance with the FDCPA and related state laws, employee training and monitoring, auditing client calls, periodic review, testing and retraining of employees, and procedures for responding to client complaints. In all states where we operate, we believe that we currently hold all required state licenses or are exempt from licensing. Violations of the FDCPA may be enforced by the U.S. Federal Trade Commission, or FTC, or by a private action by an individual or class. Violations of the FDCPA are deemed to be an unfair or deceptive act under the Federal Trade Commission Act, which can be punished by fines for each violation. Class action damages can total up to one percent of the net worth of the entity violating the statute. Attorney fees and costs are also recoverable. In the ordinary course of business we are sued for alleged violations of the FDCPA and comparable state laws, although the amounts involved in the disposition or settlement of any such claims have not been significant.

**TCPA**

The Telephone Consumer Protection Act, or TCPA, regulates the initiation of calls (which includes text messages) to residential or cellular telephones, including the use of automatic telephone dialing systems as well as artificial or prerecorded voices. The TCPA requires callers to obtain prior express consent or, in some cases, prior express written consent from individuals before placing restricted calls. Our compliance efforts include confirming a consumer has provided prior express consent consistent with the requirements of the law. Violations of the TCPA may be enforced by the U.S. Federal Communications Commission, or FCC, or by a private action by an individual or class. Violations of the TCPA can be punished by recovery of damages or penalties up to \$1,500 per violation for willful violations. Attorney fees and costs are also recoverable. In the ordinary course of business we are sued for alleged violations of the TCPA and comparable state laws, although the amounts involved in the disposition or settlement of any such claims have not been significant.

**FCRA**

We are also subject to the Fair Credit Reporting Act, or FCRA, which regulates consumer credit reporting and which may impose liability on us to the extent that the adverse credit information reported on a consumer to a credit bureau is false or inaccurate. State law, to the extent it is not preempted by the FCRA, may also impose restrictions or liability on us with respect to reporting adverse credit information. Our compliance efforts include initial and ongoing training of employees working with consumer credit reports and the monitoring of usage. Violations of FCRA, which are deemed to be unfair or deceptive acts under the Federal Trade Commission Act, are enforced by the FTC or by a private action by an individual or class. Civil actions by consumers may seek damages per violation, with punitive damages, attorney's fees and costs also recoverable. Under the Federal Trade Commission Act, penalties for engaging in unfair or deceptive acts can be punished by fines for each violation.

**CFPB**

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The CFPB was created as part of the Dodd-Frank Act in 2011, with primary implementing and interpretative authority for many federal consumer protection laws, for example the FDCPA, transferred to the CFPB. Among other things, the CFPB was given the authority to issue interpretive regulations for the FDCPA.

In addition to its authority in regard to federal consumer protection laws, the CFPB was also provided direct jurisdiction over certain consumer financial service providers. In October of 2012, the CFPB issued a rule asserting direct jurisdiction over large consumer debt collectors, which includes debt collectors with annual assets of more than \$10 million. In

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accordance with the calculations included in this rule, we are subject to direct jurisdiction of the CFPB and in the future may be directly examined and supervised by the CFPB. In that regard, the CFPB has also released examination guidance that its examiners will use when reviewing compliance by debt collectors subject to its direct supervision. The CFPB focuses on service providers involved in collecting debt related to any consumer financial product from committing unfair, deceptive, or abusive acts or practices, or UDAAPs, in violation of the Dodd-Frank Act. UDAAPs include actions that are unfair and likely to cause substantial injury to consumers, deceptive actions that mislead or likely to mislead a consumer and abusive acts that interfere with the ability of a consumer to understand a term or condition of a consumer financial product or takes unreasonable advantage of a consumer's lack of understanding of a consumer financial product. Although abusive acts or practices may also be unfair or deceptive, each of these prohibitions are separate and distinct, and are governed by separate legal standards. Original creditors and other covered persons and service providers involved in collecting debt related to any consumer financial product or service are subject to the prohibition against UDAAPs. The CFPB has indicated that it will continue to review closely the practices of those engaged in the collection of consumer debts for potential UDAAPs in violation of the Dodd-Frank Act.

### State Law Compliance and Security Breach Response

Many states impose an obligation on any entity that holds personally identifiable information or health information to adopt appropriate security to protect such data against unauthorized access, misuse, destruction, or modification. Many states have enacted laws requiring holders of personal information to take certain actions in response to data breach incidents, such as providing prompt notification of the breach to affected individuals and government authorities. In many cases, these laws are limited to electronic data, but states are increasingly enacting or considering stricter and broader requirements. Massachusetts has enacted a regulation that requires any entity that holds, transmits or collects certain personal information about its residents to adopt a written data security plan meeting the requirements set forth in the statute. We have implemented and maintain physical, technical and administrative safeguards intended to protect all personal data and have processes in place to assist us in complying with applicable laws and regulations regarding the protection of this data and properly responding to any security incidents. We have adopted a system security plan and security breach incident response plans to address our compliance with these laws.

### Intellectual Property

Our intellectual property is a significant component of our business, including, most notably, the intellectual property underlying our proprietary technology-enabled services platform through which we provide our defaulted asset recovery and other services. To protect our intellectual property, we rely on a combination of intellectual property rights, including patents, trade secrets, trademarks and copyrights. We also utilize customary confidentiality and other contractual protections, including employee and third-party confidentiality and invention assignment agreements. As of December 31, 2016, we had two U.S. patents, both covering aspects of the workflow management systems and methods incorporated into our technology-enabled services platform. These patents will expire in September 2024. We routinely assess appropriate occasions for seeking additional patent protection for those aspects of our platform and other technologies that we believe may provide competitive advantages to our business. We also rely on certain unpatented proprietary expertise and other know-how, licensed and acquired third-party technologies, and continuous improvements and other developments of our various technologies, all intended to maintain our leadership position in the industry.

As of December 31, 2016, we had five trademarks registered with the U.S. Patent and Trademark office: DCS, Performant Recovery, Performant Technologies, Discovery Analytics, and Performant Insight.

We have registered copyrights covering various copyrighted material relevant to our business. We also have unregistered copyrights in many components of our software systems. We may not be able to use these unregistered copyrights to prevent misappropriation of such content by unauthorized parties in the future; however, we rely on our extensive information technology security measures and contractual arrangements with employees and third-party contractors to minimize the opportunities for any such misuse of this content.

We are not subject to any material intellectual property claims alleging that we infringe, misappropriate or otherwise violate the intellectual property rights of any third party, nor have we asserted any material intellectual property infringement claim against any third party.



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Employees

As of December 31, 2016, we had approximately 1,211 full-time employees. None of our employees is a member of a labor union and we consider our employee relations to be good.

Available Information

The SEC maintains an Internet site at <http://www.sec.gov> that contains our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, if any, or other filings filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, proxy and information statements. All reports that we file with the SEC may be read and copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, DC, 20549. Information about the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

ITEM 1A. Risk Factors

Our business, financial condition, results of operations and liquidity are subject to various risks and uncertainties, including those described below, and as a result, the trading price of our common stock could decline.

We have significant indebtedness maturing in March 2018 and we do not anticipate that our existing cash resources and expected cash flows from operations will be sufficient to repay the principal at maturity. There is no assurance that we will be able to refinance our indebtedness due in March 2018 prior to maturity or that we will be able to restructure or obtain modifications to the terms of our existing indebtedness from our lenders that would allow us to avoid a default at maturity.

As of December 31, 2016, we had outstanding indebtedness under our credit agreement in the principal amount of \$55.2 million, of which \$3.2 million matures on March 19, 2017 and \$52.0 million matures on March 19, 2018. Our existing cash resources and cash flows expected from operations over the next twelve months are not expected to be sufficient for us to pay the principal amount that will be due on March 19, 2018, although our current financial projections show that we will be able to maintain compliance with our debt covenants and make all scheduled debt service payments prior to that time, including payment of the portion of our indebtedness maturing in March 2017. Accordingly, we expect that it will be necessary to refinance our indebtedness due in March 2018 prior to maturity or restructure or obtain modifications to the terms of that indebtedness from our lenders. There is no assurance that new financing will be available to us in amounts sufficient to refinance this indebtedness or that any financing will be available on reasonable terms. Further, any new financing may result in a potentially dilutive issuance of equity securities or the issuance of new debt at higher interest rates and require us to comply with more restrictive covenants. In the absence of new financing, there is no assurance that our existing lenders will agree to restructure or modify the terms of our existing indebtedness on or before the March 2018 maturity date. Our ability to refinance or restructure our indebtedness will depend on the financial condition and results of operations of our business, which have suffered in recent periods as further described in these Risk Factors and elsewhere in this Report, and will also depend on factors completely outside of our control such as the condition of the capital markets at the time of any potential financing. If we cannot make scheduled payments on our debt, we will be in default and, as a result, our lenders could declare all outstanding principal and interest to be due and payable, and our lenders could foreclose against the assets securing our borrowings and we could be forced into bankruptcy or liquidation.

The Department of Education, our longstanding and significant client, recently announced that we would not receive a new contract for the recovery of student loans. We have filed a protest of this contracting decision with the GAO. If we are not successful in obtaining a contract award from the Department of Education through this process, our results of operations and cash flows will be harmed and it will be more difficult for us to repay or refinance our indebtedness. We have had a more than 25 year relationship with the Department of Education as a key contractor in the recovery of student loans and this relationship has been responsible for a significant portion of our annual revenues. Our revenues from the Department of Education were \$21.9 million in 2016, \$37.9 million in 2015 and \$53.2 million in 2014, representing 15.5%, 23.8% and 27.2% of our revenues, respectively. Further, we expected the Department of Education to become an increasingly important client because all federally-supported student loans have been originated by the Department of Education since 2010, meaning that there will be no further growth in student loans held by the GAs. Our most recent contract with the Department of Education expired in April 2015, and we have not received new placements of student loans from the Department of Education since that time pending the award of new

contracts.

In December 2016, the Department of Education announced the award of seven new contracts and we did not receive one of the new awards. We have filed a protest of this contracting decision with the GAO. While we believe that there are

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strong grounds for our protest, there is no assurance that our protest will be upheld. If we are not successful in obtaining a contract award from the Department of Education through this process, our results of operations and cash flows will be harmed and it will be more difficult for us to repay or refinance our indebtedness.

Over the course of our first RAC contract, there has been an increase in the number of appeals by healthcare providers to the third, or ALJ, level of appeal relating to claims we have audited, and there can be no assurance that our estimated liability for such appeals will be adequate.

Under our RAC contract with CMS, we recognize revenues when the healthcare provider has paid CMS for a claim or has agreed to an offset against other claims by the provider. Healthcare providers have the right to appeal a claim and may pursue additional levels of appeal if the initial appeal is found in favor of CMS. We accrue an estimated liability for appeals at the time revenue is recognized based on our estimate of the amount of revenue probable of being refunded to CMS following successful appeal based on historical data and other trends relating to such appeals. In addition, if our estimate of liability for appeals with respect to revenues recognized during a prior period changes, we increase or decrease the estimated liability reserve in the current period. Over the course of our first RAC contract, healthcare providers have increased their pursuit of appeals beyond the first and second levels of appeal to the third level of appeal, where cases are heard by administrative law judges, or ALJs. In our experience, decisions at the third level of appeal are the least favorable as ALJs exercise greater discretion and there is less predictability in the ALJ decisions as compared to appeals at the first or second levels. The pursuit of third level appeals by healthcare providers has also resulted in a backlog of claims at that level of appeal. This increase of ALJ appeals and backlog of claims at the third level of appeal is the primary reason our total estimated liability for appeals (consisting of the estimated liability for appeals plus the contra-accounts-receivable estimated allowance for appeals) has grown from a balance of \$16.4 million at December 31, 2013 to \$18.6 million as of December 31, 2014 to \$19.0 million as of both December 31, 2015, and December 31, 2016. Our estimates for our appeal reserve are subject to uncertainties, and accordingly we may underestimate the number of successful appeals or the financial impact of successful appeals in a given year or period. To the extent that the amount of commissions that we are required to return to CMS as a result of successful appeals exceeds our estimated appeals reserve, our revenues in the applicable period will be reduced by the amount of such excess. If we underestimate the amount of commissions that are subject to successful appeal, our revenues in future periods could be adversely affected. In addition, each of the subcontractors we engaged to assist in the recovery services under our RAC contract are similarly obligated to refund fees that they received from claims that are later overturned on appeal. To the extent any of our subcontractors fail to refund amounts that are due upon an appeals relating to claim that they were responsible for, we may be obligated to pay such amounts directly to CMS, which could have a material impact on our financial position.

Further, in August 2014 CMS offered to pay hospitals 68% of what they have billed Medicare to settle a backlog of pending appeals challenging Medicare's denials of reimbursement for certain types of short term care. The implication of these settlement offers related to claims for which recovery auditors have already been paid under the first RAC contracts remain uncertain at this time. Any payments we are required to make to CMS under our first RAC contract in connection with such settlement offers may be significant and in excess of the amount we have reserved for appeals, which could have a material negative impact our financial position and liquidity.

Limitations on the scope of recovery services we can provide under our new RAC contract will have a material impact on our revenues and these limitations may continue under the newly awarded RAC contracts.

Our ability to make claims under the first RAC contract was limited during each of the last three years by restrictions imposed on the scope of our audit activities and by contract transition rules announced by CMS that involved periodic suspension of audit activities. These limitations had a material adverse effect on our revenues and operating results. Our revenues from CMS during the year ended December 31, 2016 were \$5.7 million compared to \$12.5 million during the year ended December 31, 2015 and \$29.2 million for the year ended December 31, 2014. While we were recently awarded two new RAC contracts, we are uncertain about the scope of permitted audit and if the scope of audit is not increased, our revenues and the value of the new RAC contracts will be constrained. In addition, we expect there will be an approximately four to six month period from the date that we are permitted to start performing recovery services until we start to recognize revenues under our new RAC contracts. Accordingly, the currently expected start date of April 2017 for the new RAC contracts means that these new contracts will not have a significant

impact on our 2017 revenues, although we will incur related start-up expenses in 2017.

Revenues generated from our three largest clients represented 55% of our revenues in both 2016 and 2015. We are currently protesting a decision that would end our relationship with one of these clients and any termination of or deterioration in our relationship with any of our other significant clients would result in a further decline in our revenues.

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We have derived a substantial majority of our revenues from a limited number of clients, including the Department of Education, and several GAs. Revenues from our three largest clients represented 55% of our revenues for the year ended December 31, 2016 and 55% of our revenues for the year ended December 31, 2015. The Department of Education was responsible for approximately 16% of our revenues for the year ended December 31, 2016 and the Department of Education recently announced that we were not selected as one of the contractors under its new student loan recovery contract, a decision we are protesting. We have a relationship with numerous GAs in the U.S. including Great Lakes Higher Education Guaranty Corporation and Pennsylvania Higher Education Assistance Authority, which were responsible for 24% and 16%, respectively, of revenues for the year ended December 31, 2016. If our protest of the Department of Education's contract award does not result in our receiving new contract award, our business, will become even more dependent on our business relationships with our GA clients. All of our contracts with our significant clients are subject to periodic renewal and re-bidding processes and if we lose one of these clients or if the terms of our relationships with any of these clients become less favorable to us, our revenues would decline, which would harm our business, financial condition and results of operations.

Many of our contracts with our clients for the recovery of student loans and other receivables are not exclusive and do not commit our clients to provide specified volumes of business. In addition, the terms of these contracts may be changed unilaterally and on short notice by our clients. As a consequence, there is no assurance that we will be able to maintain our revenues and operating results.

Substantially all of our existing contracts for the recovery of student loans and other receivables, which represented approximately 92% of our revenues for the year ended December 31, 2016 and 88% of our revenues in the year ended December 31, 2015, enable our clients to unilaterally terminate their contractual relationship with us at any time without penalty, potentially leading to loss of business or renegotiation of terms. Further, most of our contracts in these markets allow our clients to unilaterally change the volume of loans and other receivables that are placed with us or the payment terms at any given time. In addition, most of our contracts are not exclusive, with our clients retaining multiple service providers with whom we must compete for placements of loans or other obligations. Therefore, despite our contractual relationships with our clients, our contracts do not provide assurance that we will generate a minimum amount of revenues or that we will receive a specific volume of placements.

Our revenues and operating results would be negatively affected if our student loan and receivables clients, which include our five largest clients in 2016 and four of our five largest clients in 2015, reduce the volume of student loan placements provided to us, modify the terms of service, including the success fees we are able to earn upon recovery of defaulted student loans, or any of these clients establish more favorable relationships with our competitors. For example, effective July 1, 2015, the Department of Education implemented a fixed fee of \$1,710 payable for each loan that is rehabilitated in place of a recovery fee that historically had been based on a percentage of the balance of the rehabilitated loan. Further, in December 2016, the Department of Education announced the award of seven new contracts and we did not receive one of the new awards. While we have filed a protest on these contracting decisions, there is no assurance that our protest will be upheld. If we are not successful in obtaining a contract award from the Department of Education through this process, the volume of student loan placements to us will be significantly harmed, which will result in a material negative impact on our results of operations and cash flows and our ability to repay or refinance our indebtedness.

Our ability to derive revenues under our new RAC contracts will depend in part on the number and types of potentially improper claims that we are allowed to pursue by CMS, and our results of operations may be harmed if the scope of claims that we are allowed to pursue and be compensated for is limited.

Under CMS's Medicare recovery audit program, RAC contractors have not been permitted to seek the recovery of an improper claim unless that particular type of claim has been pre-approved by CMS to ensure compliance with applicable Medicare payment policies, as well as national and local coverage determinations. As work under the first RAC contract progressed, CMS placed increasing restrictions on the scope of audits permitted by RAC contractors and has not indicated that those restrictions will be relaxed when work commences under the newly awarded RAC contracts. Accordingly, the long-term growth of the revenues we derive under our two newly awarded RAC contracts will also depend in significant part on the scope of potentially improper claims that we are allowed to pursue.

In particular, in September 2013, CMS implemented rules that prevent RAC contractors from being able to review and audit (i) whether inpatient care delivered to patients with hospital stays lasting less than two midnights was medically necessary and therefore deserving of the higher reimbursement levels under Medicare Part A or (ii) whether inpatient treatment was medically necessary for admissions spanning more than two midnights. In connection with these restrictions, hospitals cannot bill CMS for outpatient services on hospital stays lasting less than two midnights during such period. Fees associated with recoveries initiated by us based upon improper claims for inpatient reimbursement of these short stays had represented a substantial portion of the revenues we have earned under our RAC contract. The continued suspension of this type of review

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activity has had and may continue to have a material adverse effect on our future healthcare revenues and operating results, depending on a variety of factors including, among other things, CMS's evaluation of provider compliance with the new rules, the rules ultimately adopted by CMS with respect to medical necessity reviews of Medicare reimbursement claims associated with short stay inpatient admissions and, more generally, the scope of improper claims that CMS allows us to pursue and our ability to successfully identify improper claims within the permitted scope.

We face significant competition in connection with obtaining, retaining and performing under our client contracts, and an inability to compete effectively in the future could harm our relationships with our clients, which would impact our ability to maintain our revenues and operating results.

We operate in very competitive markets. In providing our services to the student loan and other receivables markets, we face competition from many other companies. Initially, we compete with these companies to be one of typically several firms engaged to provide recovery services to a particular client and, if we are successful in being engaged, we then face continuing competition from the client's other retained firms based on the client's benchmarking of the recovery rates of its several vendors. In addition, those recovery vendors who produce the highest recovery rates from a client often will be allocated additional placements and in some cases additional success fees. Accordingly, maintaining high levels of recovery performance, and doing so in a cost-effective manner, are important factors in our ability to maintain and grow our revenues and net income and the failure to achieve these objectives could harm our business, financial condition and results of operations. Some of our current and potential competitors in the markets in which we operate may have greater financial, marketing, technological or other resources than we do. The ability of any of our competitors and potential competitors to adopt new and effective technology to better serve our markets may allow them to gain market strength. Increasing levels of competition in the future may result in lower recovery fees, lower volumes of contracted recovery services or higher costs for resources. Any inability to compete effectively in the markets that we serve could adversely affect our business, financial condition and results of operations.

The U.S. federal government accounts for a significant portion of our revenues, and any loss of business from, or change in our relationship with, the U.S. federal government would result in a significant decrease in our revenues and operating results.

We have historically derived and are likely to continue to derive a significant portion of our revenues from the U.S. federal government. For the year ended December 31, 2016, revenues under contracts with the U.S. federal government accounted for approximately 24% of our total revenues. The continuation and exercise of renewal options on government contracts and any new government contracts are, among other things, contingent upon the availability of adequate funding for the applicable federal government agency. Changes in federal government spending could directly affect our financial performance.

For example, the Bipartisan Budget Act of 2013 reduced the compensation paid to GAs for the rehabilitation of student loans, effective July 1, 2014. This "revenue enhancement" measure reduced from 18.5% to 16.0% of the outstanding loan balance, the amount that GAs can charge borrowers when a rehabilitated loan is sold by the GA and eliminated entirely the GAs retention of 18.5% of the outstanding loan balance as a fee for rehabilitation services. The reduction in compensation the GAs receive resulted in a decrease of approximately 25.0% in the contingency fee percentage that we receive from the GAs for assisting in the rehabilitation of defaulted student loans. The loss of business from the U.S. federal government, or significant policy changes or financial pressures within the agencies of the U.S. federal government that we serve would result in a significant decrease in our revenues, which would adversely affect our business, financial condition and results of operations.

Future legislative or regulatory changes affecting the markets in which we operate could impair our business and operations.

The two principal markets in which we provide our recovery services, government-supported student loans and the Medicare program, are a subject of significant legislative and regulatory focus and we cannot anticipate how future changes in government policy may affect our business and operations. For example, SAFRA significantly changed the structure of the government-supported student loan market by assigning responsibility for all new government-supported student loan originations to the Department of Education, rather than originations by private institutions and backed by one of 30 government-supported GAs. This legislation, and any future changes in the

legislation and regulations that govern these markets, may require us to adapt our business to the new circumstances and we may be unable to do so in a manner that does not adversely affect our business and operations.

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We could lose clients as a result of consolidation among the GAs, which would decrease our revenues. As a result of SAFRA, which terminated the ability of the GAs to originate government-supported student loans, some have speculated that there may be consolidation among the remaining GAs. This speculation has heightened as a result of the reduction of fees that the GAs will receive for rehabilitating student loans as a result of the Bipartisan Budget Act of 2013. If GAs that are our clients are combined with GAs with whom we do not have a relationship, we could suffer a loss of business. Two of our GA clients were each responsible for more than 10% of our total revenues in the year ended December 31, 2016: Great Lakes Higher Education Guaranty Corporation and Pennsylvania Higher Education Assistance Authority were responsible for 24% and 16%, respectively, of revenues for the year ended December 31, 2016. The consolidation of our GA clients with others and the failure to provide recovery services to the consolidated entity could decrease our revenues, which could negatively impact our business, financial condition and results of operations.

Our results of operations may fluctuate on a quarterly or annual basis and cause volatility in the price of our stock. Our revenues and operating results could vary significantly from period-to-period and may fail to match our past performance because of a variety of factors, some of which are outside of our control. Any of these factors could cause the price of our common stock to fluctuate. Factors that could contribute to the variability of our operating results include:

- the amount of defaulted student loans and other receivables that our clients place with us for recovery;
- the timing of placements of student loans and other receivables which are entirely in the discretion of our clients;
- the schedules of government agencies for awarding contracts including the result of our protest against the Department of Education's contract award decision;
- our ability to successfully identify improper Medicare claims and the number and type of potentially improper claims that CMS authorizes us to pursue under our RAC contract;
- the loss or gain of significant clients or changes in the contingency fee rates or other significant terms of our business arrangements with our significant clients;
- technological and operational issues that may affect our clients and regulatory changes in the markets we service; and
- general industry and macroeconomic conditions.

Downturns in domestic or global economic conditions and other macroeconomic factors could harm our business and results of operations.

Various macroeconomic factors influence our business and results of operations. These include the volume of student loan originations in the United States, together with tuition costs and student enrollment rates, the default rate of student loan borrowers, which is impacted by domestic and global economic conditions, rates of unemployment and similar factors, and the growth in Medicare expenditures resulting from changes in healthcare costs. For example, during the global financial crisis beginning in 2008, the market for securitized student loan portfolios was disrupted, resulting in delays in the ability of some GA clients to resell rehabilitated student loans and, as a result, delays our ability to recognize revenues from these rehabilitated loans. Changes in the overall economy could lead to a reduction in overall recovery rates by our clients, which in turn could adversely affect our business, financial condition and results of operations.

We may not be able to manage our potential growth effectively and our results of operations could be negatively affected.

Our newly awarded RAC contracts provide the potential opportunity to restore the growth in our business. However, our focus on growth and the expansion of our business may place additional demands on our management, operations and financial resources and will require us to incur additional expenses. We cannot be sure that we will be able to manage our performance under any significant new contracts effectively. In order to successfully perform under any significant new contracts, our expenses will increase to recruit, train and manage additional qualified employees and subcontractors and to expand and enhance our administrative infrastructure and continue to improve our management, financial and information systems and controls. If we cannot manage our growth effectively, our expenses may increase and our results of operations could be negatively affected.





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A failure of our operating systems or technology infrastructure, or those of our third-party vendors and subcontractors, could disrupt the operation of our business.

A failure of our operating systems or technology infrastructure, or those of our third-party vendors and subcontractors, could disrupt our operations. Our operating systems and technology infrastructure are susceptible to damage or interruption from various causes, including acts of God and other natural disasters, power losses, computer systems failures, Internet and telecommunications or data network failures, operator error, computer viruses, losses of and corruption of data and similar events. The occurrence of any of these events could result in interruptions, delays or cessations in service to our clients, reduce the attractiveness of our recovery services to current or potential clients and adversely impact our financial condition and results of operations. While we have backup systems in many of our operating facilities, an extended outage of utility or network services may harm our ability to operate our business. Further, the situations we plan for and the amount of insurance coverage we maintain for losses as result of failures of our operating systems and infrastructure may not be adequate in any particular case.

If our security measures are breached or fail and unauthorized access is obtained to our clients' confidential data, our services may be perceived as insecure, the attractiveness of our recovery services to current or potential clients may be reduced, and we may incur significant liabilities.

Our recovery services involve the storage and transmission of confidential information relating to our clients and their customers, including health, financial, credit, payment and other personal or confidential information. Although our data security procedures are designed to protect against unauthorized access to confidential information, our computer systems, software and networks may be vulnerable to unauthorized access and disclosure of our clients' confidential information. Further, we may not effectively adapt our security measures to evolving security risks, address the security and privacy concerns of existing or potential clients as they change over time, or be compliant with federal, state, and local laws and regulations with respect to securing confidential information. Unauthorized access to confidential information relating to our clients and their customers could lead to reputational damage which could deter our clients and potential clients from selecting our recovery services, or result in termination of contracts with those clients affected by any such breach, regulatory action, and claims against us.

In the event of any unauthorized access to personal or other confidential information, we may be required to expend significant resources to investigate and remediate vulnerabilities in our security procedures, and we may be subject to fines, penalties, litigation costs, and financial losses that are either not insured against or not fully covered through any insurance maintained by us. If one or more of such failures in our security and privacy measures were to occur, our business, financial condition and results of operations could suffer.

Our business may be harmed if we lose members of our management team or other key employees.

We are highly dependent on members of our management team and other key employees and our future success depends in part on our ability to retain these people. Our inability to continue to attract and retain members of our management team and other key employees could adversely affect our business, financial condition and results of operations.

The growth of our healthcare business will require us to hire and retain employees with specialized skills and failure to do so could harm our ability to grow our business.

The growth of our healthcare business will depend in part on our ability to recruit, train and manage additional qualified employees. Our healthcare-related operations require us to hire registered nurses and experts in Medicare coding. Finding, attracting and retaining employees with these skills is a critical component of providing our healthcare-related recovery and audit services, and our inability to staff these operations appropriately represents a risk to our healthcare service offering and associated revenues. An inability to hire qualified personnel, particularly to serve our healthcare clients, may restrain the growth of our business.

We rely on subcontractors to provide services to our clients and the failure of subcontractors to perform as expected could harm our business operations and our relationships with our clients.

We engage subcontractors to provide certain services to our clients. These subcontractors participate to varying degrees in our recovery activities with regards to all of the services we provide. While we believe that we perform appropriate due diligence before we hire subcontractors, our subcontractors may not provide adequate service or otherwise comply with the terms set forth in their agreements. In the event a subcontractor provides deficient

performance to one or more of our clients, any such client may reduce the volume of services we are providing under an existing contract or may terminate the relevant

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contract entirely and we may face claims for breach of contract. Any such disruption in our relations with our clients as a result of services provided by any of our subcontractors could adversely affect our revenues and operating results. If our software vendors or utility and network providers fail to deliver or perform as expected our business operations could be adversely affected.

Our recovery services depend in part on third-party providers, including software vendors and utility and network providers. Our ability to service our clients depends on these third-party providers meeting our expectations and contractual obligations in a timely and effective manner. Our business could be materially and adversely affected, and we might incur significant additional liabilities, if the services provided by these third-party providers do not meet our expectations or if they terminate or refuse to renew their relationships with us on similar contractual terms.

We are subject to extensive regulations regarding the use and disclosure of confidential personal information and failure to comply with these regulations could cause us to incur liabilities and expenses.

We are subject to a wide array of federal and state laws and regulations regarding the use and disclosure of confidential personal information and security. For example, the federal Health Insurance Portability and Accountability Act of 1996, as amended, or HIPAA, and related state laws subject us to substantial restrictions and requirements with respect to the use and disclosure of the personal health information that we obtain in connection with our audit and recovery services under our contract with CMS and we must establish administrative, physical and technical safeguards to protect the confidentiality of this information. Similar protections extend to the type of personal financial and other information we acquire from our student loan, state tax and federal receivables clients.

We are required to notify affected individuals and government agencies of data security breaches involving protected health and certain personally identifiable information. These laws and regulations also require that we develop, implement and maintain written, comprehensive information security programs containing safeguards that are appropriate to protect personally identifiable information or health information against unauthorized access, misuse, destruction or modification. Federal law generally does not preempt state law in the area of protection of personal information, and as a result we must also comply with state laws and regulations. Regulation of privacy, data use and security requires that we incur significant expenses, which could increase in the future as a result of additional regulations, all of which adversely affects our results of operations. Failure to comply with these laws and regulations can result in penalties and in some cases expose us to civil lawsuits.

Our student loan recovery business is subject to extensive regulation and consumer protection laws and our failure to comply with these regulations and laws may subject us to liability and result in significant costs.

Our student loan recovery business is subject to regulation and oversight by various state and federal agencies, particularly in the area of consumer protection. The Fair Debt Collection Practices Act, or FDCPA, and related state laws provide specific guidelines that we must follow in communicating with holders of student loans and regulates the manner in which we can recover defaulted student loans. Some state attorney generals have been active in this area of consumer protection regulation. We are subject, and may be subject in the future, to inquiries and audits from state and federal regulators, as well as frequent litigation from private plaintiffs regarding compliance under the FDCPA and related state regulations. We are also subject to the Fair Credit Reporting Act, or FCRA, which regulates consumer credit reporting and may impose liability on us to the extent adverse credit information reported to a credit bureau is false or inaccurate. Our compliance with the FDCPA, FCRA and other federal and state regulations that affect our student loan recovery business may result in significant costs, including litigation costs. We may also become subject to regulations promulgated by the United States Consumer Financial Protection Bureau, or CFPB, which was established in July 2011 as part of the Dodd-Frank Act to, among other things, establish regulations regarding consumer financial protection laws. In addition, the CFPB has investigatory and enforcement authority with respect to whether persons are engaged in unlawful acts or practices in connection with the collection of consumer debts.

Litigation may result in substantial costs of defense, damages or settlement, any of which could subject us to significant costs and expenses.

We are party to lawsuits in the normal course of business, particularly in connection with our student loan recovery services. For example, we are regularly subject to claims that we have violated the guidelines and procedures that must be followed under federal and state laws in communicating with consumer debtors. We may not ultimately

prevail or otherwise be able to satisfactorily resolve any pending or future litigation, which may result in substantial costs of defense, damages or settlement. In the future, we may be required to alter our business practices or pay substantial damages or settlement costs as a result of litigation proceedings, which could adversely affect our business operations and results of operations.

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We typically face a long period to implement a new contract which may cause us to incur expenses before we receive revenues from new client relationships.

If we are successful in obtaining an engagement with a new client or a new contract with an existing client, we typically have a subsequent long implementation period in which the services are planned in detail and we integrate our technology, processes and resources with the client's operations. If we enter into a contract with a new client, we typically will not receive revenues until implementation is completed and work under the contract actually begins. Our clients may also experience delays in obtaining approvals or delays associated with technology or system implementations, such as the delays experienced with the implementation of our first RAC contract with CMS due to an appeal by competitors who were unsuccessful in bidding on the contract. Because we generally begin to hire new employees to provide services to a new client once a contract is signed, we may incur significant expenses associated with these additional hires before we receive corresponding revenues under any such new contract. If we are not successful in maintaining contractual commitments after the expenses we incur during our typically long implementation cycle, our results of operations could be adversely affected.

If we are unable to adequately protect our proprietary technology, our competitive position could be harmed or we could be required to incur significant costs to enforce our rights.

The success of our business depends in part upon our proprietary technology platform. We rely on a combination of copyright, patent, trademark, and trade secret laws, as well as on confidentiality procedures and non-compete agreements, to establish and protect our proprietary technology rights. The steps we have taken to deter misappropriation of our proprietary technology may be insufficient to protect our proprietary information. In particular, we may not be able to protect our trade secrets, know how and other proprietary information adequately. Although we use reasonable efforts to protect this proprietary information and technology, our employees, consultants and other parties may unintentionally or willfully disclose our information or technology to competitors. Enforcing a claim that a third party illegally obtained and is using any of our proprietary information or technology is expensive and time consuming, and the outcome is unpredictable. We rely, in part, on non disclosure, confidentiality and invention assignment agreements with our employees, consultants and other parties to protect our trade secrets, know how and other intellectual property and proprietary information. These agreements may not be self executing, or they may be breached and we may not have adequate remedies for such breach. Moreover, third parties may independently develop similar or equivalent proprietary information or otherwise gain access to our trade secrets, know how and other proprietary information. Any infringement, misappropriation or other violation of our patents, trademarks, copyrights, trade secrets, or other intellectual property rights could adversely affect any competitive advantage we currently derive or may derive from our proprietary technology platform and we may incur significant costs associated with litigation that may be necessary to enforce our intellectual property rights.

Claims by others that we infringe their intellectual property could force us to incur significant costs or revise the way we conduct our business.

Our competitors protect their proprietary rights by means of patents, trade secrets, copyrights, trademarks and other intellectual property. Any party asserting that we infringe, misappropriate or violate their intellectual property rights may force us to defend ourselves, and potentially our clients, against the alleged claim. These claims and any resulting lawsuit, if successful, could be time-consuming and expensive to defend, subject us to significant liability for damages or invalidation of our proprietary rights, prevent us from operating all or a portion of our business or force us to redesign our services or technology platform or cause an interruption or cessation of our business operations, any of which could adversely affect our business and operating results. In addition, any litigation relating to the infringement of intellectual property rights could harm our relationships with current and prospective clients. The risk of such claims and lawsuits could increase if we increase the size and scope of our services in our existing markets or expand into new markets.

We may make acquisitions that prove unsuccessful, strain or divert our resources and harm our results of operations and stock price.

We may consider acquisitions of other companies in our industry or in new markets. We may not be able to successfully complete any such acquisition and, if completed, any such acquisition may fail to achieve the intended financial results. We may not be able to successfully integrate any acquired businesses with our own and we may be

unable to maintain our standards, controls and policies. Further, acquisitions may place additional constraints on our resources by diverting the attention of our management from other business concerns. Moreover, any acquisition may result in a potentially dilutive issuance of equity securities, the incurrence of additional debt and amortization of expenses related to intangible assets, all of which could adversely affect our results of operations and stock price.

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The price of our common stock could be volatile, and you may not be able to sell your shares at or above the public offering price.

Since our initial public offering in August 2012, the price of our common stock, as reported by NASDAQ Global Select Market, has ranged from a low sales price of \$1.51 on July 7, 2016 to a high sales price of \$14.09 on March 4, 2013. The trading price of our common stock may be significantly affected by various factors, including: quarterly fluctuations in our operating results; the financial projections we may provide to the public, any changes in those projections or our failure to meet those projections; changes in investors' and analysts' perception of the business risks and conditions of our business; our ability to meet the earnings estimates and other performance expectations of financial analysts or investors; unfavorable commentary or downgrades of our stock by equity research analysts; changes in our capital structure, such as future issuances of debt or equity securities; our success or failure to obtain new contract awards; lawsuits threatened or filed against us; strategic actions by us or our competitors, such as acquisitions or restructurings; new legislation or regulatory actions; changes in our relationship with any of our significant clients; fluctuations in the stock prices of our peer companies or in stock markets in general; and general economic conditions.

Our significant stockholders have the ability to influence significant corporate activities and our significant stockholders' interests may not coincide with yours.

Parthenon Capital Partners and Invesco Ltd. beneficially owned approximately 26.9% and 19.1% of our common stock, respectively, as of December 31, 2016. As a result of their ownership, Parthenon Capital Partners and Invesco Ltd. have the ability to influence the outcome of matters submitted to a vote of stockholders and, through our board of directors, the ability to influence decision making with respect to our business direction and policies.

Parthenon Capital Partners and Invesco Ltd. may have interests different from our other stockholders' interests, and may vote in a manner adverse to those interests. Matters over which Parthenon Capital Partners and Invesco Ltd. can, directly or indirectly, exercise influence include:

- mergers and other business combination transactions, including proposed transactions that would result in our stockholders receiving a premium price for their shares;

- other acquisitions or dispositions of businesses or assets;

- incurrence of indebtedness and the issuance of equity securities;

- repurchase of stock and payment of dividends; and

- the issuance of shares to management under our equity incentive plans.

In addition, Parthenon Capital Partners has a contractual right to designate a number of directors proportionate to its stock ownership. Further, under our amended and restated certificate of incorporation, Parthenon Capital Partners does not have any obligation to present to us, and Parthenon Capital Partners may separately pursue, corporate opportunities of which it becomes aware, even if those opportunities are ones that we would have pursued if granted the opportunity.

Anti-takeover provisions contained in our certificate of incorporation and bylaws could impair a takeover attempt that our stockholders may find beneficial.

Our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that could have the effect of rendering more difficult or discouraging an acquisition deemed undesirable by our board of directors. Our corporate governance documents include the following provisions: establishing a classified board of directors so that not all members of our board are elected at one time; providing that directors may be removed by stockholders only for cause; authorizing blank check preferred stock, which could be issued with voting, liquidation, dividend and other rights superior to our common stock; limiting the ability of our stockholders to call and bring business before special meetings and to take action by written consent in lieu of a meeting; limiting our ability to engage in certain business combinations with any "interested stockholder," other than Parthenon Capital Partners, for a three-year period following the time that the stockholder became an interested stockholder; requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors; requiring a super majority vote for certain amendments to our amended and restated certificate of incorporation and amended and restated bylaws; and limiting the determination of the number of directors on our board of directors and the filling of vacancies or newly created seats on the board, to

our board of directors then in office. These provisions, alone or together, could have the effect of delaying or deterring a change in control, could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.



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ITEM 1B. Unresolved Staff Comments

None.

ITEM 2. Properties

Facilities

As of December 31, 2016, we operated six separate office locations throughout the United States. The largest of these facilities is in Livermore, California and serves as our corporate headquarters, as well as a data center and production location. Our Livermore facility is comprised of approximately 50,291 square feet of space and has a lease expiration of September 2017 with an option for a five year extension of the lease. We also lease production centers in California, Oregon, Florida and Texas and own a production/data center in Oregon.

We believe that our facilities are adequate for current operations and that additional space will be available as required. See note (5) to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for information regarding our lease obligations.

ITEM 3. Legal Proceedings

We are involved in various legal proceedings that arise from our normal business operations. These actions generally derive from our student loan recovery services, and generally assert claims for violations of the Fair Debt Collection Practices Act or similar federal and state consumer credit laws. While litigation is inherently unpredictable, we believe that none of these legal proceedings, individually or collectively, will have a material adverse effect on our financial condition or our results of operations.

ITEM 4. Mine Safety Disclosures

Not applicable.

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PART II

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

Market For Our Common Equity

Our common stock began trading on the NASDAQ Global Select Market under the symbol “PFMT” on August 10, 2012. Prior to that, there was no public market for our common stock. The table sets forth, for the periods indicated below, the high and low sales prices per share of our common stock as reported by NASDAQ.

2015	High	Low
First Quarter	6.69	3.28
Second Quarter	3.67	2.33
Third Quarter	3.39	2.26
Fourth Quarter	3.29	1.65
2016		
First Quarter	1.95	1.51
Second Quarter	1.95	1.51
Third Quarter	3.46	1.51
Fourth Quarter	4.07	1.94

On March 10, 2017, the closing price as reported by NASDAQ of our common stock was \$1.58 per share.

Stockholders

As of December 31, 2016, we had approximately 15 holders of record of our common stock.

Dividends

Our board of directors does not currently intend to pay regular dividends on our common stock. Our credit agreement contains a covenant prohibiting the payment of cash dividends.

Securities Authorized for Issuance Under Equity Compensation Plans

Information regarding the securities authorized for issuance under our equity compensation plans can be found under Item 12 of this Annual Report on Form 10-K.

Issuer Purchases of Equity Securities

None.

ITEM 6. Selected Financial Data

The selected consolidated balance sheet data as of December 31, 2016 and 2015, and the selected consolidated statements of operations data for each year ended December 31, 2016, 2015 and 2014, have been derived from our audited consolidated financial statements which are included elsewhere in this annual report. The selected consolidated balance sheet data as of December 31, 2013 and 2012, and the selected consolidated statements of operations data for the years ended December 31, 2013 and 2012 have been derived from our audited consolidated financial statements not included in this annual report. Historical results are not necessarily indicative of future results. You should read the following selected consolidated historical financial data below in conjunction with the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the consolidated financial statements, related notes, and other financial information included in this Annual Report on Form 10-K. The selected consolidated financial data in this section is not intended to replace the consolidated financial statements and is qualified in its entirety by the consolidated financial statements and related notes and schedule included in this Annual Report on Form 10-K.

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	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Consolidated Statement of Operations Data:					
Revenues	\$ 141,360	\$ 159,381	\$ 195,378	\$ 255,302	\$ 210,073
Operating expenses:					
Salaries and benefits	78,863	88,077	93,676	96,762	83,002
Other operating expense	54,985	64,360	74,433	85,671	71,305
Impairment of customer relationship	15,438	236	—	—	—
Total operating expenses	149,286	152,673	168,109	182,433	154,307
Income from operations	(7,926 )	6,708	27,269	72,869	55,766
Debt extinguishment costs <sup>(1)</sup>	—	—	—	—	(3,679 )
Interest expense	(7,897 )	(8,889 )	(10,171 )	(11,564 )	(12,414 )
Interest income	—	—	1	1	64
Income (loss) before provision for income taxes	(15,823 )	(2,181 )	17,099	61,306	39,737
Provision for (benefit from) income taxes	(4,370 )	(386 )	7,699	24,967	16,786
Net income (loss)	(11,453 )	(1,795 )	9,400	36,339	22,951
Accrual for preferred stock dividends	—	—	—	—	2,038
Net income (loss) available to common shareholders	\$(11,453 )	\$(1,795 )	\$9,400	\$36,339	\$20,913
Net income (loss) per share attributable to common shareholders <sup>(2)</sup>					
Basic	\$(0.23 )	\$(0.04 )	\$0.19	\$0.77	\$0.48
Diluted	\$(0.23 )	\$(0.04 )	\$0.19	\$0.74	\$0.44
Weighted average shares (in thousands)					
Basic	50,038	49,415	48,816	47,492	43,985
Diluted	50,038	49,415	49,834	49,386	47,599

Represents debt extinguishment costs comprised of approximately \$3.3 million of fees paid to lenders in (1) connection with our new credit facility and approximately \$0.3 million of unamortized debt issuance costs in connection with our old credit facility.

(2) Please see Note 1 to our consolidated financial statements for an explanation of the calculations of our basic and diluted net income per share of common stock.

	As of December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Consolidated Balance Sheet Data:					
Cash and cash equivalents	\$32,982	\$71,182	\$80,298	\$81,909	\$37,843
Total assets	185,078	244,656	262,829	257,260	211,745
Total debt	55,182	94,258	111,795	133,304	147,769
Total liabilities	98,833	150,800	171,657	183,026	187,672
Total stockholders' equity	86,245	93,856	91,172	74,234	24,073

## ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

## Overview

We provide technology-enabled recovery and related analytics services in the United States. Our services help identify and recover delinquent or defaulted assets and improper payments for both government and private clients in a broad range of markets. Our clients typically operate in complex and regulated environments and outsource their recovery needs in order to reduce losses on billions of dollars of defaulted student loans, improper healthcare payments and delinquent state tax and



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federal treasury and other receivables. We generally provide our services on an outsourced basis, where we handle many or all aspects of our clients' recovery processes.

Our revenue model is generally success-based as we earn fees on the aggregate amount of funds that we enable our clients to recover. Our services do not require any significant upfront investments by our clients and offer our clients the opportunity to recover significant funds otherwise lost. Because our model is based upon the success of our efforts and the dollars we enable our clients to recover, our business objectives are aligned with those of our clients and we are generally not reliant on their spending budgets. Furthermore, our business model does not require significant capital expenditures and we do not purchase loans or obligations.

**Sources of Revenues**

We derive our revenues from services for clients in a variety of different markets. These markets include our two largest markets, student lending and healthcare, as well as our other markets which include but are not limited to delinquent state taxes and federal Treasury and other receivables.

	Year Ended December 31,		
	2016	2015	2014
	(in thousands)		
<b>Student Lending:</b>			
Department of Education	\$21,949	\$37,878	\$53,211
Guaranty Agencies & Other	87,616	81,518	85,064
Total of Student Lending	109,565	119,396	138,275
<b>Healthcare:</b>			
CMS RAC	5,733	12,490	29,173
Commercial	5,662	7,424	3,353
Total of Healthcare	11,395	19,914	32,526
Other	20,400	20,071	24,577
<b>Total Revenues</b>	<b>\$141,360</b>	<b>\$159,381</b>	<b>\$195,378</b>

**Student Lending**

We derive the majority of our revenues from the recovery of student loans. These revenues are contract-based and consist primarily of contingency fees based on a specified percentage of the amount we enable our clients to recover. Our contingency fee percentage for a particular recovery depends on the type of recovery facilitated. Our clients in the student loan recovery market mainly consist of several of the largest guaranty agencies, or GAs. In addition, we have a long history of also providing recovery services to the Department of Education. However, in December 2016, the Department of Education awarded contracts for student loan recovery services to seven contractors and we were not a recipient of one of these contract awards. We, along with 19 other contractors who did not receive contract awards from the Department of Education, have filed protests with the GAO regarding the Department of Education's award of these contracts. The outcome of our protest is pending, with a decision expected in April 2017.

We believe the size and the composition of our student loan inventory at any point provides us with a significant degree of revenue visibility for our student loan revenues. Based on data compiled from over two decades of experience with the recovery of defaulted student loans, at the time we receive a placement of student loans, we are able to make a reasonably accurate estimate of the recovery outcomes likely to be derived from such placement and the revenues we are likely able to generate based on the anticipated recovery outcomes.

Our key metric in evaluating our student lending business is Placement Volume. Our Placement Volume represents the dollar volume of defaulted student loans first placed with us during the specified period by public and private clients for recovery. Placement Volume allows us to measure and track trends in the amount of inventory our clients in the student lending market are placing with us during any period. The revenues associated with the recovery of a portion of these loans may be recognized in subsequent accounting periods, which assists management in estimating future revenues and in allocating resources necessary to address current Placement Volumes.

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Year Ended December 31,  
2016      2015      2014  
(in thousands)

## Student Lending Placement Volume:

Department of Education	\$5,082	\$1,549,595	\$2,543,606
Guaranty Agencies and Other	3,168,840	3,765,049	4,135,797

Total Student Lending Placement Volume	\$3,173,922	\$5,314,644	\$6,679,403
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There are five potential outcomes to the student loan recovery process from which we generate revenues. These outcomes include: full repayment, recurring payments, rehabilitation, loan restructuring and wage garnishment. Of these five potential outcomes, our ability to rehabilitate defaulted student loans is the most significant component of our revenues in this market. Generally, a loan is considered successfully rehabilitated after the student loan borrower has made nine consecutive qualifying monthly payments and our client has notified us that it is recalling the loan. Once we have structured and implemented a repayment program for a defaulted borrower, we (i) earn a percentage of each periodic payment collected up to and including the final periodic payment prior to the loan being considered “rehabilitated” by our clients, and (ii) if the loan is “rehabilitated,” then we are paid a one-time percentage of the total amount of the remaining unpaid balance or in the case of our work for the Department of Education, a fixed fee of \$1,710 for each rehabilitated loan. The fees we are paid vary by recovery outcome as well as by contract. For non-government-supported student loans we are generally only paid contingency fees on two outcomes: full repayment or recurring repayments. The table below describes our typical fee structure for each of these five outcomes.

## Student Loan Recovery Outcomes

Full Repayment	Recurring Payments	Rehabilitation	Loan Restructuring	Wage Garnishment
<ul style="list-style-type: none"> <li>• Repayment in full of the loan</li> </ul>	<ul style="list-style-type: none"> <li>• Regular structured payments, typically according to a renegotiated payment plan</li> </ul>	<ul style="list-style-type: none"> <li>• After a defaulted borrower has made nine consecutive recurring payments, the loan is eligible for rehabilitation</li> </ul>	<ul style="list-style-type: none"> <li>• Restructure and consolidate a number of outstanding loans into a single loan, typically with one monthly payment and an extended maturity</li> </ul>	<ul style="list-style-type: none"> <li>• If we are unable to obtain voluntary repayment, payments may be obtained through wage garnishment after certain administrative requirements are met</li> </ul>
<ul style="list-style-type: none"> <li>• We are paid a percentage of the full payment that is made</li> </ul>	<ul style="list-style-type: none"> <li>• We are paid a percentage of each payment</li> </ul>	<ul style="list-style-type: none"> <li>• We are paid based on a percentage of the overall value of the rehabilitated loan or for the Department of Education, a fixed fee</li> </ul>	<ul style="list-style-type: none"> <li>• We are paid based on a percentage of overall value of the restructured loan</li> </ul>	<ul style="list-style-type: none"> <li>• We are paid a percentage of each payment</li> </ul>

For certain guaranty agency, or GA, clients, we have entered into Master Service Agreements, or MSAs. Under these agreements, clients provide their entire inventory of outsourced loans or receivables to us for recovery on an exclusive basis, rather than just a portion, as with traditional contracts that are split among various service providers. In certain circumstances, we engage subcontractors to assist in the recovery of a portion of the client’s portfolio. We also receive success fees for the recovery of loans under MSAs and our revenues under MSA arrangements include fees earned by the activities of our subcontractors. As of December 31, 2016, we had three MSA clients in the student loan market.

In October 2014, the Department of Education announced a change in the structure for the payment of fees to recovery contractors upon rehabilitation of student loans under the existing recovery contract. The new fee structure provides for a fixed fee of \$1,710 for each loan that is rehabilitated. Previously, the fee had been based on a percentage of the principal amount of the rehabilitated loan. The change to the fee structure became effective for student loans that were rehabilitated on or following July 1, 2015.

Further, the Bipartisan Budget Act of 2013, which was signed into law by President Obama on December 26, 2013, reduced the compensation paid to GAs for the rehabilitation of student loans, effective July 1, 2014. This “revenue enhancement” measure reduced from 18.5% to 16.0% of the outstanding loan balance, the amount that GAs can charge borrowers when a rehabilitated loan is sold by the GA and eliminated entirely the GAs retention of 18.5% of the outstanding loan balance as a fee for rehabilitation services. The reduction in compensation the GAs receive resulted in a decrease in the contingency fee percentage that we receive from the GAs for assisting in the rehabilitation of defaulted student loans.

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As a result of the fee reductions from the Department of Education and the GAs discussed above, our revenues from student lending in 2015 were approximately 14% lower than in 2014. Our revenues from student lending were approximately 8% lower in 2016 compared to 2015 as a result of the expiration of our contract with the Department of Education in April 2015 and because the revenues associated with placements received prior to such contract expiration have been tailing off as we have worked through this inventory. Revenues from the Department of Education fell by approximately 42% in 2016, although this decrease was partially offset by an approximately 7% increase in revenues from GAs and other student lending clients.

Healthcare

We derive revenues from the healthcare market primarily from our RAC contracts, under which we are responsible for detecting improperly paid Part A and Part B Medicare claims. Revenues earned under the RAC contracts are driven by the identification of improperly paid Medicare claims through both automated and manual review of such claims. We are paid contingency fees by CMS based on a percentage of the dollar amount of claims recovered by CMS as a result of our efforts. We recognize revenue when the provider pays CMS or incurs an offset against future Medicare claims. The revenues we recognize are net of our estimate of claims that will be overturned by appeal following payment by the provider.

Our first RAC contract was wound down and then terminated in 2016 in connection with CMS's plan to award new contracts. On October 26, 2016, CMS awarded new RAC contracts and we received RAC contracts for audit Regions 1 and 5. The RAC contract award for Region 1 allows us to continue our audit of payments under Medicare's Part A and Part B for all provider types other than DMEPOS and home health and hospice within an 11 state region in the Northeast and Midwest. The Region 5 RAC contract provides for the post-payment review of DMEPOS and home health and hospice claims nationally. While the new RAC contracts have been awarded, the Company does not expect audit and recovery services under the new contracts to begin before April 2017. There is also uncertainty regarding the scope of audit that will be permitted by CMS under the new RAC contracts. In connection with the wind down of our first RAC contract, CMS adopted a series of contract transition procedures and other restrictions, beginning in 2013, that limited the types of claims we are permitted to audit and our ability to request medical records for audit and CMS suspended our ability to perform any audit services for certain periods of time, thus materially adversely affecting our revenues under that contract. In May 2016, CMS announced that the recovery audit contractors would not be able to request documents from providers for audit after May 16, 2016 and would not be able to submit claims for improper payments after July 29, 2016, effectively terminating additional revenue generating activity under our first RAC contract. Revenues for the year ended December 31, 2016 from our first RAC contract were \$5.7 million, compared with \$12.5 million for 2015 and \$29.2 million in 2014. We do not expect to recognize significant revenues from the newly awarded RAC contracts for four to six months after we are permitted to begin performing recovery services under the new RAC contracts. Accordingly, the currently expected start date of April 2017 for the new RAC contracts means that these new contracts will not have a significant impact on 2017 revenues, although we will incur related start-up expenses in 2017.

In connection with our first RAC contract, CMS announced a settlement offer to pay hospitals 68% of what they have billed Medicare to settle a backlog of pending appeals challenging Medicare's denials of reimbursement for certain types of short-term care. The implication of this settlement offer related to claims for which fees have already been paid to recovery auditors under existing RAC contracts is unclear at this time, but we may be obligated to repay certain amounts that we previously received from CMS depending on the final terms of any such settlement. We accrue an estimated liability for appeals based on the amount of commissions received which are subject to appeal and which we estimate are probable of being returned to providers following successful appeal. The \$19.0 million balance as of December 31, 2016, represents our best estimate of the probable amount of we may be required to refund related to appeals of claims for which commissions were previously collected. We estimate that it is reasonably possible that we could be required to pay an additional amount up to approximately \$5.4 million as a result of potentially successful appeals in excess of the amount we accrued as of December 31, 2016.

In connection with the award of our first RAC contract, we outsourced certain aspects of our healthcare recovery process to three different subcontractors. Two of these subcontractors provided a specific service to us in connection with our claims recovery process, with the third subcontractor, whose services were terminated in December 2016,



formerly providing all of the audit and recovery services for claims within a portion of our region. We recognize all of the revenues generated by the claims recovered through our subcontractor relationships, and we recognize the fees that we pay to these subcontractors in our expenses.

For our commercial healthcare business, our business strategy is focused on utilizing our technology-enabled services platform to provide audit, recovery and analytical services for private healthcare payors. We have entered into contracts with several private payors, although these contracts are in the early stage of implementation. Revenues from our commercial healthcare clients were \$5.7 million for 2016, compared to revenues of \$7.4 million that we earned from our commercial healthcare clients in 2015.

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### Other

We also derive revenues from the recovery of delinquent state taxes, and federal Treasury and other receivables, default aversion services for certain clients including financial institutions and the licensing of hosted technology solutions to certain clients. For our hosted technology services, we license our system and integrate our technology into our clients' operations, for which we are paid a licensing fee. Our revenues for these services include contingency fees, fees based on dedicated headcount to our clients and hosted technology licensing fees.

### Costs and Expenses

We generally report two categories of operating expenses: salaries and benefits and other operating expense. Salaries and benefits expenses consist primarily of salaries and performance incentives paid and benefits provided to our employees. Other operating expense includes expenses related to our use of subcontractors, other production related expenses, including costs associated with data processing, retrieval of medical records, printing and mailing services, amortization and other outside services, as well as general corporate and administrative expenses. We expect a significant portion of our expenses to increase as we grow our business. However, we expect certain expenses, including our corporate and general administrative expenses, to grow at a slower rate than our revenues. As a result, and over the long term, we expect our overall expenses to modestly decline as a percentage of revenues.

### Factors Affecting Our Operating Results

Our results of operations are influenced by a number of factors, including allocation of placement volume, claim recovery volume, contingency fees, regulatory matters, client retention and macroeconomic factors.

### Allocation of Placement Volume

Our clients have the right to unilaterally set and increase or reduce the volume of defaulted student loans or other receivables that we service at any given time. In addition, many of our recovery contracts for student loans and other receivables are not exclusive, with our clients retaining multiple service providers to service portions of their portfolios. Accordingly, the number of delinquent student loans or other receivables that are placed with us may vary from time to time, which may have a significant effect on the amount and timing of our revenues. We believe the major factors that influence the number of placements we receive from our clients in the student loan market include our performance under our existing contracts and our ability to perform well against competitors for a particular client. To the extent that we perform well under our existing contracts and differentiate our services from those of our competitors, we may receive a relatively greater number of placements under these existing contracts and may improve our ability to obtain future contracts from these clients and other potential clients. Further, delays in placement volume, as well as acceleration of placement volume, from any of our large clients may cause our revenues and operating results to vary from quarter to quarter.

Typically we are able to anticipate with reasonable accuracy the timing and volume of placements of defaulted student loans and other receivables based on historical patterns and regular communication with our clients. Occasionally, however, placements are delayed due to factors outside of our control.

### Contingency Fees

Our revenues consist primarily of contract-based contingency fees. The contingency fee percentages that we earn are set by our clients or agreed upon during the bid process, and may change from time to time either under the terms of existing contracts or pursuant to the terms of contract renewals. For example, the fees that we earned under our contractual arrangement with the Department of Education were subject to unilateral change by the Department of Education as a result of the Department of Education's decision to have its recovery vendors promote IBR to defaulted student loans. In connection with the implementation of the IBR program, the Department of Education reduced the contingency fee rate that we receive for rehabilitating student loans by approximately 13% effective March 1, 2013. Further, the Department of Education changed its fee structure to a fixed recovery fee of \$1,710 for each rehabilitated loan, effective as of July 1, 2015. The fixed recovery fee is payable for each loan that is rehabilitated and replaced a recovery fee structure that historically had been based on a percentage of the balance of the rehabilitated loan.

### Regulatory Matters

Each of the markets which we serve is highly regulated. Accordingly, changes in regulations that affect the types of loans, receivables and claims that we are able to service or the manner in which any such delinquent loans, receivables and claims can be recovered will affect our revenues and results of operations. For example, the passage of the

Student Aid and Fiscal Responsibility Act, or SAFRA, in 2010 had the effect of transferring the origination of all government-supported student

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loans to the Department of Education, thereby ending all student loan originations guaranteed by the GAs. Loans guaranteed by the GAs represented approximately 70% of government-supported student loans originated in 2009. While the GAs will continue to service existing outstanding student loans for years to come, this legislation will over time shift the portfolio of defaulted student loans toward the Department of Education for which we are no longer a contractor (subject to our pending protest). In addition, our entry into the healthcare market was facilitated by passage of the Tax Relief and Health Care Act of 2006, which mandated CMS to contract with private firms to audit Medicare claims in an effort to increase the recovery of improper Medicare payments. Any changes to the regulations that affect the student loan industry or the recovery of defaulted student loans or the Medicare program generally or the audit and recovery of Medicare claims could have a significant impact on our revenues and results of operations.

### Client Retention

Our revenues from the student loan market depend on our ability to maintain our contracts with some of the largest providers of student loans. In 2016 and 2015, three providers of student loans each accounted for more than 10% of our revenues and they collectively accounted for 55% of our total revenues in each year. Our contract with the Department of Education, which generated 16% of our revenues in 2016, expired in April 2015 and we were not selected as a vendor on the new contract announced in December 2016. If we are not successful in obtaining a new contract as a result of a pending appeal, the absence of a contract with the Department of Education will have a material adverse effect on our financial condition and results of operations in 2017 and beyond. Our contracts with our other large clients entitle them to unilaterally terminate their contractual relationship with us at any time without penalty. If we lose one of our other significant clients, including if one of our significant clients is consolidated by an entity that does not use our services, if the terms of compensation for our services change or if there is a reduction in the level of placements provided by any of these clients, our revenues could decline.

The award of our two new RAC contracts in October 2016 has removed the uncertainty related to the retention of our relationship with CMS, although the start date for work under these contracts and the scope of our permitted audit activity remain uncertain. We do not expect to recognize significant revenue under our newly awarded RAC contracts for four to six months after we are permitted to begin performing recovery services under the new RAC contracts which we expect will commence in April 2017.

### Macroeconomic Factors

Certain macroeconomic factors influence our business and results of operations. These include the increasing volume of student loan originations in the U.S. as a result of increased tuition costs and student enrollment, the default rate of student loan borrowers, the growth in Medicare expenditures resulting from increasing healthcare costs, as well as the fiscal budget tightening of federal, state and local governments as a result of general economic weakness and lower tax revenues.

### Critical Accounting Policies

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States, or GAAP. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period-to-period. Accordingly, actual results could differ significantly from the estimates made by our management. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected. We believe that the accounting policies discussed below are critical to understanding our historical and future performance, as these policies relate to the more significant areas involving management's judgments and estimates.

### Revenue Recognition

The majority of our contracts are contingency fee based. We recognize revenues on these contingency fee based contracts when third-party payors remit payments to our clients or remit payments to us on behalf of our clients, and, consequently, the contingency is deemed to have been satisfied. Under our RAC contracts with CMS, we recognize revenues when the healthcare provider has paid CMS for a claim or has agreed to an offset against other claims by the

provider. Healthcare providers have the right to appeal a claim and may pursue additional level of appeals if the initial appeal is found in favor of CMS. We accrue an estimated liability for appeals at the time revenue is recognized based on our estimate of the amount of revenue probable of being returned to CMS following successful appeal based on historical data and other trends relating to such appeals. In addition, if our estimate of liability for appeals with respect to revenues recognized during a prior period changes, we increase or decrease the estimated liability for appeals in the current period.

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This estimated liability for appeals is an offset to revenues on our income statement. Resolution of appeals can take a very long time to resolve and there is a significant backlog in the system for resolving appeals, as over the course of our existing RAC contract, healthcare providers have increased their pursuit of appeals beyond the first and second levels of appeal to the third level of appeal, where cases are heard by administrative law judges, or ALJs. In our experience, decisions at the third level of appeal are the least favorable as ALJs exercise greater discretion and there is less predictability in the ALJ decisions as compared to appeals at the first or second levels. This increase of ALJ appeals and backlog of claims at the third level of appeal is the primary reason our total estimated liability for appeals (consisting of the estimated liability for appeals plus the contra-accounts-receivable estimated allowance for appeals) has remained at a consistent level despite decreasing revenue from CMS. The balance of the estimated liability for appeals remained at \$19.0 million as of December 31, 2016 primarily due to new accruals for the audits we performed in 2015 for which ALJ appeals are anticipated. In addition to the \$19.0 million related to the RAC contract with CMS, the Company has accrued \$0.3 million of additional estimated liability for appeals related to other healthcare contracts. The total accrued liability for appeals is therefore \$19.3 million at December 31, 2016.

The \$19.3 million balance as of December 31, 2016, represents our best estimate of the probable amount of losses related to appeals of claims for which commissions were previously collected. We estimate that it is reasonably possible that we could be required to pay up to an additional approximately \$5.4 million as a result of potentially successful appeals. To the extent that required payments by us related to successful appeals exceed the amount accrued, revenues in the applicable period would be reduced by the amount of the excess.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued an ASU that amends the FASB ASC by creating a new Topic 606, Revenue from Contracts with Customers. The new guidance will supersede the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance on revenue recognition throughout the Industry Topics of the Codification. The core principle of the guidance is that an entity should 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. To achieve that core principle, an entity should apply a five step model for recognizing and measuring revenue from contracts with customers. In addition, an entity should disclose sufficient qualitative and quantitative 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 revenue recognition guidance, including subsequent amendments, is effective for annual reporting periods beginning on or after December 15, 2017, including interim periods within that reporting period, with the option to early adopt the standard for annual periods beginning on or after December 15, 2016.

We are currently in the process of its initial assessment to evaluate the impact from the adoption of this guidance on its consolidated financial statements. As part of this process, we are considering our major revenue streams and evaluating our significant contracts therein for potential changes in the amounts and timing of revenue recognition under the new guidance. Based on the work performed to date, we have determined that the following areas are of primary focus: consideration of termination rights and resulting impact on the duration of a contract, applicability of treatment as variable consideration for certain incentive payments, ability to use the ‘right to invoice’ practical expedient for measuring satisfaction of a performance obligation, and potential deferral of certain costs to obtain a contract. We expect to have our preliminary evaluation, including the selection of an adoption method, completed by the first half of 2017. We expect to adopt the new revenue recognition guidance in the first quarter of 2018.

### Goodwill

We periodically review the carrying value of intangible assets not subject to amortization, including goodwill, to determine whether an impairment may exist. GAAP requires that goodwill and certain intangible assets not subject to amortization be assessed annually for impairment using fair value measurement techniques.

We assess goodwill for impairment on an annual basis as of November 30 of each year or more frequently if an event occurs or changes in circumstances would more likely than not reduce the fair value of a reporting unit below its carrying amount. We have the option to perform a qualitative assessment to determine if an impairment is more likely than not to have occurred. If we can support the conclusion that it is more likely than not that the fair value of a reporting unit is greater than its carrying amount, then we would not need to perform the two-step impairment test. If we cannot support such a conclusion, or we do not elect to perform the qualitative assessment, then the first step of the

goodwill impairment test is used to identify potential impairment by comparing the fair value of a reporting unit with its carrying amount, including goodwill. We performed a qualitative assessment of whether it is more likely than not that goodwill fair value is less than its carrying amount as of November 30, 2016, and concluded that there was no need to perform an impairment test. In December 2016, the Department of Education awarded contracts for student loan recovery services to seven contractors, and we were not selected to receive one of these contract awards. Based on this event, we performed a Step 1 impairment assessment as of December 31, 2016 and concluded that it was not necessary to perform a Step 2 impairment assessment. During 2015, we performed a Step 1

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impairment assessment as of November 30, 2015 and concluded that it was not necessary to perform a Step 2 impairment assessment. We performed a qualitative assessment of whether it is more likely than not that goodwill fair value is less than its carrying amount for 2014 and concluded that there was no need to perform an impairment test.

**Impairments of Depreciable Intangible Assets**

The balance of depreciable intangible assets was \$5.9 million as of December 31, 2016. We evaluate depreciable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Depreciable intangible assets consist of client contracts and related relationships, and are being amortized over their estimated useful life, which is generally 20 years. We evaluate the client contracts intangible at the individual contract level. The recoverability of such assets is measured by a comparison of the carrying amount of the assets to future undiscounted net cash flows expected to be generated by the assets. If the assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. For the year ended December 31, 2016, an impairment expense of \$15.4 million was recognized relating to the Department of Education customer relationship and has been presented as a separate caption in the consolidated statements of operations. For the year ended December 31, 2015, an impairment expense of \$0.2 million was recognized to account for the loss of a client and it has been included in other operating expenses in the consolidated statements of operations. There was no impairment expense for depreciable intangible assets in 2014.

**Results of Operations**

Year Ended December 31, 2016 compared to the Year Ended December 31, 2015

The following table represents our historical operating results for the periods presented:

	Year Ended December 31,			
	2016	2015	\$ Change	% Change
	(in thousands)			
<b>Consolidated Statements of Operations Data:</b>				
Revenues	\$141,360	\$159,381	\$(18,021)	(11)%
Operating expenses:				
Salaries and benefits	78,863	88,077	(9,214)	(10)%
Other operating expense	54,985	64,360	(9,375)	(15)%
Impairment of customer relationship	15,438	236	15,202	6,442%
Total operating expenses	149,286	152,673	(3,387)	(2)%
Income (loss) from operations	(7,926)	6,708	(14,634)	(218)%
Interest expense	(7,897)	(8,889)	992	(11)%
Interest income	—	—	—	—%
Loss before benefit from income taxes	(15,823)	(2,181)	(13,642)	(625)%
Benefit from income taxes	(4,370)	(386)	(3,984)	(1,032)%
Net Loss	\$(11,453)	\$(1,795)	\$(9,658)	(538)%

**Revenues**

Total revenues were \$141.4 million for the year ended December 31, 2016, a decrease of \$18.0 million or 11%, compared to total revenues of \$159.4 million for the year ended December 31, 2015. The decrease is due to a decline in revenues in both our student lending and healthcare markets.

Student lending revenues were \$109.6 million for the year ended December 31, 2016, representing a decrease of \$9.8 million, or 8%, compared to the year ended December 31, 2015. This decrease was primarily a result of the reduction of revenues from the Department of Education due to the lack of placements of new student loans following the expiration of our contract in April 2015. This decrease was partially offset by an increase in revenue as a result of an increase in the number of borrowers that are participating in the rehabilitation programs with our Guaranty Agency clients.

Healthcare revenues were \$11.4 million for the year ended December 31, 2016, representing a decrease of \$8.5 million, or 43%, compared to the year ended December 31, 2015. This decrease was due primarily to reduced levels of





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permitted healthcare audit and recovery activities under our first CMS RAC contract during 2016 and an approximately \$1.8 million reduction in revenues from commercial healthcare customers.

Salaries and Benefits

Salaries and benefits expense was \$78.9 million for the year ended December 31, 2016, a decrease of \$9.2 million, or 10%, compared to salaries and benefits expense of \$88.1 million for the year ended December 31, 2015. The decrease in salaries and benefits expense was primarily due to a reduction in employee headcount during 2016 undertaken as a result of reduced business volumes.

Other Operating Expense

Other operating expense was \$55.0 million for the year ended December 31, 2016, a decrease of \$9.4 million, or 15%, compared to other operating expense of \$64.4 million for the year ended December 31, 2015. The decrease in other operating expenses was primarily due to lower communication and postage expenses and lower outside services and collections costs resulting from the wind-down of our Department of Education contract and our first RAC contract, and approximately \$3.3 million in transaction expenses associated with a proposed acquisition that did not occur in 2015.

Impairment of Customer Relationship

Impairment of customer relationship was \$15.4 million for the year ended December 31, 2016, an increase of \$15.2 million, compared to impairment of customer relationship of \$0.2 million for the year ended December 31, 2015. The increase in the impairment of customer relationship was due to the write off of \$15.4 million related to the Department of Education customer relationship intangible in 2016 after the Department of Education announced in December 2016 that we would not be a recipient of the new contract awards. We are currently protesting that contract award decision.

Income (Loss) from Operations

As a result of the factors described above, loss from operations was \$7.9 million for the year ended December 31, 2016, compared to income from operations of \$6.7 million for the year ended December 31, 2015, representing a decrease of \$14.6 million, or 218%.

Interest Expense

Interest expense was \$7.9 million for the year ended December 31, 2016 compared to \$8.9 million for the year ended December 31, 2015, representing a decrease of 11%. Interest expense decreased due to repayments of principal under our credit agreement, resulting in a lower outstanding balance during 2016.

Income Taxes

The income tax benefit was \$4.4 million for the year ended December 31, 2016 compared to an income tax benefit of \$0.4 million for the year ended December 31, 2015. Our effective income tax rate increased to 28% for the year ended December 31, 2016 from 18% for the year ended December 31, 2015. The increase in the effective tax rate is primarily due to the increase in the 2016 net loss, as the net loss in 2015 was closer to breakeven, and the impact of permanent differences and state taxes was therefore reduced on a percentage basis by the larger loss in 2016, offset by the recorded valuation allowance in 2016.

Net Loss

As a result of the factors described above, net loss was \$11.5 million for the year ended December 31, 2016, which represents an increase of \$9.7 million compared to net loss of \$1.8 million for the year ended December 31, 2015.

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Year Ended December 31, 2015 compared to the Year Ended December 31, 2014

The following table presents our historical operating results for the periods presented:

	Year Ended December 31,			
	2015	2014	\$ Change	% Change
	(in thousands)			
Consolidated Statements of Operations Data:				
Revenues	\$159,381	\$195,378	\$(35,997)	(18)%
Operating expenses:				
Salaries and benefits	88,077	93,676	(5,599)	(6)%
Other operating expense	64,596	74,433	(9,837)	(13)%
Total operating expenses	152,673	168,109	(15,436)	(9)%
Income from operations	6,708	27,269	(20,561)	(75)%
Interest expense	(8,889)	(10,171)	1,282	(13)%
Interest income	—	1	(1)	(100)%
Income (loss) before provision for (benefit from) income taxes	(2,181)	17,099	(19,280)	(113)%
Provision for (benefit from) income taxes	(386)	7,699	(8,085)	(105)%
Net income (loss)	(1,795)	9,400	(11,195)	(119)%

#### Revenues

Total revenues were \$159.4 million for the year ended December 31, 2015, a decrease of \$36.0 million or 18%, compared to total revenues of \$195.4 million for the year ended December 31, 2014. The decrease is due to a decline in revenues in both our student lending and healthcare markets.

Student lending revenues were \$119.4 million for the year ended December 31, 2015, representing a decrease of \$18.9 million, or 14%, compared to the year ended December 31, 2014. This decrease was primarily due to the full year impact of lower rehabilitation fees paid to us by our guaranty agency clients that was effective July 1, 2014 and partial year impact of Department of Education's rehabilitation fee decreases that became effective July 1, 2015. The reduction in rehabilitation fees is due to the Bipartisan Budget Act of 2013 that became effective July 1, 2014 which reduces what guaranty agencies can charge borrowers.

Healthcare revenues were \$19.9 million for the year ended December 31, 2015, representing a decrease of \$12.6 million, or 39%, compared to the year ended December 31, 2014. This decrease was due primarily to reduced audit activity in 2015 as the result of the wind-down of our current RAC contract, resulting in substantially reduced levels of permitted healthcare audit and recovery activities.

#### Salaries and Benefits

Salaries and benefits expense was \$88.1 million for the year ended December 31, 2015, a decrease of \$5.6 million, or 6%, compared to salaries and benefits expense of \$93.7 million for the year ended December 31, 2014. The decrease in salaries and benefits expense was primarily due to a reduction in headcount during 2015.

#### Other Operating Expense

Other operating expense was \$64.6 million for the year ended December 31, 2015, a decrease of \$9.8 million, or 13%, compared to other operating expense of \$74.4 million for the year ended December 31, 2014. The decrease in other operating expenses was primarily due to lower third party collection fees and lower outside services and collections costs resulting from the wind-down of our current RAC contract, which was offset by approximately \$3.3 million in transaction expenses associated with a contemplated acquisition that did not occur.

#### Income from Operations

As a result of the factors described above, income from operations was \$6.7 million for the year ended December 31, 2015, compared to \$27.3 million for the year ended December 31, 2014, representing a decrease of \$20.6 million, or 75%.

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## Interest Expense

Interest expense was \$8.9 million for the year ended December 31, 2015 compared to \$10.2 million for the year ended December 31, 2014, representing a decrease of 13%. Interest expense decreased due to repayments of principal under our credit agreement, resulting in a lower outstanding balance during 2015.

## Income Taxes

The income tax benefit was \$0.4 million for the year ended December 31, 2015 compared to an income tax expense of \$7.7 million for the year ended December 31, 2014, representing a decrease of 105%, consistent with the decrease in income before provision for income taxes. Our effective income tax rate decreased to 18% for the year ended December 31, 2015 from 45% for the year ended December 31, 2014. The decrease in the effective tax rate is primarily the result of the loss from operations incurred in 2015 compared to the income from operations in 2014 and the resulting impact of the state income tax expense accrued in 2015 related to state income tax expense accrued on income from operations that is taxed in separate state jurisdictions.

## Net Income (loss)

As a result of the factors described above, net loss was \$1.8 million for the year ended December 31, 2015, which represents a decrease of \$11.2 million compared to net income of \$9.4 million for the year ended December 31, 2014.

## Liquidity and Capital Resources

Our principal sources of liquidity are cash on hand and cash flows from operations. Cash and cash equivalents, which excludes restricted cash, totaled \$33.0 million as of December 31, 2016. Due to our operating cash flows and our existing cash and cash equivalents and our ability to restructure both our variable and fixed expenses, we believe that we have the ability to meet our working capital and capital expenditure needs through the fourth quarter of 2017 and up until the March 19, 2018 maturity date of all remaining balance outstanding on our existing credit facility.

The \$38.2 million decrease in the balance of our cash and cash equivalents at December 31, 2016 compared with December 31, 2015 was primarily due to the principal repayments of \$39.1 million on our long-term debt in 2016 as compared to similar repayments of \$17.5 million in 2015 and a \$7.5 million restricted cash deposit made in connection with an amendment to our credit agreement in 2016.

The following table presents information regarding our cash flows for the years ended December 31, 2016, 2015 and 2014:

	Year Ended December 31,		
	2016	2015	2014
	(in thousands)		
Net cash provided by operating activities	\$17,784	\$16,171	\$27,866
Net cash used in investing activities	(7,866 )	(6,627 )	(10,146 )
Net cash used in financing activities	(48,139 )	(18,691 )	(19,331 )

## Cash flows from operating activities

Operating activities provided \$17.8 million of cash during the year ended December 31, 2016, representing an increase of \$1.6 million, compared to cash provided by operating activities of \$16.2 million for the year ended December 31, 2015. Our net loss of \$11.5 million in 2016 includes \$15.4 million of non-cash customer-relationship impairment expense. Taking account of this non-cash expense, operating activities during 2016 provided cash at a level similar to 2015. Additional operating cash was provided by a reduction in trade receivables of \$6.5 million.

These items were partially offset by various working capital fluctuations such as an increase in our income tax receivable of \$2.0 million and a decrease in net payable to client of \$1.3 million.

Operating activities provided \$16.2 million of cash during the year ended December 31, 2015, representing a decrease of \$11.7 million, compared to cash provided by operating activities of \$27.9 million for the year ended December 31, 2014, primarily due to a reduction of net income from \$9.4 million to a net loss of \$1.8 million in 2015, an increase in net payable to client of \$2.3 million, collection of trade receivables of \$2.9 million and an increase in our income tax receivables and payables of \$5.3 million and a decrease in other prepaid expenses. These items were partially offset by various working capital



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fluctuations such as an increase in the estimated liability for appeals of \$0.5 million associated with our RAC contract with CMS and a decrease in accrued salaries and benefits.

Operating activities provided \$27.9 million of cash during the year ended December 31, 2014, representing a decrease of \$33.3 million, compared to cash provided by operating activities of \$61.2 million for the year ended December 31, 2013, primarily due to a reduction of net income to \$9.4 million in 2014, an increase in net payable to client of \$12.1 million, collection of trade receivables of \$4.6 million and an increase in the estimated liability for appeals of \$3.3 million associated with our RAC contract with CMS. These items were partially offset by various working capital fluctuations such as an increase in other prepaid expenses and a decrease in accrued salaries and benefits.

Cash flows from investing activities

Investing activities resulted in cash outflow of \$7.9 million during the year ended December 31, 2016 and was primarily for capital expenditures related to information technology, data storage, hardware, telecommunication systems and security enhancements to our proprietary software.

Investing activities resulted in cash outflow of \$6.6 million during the year ended December 31, 2015. The primary uses of cash associated with investing activities were \$7.9 million for capital expenditures related to information technology, data storage, hardware, furniture and equipment and security enhancements to our proprietary software, which was offset by proceeds from a sale of land for \$1.3 million.

We used \$10.1 million of cash in investment activities for the purchase of property, equipment and leasehold improvements during 2014, primarily for investments in information technology, data storage, hardware, telecommunication systems and security enhancements to our proprietary software.

Cash flows from financing activities

Cash used in financing activities of \$48.1 million during the year ended December 31, 2016 was primarily due to the repayment of principal on outstanding debt and other contractual obligations of \$39.1 million, a \$7.5 million restricted cash deposit made in connection with an amendment to our credit agreement and \$1.2 million in debt issuance costs for amendments to our credit agreement.

Cash used in financing activities of \$18.7 million during the year ended December 31, 2015 was primarily due to the repayment of principal on outstanding debt and other contractual obligations of \$18.7 million.

Cash used in financing activities of \$19.3 million during the year ended December 31, 2014 was primarily due to the repayment of principal on outstanding debt and other contractual obligations of \$22.5 million. This was partially offset by an income tax benefit of \$3.2 million associated with the exercise of employee stock options, and \$0.6 million in proceeds received from the exercise of employee stock options.

Restricted Cash

As of December 31, 2016, restricted cash included in current assets on our consolidated balance sheet was \$7.5 million. On February 19, 2016, the Company deposited \$7.5 million into a segregated deposit account in connection with the Fourth Amendment to our credit agreement. The cash in this segregated deposit account is restricted because it is subject to the exclusive control of the Agent.

Estimated liability for appeals and Net payable to client

The December 31, 2016 balances of \$19.3 million and \$13.1 million for the Estimated liability for appeals and the Net payable to client, respectively, represent obligations that we expect to pay in the near term, although it is difficult to predict the precise timing of the associated cash outflows as they are dependent on the processing and resolution of audit appeals.

Long-term Debt

On March 19, 2012, we, through our wholly owned subsidiary, entered into a \$147.5 million credit agreement, as amended and restated, with Madison Capital Funding LLC as administrative agent, ING Capital LLC as syndication agent, and other lenders party thereto. The senior credit facility consists of (i) a \$57.0 million Term A loan that matures in March 2017, (ii) a \$79.5 million Term B loan that matures in March 2018, and (iii) a \$11.0 million revolving credit facility that expires in March 2017. As of December 31, 2016, the outstanding loan balance, under our credit agreement, including the current portion was \$55.2 million, consisting of \$3.2 million under the Term A loan and \$52.0 million under the Term B loan. On each of



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November 4, 2014, January 28, 2015, February 19, 2016, July 26, 2016, and October 27, 2016, we further amended the credit agreement to modify a number of existing covenants and add certain new covenants.

All borrowings under the credit agreement bear interest at a rate per annum equal to an applicable margin plus, at our option, either (i) a base rate determined by reference to the highest of (a) the prime rate published in the Wall Street Journal or another national publication, (b) the federal funds rate plus 0.5%, (c) the sum of (A) the 1-month LIBOR rate and (B) the difference between the then effective applicable margins for LIBOR loans and base rate loans and (d) 2.5% or (ii) a LIBOR rate determined by reference to the highest of (a) a LIBOR rate published in Reuters or another national publication and (b) 1.5%. The Term A loan and the revolving credit facility have an applicable margin of 5.75% for base rate loans and 6.75% for LIBOR rate loans, in each case based on a total debt to EBITDA ratio of less than 4.75 to 1.00. The Term B loan (including the incremental Term B loan) has an applicable margin of 6.25% for base rate loans and 7.25% for LIBOR rate loans. Interest is due at the end of each month for base rate loans and at the end of each LIBOR period for LIBOR rate loans unless the LIBOR period is greater than 3 months, in which case interest is due at the last day of each 3-month interval of such LIBOR period.

The credit agreement requires us to prepay the two term loans on a prorated basis and then to prepay the revolving credit facility under certain circumstances: (i) with 100% of the net cash proceeds of any asset sale or other disposition of assets by us or our subsidiaries where the net cash proceeds exceed \$1 million and (ii) with a percentage of our annual excess cash flow each year where such percentage ranges from 25%-75% depending on our total debt to EBITDA ratio reduced by any voluntary prepayments that are made on our term loans during the same period, unless we elect to apply voluntary prepayments in the inverse order of maturity, in which case only voluntary prepayments in excess of \$10 million shall reduce the amount of excess cash flow we are required to prepay. With respect to (ii) above, in May 2015 and May 2014, the Company made payments of \$7.0 million and \$11.5 million, respectively, to the lenders. In addition, the Company made a prepayment of \$1.3 million to the lenders in July 2015 with proceeds from a sale of land in San Angelo, TX.

We have to abide by certain negative covenants for our credit agreement, which limit the ability for our subsidiaries and us to:

- incur additional indebtedness;
- create or permit liens;
- pay dividends or other distributions to our equity holders;
- purchase or redeem certain equity interests of our equity holders, including any warrants, options and other security rights;
- pay management fees or similar fees to any of our equity holders;
- make any redemption, prepayment, defeasance, repurchase or any other payment with respect to any subordinated debt;
- consolidate, merge or make any acquisitions;
- sell assets, including the capital stock of our subsidiaries;
- enter into transactions with our affiliates;
- enter into different business lines;
- permit the aggregate amount of capital expenditures to exceed a certain amount; and
- make investments.

The credit agreement also requires us to meet certain financial covenants, including maintaining (i) a fixed charge coverage ratio, (ii) a total debt to EBITDA ratio, (iii) an interest coverage ratio, (iv) a minimum EBITDA amount, (v) a minimum required adjusted cash amount, and (vi) maximum capital expenditures, as such terms are defined in our credit agreement. These financial covenants are tested at the end of each year, quarter or month, as applicable. The table below further describes these financial covenants, as well as our current status under these covenants as of December 31, 2016.

Financial Covenant	Covenant Requirement	Actual Ratio at December 31, 2016
Fixed charge coverage ratio (minimum) <sup>1</sup>	N/A	N/A



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Total debt to EBITDA ratio (maximum) <sup>2</sup>	4.75 to 1.0	1.79
Interest coverage ratio (minimum) <sup>3</sup>	2.0 to 1.0	4.34
EBITDA (minimum) <sup>4</sup>	\$20,000,000	N/A
Required Adjusted Cash Amount (minimum) <sup>5</sup>	\$10,000,000	N/A
Capital Expenditures <sup>6</sup>	\$8,000,000	\$7,866,000

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- (1) The fixed charge coverage ratio will no longer apply to any future computation periods.
- (2) The total debt to EBITDA ratio will apply to computation periods ending December 31, 2017.
- (3) The interest coverage ratio will apply to computation periods ending December 31, 2017.
- (4) This requirement was effective through June 30, 2016.
- (5) This requirement was effective through September 30, 2016.
- (6) This requirement is an annual limitation and adjusted to \$8,000,000 for the years ending December 31, 2016 and December 31, 2017.

Pursuant to the Fourth, Fifth and Sixth amendments to our credit agreement dated February 19, 2016, July 27, 2016 and October 27, 2016, respectively, our financial covenants were modified as follows:

The annual capital expenditure limitation of \$12.5 million, which was in effect for the year ending December 31, 2016, has been revised to be \$8 million for the years ending December 31, 2016 and December 31, 2017.

The total debt to EBITDA ratio of 3.25 to 1.0, which was in effect for the computation periods ending as of March 31, 2017, June 30, 2017, September 30, 2017, and December 31, 2017, has been revised to be 4.75 to 1.0 for those periods.

The interest coverage ratio of 2.5 to 1.0 in effect for the computation period ending September 30, 2016, and 2.0 to 1.0 in effect for the computation period ending December 31, 2016, and 1.75 to 1.0 in effect for the computation periods ending as of March 31, 2017, June 30, 2017, September 30, 2017 has been revised to include December 31, 2017.

The fixed charge coverage ratio of 1.20 to 1.0, which was in effect for the computation period ending as of December 31, 2017, has been revised to no longer apply to that period.

The required minimum adjusted cash balance of \$30.0 million, which was in effect from March 31, 2016 through December 31, 2016, has been revised to be \$10.0 million from March 31, 2016 through September 30, 2016.

The minimum trailing twelve month EBITDA of \$20.0 million, which was in effect from March 31, 2016 through December 31, 2016, has been revised by shortening such period to extend until June 30, 2016.

Our obligation to apply, on an annual basis, a percentage, which may fluctuate between 25% and 75% (determined based upon the Company's total debt to EBITDA ratio), of our annual excess cash flow as a mandatory prepayment of the loans under the Credit Agreement has also been modified. Pursuant to the Fifth Amendment, we are required to apply 75% of our excess cash flow each quarter as a mandatory prepayment of the loans under the Credit Agreement. In addition, without the consent of the Agent and lenders holding more than 50% of the revolving loan commitments under the Credit Agreement, we are no longer permitted to request revolving loans; however, this will not affect our ability to utilize the letter of credit sub-facility under the Credit Agreement.

In connection with the Fourth amendment, we voluntarily prepaid \$22.5 million under the credit agreement, which was applied ratably to the Term A loan and the Term B loan. In addition, we deposited \$7.5 million into a deposit account which is subject to the exclusive control of the Agent. These funds will be remitted to the Agent for application to the term loans or other obligations, as applicable, under the credit agreement on the earlier to occur of (i) March 10, 2017 (or such later date not more than thirty (30) days thereafter as may be agreed by Agent in its sole discretion) and (ii) the occurrence and continuation of an event of default; however, all or a portion of these funds may also be returned to us if the Agent and the requisite lenders under the credit agreement elect otherwise in their sole discretion. In connection with the most recent amendment, we voluntarily prepaid \$7.5 million under the credit agreement, which was applied ratably to the Term A loan and the Term B loan.

As of December 31, 2016, we had outstanding indebtedness under our credit agreement in the principal amount of \$55.2 million, of which \$3.2 million matures on March 19, 2017 and \$52.0 million matures on March 19, 2018. Our existing cash resources and cash flows expected from operations over the next twelve months are not expected to be

sufficient for us to pay the principal amount that will be due on March 19, 2018, although our current financial projections show that we will be able to maintain compliance with our debt covenants and make all scheduled debt service payments prior to that time, including payment of the portion of our indebtedness maturing in March 2017. Accordingly, we expect that it will be necessary to refinance our indebtedness due in March 2018 prior to maturity or restructure or obtain modifications to the terms of that indebtedness from our lenders. There is no assurance that new financing will be available to us in amounts sufficient to

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refinance this indebtedness or that any financing will be available on reasonable terms. Further, any new financing may result in a potentially dilutive issuance of equity securities or the issuance of new debt at higher interest rates and require us to comply with more restrictive covenants. In the absence of new financing, there is no assurance that our existing lenders will agree to restructure or modify the terms of our existing indebtedness on or before the March 2018 maturity date. Our ability to refinance or restructure our indebtedness will depend on the financial condition and results of operations of our business, which have suffered in recent periods as further described in the Risk Factors, and will also depend on factors completely outside of our control such as the condition of the capital markets at the time of any potential financing. If we cannot make scheduled payments on our debt, we will be in default and, as a result, our lenders could declare all outstanding principal and interest to be due and payable, and our lenders could foreclose against the assets securing our borrowings and we could be forced into bankruptcy or liquidation.

**Contractual Obligations**

The following summarizes our contractual obligations as of December 31, 2016:

Contractual Obligations	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Long-Term Debt Obligations	\$55,182	\$11,032	\$44,150	\$—	\$ —
Interest Payments	4,887	4,061	826	—	—
Operating Lease Obligations	4,841	1,800	1,880	1,161	—
Purchase Obligations	3,627	3,427	200	—	—
Total	\$68,537	\$20,320	\$47,056	\$1,161	\$ —

**Off-Balance Sheet Arrangements**

We have no off-balance sheet arrangements.

**Adjusted EBITDA and Adjusted Net Income**

To provide investors with additional information regarding our financial results, we have disclosed in the table below and within this report adjusted EBITDA and adjusted net income, both of which are non-GAAP financial measures.

We have provided a reconciliation below of adjusted EBITDA to net income and adjusted net income to net income, the most directly comparable GAAP financial measure to these non-GAAP financial measures.

We have included adjusted EBITDA and adjusted net income in this report because they are key measures used by our management and board of directors to understand and evaluate our core operating performance and trends and to prepare and approve our annual budget. Accordingly, we believe that adjusted EBITDA and adjusted net income provide useful information to investors and analysts in understanding and evaluating our operating results in the same manner as our management and board of directors.

Our use of adjusted EBITDA and adjusted net income has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and adjusted EBITDA does not reflect cash capital expenditure requirements for such replacements or for new capital expenditure requirements;

adjusted EBITDA does not reflect interest expense on our indebtedness;

adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;

adjusted EBITDA does not reflect tax payments;

adjusted EBITDA and adjusted net income do not reflect the potentially dilutive impact of equity-based compensation;

adjusted EBITDA and adjusted net income do not reflect the impact of certain non-operating expenses resulting from matters we do not consider to be indicative of our core operating performance; and



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other companies may calculate adjusted EBITDA and adjusted net income differently than we do, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider adjusted EBITDA and adjusted net income alongside other financial performance measures, including net income and our other GAAP results.

The following tables present a reconciliation of adjusted EBITDA and adjusted net income for the years ended December 31, 2016, 2015 and 2014 to actual net income for these periods:

	Year Ended December 31,		
	2016	2015	2014
	(in thousands)		
Reconciliation of Adjusted EBITDA:			
Net income (loss)	\$(11,453)	\$(1,795)	\$9,400
Provision for (benefit from) income taxes	(4,370)	(386)	7,699
Gain on sale of land <sup>(6)</sup>	—	(636)	—
Interest expense	7,897	8,889	10,171
Interest income	—	—	(1)
Transaction expenses <sup>(1)</sup>	—	3,270	1,276
Restructuring and other expenses <sup>(4)</sup>	329	1,079	—
Depreciation and amortization	13,380	13,132	12,450
Impairment of customer relationship <sup>(7)</sup>	15,438	236	—
Stock based compensation	4,713	5,009	3,707
Adjusted EBITDA	\$25,934	\$28,798	\$44,702

	Year Ended December 31,		
	2016	2015	2014
	(in thousands)		
Reconciliation of Adjusted Net Income:			
Net income (loss)	\$(11,453)	\$(1,795)	\$9,400
Gain on sale of land <sup>(6)</sup>	—	(636)	—
Transaction expenses <sup>(1)</sup>	—	3,270	1,276
Stock based compensation	4,713	5,009	3,707
Amortization of intangibles <sup>(2)</sup>	3,736	3,790	3,737
Impairment of customer relationship <sup>(7)</sup>	15,438	236	—
Deferred financing amortization costs <sup>(3)</sup>	1,732	1,191	1,055
Restructuring and other expenses <sup>(4)</sup>	329	1,079	—
Tax adjustments <sup>(5)</sup>	(10,379)	(5,576)	(3,910)
Adjusted Net Income (Loss)	\$4,116	\$6,568	\$15,265

(1) Represents direct and incremental costs associated with expenses incurred in 2015 for a potential acquisition and related financing.

(2) Represents amortization of capitalized expenses related to the acquisition of Performant by an affiliate of Parthenon Capital Partners in 2004, and also an acquisition in the first quarter of 2012 to enhance our analytics capabilities.

(3) Represents amortization of capitalized financing costs related to financing conducted in 2012 and costs related to the amendment of the terms of the note payable in 2014 and 2016.

(4) Represents restructuring costs and severance and termination expenses incurred in connection with termination of employees and consultants in 2015.

(5) Represents tax adjustments assuming a marginal tax rate of 40%.



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(6) Represents gain on the sale of land in San Angelo, TX in 2015.

(7) Represents impairment expense was recognized relating to the Department of Education customer relationship in 2016 and account for the loss of a client in 2015.

Recent Accounting Pronouncements

See "Recent Accounting Pronouncements" in Note 1(v) of the Consolidated Financial Statements included in Part IV - Item 15 of this report.

ITEM 7A. Quantitative and Qualitative Disclosures about Market Risk

We do not hold or issue financial instruments for trading purposes. We conduct all of our business in U.S. currency and therefore do not have any direct foreign currency risk. We do have exposure to changes in interest rates with respect to the borrowings under our senior secured credit facility, which bear interest at a variable rate based on the prime rate or LIBOR. For example, if the interest rate on our borrowings increased 100 basis points (1%) from the credit facility floor of 1.5%, our annual interest expense would increase by approximately \$0.6 million.

While we currently hold our excess cash in an operating account, in the future we may invest all or a portion of our excess cash in short-term investments, including money market accounts, where returns may reflect current interest rates. As a result, market interest rate changes impact our interest expense and interest income. This impact will depend on variables such as the magnitude of interest rate changes and the level of our borrowings under our credit facility or excess cash balances.

ITEM 8. Financial Statements and Supplementary Data

Our consolidated financial statements and notes thereto and the report of KPMG LLP are set forth in the Index to Financial Statements under Item 15, Exhibits, Financial Statement Schedules, and is incorporated herein by reference.

ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

ITEM 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain a system of disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

Management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Exchange Act, as of the fiscal year covered by this Annual Report on Form 10-K. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were functioning effectively at the reasonable assurance level as of December 31, 2016.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of our consolidated financial statements for external purposes in accordance with United States Generally Accepted Accounting Principles ("US GAAP"). Under the supervision of, and with the participation of our Chief Executive Officer and Chief Financial Officer, management assessed the effectiveness of internal control over financial reporting as of December 31, 2016. The criteria established in "Internal Control Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") were updated in May 2013, when COSO issued an updated framework (the "2013 COSO Framework"). Management based its assessment on the criteria established in



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the 2013 COSO Framework. Based on this evaluation, management concluded that its internal control over financial reporting was effective as of December 31, 2016.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting during the year ended December 31, 2016, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting, other than those noted above.

ITEM 9B. Other Information

None.

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PART III

ITEM 10. Directors, Executive Officers and Corporate Governance

This Item is incorporated by reference to our definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if our proxy statement is not filed by that date, will be included in an amendment to this Report on Form 10-K.

ITEM 11. Executive Compensation

This Item is incorporated by reference to our definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if our proxy statement is not filed by that date, will be included in an amendment to this Report on Form 10-K.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This Item is incorporated by reference to our definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if our proxy statement is not filed by that date, will be included in an amendment to this Report on Form 10-K.

ITEM 13. Certain Relationships and Related Transactions, and Director Independence

This Item is incorporated by reference to our definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if our proxy statement is not filed by that date, will be included in an amendment to this Report on Form 10-K.

ITEM 14. Principal Accounting Fees and Services

This Item is incorporated by reference to our definitive proxy statement on Schedule 14A, which will be filed within 120 days after the close of the fiscal year covered by this report on Form 10-K, or if our proxy statement is not filed by that date, will be included in an amendment to this Report on Form 10-K.

PART IV

ITEM 15. Exhibits, Financial Statement Schedules

(a) Financial Statements

(1) Financial Statements. The financial statements filed as part of this report are identified in the Index to Consolidated Financial Statements on page F-1.

(2) Financial Statement Schedules. See Item 15(c) below.

(3) Exhibits. See Item 15(b) below.

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(b) Exhibits

The following exhibits are filed herewith or are incorporated by reference to exhibits previously filed with the Securities and Exchange Commission. The Company shall furnish copies of exhibits for a reasonable fee (covering the expense of furnishing copies) upon request.

Exhibit Number	Description
2.1	Agreement and Plan of Merger, dated as of January 28, 2015, by and among Performant Financial Corporation, Project Phoenix Merger Sub, Inc. Premier Healthcare Exchange, Inc. and the other parties thereto (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed January 29, 2015)
3.1	Restated Certificate of Incorporation of Registrant (incorporated by reference to Exhibit 3.1(b) to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
3.2	Amended and Restated Bylaws of Registrant (incorporated by reference to Exhibit 3.2(b) to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
4.2	Amended and Restated Registration Rights Agreement, dated as of August 15, 2012, among the Registrant and the persons listed thereon (incorporated by reference to Exhibit 4.2 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
10.1	Form of Indemnification Agreement between the Registrant and its officers and directors (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
10.2	2004 Equity Incentive Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.2 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
10.3	2004 DCS Holdings Stock Option Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.3 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
10.4	2007 Stock Option Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.4 to the Company's Registration Statement on Form S-1 filed July 23, 2012)
10.5	Recovery Audit Contractor contract by and between Diversified Collection Services, Inc. and Center for Medicare and Medicaid Services dated as of October 3, 2008, as amended (incorporated by reference to Exhibit 10.5 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
10.6	Credit Agreement, dated as of March 19, 2012, by and among DCS Business Services, Inc., the Lenders party Hereto, Madison Capital Funding LLC, and ING Capital (incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
10.7	Form of Change of Control Agreement, as amended (incorporated by reference to Exhibit 10.7 to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
10.8	Employment Agreement between the Registrant and Lisa Im, dated as of April 15, 2012, as amended (incorporated by reference to Exhibit 10.8 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)

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- 10.9 Employment Agreement between the Registrant and Jon D. Shaver dated as of March 31, 2003, as amended (incorporated by reference to Exhibit 10.9 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.10 Repurchase Agreement between the Registrant and Lisa C. Im dated as of July 3, 2012 (incorporated by reference to Exhibit 10.10 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
- 10.11 Repurchase Agreement between the Registrant and Jon D. Shaver dated as of July 3, 2012 (incorporated by reference to Exhibit 10.11 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
- 10.12 Director Nomination Agreement between the Registrant and Parthenon DCS Holdings, LLC dated as of July 20, 2012 (incorporated by reference to Exhibit 10.12 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.13 Advisory Services Agreement between Diversified Collection Services, Inc. and Parthenon Capital, LLC dated as of January 8, 2004, as amended (incorporated by reference to Exhibit 10.13 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)

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Exhibit Number	Description
10.14	Termination of the Advisory Services Agreement between Diversified Collection Services, Inc. and Parthenon Capital, LLC dated as of January 8, 2004, as amended, dated as of April 13, 2012 (incorporated by reference to Exhibit 10.14 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
10.15	2012 Stock Incentive Plan (incorporated by reference to Exhibit 10.15 to the Company's Annual Report on Form 10-K filed March 13, 2015)
10.16	Amendment No. 1 to Credit Agreement dated as of March 19, 2012, by and among DCS Business Services, Inc., the Lenders party thereto, Madison Capital Funding LLC, and ING Capital (incorporated by reference to Exhibit 10.16 to the Company's Annual Report on Form 10-K filed March 13, 2015)
10.17	Amendment No. 2 Credit Agreement, dated as of November 4 2014, by and among Performant Business Services, Inc., the Lenders party thereto, and Madison Capital Funding LLC. (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q filed November 10, 2014)
10.18	Amendment No. 4 to Credit Agreement, dated as of February 19, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC.(incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed February 25, 2016)
10.19	Amendment No. 5 to Credit Agreement, dated as of July 26, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed August 1, 2016)
10.20	Amendment No. 6 to Credit Agreement, dated as of October 27, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed October 31, 2016)
21	List of Subsidiaries
23	Consent of KPMG LLP, Independent Registered Public Accounting Firm
24	Powers of Attorney (included in the signature page to this report)
31.1	Rule 13a-14(a)/15d-14(a) Certification, executed by Lisa C. Im
31.2	Rule 13a-14(a)/15d-14(a) Certification, executed by Hakan L. Orvell
32.1	Furnished Statement of the Chief Executive Officer under 18 U.S.C. Section 1350
32.2	Furnished Statement of the Chief Financial Officer under 18 U.S.C. Section 1350
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Scheme
101.CAL	XBRL Taxonomy Extension Calculation Linkbase

101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.LAB XBRL Taxonomy Extension Label Linkbase

101.PRE XBRL Taxonomy Extension Presentation Linkbase

\*Filed herewith

Schedules not listed above have been omitted because they are not applicable or required, or the information required to be set forth therein is included in the Consolidated Financial Statements or Notes hereto.

ITEM 16. Form 10-K Summary

Not applicable

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Index to Consolidated Financial Statements

	Page
Consolidated Financial Statements of Performant Financial Corporation and Subsidiaries as of December 31, 2016 and 2015 and for the years ended December 31, 2016, 2015 and 2014	
<u>Report of Independent Registered Public Accounting Firm</u>	<u>F-2</u>
<u>Consolidated Balance Sheets</u>	<u>F-3</u>
<u>Consolidated Statements of Operations</u>	<u>F-4</u>
<u>Consolidated Statements of Comprehensive Income (Loss)</u>	<u>F-5</u>
<u>Consolidated Statements of Changes in Stockholders' Equity</u>	<u>F-6</u>
<u>Consolidated Statements of Cash Flows</u>	<u>F-7</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F-8</u>

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

Performant Financial Corporation:

We have audited the accompanying consolidated balance sheets of Performant Financial Corporation and subsidiaries as of December 31, 2016 and 2015 and the related consolidated statements of operations, comprehensive income (loss), changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2016, and the related Schedule II for the three-year period ended December 31, 2016. 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 and Schedule II referred to above present fairly, in all material respects, the financial position of Performant Financial Corporation and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

San Francisco, California

March 13, 2017

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## PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

## Consolidated Balance Sheets

(In thousands, except per share amounts)

	December 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 32,982	\$ 71,182
Restricted cash	7,502	—
Trade accounts receivable, net of allowance for doubtful accounts of \$224 and \$386, respectively	11,484	17,965
Deferred income taxes	5,331	7,170
Prepaid expenses and other current assets	12,686	12,933
Income tax receivable	2,027	—
Total current assets	72,012	109,250
Property, equipment, and leasehold improvements, net	23,735	25,515
Identifiable intangible assets, net	5,895	25,074
Goodwill	82,522	82,522
Other assets	914	179
Total assets	\$ 185,078	\$ 242,540
Liabilities and Stockholders' Equity		
Current liabilities:		
Current maturities of notes payable, net of unamortized debt issuance costs of \$1,294 and \$1,078, respectively	\$ 9,738	\$ 7,998
Accrued salaries and benefits	4,315	4,761
Accounts payable	628	929
Other current liabilities	4,409	5,615
Income taxes payable	—	895
Estimated liability for appeals	19,305	19,118
Net payable to client	13,074	14,400
Total current liabilities	51,469	53,716
Notes payable, net of current portion and unamortized debt issuance costs of \$272 and \$1,038, respectively	43,878	84,144
Deferred income taxes	1,130	8,818
Other liabilities	2,356	2,006
Total liabilities	98,833	148,684
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$0.0001 par value. Authorized, 500,000 shares at December 31, 2016 and 2015, respectively; issued and outstanding, 50,234 and 49,479 shares at December 31, 2016 and 2015, respectively	5	5
Additional paid-in capital	65,650	61,808
Retained earnings	20,590	32,043
Total stockholders' equity	86,245	93,856
Total liabilities and stockholders' equity	\$ 185,078	\$ 242,540
See accompanying notes to consolidated financial statements.		

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## PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Operations

(In thousands, except per share amounts)

	For the Years Ended December		
	31,		
	2016	2015	2014
Revenues	\$141,360	\$159,381	\$195,378
Operating expenses:			
Salaries and benefits	78,863	88,077	93,676
Other operating expenses	54,985	64,360	74,433
Impairment of customer relationship	15,438	236	—
Total operating expenses	149,286	152,673	168,109
Income (loss) from operations	(7,926 )	6,708	27,269
Interest expense	(7,897 )	(8,889 )	(10,171 )
Interest income	—	—	1
Income (loss) before provision for (benefit from) income taxes	(15,823 )	(2,181 )	17,099
Provision for (benefit from) income taxes	(4,370 )	(386 )	7,699
Net income (loss)	\$(11,453 )	\$(1,795 )	\$9,400
Net income per share attributable to common shareholders (see Note 1)			
Basic	\$(0.23 )	\$(0.04 )	\$0.19
Diluted	\$(0.23 )	\$(0.04 )	\$0.19
Weighted average shares (see Note 1)			
Basic	50,038	49,415	48,816
Diluted	50,038	49,415	49,834
See accompanying notes to consolidated financial statements.			

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PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income (Loss)

(In thousands)

	For the Years Ended		
	December 31,		
	2016	2015	2014
Net income (loss)	\$(11,453)	\$(1,795)	\$9,400
Other comprehensive income:			
Foreign currency translation adjustment	21	31	—
Comprehensive income (loss)	\$(11,432)	\$(1,764)	\$9,400

See accompanying notes to consolidated financial statements.

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## PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Changes in Stockholders' Equity

For the Years Ended December 31, 2016, 2015 and 2014

(In thousands)

	Common Stock	Additional	Retained		
	Shares	Amount	Paid-In Capital	Earnings (Deficit)	Total
Balance, December 31, 2013	48,316	\$ 5	\$ 49,791	\$ 24,438	\$ 74,234
Exercise of stock options	1,034	—	610	—	610
Stock-based compensation expense	—	—	3,707	—	3,707
Income tax benefit from employee stock options	—	—	3,221	—	3,221
Net income	—	—	—	9,400	9,400
Balance, December 31, 2014	49,350	5	57,329	33,838	91,172
Common stock issued under stock plans, net of shares withheld for employee taxes	129	—	(54 )	—	(54 )
Stock-based compensation expense	—	—	5,009	—	5,009
Income tax (shortfall) from employee stock awards	—	—	(507 )	—	(507 )
Other comprehensive income	—	—	31	—	31
Net loss	—	—	—	(1,795 )	(1,795 )
Balance, December 31, 2015	49,479	5	61,808	32,043	93,856
Common stock issued under stock plans, net of shares withheld for employee taxes	755	—	71	—	71
Stock-based compensation expense	—	—	4,713	—	4,713
Income tax (shortfall) from employee stock awards	—	—	(963 )	—	(963 )
Other comprehensive income	—	—	21	—	21
Net loss	—	—	—	(11,453 )	(11,453 )
Balance, December 31, 2016	50,234	\$ 5	\$ 65,650	\$ 20,590	\$ 86,245

See accompanying notes to consolidated financial statements.

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## PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(In thousands)

	For the Years Ended December 31,		
	2016	2015	2014
Cash flows from operating activities:			
Net income (loss)	\$ (11,453 )	\$ (1,795 )	\$ 9,400
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
(Gain) loss on disposal of assets	12	(585 )	33
Depreciation, amortization, and impairment of customer relationship	28,818	13,368	12,450
Deferred income taxes	(6,912 )	(2,943 )	(1,703 )
Stock-based compensation	4,713	5,009	3,707
Interest expense from debt issuance costs and amortization of discount note payable	1,264	1,242	1,177
Write-off of unamortized debt issuance costs	468	—	—
Changes in operating assets and liabilities:			
Trade accounts receivable	6,481	(2,918 )	4,602
Prepaid expenses and other current assets	247	(374 )	(8,159 )
Income tax receivable	(2,027 )	4,394	(4,394 )
Other assets	(740 )	174	57
Accrued salaries and benefits	(446 )	(619 )	(6,446 )
Accounts payable	(301 )	(441 )	(1,013 )
Other current liabilities	(656 )	(1,766 )	1,873
Income taxes payable	(895 )	895	(103 )
Estimated liability for appeals	187	493	3,342
Net payable to client	(1,326 )	2,290	12,110
Other liabilities	350	(253 )	933
Net cash provided by operating activities	17,784	16,171	27,866
Cash flows from investing activities:			
Proceeds from sale of property, equipment, and leasehold improvements	—	1,268	—
Purchase of property, equipment, and leasehold improvements	(7,866 )	(7,895 )	(10,146 )
Net cash used in investing activities	(7,866 )	(6,627 )	(10,146 )
Cash flows from financing activities:			
Repayment of notes payable	(39,076 )	(17,537 )	(21,509 )
Restricted cash for repayment of notes payable	(7,502 )	—	—
Debt issuance costs paid	(1,181 )	—	(653 )
Taxes paid related to net share settlement of stock awards	(266 )	(90 )	—
Proceeds from exercise of stock options	337	37	610
Income tax benefit from employee stock awards	103	22	3,221
Payment of purchase obligation	(554 )	(1,123 )	(1,000 )
Net cash used in financing activities	(48,139 )	(18,691 )	(19,331 )
Effect of foreign currency exchange rate changes on cash	21	31	—
Net decrease in cash and cash equivalents	(38,200 )	(9,116 )	(1,611 )
Cash and cash equivalents at beginning of year	71,182	80,298	81,909
Cash and cash equivalents at end of year	\$ 32,982	\$ 71,182	\$ 80,298
Supplemental disclosures of cash flow information:			
Cash paid (received) for income taxes	\$ 5,273	\$ (2,726 )	\$ 10,185
Cash paid for interest	\$ 6,156	\$ 7,650	\$ 8,978

See accompanying notes to consolidated financial statements.

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PERFORMANT FINANCIAL CORPORATION AND SUBSIDIARIES

Notes To Consolidated Financial Statements

For the Years Ended December 31, 2016, 2015 and 2014

1. Summary of Significant Accounting Policies

(a) Organization and Nature of Business

Performant Financial Corporation (the Company) is a leading provider of technology-enabled recovery and analytics services in the United States. The Company's services help identify, restructure and recover delinquent or defaulted assets and improper payments for both government and private clients in a broad range of markets. Company clients typically operate in complex and regulated environments and outsource their recovery needs in order to reduce losses on billions of dollars of defaulted student loans, improper healthcare payments and delinquent state tax and federal treasury receivables. The Company generally provides our services on an outsourced basis, where we handle many or all aspects of the clients' recovery processes.

The Company's consolidated financial statements include the operations of Performant Financial Corporation (PFC), its wholly owned subsidiary Performant Business Services, Inc., and its wholly owned subsidiaries Performant Recovery, Inc. (Recovery), Performant Technologies, Inc., and Performant Europe Ltd. Effective August 13, 2012, we changed the name of our wholly owned subsidiary from DCS Business Services, Inc. (DCSBS) to Performant Business Services, Inc., and DCSBS' wholly owned subsidiaries from Diversified Collection Services, Inc. (DCS), and Vista Financial, Inc. (VFI), to Performant Recovery, Inc., and Performant Technologies, Inc., respectively. PFC is a Delaware corporation headquartered in California and was formed in 2003. Performant Business Services, Inc. is a Nevada corporation founded in 1997. Recovery is a California corporation founded in 1976. Performant Technologies, Inc. is a California corporation that was formed in 2004.

The Company is managed and operated as one business, with a single management team that reports to the Chief Executive Officer.

(b) Principles of Consolidation

The accompanying consolidated financial statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles, or U.S. GAAP. The Company consolidates entities in which it has controlling financial interest, and as of December 31, 2016, all of the Company's subsidiaries are 100% owned. All significant intercompany balances and transactions have been eliminated in consolidation. Certain prior year amounts have been reclassified for consistency with the current period presentation.

(c) Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of the consolidated financial statements in conformity with U.S. GAAP, requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, primarily accounts receivable, intangible assets, goodwill, estimated liability for appeals, other liabilities, deferred income taxes and income tax expense, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Our actual results could differ from those estimates.

(d) Liquidity

As of December 31, 2016, we had outstanding indebtedness under our credit agreement in the principal amount of \$55.2 million, of which \$3.2 million matures on March 19, 2017 and \$52.0 million matures on March 19, 2018. Our existing cash resources and cash flows expected from operations over the next twelve months are not expected to be sufficient for us to pay the principal amount that will be due on March 19, 2018, although our current financial projections show that we will be able to maintain compliance with our debt covenants and make all scheduled debt service payments prior to that time, including payment of the portion of our indebtedness maturing in March 2017. Accordingly, we expect that it will be necessary to refinance our indebtedness due in March 2018 prior to maturity or restructure or obtain modifications to the terms of that indebtedness from our lenders. There is no assurance that new financing will be available to us in amounts sufficient to refinance this indebtedness or that any financing will be available on reasonable terms. Further, any new financing may result in a potentially dilutive issuance of equity securities or the issuance of new debt at higher interest rates and require us to comply with more restrictive covenants. In the absence of new financing, there is no assurance that our existing lenders will agree to restructure or

modify the

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terms of our existing indebtedness on or before the March 2018 maturity date. Our ability to refinance or restructure our indebtedness will depend on the financial condition and results of operations of our business, which have suffered in recent periods, and will also depend on factors completely outside of our control such as the condition of the capital markets at the time of any potential financing. If we cannot make scheduled payments on our debt, we will be in default and, as a result, our lenders could declare all outstanding principal and interest to be due and payable, and our lenders could foreclose against the assets securing our borrowings and we could be forced into bankruptcy or liquidation.

### (e) Cash and Cash Equivalents

Cash and cash equivalents include demand deposits and highly liquid debt instruments with original maturities of three months or less when purchased. These investments can include money market funds that invest in highly liquid U.S. government and agency obligations, certificates of deposit, bankers' acceptances, and commercial paper.

The Company collects monies on behalf of its clients. Cash is often held on behalf of the clients in various trust accounts and is subsequently remitted to the clients based on contractual agreements. Cash held in these trust accounts for contracting agencies is not included in the Company's assets (Note 11(a)).

### (f) Restricted Cash

At December 31, 2016, restricted cash included in current assets on our consolidated balance sheet was \$7.5 million. In February 2016, the Company deposited \$7.5 million into a segregated deposit account in connection with the Fourth Amendment to our credit agreement. The cash in this segregated deposit account is restricted because it is subject to the exclusive control of the administrative agent as set forth in our credit agreement.

### (g) Hosted Service Installation and Implementation Deliverables

In 2008, the Company entered into a long-term contract to provide hosted services to a client beginning in March 2009. The Company determined that certain installation and implementation deliverables were not separate units of accounting within the contract, and should be combined for revenue recognition purposes with the hosted service deliverable. Accordingly, revenue for these contract elements is being taken ratably from the commencement of hosted services in March 2009 through the contract period of March 2018. Additionally, the Company deferred the direct incremental costs associated with the installation and implementation deliverables, with the costs being expensed ratably from the March 2009 commencement of services through March 2018.

### (h) Property, Equipment, and Leasehold Improvements

Property, equipment, and leasehold improvements are stated at cost, net of accumulated depreciation. Furniture and equipment are depreciated using the straight-line method over estimated useful lives ranging from 7 to 5 years. Buildings are depreciated using the straight-line method over 31.5 years. Leasehold improvements are amortized using the straight-line method over the shorter of the estimated life of the asset or the remaining term of the lease. Computer software and computer hardware are depreciated using the straight-line method over 3 years and 5 years, respectively.

Maintenance and repairs are charged to expense as incurred. Improvements that extend the useful lives of assets are capitalized.

When property is sold or retired, the cost and the related accumulated depreciation are removed from the consolidated balance sheet and any gain or loss from the transaction is included in the consolidated statements of operations.

### (i) Goodwill and Other Intangible Assets

Goodwill represents the excess of purchase price and related costs over the fair value assigned to the net assets of businesses acquired. Goodwill is not amortized, but instead is reviewed for impairment at least annually. Impairment is the condition that exists when the carrying amount of goodwill is not recoverable and its carrying amount exceeds its fair value. The Company performs its assessment of whether it is more likely than not that goodwill fair value is less than its carrying amount in November of each year to allow the Company additional time to evaluate its assessment prior to reporting its results.

The Company performed a qualitative assessment of whether it is more likely than not that goodwill fair value is less than its carrying amount as of November 30, 2016, and concluded that there was no need to perform an impairment test. In December 2016, the Department of Education awarded contracts for student loan recovery services to seven contractors, and we were not selected to receive one of these contract awards. Based on this event, Company



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performed a Step 1 impairment assessment as of December 31, 2016 and concluded that it was not necessary to perform a Step 2 impairment assessment. During 2015, the Company performed a Step 1 impairment assessment as of November 30, 2015 and concluded that it was not necessary to perform a Step 2 impairment assessment.

Identifiable intangible assets consist of customer contracts and related relationships, a perpetual license, and covenants not to compete. Customer contracts and related relationships are amortized over their estimated useful life of 4 to 20 years. The perpetual license is amortized over its estimated useful life of 5 years.

**(j) Impairment of Long-Lived Assets**

Long-lived assets are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or intangibles may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the assets to future undiscounted net cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets.

**(k) System Developments**

The Company follows the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Subtopic 350-40, Internal-Use Software, which specifies that costs incurred during the application stage of development should be capitalized. All other costs are expensed as incurred. During 2016, 2015 and 2014, costs of \$6.9 million, \$7.0 million and \$7.2 million respectively, were capitalized for projects in the application stage of development, with depreciation expense of \$5.8 million, \$4.8 million and \$4.0 million respectively, for completed projects.

**(l) Debt Issuance Costs**

Debt issuance costs represent loan and legal fees paid in connection with the issuance of long-term debt. Debt issuance costs are deducted from current and non-current notes payable and are amortized to interest expense in accordance with key terms of the notes as amended.

**(m) Revenues, Accounts Receivable, and Estimated Liability for Appeals**

Revenue is recognized upon the collection of defaulted loan and debt payments. Loan rehabilitation revenue is recognized when the rehabilitated loans are sold (funded) by clients. Incentive revenue is recognized upon receipt of official notification of incentive award from customers. Under the Company's RAC contract with CMS, the Company recognizes revenues when the healthcare provider has paid CMS for a given claim or has agreed to an offset against other claims by the provider. Providers have the right to appeal a claim and may pursue additional appeals if the initial appeal is found in favor of CMS. The Company accrues an estimated liability for appeals at the time revenue is recognized based on the Company's estimate of the amount of revenue probable of being refunded to CMS following successful appeal. In addition, if the Company's estimate of the liability for appeals with respect to revenues recognized during a prior period changes, the Company increases or decreases current period accruals based on such change in estimated liability. At December 31, 2016, a total of \$19.0 million was presented as an allowance against revenue, representing the Company's estimate of claims that may be overturned. Of this amount, none was related to amounts in accounts receivable and \$19.0 million was related to commissions which had already been received. The zero allowance against accounts receivable at December 31, 2016 is due to the fact that the receivable from CMS is netted against an offsetting payable for overturned audits, and at December 31, 2016, the amount of the payable exceeded the amount of the receivable as discussed in note 1(n). In addition to the \$19.0 million related to the RAC contract with CMS, the Company has accrued \$0.3 million of additional estimated liability for appeals related to other healthcare contracts. The total accrued liability for appeals of \$19.3 million has therefore been presented in the caption estimated liability for appeals at December 31, 2016. Similarly, at December 31, 2015, the total appeals-related liability was \$19.1 million, comprised of an estimated liability for appeals of \$19.0 million. The \$19.3 million balance at December 31, 2016 and the \$19.1 million balance as of December 31, 2015, represents the Company's best estimate of the probable amount of losses related to appeals of claims for which commissions were previously collected. In addition to the \$19.3 million amount accrued at December 31, 2016, the Company estimates that it is reasonably possible that it could be required to pay an additional amount up to approximately \$5.4 million as a result of potentially successful appeals. To the extent that required payments by the Company exceed the amount accrued, revenues in the applicable period would be reduced by the amount of the excess.



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For the year ended December 31, 2016, the Company had 3 clients whose individual revenues exceeded 10% of the Company's total revenues. The dollar amount and percent of total revenue of each of the 3 clients is summarized in the table below (in thousands):

Rank	2016 Revenue	Percent of total revenue
1	\$33,243	23.5%
2	23,196	16.4%
3	21,949	15.5%

For the year ended December 31, 2015, the Company had 3 clients whose individual revenues exceeded 10% of the Company's total revenues. The dollar amount and percent of total revenue of each of the 3 clients is summarized in the table below (in thousands):

Rank	2015 Revenue	Percent of total revenue
1	\$37,878	23.8%
2	31,709	19.9%
3	17,696	11.1%

For the year ended December 31, 2014, the Company had 4 clients whose individual revenues exceeded 10% of the Company's total revenues. The dollar amount and percent of total revenue of each of the 4 clients is summarized in the table below (in thousands):

Rank	2014 Revenue	Percent of total revenue
1	\$53,211	27.2%
2	29,444	15.1%
3	29,171	14.9%
4	24,855	12.7%

Revenue from the largest three customers was 55%, 55% and 57% of total revenue in 2016, 2015 and 2014, respectively. Accounts receivable due from these three customers were 57%, 54% and 39% of total trade receivables at December 31, 2016, 2015 and 2014, respectively. Trade accounts receivable are recorded at the invoiced amount and do not bear interest. Amounts collected on trade accounts receivable are included in net cash provided by operating activities in the consolidated statements of cash flows. The Company determines the allowance for doubtful accounts by specific identification. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The allowance for doubtful accounts was \$0.2 million and \$0.4 million for December 31, 2016 and December 31, 2015, respectively.

**(n) Net Payable to Client**

The Company nets outstanding accounts receivable invoices from an audit & recovery contract against payables for overturned audits. The overturned audits are netted against current fees due on the invoice to the client when they are processed by the client's system. The "Net payable to client" balance of \$13.1 million represents the excess of payables for overturned audits at December 31, 2016. At December 31, 2015, the "Net payable to client" balance of \$14.4 million represents the excess of payables of \$15.4 million for overturned audits offset by outstanding accounts receivable of \$1.0 million. The Company expects that the net payable-to-client balance will be paid to the client within the next twelve months.

**(o) Prepaid Expenses and Other Current Assets**

At December 31, 2016, prepaid expenses and other current assets includes \$5.7 million of amounts estimated to become due from subcontractors. The Company employs subcontractors to audit claims as part of an audit & recovery contract, and to the extent that audits by these subcontractors are overturned on appeal, the fees associated with such claims are contractually refundable to the Company. At December 31, 2016, the receivable associated with estimated future overturns of subcontractor audits was \$5.7 million. In addition, at December 31, 2016, Prepaid expenses and other current assets includes a net receivable of \$3.7 million for subcontractor fees for already overturned audits



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refundable to the Company once the Company refunds its fees to the client as prime contractor. By comparison, at December 31, 2015, the receivable associated with the estimated future overturns of subcontractor audits was \$5.7 million, and the receivable for subcontractor fees for already overturned audits refundable to the Company once the Company refunds its fees to the client as prime contractor was \$3.8 million.

(p) Legal Expenses

The Company recognizes legal fees related to litigation as they are incurred.

(q) Comprehensive Income (Loss)

The Company has a single component of comprehensive income (loss) on the Consolidated Statements of Comprehensive Income (Loss) related to foreign currency translation adjustments for its subsidiary Performant Europe Ltd. for the years ended December 31, 2016 and 2015. The Company had no components of comprehensive income other than its net income in 2014.

(r) Fair Value of Financial Instruments

The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, short-term debt and long-term debt. The carrying values of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate their fair values based on or due to their short-term maturities. The carrying values of short-term debt and long-term debt approximate fair value, in which their variable interest rates approximate market rates.

(s) Income Taxes

The Company accounts for income taxes under the asset-and-liability method. Deferred income tax assets and liabilities are recognized for future tax consequences attributable to differences between the carrying value of assets and liabilities for financial reporting purposes and for taxation purposes. Deferred income tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred income tax assets and liabilities is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. 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. Interest expense and penalties related to unrecognized tax benefits are recorded in income tax expense.

(t) Stock Options

The Company accounts for its employee stock-based compensation awards in accordance with FASB ASC Topic 718, Compensation – Stock Compensation. FASB ASC Topic 718 requires that all employee stock-based compensation is recognized as a cost in the financial statements and that for equity-classified awards, such cost is measured at the grant date fair value of the award. The Company estimates grant date fair value using the Black-Scholes-Merton option-pricing model.

FASB ASC Topic 718 also requires that excess tax benefits recognized in equity related to stock option exercises are reflected as financing cash inflows. The Company recognized an income tax benefit resulting from the exercise of stock options in 2016 and 2015 of \$0.1 million and \$0.02 million, respectively. The Company recognized income tax benefits resulting from the exercise of stock options in 2014 of \$3.2 million.

(u) Earnings per Share

For the years ended December 31, 2016, 2015, and 2014, basic earnings per share is calculated by dividing net income available to common shareholders by the sum of the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated by dividing net income available to common shareholders by the weighted average number of common shares and dilutive common shares equivalents outstanding during the period. The Company's common share equivalents consist of stock options, restricted stock units, and performance stock units.

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The following table reconciles the basic to diluted weighted average shares outstanding using the treasury stock method (shares in thousands):

	Years Ended		
	December 31,		
	2016	2015	2014
Weighted average shares outstanding – basic	50,038	49,415	48,816
Dilutive effect of stock options	—	—	1,018
Weighted average shares outstanding – diluted	50,038	49,415	49,834

The following table shows the number of shares of Common Stock subject to options and restricted stock awards that were outstanding for the years ended December 31, 2016, 2015 and 2014, which were not included in the net income per diluted share calculation because to do so would have been anti-dilutive:

	Years Ended December 31,		
	2016	2015	2014
Number of shares	3,996,701 <sup>(a)</sup>	4,430,292	2,894,013

(a) Includes 3,360,384 options to purchase shares at exercise prices greater than the average market price of the common stock and 636,317 options to purchase shares that were excluded because the effect of including them was anti-dilutive.

**(v) New Accounting Pronouncements****Recently Adopted Accounting Pronouncements**

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, “Presentation of Financial Statements - Going Concern”, which addresses management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. Management’s evaluation should be based on relevant conditions and events that are known, and reasonably knowable, at the date that the financial statements are issued. This new guidance was effective for our annual reporting period ending December 31, 2016.

Effective in the first quarter of 2016, we adopted FASB's ASU 2015-03, “Simplifying the Presentation of Debt Issuance Costs,” in conjunction with their initiative to reduce complexity in accounting standards. This guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with presentation of a debt discount. The standard requires retrospective application and represents a change in accounting principle. Although the new guidance had no impact on the Company’s results of operations, the debt issuance costs presented as assets within the Company’s consolidated balance sheet which amounted to \$1.6 million and \$2.1 million, as of December 31, 2016 and December 31, 2015, respectively, have been reclassified as a reduction of the related debt liability.

Effective in the first quarter of 2016, the FASB issued ASU 2015-16, “Simplifying the Accounting for Measurement-Period Adjustments,” that eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. The adoption of ASU 2015-16 did not have a material impact on the Company’s consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, "Restricted Cash" which clarifies guidance on the classification and presentation of restricted cash in the statement of cash flows. The standard states that restricted cash should be included within cash and cash equivalents on the statement of cash flows. This new guidance is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2017, and early adoption is permitted. We have adopted this guidance early and have included restricted cash in a separate line in the financing activities section on our consolidated statements of cash flows.

**Recently Issued Accounting Pronouncements Not Yet Adopted**

In May 2014, the Financial Accounting Standards Board (“FASB”) issued an ASU that amends the FASB ASC by creating a new Topic 606, Revenue from Contracts with Customers. The new guidance will supersede the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance on revenue recognition throughout the Industry Topics of the Codification. The core principle of the guidance is that an entity should 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. To achieve that core principle, an entity should apply

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a five step model for recognizing and measuring revenue from contracts with customers. In addition, an entity should disclose sufficient qualitative and quantitative 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 revenue recognition guidance, including subsequent amendments, is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, with the option to early adopt the standard for annual periods beginning after December 15, 2016. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17, "Income Taxes: Balance Sheet Classification of Deferred Taxes" which simplifies the current presentation of separately classifying deferred tax assets and deferred tax liabilities as current and noncurrent in a classified balance sheet by requiring companies to present them as noncurrent. This new guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within such annual reporting periods with early adoption permitted. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases", which, for operating leases, requires a lessee to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in its balance sheet. The standard also requires a lessee to recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term, on a generally straight-line basis. This new guidance is effective for annual reporting periods beginning after December 15, 2018 with early adoption permitted. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting". The standard is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. This new guidance is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2016, and early adoption is permitted. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments" which provides guidance on the presentation of certain cash receipts and cash payments in the statement of cash flows in order to reduce diversity in existing practice. This new guidance is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2017, and early adoption is permitted. This new standard requires retrospective adoption, with a provision for impracticability. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, "Simplifying the Test for Goodwill Impairment" to simplify the goodwill impairment testing process. The new standard eliminates Step 2 of the goodwill impairment test. If a company determines in Step 1 of the goodwill impairment test that the carrying value of goodwill is less than the fair value, an impairment in that amount should be recorded to the income statement, rather than proceeding to Step 2. This new guidance is effective for annual reporting periods, and interim periods with goodwill impairment tests within those years, beginning after December 15, 2019, and early adoption is permitted for testing periods after January 1, 2017. We have not adopted this guidance early and are currently evaluating the effect on our consolidated financial statements.

## 2. Property, Equipment, and Leasehold Improvements

Property, equipment, and leasehold improvements consist of the following at December 31, 2016 and 2015 (in thousands):

	December 31, 2016	December 31, 2015
Land	\$ 1,122	\$ 1,122
Building and leasehold improvements	6,203	6,053
Furniture and equipment	5,656	5,390
Computer hardware and software	67,861	67,353
	80,842	79,918

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Less accumulated depreciation and amortization	(57,107 )	(54,403 )
Property, equipment and leasehold improvements, net	\$ 23,735	\$ 25,515

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Depreciation and amortization expense of property, equipment and leasehold improvements was \$9.6 million, \$9.3 million and \$8.7 million for the years ended December 31, 2016, 2015 and 2014, respectively. During 2015, the Company sold land in Texas for \$1.3 million in cash for a gain of \$0.6 million.

## 3. Identifiable Intangible Assets

Identifiable intangible assets consist of the following at December 31, 2016 and 2015 (in thousands):

December 31, 2016	Gross Amounts	Accumulated Amortization	Net
Amortizable intangibles:			
Customer contracts and related relationships	\$ 22,381	\$ (16,560 )	\$ 5,821
Perpetual license	3,313	(3,239 )	74
Total intangible assets	\$ 25,694	\$ (19,799 )	\$ 5,895

December 31, 2015	Gross Amounts	Accumulated Amortization	Net
Amortizable intangibles:			
Customer contracts and related relationships	\$ 62,215	\$ (37,886 )	\$ 24,329
Perpetual license	3,313	(2,568 )	745
Total intangible assets	\$ 65,528	\$ (40,454 )	\$ 25,074

For the years ended December 31, 2016, 2015 and 2014, amortization expense related to intangible assets amounted to \$3.7 million, \$3.8 million and \$3.7 million, respectively. For the year ended December 31, 2016, an impairment expense of \$15.4 million was recognized relating to the Department of Education customer relationship and has been presented as a separate caption in the consolidated statements of operations. For the year ended December 31, 2015, an impairment expense of \$0.2 million was recognized to account for the loss of a client and it has been included in the other operating expenses in the consolidated statements of operations. The Company did not recognize an impairment expense for intangible assets in 2014.

The estimated aggregate amortization expense for each of the five following fiscal years is as follows (in thousands):

Year Ending December 31,	Amount
2017	\$ 933
2018	861
2019	857
2020	811
2021	811
Thereafter	1,622
Total	\$ 5,895

## 4. Credit Agreement

On March 19, 2012, we, through our wholly owned subsidiary, entered into a \$147.5 million credit agreement, as amended and restated, with Madison Capital Funding LLC as administrative agent, ING Capital LLC as syndication agent, and other lenders party thereto. The senior credit facility consists of (i) a \$57.0 million Term A loan that matures in March 2017, (ii) a \$79.5 million Term B loan that matures in March 2018, and (iii) a \$11.0 million revolving credit facility that expires in March 2017. On June 28, 2012, we amended the credit agreement to increase the amount of our borrowings under our Term B loan by \$19.5 million. On November 4, 2014, February 19, 2016, July 26, 2016, and October 27, 2016, the Agreement was further amended to, among other things, modify a number of existing covenants and add new covenants requiring the Company to maintain a minimum cash balance, comply with an interest coverage ratio and achieve minimum EBITDA levels. Scheduled payments under the Agreement for the next five years and thereafter are as follows (in thousands):

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Year Ending December 31, Amount	
2017	\$11,032
2018	44,150
2019	—
2020	—
Total	\$55,182

The Term A Loan is charged interest either at Prime (subject to a 2.5% floor) +5.75% or LIBOR (subject to a 1.5% floor) +6.75%, which was 6.75% at December 31, 2016. The Term A loan requires quarterly payments of \$2.1 million, with the remaining outstanding principal balance due March 19, 2017. As of December 31, 2016, the Term A loan ending balance, including the current portion was \$3.2 million.

The Term B loan is charged interest at Prime +6.25% (subject to a 2.50% floor) or LIBOR (subject to a 1.50% floor) +7.25% which was 7.25% at December 31, 2016. The Term B loan requires quarterly payments of \$0.2 million beginning in June 2012, with the outstanding principal balance due March 19, 2018. As of December 31, 2016, the Term B loan ending balance, including the current portion was \$52.0 million.

The Company has a line of credit under the Agreement which allows for borrowings of up to \$11 million. Borrowings accrue interest at Prime +5.75% or LIBOR +6.75%, which was 6.75% at December 31, 2016. Both the Prime and the LIBOR alternatives are subject to minimum rate floors. In addition, a facility fee of 0.5% is assessed on the commitment amount. There were no outstanding borrowings under this line of credit at December 31, 2016, but there are letters of credit outstanding in the amount of \$2.0 million, leaving remaining borrowing capacity under the line of credit of \$9.0 million at December 31, 2016. The line of credit will terminate on March 19, 2017.

The Agreement contains certain restrictive financial covenants, which require, among other things, that we meet a minimum interest coverage ratio of 2.0 and maximum total debt to EBITDA ratio of 4.75. Additionally, these covenants restrict the Company and its subsidiaries' ability to incur certain types or amounts of indebtedness, incur liens on certain assets, make material changes in corporate structure or the nature of its business, dispose of material assets, engage in a change in control transaction, make certain foreign investments, enter into certain restrictive agreements, or engage in certain transactions with affiliates. We were in compliance with all such covenants at December 31, 2016.

The Agreement contains a prepayment provision which requires the Company to perform an annual excess cash flow computation based on earnings before interest, taxes, depreciation and amortization compared to changes in working capital. Based on the results of this computation, in May 2015 and May 2014, the Company made payments of \$7.0 million and \$11.5 million, respectively, to the lenders. In addition, the Company made a prepayment of \$1.3 million to the lenders in July 2015 from the sale of land in San Angelo, TX.

As part of our March 19, 2012 credit agreement (the Agreement), debt issuance costs of \$5.0 million were capitalized, including \$1.5 million of agent fees paid to an entity associated with our majority stockholder, and \$0.8 million paid to third parties for legal and other services and a grant of 215,000 shares of Common Stock issued as compensation to an investment bank acting as financial advisor valued at approximately \$2.8 million, based upon a price of \$13 per share. These costs are being amortized to expense over the life of the new loans.

The Company capitalized an additional \$0.8 million related to our June 28, 2012 amendment to the Agreement, which included \$0.2 million of agent fees paid to an entity associated with our majority stockholders, and \$0.0 million paid to third parties for legal and other services. Debt issuance costs are being amortized to interest expense over the life of the new loans.

On November 4, 2014, the Company entered into Amendment No. 2 to its Credit Agreement (Second Amendment) in which certain financial covenants were amended and additional financial covenants were added. Under the Second Amendment, the total debt to EBITDA ratio, which required the Company to maintain a ratio of 3.25 to 1.0 as of September 30, 2014 was revised as follows:

- for the computation periods ending December 31, 2014, March 31, 2015, June 30, 2015, September 30, 2015 and December 31, 2015, the Company must maintain a total debt to EBITDA ratio of 5.00 to 1.0

- for the computation periods ending March 31, 2016, June 30, 2016, September 30, 2016 and December 31, 2016, the Company must maintain a total debt to EBITDA ratio of 4.75 to 1.0; and

for each computation period ending March 31, 2017 and thereafter, the Company must maintain a total debt to EBITDA ratio of 3.25 to 1.0

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In addition, the fixed charge coverage ratio of 1.20 to 1.0, which was in effect for every computation period under the Credit Agreement as of September 30, 2014, has been revised under the Second Amendment to apply only to the computation periods ending September 30, 2014, March 31, 2017, and each computation period thereafter.

The Second Amendment also added an interest coverage ratio, defined as the ratio of EBITDA compared to interest expense paid in cash for the computation period. Under this new financial covenant, the Company is required to maintain:

- an interest coverage ratio not to be less than 2.25 to 1.0 for the computation periods ending December 31, 2014, March 31, 2015, June 30, 2015, September 30, 2015, and December 31, 2015; and

- an interest coverage ratio not to be less than of 2.50 to 1.0 for the computation period ending March 31, 2016, June 30, 2016, September 30, 2016 and December 31, 2016.

In addition, among other things, under the Second Amendment, the Company is now required to maintain minimum adjusted cash balances of \$35.0 million from November 4, 2014 through December 31, 2015, and minimum adjusted cash balances of \$30.0 million from January 1, 2016 through December 31, 2016. Further, under the Second Amendment, the Company must maintain EBITDA for any trailing twelve month period of not less than \$20.0 million beginning with the month ending November 30, 2014 through the month ending December 31, 2016. Also, pursuant to the terms of the Second Amendment, the lenders are not required to make new loans or issue new letters of credit under the Company's line of credit when the total debt to EBITDA ratio exceeds 3.25 to 1.0. Lastly, under the Second Amendment, capital expenditures of the Company in the years ending December 31, 2014, December 31, 2015, and December 31, 2016, are not permitted to exceed \$12.5 million. We were in compliance with all such Second Amendment covenants at December 31, 2016.

Interest charged under the Credit Agreement as revised by the Second Amendment is a function of the total debt to EBITDA ratio, adjusted quarterly. When the total debt to EBITDA ratio is greater than 4.0 to 1.00, the Term A loan is charged interest either at Prime + 4.75% or LIBOR + 5.75% , while the Term B loan is charged interest either at Prime + 5.25% or LIBOR + 6.25% . When the total debt to EBITDA ratio is equal to or less than 4.0 to 1.00, the Term A loan is charged interest either at Prime + 4.25% or LIBOR + 5.25% , while the Term B loan is charged interest either at Prime + 4.75% or LIBOR + 5.75% .

Fees for the Second Amendment of \$0.5 million were paid to the lenders on November 4, 2014.

On February 19, 2016, we entered into the Fourth Amendment to our Credit Agreement, on July 27, 2016, we entered into the Fifth Amendment to our Credit Agreement, and on October 27, 2016 we entered into the Sixth Amendment to our Credit Agreement. Pursuant to these amendments, our financial covenants were modified as follows:

- The annual capital expenditure limitation of \$12.5 million, which was in effect for the year ending December 31, 2016, has been revised to be \$8 million for the years ending December 31, 2016 and December 31, 2017.

- The total debt to EBITDA ratio of 3.25 to 1.0, which was in effect for the computation periods ending as of March 31, 2017, June 30, 2017, September 30, 2017, and December 31, 2017, has been revised to be 4.75 to 1.0 for those periods.

- The interest coverage ratio of 2.5 to 1.0 in effect for the computation period ending September 30, 2016, and 2.0 to 1.0 in effect for the computation period ending December 31, 2016, and 1.75 to 1.0 in effect for the computation periods ending as of March 31, 2017, June 30, 2017, September 30, 2017 has been revised to include December 31, 2017.

- The fixed charge coverage ratio of 1.20 to 1.0, which was in effect for the computation period ending as of December 31, 2017, has been revised to no longer apply to that period.

- The required minimum adjusted cash balance of \$30.0 million, which was in effect from March 31, 2016 through December 31, 2016, has been revised to be \$10.0 million from March 31, 2016 through September 30, 2016.

- The minimum trailing twelve month EBITDA of \$20.0 million, which was in effect from March 31, 2016 through December 31, 2016, has been revised by shortening such period to extend until June 30, 2016.

Our obligation to apply, on an annual basis, a percentage, which may fluctuate between 25% and 75% (determined based upon the Company's total debt to EBITDA ratio), of our annual excess cash flow as a mandatory prepayment of the loans under the Credit Agreement has also been modified. Pursuant to the Fifth Amendment, we are required to apply 75% of our excess cash flow each quarter as a mandatory prepayment of the loans under the Credit Agreement.

In addition, without the consent of the Agent and lenders holding more than 50% of the revolving loan commitments under the Credit Agreement,

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we are no longer permitted to request revolving loans; however, this will not affect our ability to utilize the letter of credit sub-facility under the Credit Agreement.

In connection with the Fourth amendment, we voluntarily prepaid \$22.5 million under the credit agreement, which was applied ratably to the Term A loan and the Term B loan. In addition, we deposited \$7.5 million into a deposit account which is subject to the exclusive control of the Agent. These funds will be remitted to the Agent for application to the term loans or other obligations, as applicable, under the credit agreement on the earlier to occur of (i) March 10, 2017 (or such later date not more than thirty (30) days thereafter as may be agreed by Agent in its sole discretion) and (ii) the occurrence and continuation of an event of default; however, all or a portion of these funds may also be returned to us if the Agent and the requisite lenders under the credit agreement elect otherwise in their sole discretion. In connection with the most recent amendment, we voluntarily prepaid \$7.5 million under the credit agreement, which was applied ratably to the Term A loan and the Term B loan. Accumulated amortization of debt issuance costs amounted to \$5.5 million at December 31, 2016.

#### 5. Commitments and Contingencies

We have entered into various non-cancelable operating lease agreements for certain of our office facilities and equipment with original lease periods expiring between 2017 and 2021. Certain of these arrangements have free rent periods and /or escalating rent payment provisions, and we recognize rent expense under such arrangements on a straight-line basis.

Future minimum rental commitments under non-cancelable leases as of December 31, 2016 are as follows (in thousands):

Year Ending December 31,	Amount
2017	\$ 1,800
2018	977
2019	903
2020	851
2021	310
Thereafter	—
Total	\$ 4,841

Lease expense was \$2.8 million, \$3.0 million and \$2.9 million for the years ended December 31, 2016, 2015 and 2014, respectively.

#### 6. Capital Stock

Since August 15, 2012, the authorized Common Stock has been 500,000,000 shares and the authorized preferred stock has been 50,000,000 shares.

#### 7. Stock-based Compensation

##### (a) Stock Options

Under the terms of the Performant Financial Corporation 2007 Stock Option Plan, incentive and nonqualified stock options may be granted for up to 4,000,000 shares of the Company's authorized but unissued Common Stock. Options granted under the Performant Financial Corporation 2007 Stock Option Plan generally vest over a five-year period. Performant Financial Corporation 2007 Stock Option Plan was terminated on the completion of its initial public offering in August 2012. No shares of our common stock are available under our 2007 Stock Option Plan other than for satisfying exercises of stock options granted under this plan prior to termination.

The terms of the Performant Financial Corporation 2012 Stock Incentive Plan provide for the granting of incentive stock options within the meaning of Section 422 of the Code to employees and the granting of nonstatutory stock options, restricted stock, stock appreciation rights, stock unit awards and cash-based awards to employees, non-employee directors and consultants. The Company has reserved 6,550,000 shares of common stock under the 2012 Plan. Options granted under the Performant Financial Corporation 2012 Stock Incentive Plan generally vest over periods of four or five-years.

The exercise price of incentive stock options shall generally not be less than 100% of the fair market value of the Common Stock subject to the option on the date that the option is granted. The exercise price of nonqualified stock



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options shall generally not be less than 85% of the fair market value of the Common Stock subject to the option on the date that the option is granted. Options issued under the Plans have a maximum term of 10 years and vest over schedules determined by the board of directors. Options issued under the Plans generally provide for immediate vesting of unvested shares in the event of a sale of the Company.

Total stock-based compensation expense charged as salaries and benefits expense in the consolidated statements of operations was \$4.7 million, \$5.0 million and \$3.7 million for the years ended December 31, 2016, 2015, and 2014, respectively. The following table sets forth a summary of our stock option activity for the year ended December 31:

	Outstanding Options	Weighted average exercise price per share	Weighted average remaining contractual life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2013	5,212,821	\$ 6.03	6.62	
Granted	254,000	9.69		
Forfeited	(410,625 )	10.53		
Exercised	(1,032,813 )	0.62		
Outstanding at December 31, 2014	4,023,383	7.18	6.41	
Granted	294,500	3.57		
Forfeited	(171,625 )	8.25		
Exercised	(29,135 )	1.62		
Outstanding at December 31, 2015	4,117,123	6.92	5.64	
Granted	115,000	1.74		
Forfeited	(327,327 )	8.26		
Exercised	(398,267 )	0.85		
Outstanding December 31, 2016	3,506,529	\$ 7.32	5.04	\$ 1,367
Vested, exercisable, and expected to vest <sup>(1)</sup> at December 31, 2016	3,475,885	\$ 7.32	5.02	\$ 1,364
Exercisable at December 31, 2016	2,871,260	\$ 7.33	4.57	\$ 1,297

(1) Options expected to vest reflect an estimated forfeiture rate.

The weighted-average grant-date exercise price of stock options granted during the years ended December 31, 2016, 2015 and 2014 was \$1.74, \$3.57 and \$9.69, respectively, per share. The aggregate intrinsic value of our stock options (the amount by which the market price of the stock on the date of exercise exceeded the exercise price of the option) exercised during the years ended December 31, 2016, 2015 and 2014, was \$0.4 million, \$0.1 million and \$8.8 million, respectively. At December 31, 2016, 2015, and 2014, there was \$2.0 million, \$4.7 million and \$7.5 million, respectively, of unrecognized stock-based compensation expense related to non-vested stock-based compensation arrangements, which the Company expects to recognize over a weighted-average period of 1.13 years as stock-based compensation expense.

Net cash proceeds from the exercise of stock options were \$0.3 million, \$0.04 million and \$0.6 million during 2016, 2015 and 2014, respectively. For the years ended December 31, 2016, 2015 and 2014, we realized a \$0.1 million, \$0.02 million and \$3.2 million tax benefit from the exercise of stock options, respectively.

The fair value of each option grant was estimated using the Black-Scholes option pricing model. Expected volatilities are calculated based on the historical volatility data of comparable peer companies over a term comparable to the expected term of the options issued. The expected term of the award is determined based on the average of the vesting term and the contractual term. Management monitors share option exercise and employee termination patterns to estimate forfeiture rates within the valuation model.

We estimated the fair value of options granted using a Black-Scholes option pricing model with the following assumptions:



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	For the Years Ended December 31,		
	2016	2015	2014
Expected volatility	51.5%	48.6%	51.0%
Expected dividends	—%	—%	—%
Expected term (years)	6.1	6.1	6.1
Risk-free interest rate	1.4%	1.7%	1.9%
Weighted-average estimated fair value of options granted during the year	\$0.86	\$1.71	\$4.85

Valuation and Amortization Method – The Company estimates the fair value of stock options granted using the Black-Scholes-Merton option pricing model. The fair value is then amortized on a straight line basis over the requisite service periods of the awards, which is generally the vesting period. Stock options typically have a ten year life from the grant date and vesting periods of four to five years. The fair value of the Company's common stock is based on the market price of the stock on the date of grant.

Expected Term – The Company's expected term represents the period that the Company's stock-based awards are expected to be outstanding. For awards granted subject only to service vesting requirements, the Company utilizes the simplified method under the provisions of FASB ASC 718-10-S99-1 (Staff Accounting Bulletin No. 107) for estimating the expected term of the stock-based award.

Expected Volatility – Because there is insufficient history of the Company's stock price returns, the Company lacks sufficient historical volatility data for its equity awards. Accordingly, the Company calculates the expected volatility using a composite made up of comparable peer companies and an approximate 54% company weighting over a term comparable to the expected term of the options issued.

Expected Dividend – The Company has never paid dividends on its common shares and currently does not intend to do so. Accordingly, the dividend yield percentage is zero for all periods.

Risk-Free Interest Rate – The risk-free interest rate used in the Black Scholes valuation method is based on the U.S. Treasury constant maturity interest rate whose term is consistent with the expected life of our stock options.

**(b) Restricted Stock Units**

The following table summarizes restricted stock unit activity for the year ended December 31:

	Number of Awards	Weighted average grant date fair value
Outstanding at December 31, 2014	461,592	\$ 9.28
Granted	954,860	3.3
Forfeited	(57,475 )	8.77
Vested and converted to shares	(129,703 )	9.15
Outstanding at December 31, 2015	1,229,274	\$ 4.67
Granted	1,470,154	1.74
Forfeited	(133,950 )	4.20
Vested and converted to shares	(505,238 )	4.31
Outstanding at December 31, 2016	2,060,240	\$ 2.70
Expected to vest at December 31, 2016	1,957,227	\$ 2.69

Share-based compensation cost for restricted stock units ("RSUs") is measured based on the closing fair market value of the Company's common stock on the date of grant. The Company recognizes share-based compensation cost over the award's requisite service period on a straight-line basis for time-based RSUs and on a graded basis for RSUs that are contingent on the achievement of performance conditions. The Company recognizes a benefit (shortfall) from share-based compensation in the Consolidated Statements of Shareholders' Equity.

The majority of RSUs that vested in 2016 and 2015 were net-share settled such that the Company withheld shares with value equivalent to the employees' minimum statutory obligation for the applicable income and other employment



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taxes, and remitted the cash to the appropriate taxing authorities. The total shares withheld were approximately 148,000 shares for 2016 and approximately 30,000 shares for 2015, and were based on the value of the RSUs on their respective vesting dates as determined by the Company's closing stock price. These net-share settlements had the effect of share repurchases by the Company as they reduced the number of shares that would have otherwise been issued as a result of the vesting and did not represent an expense to the Company.

At December 31, 2016 and 2015, there was \$3.7 million and \$4.1 million of compensation expense yet to be recognized related to non-vested restricted stock units. The unrecognized expense as of December 31, 2016 is expected to be recognized over the remaining weighted-average vested period of 2.37 years. 505,238 and 129,703 of the restricted stock units vested during the years ended December 31, 2016 and 2015, respectively. Restricted stock units granted under the Performant Financial Corporation 2012 Stock Incentive Plan generally vest over periods between one and four years.

#### 8. Employee Benefit Plan

The Company has a 401(k) Salary Deferral Plan (the Plan) covering all full-time employees who have met certain service requirements. Employees may contribute a portion of their salary up to the maximum limit established by the Internal Revenue Code for such plans. Employer contributions are discretionary. No matching contributions were made during 2016, 2015 and 2014.

#### 9. Income Taxes

The Company's income tax expense (benefit) consists of the following (in thousands):

	2016	2015	2014
Current:			
Federal	\$3,835	\$1,393	\$6,802
State	(1,293 )	1,164	2,600
	2,542	2,557	9,402
Deferred:			
Federal	\$(5,379)	\$(2,578)	\$(1,625)
State	(1,533 )	(365 )	(78 )
	(6,912 )	(2,943 )	(1,703 )
Total expense (benefit)	\$(4,370)	\$(386 )	\$7,699

The reconciliation between the amount computed by applying the U.S. federal statutory rate of 34% to income before taxes and the Company's tax provision for 2016, 2015, and 2014 is as follows:

	2016	2015	2014
Federal income at the statutory rate	34 %	35 %	35 %
State income tax, net of federal benefit	11 %	(26)%	10 %
Permanent differences	(1 )%	(9 )%	2 %
Work Opportunity Credit	1 %	9 %	(1 )%
Return to provision true-up	(1 )%	4 %	— %
Valuation Allowance	(18)%	— %	— %
Other	2 %	4 %	(1 )%
	28 %	17 %	45 %

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The following table summarizes the components of the Company's deferred tax assets and liabilities as of December 31, 2016, and 2015 (in thousands):

	2016	2015
Deferred tax assets		
Bad debt reserve	\$92	\$164
Vacation accrual	557	628
Workers Compensation	308	—
Nonqualified stock options	4,893	4,598
Debt issuance costs	279	454
Acquisition costs	66	103
State tax deferral	843	709
Deferred revenue	104	194
State tax credits	298	301
Net operating loss	217	170
Estimated liability for appeals	5,585	5,708
Other	146	114
Total deferred tax assets	13,388	13,143
Valuation allowance	(3,857 )	(452 )
Total deferred tax assets net of valuation allowance	9,531	12,691
Deferred tax liabilities:		
Identifiable intangible assets	(1,299 )	(9,157 )
Fixed assets	(4,009 )	(5,160 )
Other	(22 )	(22 )
Total deferred tax liabilities	(5,330 )	(14,339 )
Net deferred tax assets (liabilities)	\$4,201	\$(1,648)

As of December 31, 2016, the Company recorded a valuation allowance against deferred tax assets that are not more likely than not realizable based upon the assessment of all positive and negative evidence. The total amount of the valuation allowance at December 31, 2016 is \$3.9 million, which is an increase of \$3.4 million from the amount recorded as of December 31, 2015.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management has considered all potential sources of income including the reversal of deferred tax liabilities (including the impact of available carryback and carryforward periods) and projected future taxable income (loss) in making this assessment. Based upon the Company's cumulative three year loss position and projections for future taxable income (loss) over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will be unable to realize the benefits of these deductible differences. The amount of the deferred tax asset considered realizable, however, could change in the near term if estimates of future taxable income during the carryforward period change.

The Company has state tax credits of \$0.3 million, which, due to the Assembly Bill 93 and Senate Bill 90 signed on July 11, 2013, are now limited to a 10 year carryforward, and will expire in 2024.



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The following table reconciles the Company's unrecognized tax benefits as of December 31, 2016 from its unrecognized tax benefits as of December 31, 2014 (in thousands):

Unrecognized tax benefits balance at December 31, 2014	\$948
Increase related to prior year tax positions	217
Decrease related to prior year tax positions	(145 )
Increase related to current year tax positions	—
Settlements	—
Lapse of statute of limitations	(125 )
Unrecognized tax benefits balance at December 31, 2015	895
Increase related to prior year tax positions	311
Decrease related to prior year tax positions	(43 )
Increase related to current year tax positions	—
Settlements	—
Lapse of statute of limitations	(176 )
Unrecognized tax benefits balance at December 31, 2016	\$987

At December 31, 2016 and 2015, we had approximately \$1.0 million and \$0.9 million of unrecognized tax benefits, respectively. We do not expect any significant change in unrecognized tax benefits during the next twelve months.

The Company records interest expense and penalties related to unrecognized tax benefits in income tax expense. The amount of accrued interest was not material at December 31, 2016 and 2015, respectively. No penalties were recognized in 2016 or accrued at December 31, 2016, and 2015 respectively. Unrecognized tax benefits of approximately \$1 million which, if recognized, would favorably affect the Company's effective income tax rate.

The Company files federal and state income tax returns. For tax years before 2012, the Company is no longer subject to California, Texas, and certain state tax examinations. For tax years before 2013, the Company is no longer subject to Federal and certain other state tax examinations.

#### 10. Related Party Transactions

The Company did not have any material related party transactions for the years ending December 31, 2016, December 31, 2015 and December 31, 2014.

#### 11. Other Commitments and Contingencies

##### (a) Trust Funds

The Company collects principal and interest payments and collection costs on defaulted loans for various contracting agencies. Cash collections for some of the Company's customers are held in trust in bank accounts controlled by the Company. The Company remits trust funds to the contracting agencies on a regular basis. The amount of cash held in trust and the related liability are separated from and not included in the Company's assets and liabilities. Cash held in trust for customers totaled \$1.4 million and \$0.7 million at December 31, 2016 and 2015, respectively.

##### (b) Litigation

The Company, during the ordinary course of its operations, has been named in various legal suits and claims, several of which are still pending. In the opinion of management and the Company's legal counsel, such legal actions will not have a material effect on the Company's financial position or results of operations or cash flows.

#### 12. Subsequent Events

We have evaluated subsequent events through the date these consolidated financial statements were issued and there are no other events that have occurred that would require adjustments or disclosures to our consolidated financial statements.

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PERFORMANT  
FINANCIAL  
CORPORATION

By: /s/ Lisa C. Im  
Lisa C. Im  
Chief Executive Officer

Date: March 13, 2017

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Lisa C. Im and Hakan L. Orvell, and each of them, his or her true and lawful attorneys-in-fact, each with full power of substitution, for him or her in any and all capacities, to sign any amendments to this report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact or their substitute or substitutes may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Name	Title	Date
/s/ Lisa C. Im Lisa C. Im	Chief Executive Officer (Principal Executive Officer) and Board Chair	March 13, 2017
/s/ Hakan L. Orvell Hakan L. Orvell	Chief Financial Officer (Principal Financial and Accounting Officer)	March 13, 2017
/s/ Todd R. Ford Todd R. Ford	Director	March 13, 2017
/s/ Brian P. Golson Brian P. Golson	Director	March 13, 2017
/s/ Bradley F. Fluegel Bradley F. Fluegel	Director	March 13, 2017
/s/ Bruce Hansen Bruce Hansen	Director	March 13, 2017
/s/ William D. Hansen William D. Hansen	Director	March 13, 2017

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## SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS

For the years ended December 31, 2016, 2015 and 2014

Allowance for doubtful accounts (in thousands):

Description	Balance at Beginning of Period	Additions Charged against Revenue	Recoveries	Charge-offs	Balance at End of Period
2016	\$ 386	—	(162 )	—	\$ 224
2015	\$ 32	354	—	—	\$ 386
2014	\$ 32	—	—	—	\$ 32

Estimated allowance and liability for appeals (in thousands):

Description	Balance at Beginning of	Additions Charged against Revenue	Appeals found in Providers Favor	Balance at End of Period
2016	\$ 19,118	2,085	(1,898 )	\$ 19,305
2015	\$ 18,625	2,109	(1,616 )	\$ 19,118
2014	\$ 16,443	8,624	(6,442 )	\$ 18,625

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EXHIBIT INDEX

Exhibit  
Number Description

- 2.1 Agreement and Plan of Merger, dated as of January 28, 2015, by and among Performant Financial Corporation, Project Phoenix Merger Sub, Inc., Premier Healthcare Exchange, Inc. and the other parties thereto (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed January 29, 2015)
- 3.1 Restated Certificate of Incorporation of Registrant (incorporated by reference to Exhibit 3.1(b) to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
- 3.2 Amended and Restated Bylaws of Registrant (incorporated by reference to Exhibit 3.2(b) to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 4.2 Amended and Restated Registration Rights Agreement, dated as of August 15, 2012, among the Registrant and the persons listed thereon (incorporated by reference to Exhibit 4.2 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.1 Form of Indemnification Agreement between the Registrant and its officers and directors (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
- 10.2 2004 Equity Incentive Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.2 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
- 10.3 2004 DCS Holdings Stock Option Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.3 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
- 10.4 2007 Stock Option Plan and form of agreements thereunder (incorporated by reference to Exhibit 10.4 to the Company's Registration Statement on Form S-1 filed July 23, 2012)
- 10.5 Recovery Audit Contractor contract by and between Diversified Collection Services, Inc. and Center for Medicare and Medicaid Services dated as of October 3, 2008, as amended (incorporated by reference to Exhibit 10.5 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.6 Credit Agreement, dated as of March 19, 2012, by and among DCS Business Services, Inc., the Lenders party Hereto, Madison Capital Funding LLC, and ING Capital (incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.7 Form of Change of Control Agreement, as amended (incorporated by reference to Exhibit 10.7 to the Company's Registration Statement on Form S-1/A filed July 30, 2012)
- 10.8 Employment Agreement between the Registrant and Lisa Im, dated as of April 15, 2012, as amended (incorporated by reference to Exhibit 10.8 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
- 10.9 Employment Agreement between the Registrant and Jon D. Shaver dated as of March 31, 2003, as amended (incorporated by reference to Exhibit 10.9 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)

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- 10.10 Repurchase Agreement between the Registrant and Lisa C. Im dated as of July 3, 2012 (incorporated by reference to Exhibit 10.10 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
  - 10.11 Repurchase Agreement between the Registrant and Jon D. Shaver dated as of July 3, 2012 (incorporated by reference to Exhibit 10.11 to the Company's Registration Statement on Form S-1 filed July 3, 2012)
  - 10.12 Director Nomination Agreement between the Registrant and Parthenon DCS Holdings, LLC dated as of July 20, 2012 (incorporated by reference to Exhibit 10.12 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
  - 10.13 Advisory Services Agreement between Diversified Collection Services, Inc. and Parthenon Capital, LLC dated as of January 8, 2004, as amended (incorporated by reference to Exhibit 10.13 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
  - 10.14 Termination of the Advisory Services Agreement between Diversified Collection Services, Inc. and Parthenon Capital, LLC dated as of January 8, 2004, as amended, dated as of April 13, 2012 (incorporated by reference to Exhibit 10.14 to the Company's Registration Statement on Form S-1/A filed July 23, 2012)
  - 10.15 2012 Stock Incentive Plan (incorporated by reference to Exhibit 10.15 to the Company's Annual Report on Form 10-K filed March 13, 2015)
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Exhibit Number	Description
10.16	Amendment No. 1 to Credit Agreement Credit Agreement, dated as of March 19, 2012, by and among DCS Business Services, Inc., the Lenders party thereto, Madison Capital Funding LLC, and ING Capital (incorporated by reference to Exhibit 10.16 to the Company's Annual Report on Form 10-K filed March 13, 2015)
10.17	Amendment No. 2 to Credit Agreement, dated as of November 4, 2014, by and among Performant Business Services, Inc., the Lenders thereto, and Madison Capital Funding LLC. (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q filed November 10, 2014)
10.18	Amendment No. 4 to Credit Agreement, dated as of February 19, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC. (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed February 25, 2016)
10.19	Amendment No. 5 to Credit Agreement, dated as of July 26, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed August 1, 2016)
10.20	Amendment No. 6 to Credit Agreement, dated as of October 27, 2016, by and among Performant Business Services, Inc., the Lenders party hereto, and Madison Capital Funding LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed October 31, 2016)
21	List of Subsidiaries
23	Consent of KPMG LLP, Independent Registered Public Accounting Firm
24	Powers of Attorney (included in the signature page to this report)
31.1	Rule 13a-14(a)/15d-14(a) Certification, executed by Lisa C. Im
31.2	Rule 13a-14(a)/15d-14(a) Certification, executed by Hakan L. Orvell
32.1	Furnished Statement of the Chief Executive Officer under 18 U.S.C. Section 1350
32.2	Furnished Statement of the Chief Financial Officer under 18 U.S.C. Section 1350
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Scheme
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase

101.PRE XBRL Taxonomy Extension Presentation Linkbase

\* Filed herewith